

CONSOLIDATED FINANCIAL STATEMENTS AND OTHER INFORMATION
INDIANA UNIVERSITY HEALTH, INC. AND SUBSIDIARIES
AS OF JUNE 30, 2018 AND DECEMBER 31, 2017 AND FOR THE SIX MONTHS ENDED
JUNE 30, 2018 AND 2017

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MANAGEMENT'S DISCUSSION OF FINANCIAL PERFORMANCE
As of June 30, 2018 and December 31, 2017 and for the six months ended June 30, 2018
and 2017

Indiana University Health, Inc. and subsidiaries
Management's Discussion of Financial Performance
As of June 30, 2018 and December 31, 2017 and for the six months ended June 30,
2018 and 2017
(Thousands of Dollars)

The financial statement information and other data as of June 30, 2018 and December 31, 2017 and for the six months ended June 30, 2018 and 2017 are derived from the unaudited consolidated financial statements and other records of Indiana University Health, Inc. (Indiana University Health) and subsidiaries (collectively referred to herein as the Indiana University Health System). The consolidated financial statements include all adjustments, consisting of normal recurring and other accruals, which management of the Indiana University Health System considers necessary for a fair presentation of financial position, results of operations and changes in net assets, and cash flows for these periods in conformity with U.S. generally accepted accounting principles (GAAP). The financial data relating to the Obligated Group and the Obligated Group and Designated Affiliates, as defined in the Indiana University Health Obligated Group Master Trust Indenture, as amended, is provided as supplementary information.

The accompanying financial statement information should be read in conjunction with the audited consolidated financial statements and the notes thereto of Indiana University Health and subsidiaries as of and for the years ended December 31, 2017 and 2016 (not included herein).

Nature of Operations

The principal operating activities of the Indiana University Health System are conducted at owned facilities or majority-owned or controlled subsidiaries and consist of the following:

Downtown Hospitals of the Academic Health Center – Consist of three acute, tertiary, quaternary care, and diagnostic facilities, licensed as a single hospital, which constitutes the principal hospital activities of the academic health center and whose operations are located in the downtown area of Indianapolis, Indiana. These three hospitals, Methodist Hospital, University Hospital, and Riley Hospital, are located on or near the campus of Indiana University-Purdue University Indianapolis and the Indiana University School of Medicine (the School of Medicine).

Central Indiana Facilities – Consist of three acute care hospitals, a critical access hospital, and an acute care rehabilitation hospital located in the western and northern suburban areas of metropolitan Indianapolis, Indiana. Principal hospital subsidiaries include Indiana University Health North Hospital, Inc. (North), Indiana University Health West Hospital, Inc. (West), Indiana University Health Saxony Hospital (Saxony), Indiana University Health Tipton Hospital, Inc. (Tipton), and Rehabilitation Hospital of Indiana, Inc. (RHI).

Statewide Facilities – Consist of acute care hospitals and health care systems located in Lafayette, Monticello, Frankfort, Muncie, Hartford City, Portland, Bedford, Bloomington, and Paoli, Indiana. Principal hospital subsidiaries include Indiana University Health Arnett, Inc. (Arnett), Indiana University Health White Memorial Hospital, Inc. (White), Indiana University Health Frankfort Hospital, Inc. (Frankfort), Indiana University Health Ball Memorial Hospital, Inc. and subsidiaries (Ball Memorial) including Indiana University Health Blackford Hospital, Inc. (Blackford), Indiana University Health Jay, Inc. (Jay), Indiana University Health Bedford, Inc. (Bedford), and Indiana University Health Bloomington, Inc. and subsidiaries (Bloomington) including Indiana University Health Paoli, Inc. (Paoli).

Physician Operations – Consist of physician offices and physician-group practices and clinics. Principal subsidiaries or divisions include Indiana University Health Physicians (IUHP), a nonprofit organization with locations primarily in Indianapolis, Indiana, Indiana University Health Arnett Physicians, Indiana University Health Ball Memorial Physicians, Inc., and Indiana University Health Southern Indiana Physicians, Inc.

Ambulatory Care – Consists of personal and home health care services, occupational health services, outpatient oncology services, outpatient surgery centers, and urgent care centers that are located throughout the State of Indiana. Principal divisions or subsidiaries include Indiana University Health Home Care, Indiana University Health Occupational Health Centers, Workplace Health Services, Indiana University Health Central Indiana Cancer Centers, Indiana University Health Morgan, several surgery center joint ventures, and an urgent care center joint venture.

Medical Risk – Consists of the medical management of health care services of members whose health care coverage is provided by the managed care networks of the Indiana University Health System. Includes health maintenance organizations and other insurance related organizations that provide health plan services to fully-insured and self-insured members residing in Indiana. Insurance offerings include commercial group products (fully-insured and self-insured), Medicare Advantage products, and Medicaid management services. The Indiana University Health System also participates in the medical management of Medicare fee-for-service members through a NextGen Accountable Care Organization contract with the Centers for Medicare and Medicaid (CMS). The Indiana University Health System no longer provides products on the Health Insurance Marketplace (Exchange) as of January 1, 2018.

Foundations – Indiana University Health is the sole corporate member of Indiana University Health Foundation, Inc. (Indiana University Health Foundation), formerly known as Methodist Health Foundation, Inc., which aids and supports Methodist Hospital and other programs and areas of Indiana University Health. Prior to December 31, 2017, Tipton was the sole corporate member of Tipton County Health Care Foundation, Inc. (Tipton Foundation), which aids in carrying out the mission of Tipton; Arnett was the sole corporate member of Indiana University Health Arnett Hospital Foundation, Inc. (Arnett Foundation), which aids and supports Arnett; and the corporate members of Indiana University Health Paoli Hospital Foundation, Inc. (Paoli Foundation), which aids and supports Paoli, were Paoli, Bloomington, and the Board of

Commissioners of Orange County, Indiana. On December 31, 2017, Tipton Foundation, Arnett Foundation and Paoli Foundation were merged into the Indiana University Health Foundation. Those foundations will continue to serve the same purposes as prior to the mergers. Ball Memorial is the sole corporate member of Indiana University Health Ball Memorial Hospital Foundation, Inc. (BMH Foundation), which aids in carrying out the mission of Ball Memorial and Blackford. RHI is the sole corporate member of RHI Foundation, Inc. (RHI Foundation), which aids and supports RHI.

Consolidated Statement of Operations and Changes in Net Assets
(Compared to June 30, 2017)

Revenue. Total operating revenue of \$3,105,345 for the six months ended June 30, 2018 increased 4.0%, or \$118,760 compared to the six months ended June 30, 2017 \$2,986,585.

Patient service revenue, when excluding increased reimbursement related to the Medicaid Assessment Fee program, upper payment limit reimbursement (UPL), and state disproportionate share revenue (DSH), increased by \$141,468, or 5.8% for the six months ended June 30, 2018 compared to the six months ended June 30, 2017. The increase reflects the effect of annual rate increases as well as increased inpatient volumes (see below).

The table below shows discharges and surgery cases by division.

	Year over Year			
	<u>6/30/2018</u>	<u>6/30/2017</u>	<u>Variance</u>	<u>Percentage</u>
<u>Inpatient Discharges</u>				
Consolidated	58,851	55,636	3,215	5.8%
Downtown	25,219	24,250	969	4.0%
Statewide	23,424	21,435	1,989	9.3%
Central	10,208	9,951	257	2.6%
<u>Total Surgery Cases</u>				
Consolidated	53,975	53,904	71	0.1%
Downtown	16,971	17,012	(41)	-0.2%
Statewide	12,451	12,485	(34)	-0.3%
Central	6,807	6,955	(148)	-2.1%
Ambulatory	17,746	17,452	294	1.7%

During 2012, the Indiana General Assembly approved a hospital assessment fee program (Medicaid Assessment Fee). Under this program, the Office of Medicaid Policy and Planning (OMPP) collects a fee from eligible hospitals. The fee is used in part to increase reimbursement to eligible hospitals for services provided in both fee-for-service and managed care programs, and as the state share of DSH payments. The program was effective retroactively from July 1, 2011, and continued through June 30, 2013, and was

subsequently extended through June 30, 2019. For the six months ended June 30, 2018, increased reimbursement related to the Medicaid Assessment Fee program totaled \$195,629. For the six months ended June 30, 2017, increased reimbursement related to the Medicaid Assessment Fee program totaled \$124,987.

The Indiana University Health System qualifies for supplemental Medicaid payments through the UPL program under Indiana law. The UPL program was established to pay qualifying providers the difference between what Medicare would have paid and what Medicaid actually paid. As of June 30, 2018, \$26,017 of UPL revenue was recognized compared to \$3,501 for the prior year.

Certain hospitals of the Indiana University Health System are Medicaid DSH providers under Indiana law and, as such, are eligible to receive state DSH payments. The amount of these additional state DSH funds is dependent on regulatory approval by agencies of the federal and state governments and is determined by the level, extent, and cost of uncompensated care (as defined) and various other factors.

In the six months ended June 30, 2017, \$30,346 of DSH revenue was received. Based upon final rule by the Centers for Medicare and Medicaid Services, net of reserves totaling (\$18,346) and (\$15,095), related to the state fiscal years ended June 30, 2017 and 2016, respectively, were recognized against the DSH revenue received, netting (\$3,095) of DSH revenue recognized in 2017. No DSH revenue was received for the six months ended June 30, 2018. The amount of state DSH and UPL funds vary by year and the amount to be received in future periods cannot be guaranteed.

Member premium revenue aggregated \$171,286 for the six months ended June 30, 2018 and \$291,073 for the prior year. The decrease in member premium revenue is mainly related to not offering products on the Exchange in 2018.

Other operating revenue of \$115,309 for the six months ended June 30, 2018 was comparable to the six months ended June 30, 2017, \$114,483.

Expenses. Total operating expenses of \$2,826,267 increased by 1.0%, or \$27,846 compared to the six months ended June 30, 2017, \$2,798,421.

Salaries, wages, and benefits increased 6.0%, or \$84,440, to \$1,502,678 compared to the same period in the prior year. The increase is primarily a result of base pay increases effective mid-2017 and 2018, as well as an increase in full time equivalent employees (FTEs). The average number of FTEs was 29,629 and 28,349 for the six months ended June 30, 2018 and 2017, respectively.

Supplies, drugs, purchased services, and other expenses of \$1,000,387 increased 6.5%, or \$61,237, compared to the same period in the prior year, \$939,150. The increase was primarily driven by increases in supplies expense due to inpatient volumes and continued increases in pharmaceutical expenses.

Fees related to the Medicaid Assessment Fee program were \$67,631 for the six months ended June 30, 2018, compared to \$61,227 in the same period in the prior year.

Health claims to providers expenses of \$118,112 decreased by 52.6%, or \$131,309, compared to the same period in the prior year, \$249,421. The decrease in claims expense is mainly related to not offering Exchange products in 2018.

Depreciation and amortization expense of \$117,214 increased 3.3%, or \$3,725, from the same period in the prior year of \$113,489.

Interest expense of \$20,245 increased by 19.8%, or \$3,349, compared to the same period in the prior year, \$16,896, mainly due to an increase in the balance of debt outstanding, a higher proportion of underlying fixed-rate debt, and rising short-term interest rates in the market.

Investment income amounted to \$43,196 for the six months ended June 30, 2018, including \$47,846 of interest and dividend income, \$49,858 of unrealized losses on investments, and \$45,208 of realized gains on investments, net of fees. For the six months ended June 30, 2017, investment income aggregated to \$222,661, which included \$35,843 of interest and dividend income, \$175,805 of unrealized gains on investments, and \$11,013 of realized gains on investments, net of fees. Gains (losses) on interest rate swaps aggregated \$15,144 and (\$1,051) for the six months ended June 30, 2018, and 2017, respectively.

Consolidated Balance Sheet (Compared to December 31, 2017)

Consolidated Financial Position. Total cash and investments (which principally consist of cash and cash equivalents, short-term investments, current portion of assets limited as to use, board-designated funds and other investments, and donor-restricted funds) amounted to \$5,801,106 at June 30, 2018, and \$5,443,259 at December 31, 2017. The number of days cash and investments on hand, excluding donor-restricted funds, trustee-held funds and funds held by insurance captives, was 375 days at June 30, 2018 and 350 days as of December 31, 2017. The number of days revenue in receivables (excluding the increased reimbursement under the Medicaid Assessment Fee program and related receivable) was 60 days at June 30, 2018, and 62 days at December 31, 2017. The number of days expenses in accounts payable, accrued expenses, and certain other current liabilities (excluding fees associated with the Medicaid Assessment Fee program and related liability) was 50 days at June 30, 2018, and 56 days at December 31, 2017.

Net current assets, or working capital, increased 35.4% to \$835,967 at June 30, 2018 compared to \$617,365 at December 31, 2017 primarily due to the repayment of the drawn balance on the lines of credit with new debt proceeds from the issuance of the Series 2018A bonds as well as an increase in current portion of assets limited as to use in the current year. Net property and equipment of \$2,324,531 decreased \$14,866 from December 31, 2017 due to continuing depreciation, partially offset by capital purchases. Firm commitments for construction-in-progress totaled \$129,146 at June 30, 2018.

Indiana University Health Obligated Group has executed direct-pay letter-of-credit agreements in support of all of its publicly remarketed variable-rate bond series, which require the credit provider to purchase bonds in the event the bonds are not remarketed. In addition, it has executed direct purchase agreements, whereby the credit provider purchases bonds for a predetermined period of time, after which the agreement must be

extended or the bonds must be remarketed or reissued. In each of these two instances, the bonds have a longer nominal maturity than the agreement, but the existence and terms of these agreements allow for the long-term classification of the associated variable-rate bond series. When these letter of credit agreements have expiration dates within the succeeding 12-month period, a greater portion of the associated debt is classified as current, because if not otherwise extended, the agreements with the credit providers would require the principal balance of the related bonds to be repaid over a shortened time frame. No such amounts were reclassified to current portion of long-term debt as of June 30, 2018 or December 31, 2017.

On April 17, 2018, Indiana University Health issued \$354,000 in par value of Series 2018A taxable, fixed-rate bonds. A portion of the proceeds was used to advance refund \$60,500 in par amount of the Indiana Finance Authority Hospital Revenue Bonds, Series 2011N (Indiana University Health Obligated Group), to refinance all of the Indiana Finance Authority Hospital Revenue Bonds, Series 2015C (Indiana University Health Obligated Group) in the amount of \$50,000, and to repay the balance on Indiana University Health's revolving commercial bank line of credit in the amount of \$50,000. Another portion of the proceeds was used to finance the termination payments related to certain interest rate swaps (see Notes to Consolidated Financial Statements Note 6). Remaining proceeds will be used for general corporate purposes.

On October 12, 2017, through the Indiana Finance Authority, Indiana University Health amended its Series 2011H and 2011I tax exempt, variable-rate, direct-purchase bonds changing both the variable rate and principal repayment schedule. Indiana University Health sold the bonds to a new direct purchaser with the expiration date of the direct-purchase agreement being the same date as the final maturity of the bonds.

As of June 30, 2018 and December 31, 2017, the Indiana University Health System maintained several lines of credit totaling \$230,000 and \$105,000, respectively. As of June 30, 2018 no amounts are drawn on the lines of credit. As of December 31, 2017, the total balance drawn on the lines of credit was \$50,000, which was included in the current portion of long-term debt as the line of credit associated with the drawn balance had an expiration date of June 30, 2018. The balance on the line was repaid in April 2018, in conjunction with the issuance of the Series 2018A bonds.

Unrestricted net assets, or equity, amounted to \$6,907,373 at June 30, 2018 and \$6,594,120 at December 31, 2017 and includes the net unrealized losses on swaps of \$43,718 and \$75,813 at June 30, 2018 and December 31, 2017, respectively.

Strategic Initiatives

As part of its commitment to being a leader in both the treatment of patients with complex illnesses as well as in the transition from payment models that reward volume to those that reward value, the Indiana University Health System continuously evaluates its operations with goals to achieve superior clinical outcomes and to treat patients in the most beneficial and least resource-intensive settings possible as it works to effectively manage the health of populations.

As part of this continual evaluation, management engages in discussions at times with unaffiliated third parties regarding potential affiliations, acquisitions, dispositions, divestitures, joint ventures, and other transactions. In addition, management considers the potential to change the services offered at a given facility or consolidate and/or eliminate redundant services. Such changes could be material, impacting the future composition of the system.

In October 2017, Indiana University Health announced plans to open a pediatric specialty care office as well as a primary care office in Fort Wayne, Indiana in 2018. The pediatric specialty care office opened in January 2018 and the primary care office opened August 1, 2018. The office openings are in response to the Fort Wayne community's growing need for primary care, to attract and retain quality physicians in the area, and to continue efforts to make Indiana a healthier state overall.

Capital Expenditures

In December 2017, the Indiana University Health Board of Directors approved a capital expenditure plan to integrate maternity and neonatal services at Riley Hospital. When finished, Riley Hospital will be able to accommodate more than 3,800 deliveries annually (up from approximately 3,200), including those from high risk mothers, and provide care for babies with known congenital anomalies.

Also in December 2017, the Indiana University Health Board of Directors approved a capital expenditure plan to build a cancer care facility at North. The plan is to build an approximately 88,000 square foot, two-story patient experience-focused facility that will provide full service cancer treatment options and necessary support services.

In October 2017, the Indiana University Health Board of Directors approved a capital expenditure plan to build a regional health campus in Bloomington, Indiana, which will increase Bloomington's ability to improve patient care by providing more opportunities for collaboration among clinical, research, and medical staff and faculty. This plan will allow the Indiana University School of Medicine to expand its medical education programs and research opportunities on the Bloomington campus. As part of this plan, Bloomington will build a replacement hospital, which will further its mission of providing cutting-edge health services to the region.

Also in October 2017, the Indiana University Health Board of Directors approved a capital expenditure plan for expansion at West. The expansion is expected to include approximately 48 additional inpatient beds, a new operating room, and additional support services space to accommodate rising patient volumes.

In April 2015, the Indiana University Health Board of Directors approved a plan to consolidate downtown Indianapolis adult services to one medical campus centered on Capitol Avenue and 16th Street (the current site of Methodist Hospital). As Indiana University Health is committed to improving the health of its patients and communities, the plan also includes the development of an array of ambulatory care services for residents of the neighborhoods around the downtown Indianapolis campus. The adult service medical campus is expected to include a medical education building and faculty offices on-

site to enhance ongoing collaboration with the Indiana University School of Medicine and support the tripartite mission of clinical care, research, and education. While the Board has authorized certain preliminary activities, including strategic planning and analysis related to this plan, it has not approved the scope of this project or total capital expenditures related thereto.

Certain statements are forward-looking statements that are based on the beliefs of, and assumptions made by, the management of Indiana University Health. Such forward looking statements involve known and unknown risks, uncertainties and other factors that may cause the performance of the Indiana University Health System to be materially different from any expected future performance.

Strategic Transactions

On November 20, 2017, Indiana University Health entered into an Affiliation and Asset Transfer Agreement with Jay County Hospital, a 25-bed critical access hospital located in Portland, Indiana. Effective March 1, 2018, Jay County Hospital transferred substantially all of its assets and liabilities to Indiana University Health Jay, Inc., a newly created nonprofit organization, and Indiana University Health became the sole corporate member. Indiana University Health recognized the assets acquired and the liabilities assumed, measured at their fair values as of the date of acquisition, and recognized an inherent contribution as a result of the transaction in the amount of \$31,860.

Indiana University Health held 50% membership interests in both MDwise, Inc. and MDwise Medicaid Network, Inc., with Health and Hospital Corporation of Marion County (HHC) holding the other 50% membership interest. On October 31, 2017, a sponsorship transfer agreement was entered into with Michigan-based McLaren Health Care (McLaren), whereby Indiana University Health and HHC would transfer their membership interests in MDwise, Inc. and MDwise Medicaid Network, Inc. to McLaren. The transaction closed on December 29, 2017, and resulted in the recognition of a gain of \$68,152 in other revenue on the consolidated statement of operations and changes in net assets.

On June 1, 2017, Indiana University Health sold two outpatient hemodialysis in-center units in downtown Indianapolis and a home dialysis program to ISD Renal, Inc., a subsidiary of DaVita, Inc. Through the sale transaction, Indiana University Health sold substantially all of the assets owned and used by the dialysis business for \$25,763. Indiana University Health recognized a gain of \$25,285 related to the transaction.

On November 10, 2016, Indiana University Health entered into a lease agreement with Clinton County to lease the hospital building and other related property and equipment and to assume the operations of Frankfort Hospital, the Clinton County-owned hospital, effective June 1, 2017. As of the effective date, Indiana University Health began a five-year lease with renewal options for the 25-bed county-owned critical access hospital and affiliated medical offices. The annual minimum rental rate is \$1,000. Additional rent can be triggered if the hospital reaches certain net income targets, which is not expected to occur in 2018.

Adjusted Operating Income

The following table adjusts operating income for significant one-time transactions or significant items that relate to prior years. Management uses these measures internally for planning, forecasting, and evaluating the performance of the Indiana University Health System. The table also removes operating income attributable to noncontrolling interests, which primarily relates to ambulatory surgery centers in which third parties hold significant noncontrolling interests. Internally, management reviews operating results after allocation to noncontrolling interests, in part, because a significant portion of the operating results of these entities is distributed to the noncontrolling interest holders each period. Non-GAAP measures should be considered in addition to, not as a substitute for, or as superior to, measures of financial performance prepared in accordance with GAAP. For additional information on the programs that resulted in these adjustments and on noncontrolling interests refer to the consolidated financial statements and the notes thereto of Indiana University Health and subsidiaries for the six months ended June 30, 2018 and 2017.

Indiana University Health, Inc. and subsidiaries
Adjusted Operating Income
(Thousands of Dollars)

	Six Months Ended	
	June 30	
	2018	2017
Operating income as reported	\$ 279,078	\$ 188,164
Noncontrolling interests in subsidiaries	(68,019)	(53,645)
DSH	-	15,095
Gain on sale of dialysis business	-	(25,285)
Operating income adjusted	\$ 211,059	\$ 124,329
Operating margin adjusted	7.1%	4.3%

- During 2017, reserves were recorded on DSH revenue related to the state fiscal year ended 2016.
- During 2017, Indiana University Health sold its dialysis business (see Strategic Transactions).

CONSOLIDATED FINANCIAL STATEMENTS
As of June 30, 2018 and December 31, 2017 and for the six months ended June 30, 2018
and 2017

Indiana University Health, Inc. and Subsidiaries
Consolidated Balance Sheets
(Thousands of Dollars)

	June 30 2018	December 31 2017
Assets	(Unaudited)	(Audited)
Current assets:		
Cash and cash equivalents	\$ 345,513	\$ 414,674
Short-term investments	77,636	5,081
Current portion of assets limited as to use	191,667	143,611
Patient accounts receivable	863,880	870,252
Other receivables	151,230	156,281
Prepaid expenses	65,110	46,026
Inventories	89,527	85,856
Total current assets	1,784,563	1,721,781
Assets limited as to use:		
Board-designated investment funds and other investments	5,097,476	4,791,654
Donor-restricted investment funds	88,814	88,239
Total assets limited as to use, less current portion	5,186,290	4,879,893
Property and equipment:		
Cost of property and equipment in service	5,591,931	5,536,733
Less accumulated depreciation	(3,334,713)	(3,267,111)
	2,257,218	2,269,622
Construction-in-progress	67,313	69,775
Total property and equipment, net	2,324,531	2,339,397
Other assets:		
Equity interest in unconsolidated subsidiaries	42,070	44,103
Interest in net assets of foundations	22,460	22,038
Goodwill, intangibles, and other assets	314,882	341,810
Total other assets	379,412	407,951
Total assets	\$ 9,674,796	\$ 9,349,022

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Indiana University Health, Inc. and Subsidiaries
Consolidated Balance Sheets (continued)
(Thousands of Dollars)

	June 30	December 31
	2018	2017
	(Unaudited)	(Audited)
Liabilities and net assets		
Current liabilities:		
Accounts payable and accrued expenses	\$ 491,979	\$ 525,199
Accrued salaries, wages, and related liabilities	243,169	296,053
Accrued health claims	75,693	95,844
Estimated third-party payer allowances	83,127	87,215
Current portion of long-term debt	54,628	100,105
Total current liabilities	948,596	1,104,416
Noncurrent liabilities:		
Long-term debt, less current portion	1,548,500	1,351,115
Interest rate swaps	43,718	75,813
Accrued pension obligations	10,322	10,134
Accrued medical malpractice claims	66,940	63,626
Other	35,496	33,876
Total noncurrent liabilities	1,704,976	1,534,564
Total liabilities	2,653,572	2,638,980
Net assets:		
Indiana University Health	6,669,989	6,368,314
Noncontrolling interest in subsidiaries	237,384	225,806
Total unrestricted	6,907,373	6,594,120
Temporarily restricted	42,897	42,004
Permanently restricted	70,954	73,918
Total net assets	7,021,224	6,710,042
Total liabilities and net assets	\$ 9,674,796	\$ 9,349,022

Indiana University Health, Inc. and Subsidiaries
Consolidated Statements of Operations and Changes in Net Assets
(Thousands of Dollars)

	Six Months Ended June 30		Three Months Ended June 30	
	2018	2017	2018	2017
	(Unaudited)		(Unaudited)	
Revenues:				
Patient service revenue	\$ 2,818,750	\$ 2,581,029	\$ 1,433,747	\$ 1,277,827
Member premium revenue	171,286	291,073	86,197	141,057
Other revenue	115,309	114,483	55,538	85,671
Total operating revenues	3,105,345	2,986,585	1,575,482	1,504,555
Expenses:				
Salaries, wages, and benefits	1,502,678	1,418,238	758,808	717,093
Supplies, drugs, purchased services, and other	1,000,387	939,150	508,106	486,975
Hospital assessment fee	67,631	61,227	33,929	30,613
Health claims to providers	118,112	249,421	59,305	127,330
Depreciation and amortization	117,214	113,489	58,941	56,429
Interest	20,245	16,896	11,199	8,680
Total operating expenses	2,826,267	2,798,421	1,430,288	1,427,120
Operating income	279,078	188,164	145,194	77,435
Nonoperating income:				
Investment income, net	43,196	222,661	10,786	79,369
Gains (losses) on interest rate swaps, net	15,144	(1,051)	7,681	(630)
Inherent contribution of acquired entity	31,860	-	(939)	-
Debt extinguishment and other	(975)	5	(1,822)	-
Total nonoperating income	89,225	221,615	15,706	78,739
Consolidated excess of revenues over expenses	368,303	409,779	160,900	156,174
Less amounts attributable to noncontrolling interest in subsidiaries	68,019	53,645	34,177	25,642
Excess of revenues over expenses attributable to Indiana University Health and subsidiaries	300,284	356,134	126,723	130,532

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Indiana University Health, Inc. and Subsidiaries
Consolidated Statements of Operations and Changes in Net Assets (continued)
(Thousands of Dollars)

	Six Months Ended June 30 2018			Six Months Ended June 30 2017		
	(Unaudited)			(Unaudited)		
	Total	Controlling	Noncontrolling	Total	Controlling	Noncontrolling
Unrestricted net assets:						
Consolidated excess of revenues over expenses	\$ 368,303	\$ 300,284	\$ 68,019	\$ 409,779	\$ 356,134	\$ 53,645
Contributions for capital expenditures	833	833	-	1,640	1,640	-
Distributions to noncontrolling interests	(57,011)	-	(57,011)	(64,302)	-	(64,302)
Contributions from noncontrolling interests	570	-	570	-	-	-
Other	558	558	-	(16,688)	(16,957)	269
	<u>313,253</u>	<u>301,675</u>	<u>11,578</u>	<u>330,429</u>	<u>340,817</u>	<u>(10,388)</u>
Temporarily restricted net assets:						
Change in beneficial interest in net assets of foundations	694	694	-	-	-	-
Contributions	683	683	-	914	914	-
Investment return	1	1	-	1,100	1,100	-
Net assets released from restrictions	(953)	(953)	-	(994)	(994)	-
Other	468	468	-	13,736	13,736	-
	<u>893</u>	<u>893</u>	<u>-</u>	<u>14,756</u>	<u>14,756</u>	<u>-</u>
Permanently restricted net assets:						
Change in beneficial interest in net assets of foundations	(269)	(269)	-	8	8	-
Contributions and other	148	148	-	(27)	(27)	-
Beneficial interest reclassification	-	-	-	852	852	-
Other	(2,843)	(2,843)	-	-	-	-
	<u>(2,964)</u>	<u>(2,964)</u>	<u>-</u>	<u>833</u>	<u>833</u>	<u>-</u>
Increase (decrease) in net assets	311,182	299,604	11,578	346,018	356,406	(10,388)
Net assets at beginning of period	6,710,042	6,484,236	225,806	5,682,804	5,473,347	209,457
Net assets at end of period	<u>\$ 7,021,224</u>	<u>\$ 6,783,840</u>	<u>\$ 237,384</u>	<u>\$ 6,028,822</u>	<u>\$ 5,829,753</u>	<u>\$ 199,069</u>
	Three Months Ended June 30 2018			Three Months Ended June 30 2017		
	(Unaudited)			(Unaudited)		
	Total	Controlling	Noncontrolling	Total	Controlling	Noncontrolling
Unrestricted net assets:						
Consolidated excess of revenues over expenses	\$ 160,900	\$ 126,723	\$ 34,177	\$ 156,174	\$ 130,532	\$ 25,642
Contributions for capital expenditures	-	-	-	228	228	-
Distributions to noncontrolling interests	(34,622)	-	(34,622)	(33,711)	-	(33,711)
Contributions from noncontrolling interests	(161)	-	(161)	-	-	-
Other	(497)	(497)	-	(14,646)	(14,681)	35
	<u>125,620</u>	<u>126,226</u>	<u>(606)</u>	<u>108,045</u>	<u>116,079</u>	<u>(8,034)</u>
Temporarily restricted net assets:						
Contributions	378	378	-	559	559	-
Investment return	(6)	(6)	-	633	633	-
Net assets released from restrictions	(525)	(525)	-	(495)	(495)	-
Other	886	886	-	13,699	13,699	-
	<u>733</u>	<u>733</u>	<u>-</u>	<u>14,396</u>	<u>14,396</u>	<u>-</u>
Permanently restricted net assets:						
Change in beneficial interest in net assets of foundations	-	-	-	8	8	-
Contributions and other	71	71	-	(92)	(92)	-
Beneficial interest reclassification	-	-	-	852	852	-
Other	(2,843)	(2,843)	-	-	-	-
	<u>(2,772)</u>	<u>(2,772)</u>	<u>-</u>	<u>768</u>	<u>768</u>	<u>-</u>
Increase (decrease) in net assets	123,581	124,187	(606)	123,209	131,243	(8,034)
Net assets at beginning of period	6,897,643	6,659,653	237,990	5,905,613	5,698,510	207,103
Net assets at end of period	<u>\$ 7,021,224</u>	<u>\$ 6,783,840</u>	<u>\$ 237,384</u>	<u>\$ 6,028,822</u>	<u>\$ 5,829,753</u>	<u>\$ 199,069</u>

Indiana University Health, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
(Thousands of Dollars)

	Six Months Ended June 30		Three Months Ended June 30	
	2018	2017	2018	2017
	(Unaudited)		(Unaudited)	
Operating activities				
Increase in net assets	\$ 311,182	\$ 346,018	\$ 123,581	\$ 123,209
Adjustments to reconcile increase in net assets to net cash (used in) provided by operating activities:				
Change in fair value of interest rate swaps	(16,968)	(4,627)	(7,267)	(2,053)
(Gain) loss in unconsolidated subsidiaries	(329)	22,952	-	2,495
Inherent contribution of acquired entity	(31,860)	-	939	-
Contributions from noncontrolling interests	(570)	-	161	-
Gain on sale of business unit	-	(25,285)	-	(25,285)
Depreciation and amortization	117,214	113,489	58,941	56,429
Amortization of deferred gain on sale of medical office buildings	(401)	(429)	(194)	(207)
Loss on extinguishment of debt	1,653	43	1,653	-
Restricted contributions and investment return	(1,526)	(1,986)	(443)	(1,099)
Distributions to noncontrolling interests	57,011	64,302	34,622	33,711
Assets limited as to use	(427,008)	(271,365)	(265,927)	(100,906)
Net changes in operating assets and liabilities:				
Patient accounts receivable	12,359	(48,347)	6,248	(5,930)
Other assets	13,284	(43,008)	1,596	(29,694)
Accounts payable, accrued liabilities, and other liabilities	(55,591)	(34,464)	(33,550)	1,378
Accrued salaries, wages, and related liabilities	(54,906)	(6,069)	(79,463)	(42,402)
Estimated third-party payer allowances	(4,088)	30,556	(5,400)	(4,901)
Net cash (used in) provided by operating activities	<u>(80,544)</u>	141,780	<u>(164,503)</u>	4,745
Investing activities				
Proceeds from sale of a business unit	-	25,763	-	25,763
Acquisition of subsidiary, net of cash received	9,450	-	-	-
Purchase of property and equipment, net of disposals	(78,280)	(43,209)	(53,494)	(34,048)
Net cash used in investing activities	<u>(68,830)</u>	(17,446)	<u>(53,494)</u>	(8,285)
Financing activities				
Increase in restricted net assets	1,526	1,986	443	1,099
Repayments on long-term debt	(203,843)	(169,167)	(170,647)	(2,582)
Proceeds from issuance of long-term debt	354,098	93,560	354,033	1,002
Termination of swaps	(15,127)	-	(15,127)	-
Contributions from noncontrolling interests	570	-	(161)	-
Distributions to noncontrolling interests	(57,011)	(64,302)	(34,622)	(33,711)
Net cash provided by (used in) financing activities	<u>80,213</u>	(137,923)	<u>133,919</u>	(34,192)
Decrease in cash and cash equivalents	(69,161)	(13,589)	(84,078)	(37,732)
Cash and cash equivalents at beginning of period	414,674	415,860	429,591	440,003
Cash and cash equivalents at end of period	<u>\$ 345,513</u>	<u>\$ 402,271</u>	<u>\$ 345,513</u>	<u>\$ 402,271</u>

Indiana University Health, Inc. and subsidiaries
Notes to Consolidated Financial Statements (Unaudited)
As of June 30, 2018 and December 31, 2017 and for the six months ended June 30,
2018 and 2017
(Thousands of Dollars)

1. Basis of Presentation

Indiana University Health, Inc. (Indiana University Health), an Indiana private, nonprofit organization (exempt from federal income taxes as an organization described in Section 501(c)(3) of the Internal Revenue Code of 1986), as amended (the Code), and classified as a public charity under Section 509(a) of the Code, is a health care delivery system that provides services throughout the State of Indiana (the State). Indiana University Health's mission is to improve the health of its patients and the communities it serves through innovation and excellence in care, education, research, and service.

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information. Accordingly, they do not include all of the information and footnotes required by GAAP for complete, annual financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal and recurring nature. Operating results for the six months ended June 30, 2018 are not necessarily indicative of the results to be expected for the year ending December 31, 2018. For further information, refer to the audited consolidated financial statements and notes thereto for the years ended December 31, 2017 and 2016 (not included herein).

The accompanying unaudited consolidated financial statements include the accounts of Indiana University Health and all majority-owned or controlled subsidiaries (collectively referred to herein as the Indiana University Health System). The equity method of accounting is used for investments in joint ventures, partnerships, and companies where control is participatory with others or where ownership is 50% or less, but significant influence over the investee is established. All significant intercompany balances and transactions have been eliminated in consolidation.

2. Summary of Significant Accounting Policies

Revenue Recognition

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, related to recognizing revenue from contracts with customers. This new guidance dictates that the standard be applied either full retrospective to each prior reporting period presented, or modified retrospective with the cumulative effect of initially applying the standard recognized at the date of initial application. Subsequently, the FASB issued updates to this guidance to provide clarification to the aspects of collectability criterion, identifying performance obligations and the licensing implementation guidance and recognizing revenue when another party is involved in providing goods or services to a customer. As of January 1, 2018, the Indiana University Health System adopted the new standard using a full retrospective approach, as permitted.

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2. Summary of Significant Accounting Policies (continued)

As a result of the adoption, the Indiana University Health System no longer presents the provision for uncollectible accounts as a separate line within its consolidated statements of operations and changes in net assets, but rather it includes the amounts within the patient service revenue line. There were no changes to previously reported revenues as a result of the adoption (presentation only).

As its performance obligations relate to contracts with a duration of less than one year, the Indiana University Health System has applied the practical expedient, as provided in FASB Accounting Standards Codification (ASC) 606, and is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which typically occurs within days or weeks of the end of the reporting period.

As provided for under FASB ASC 606, the Indiana University Health System does not adjust the promised amount of consideration from patients and third-party payers for the effects of a significant financing component due to Indiana University Health System's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payer pays for that service will be one year or less. However, the Indiana University Health System does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

The Indiana University Health System has applied the practical expedient provided within FASB ASC 340. The Indiana University Health System does not incur significant costs in obtaining contracts with customers (patients). Any costs which are incurred, are expensed in the period of occurrence, as the amortization period of any asset that the Indiana University Health System otherwise would have recognized is one year or less in duration.

Patient Service Revenue

Revenue is recognized as performance obligations are satisfied. Performance obligations are determined based on the nature of the goods or services provided by the Indiana University Health System.

Patient service revenue is recognized at an amount that reflects the consideration to which the Indiana University Health System expects to be entitled in exchange for providing patient care. The amounts recognized reflect variable consideration, such as discounts, contractual allowances, concessions and contingent payments. These amounts

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2. Summary of Significant Accounting Policies (continued)

are due from patients, third-party payers (including health insurers and government programs), and others.

Performance obligations satisfied over time relate to patients receiving health care services. The Indiana University Health System measures the performance obligation from admission (inpatient) or check-in (outpatient) to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge (inpatient) or check-out (outpatient). Revenue for performance obligations satisfied over time is recognized based on actual charges incurred, in relation to total expected (or actual) charges. This method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation.

For the periods ended June 30, 2018 and 2017, the Indiana University Health System primarily recognized revenue from services provided over time.

The Indiana University Health System determines the transaction price based on standard charges for goods and services provided, reduced by contractual adjustments provided to third-party payers, discounts provided to uninsured patients in accordance with the Indiana University Health System's policy, and/or implicit price concessions provided to uninsured patients.

The Indiana University Health System determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies, and historical experience. Agreements with third-party payers typically provide for payments at amounts less than established charges. A summary of the payment arrangements with major third-party payers follows:

Medicare: Certain inpatient acute care services are paid at prospectively determined rates per discharge based on clinical, diagnostic and other factors. Certain services are paid based on cost-reimbursement methodologies subject to certain limits. Outpatient services are paid using prospectively determined rates. Physician services are paid based upon established fee schedules.

Medicaid: Reimbursements for Medicaid services are generally paid at prospectively determined rates per discharge, per occasion of service, or per covered member.

Other: Payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations use prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

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2. Summary of Significant Accounting Policies (continued)

Settlements with third-party payers for retroactive adjustments due to audits, reviews or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payer, correspondence from the payer, and the Indiana University Health System's historical settlement activity, including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as amounts become known (that is, new information becomes available), as years are settled or years are no longer subject to such audits, reviews, and investigations. Adjustments arising from changes in estimated contractual adjustments were not significant in 2018 or 2017.

Generally patients who are covered by third-party payers are responsible for related deductibles and coinsurance, which vary in amount. The Indiana University Health System also provides services to uninsured patients, and offers those uninsured patients a discount, either by policy or law, from standard charges. The Indiana University Health System estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions based on historical collection experience. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change.

The Indiana University Health System determines its estimate of implicit price concessions based on its historical collection experience by class of patients. Consistent with the Indiana University Health System's mission, care is provided to patients regardless of their ability to pay. Therefore, the Indiana University Health System has determined it has provided implicit price concessions to uninsured patients and patients with other uninsured balances (for example, copays and deductibles). The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients and the amounts Indiana University Health System expects to collect based on collection history with comparable patients. For the periods ended June 30, 2018 and 2017, additional revenue recognized due to changes in its estimates of implicit price concessions for performance obligations satisfied in prior periods was not significant.

Subsequent changes in transaction price that are determined to be the result of an adverse change in the patient's ability to pay are recorded as bad debt expense. Bad debt expense for the periods ended June 30, 2018 and 2017 was not significant.

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2. Summary of Significant Accounting Policies (continued)

The composition of patient service revenue by payer sources is as follows:

	Six Months Ended	
	June 30	
	2018	2017
Commercial/Managed Care	57%	54%
Medicaid	9	13
Medicare	27	25
Self-Pay and Other	7	8
	100%	100%

One managed care payer represented 31% and 29% of patient service revenue for 2018 and 2017, respectively.

Government Programs

During 2012, the Indiana General Assembly approved a hospital assessment fee program (Medicaid Assessment Fee). Under this program, the Office of Medicaid Policy and Planning (OMPP) collects a fee from eligible hospitals. The fee is used in part to increase reimbursement to eligible hospitals for services provided in both fee-for-service and managed care programs, and as the state share of Disproportionate Share Hospital (DSH) payments. The program was effective retroactively from July 1, 2011 through June 30, 2013 and was subsequently extended through June 30, 2019.

For the periods ended June 30, 2018 and 2017, payments received related to the Medicaid Assessment Fee program were recorded within patient service revenue in the consolidated statement of operations and changes in net assets totaling \$195,629 and \$124,987, respectively. During the periods ended June 30, 2018 and 2017, assessment fees were recorded within the hospital assessment fee line on the consolidated statements of operations and changes in net assets totaling \$67,631 and \$61,227, respectively.

The Indiana University Health System qualifies for supplemental Medicaid payments through the UPL program under Indiana law. The UPL program was established to pay qualifying providers the difference between what Medicare would have paid and what Medicaid actually paid. As of June 30, 2018 and 2017, the Indiana University Health System recognized UPL revenue of \$26,017 and \$3,501, respectively.

Certain hospitals of the Indiana University Health System are Medicaid DSH providers under Indiana law and, as such, are eligible to receive state DSH payments. The amount of these additional state DSH funds is dependent on regulatory approval by agencies of

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2. Summary of Significant Accounting Policies (continued)

the federal and state governments and is determined by the level, extent, and cost of uncompensated care (as defined) and various other factors. Revenue recognized for the periods ended June 30, 2018 and 2017 was not significant.

Laws and regulations governing Medicare, Medicaid, and other governmental programs are complex and subject to varying interpretation. The Indiana University Health System believes it is in compliance with applicable laws and regulations governing Medicare, Medicaid, and other governmental programs as well as contracts that it has with commercial payers and that adequate provisions have been recorded for any adjustments that may result from final settlements.

Member Premium Revenue and Health Claims

The Indiana University Health System has agreements to provide medical services to subscribing participants or members that generally provide for predefined payments (on a per member, per month basis) regardless of services actually performed. The cost to provide health care services under these agreements is accrued in the period in which the health care services are provided to a member based, in part, on estimates, including an accrual for medical services provided but not yet reported. Expenses to providers are reported as health claims to providers in the accompanying consolidated statements of operations and changes in net assets. The accrual for medical services provided but not yet reported is reflected as accrued health claims in the accompanying consolidated balance sheets.

Other Revenue

Other revenue is recognized at an amount that reflects the consideration to which the Indiana University Health System expects to be entitled in exchange for providing goods and services. The amounts recognized reflect consideration due from customers, third-party payers, and others. Primary categories of other revenue include income from joint-ventures, grant revenue, cafeteria revenue, rent and lease revenue, shared professional revenue, and other.

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(Thousands of Dollars)

2. Summary of Significant Accounting Policies (continued)

The composition of other revenue by sources is as follows:

	Six Months Ended June 30	
	2018	2017
Income (loss) from related entity operations	\$ 329	(\$22,952)
Shared health services revenue	72,731	63,033
Gain on sale of dialysis business	-	25,285
Other	42,249	49,117
	\$115,309	\$114,483

Patient Accounts Receivable

The Indiana University Health System does not require collateral or other security for the delivery of health care services from its patients, substantially all of whom are residents of the State. However, assignment of benefit payments payable under patients' health insurance programs and plans (e.g., Medicare, Medicaid, health maintenance organizations, and commercial insurance policies) is routinely obtained, consistent with industry practice. Patient service revenue and subsequently patient accounts receivable is reported at the amount that reflects the consideration to which the Indiana University Health System expects to be entitled in exchange for providing patient care (See Patient Service Revenue).

Opening and closing balances of patient accounts receivable is summarized as follows as of June 30:

	2018	2017
Commercial/Managed Care	52%	52%
Medicaid	15	16
Medicare	19	17
Self-Pay and Other	14	15
	100%	100%

One managed care payer represented 23% of patient accounts receivable at both June 30, 2018 and 2017.

As the Indiana University Health System considers that the patient simultaneously consumes the benefit of the goods and services as they are provided and rights are

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2. Summary of Significant Accounting Policies (continued)

considered unconditional, the Indiana University Health System and any related contract assets are not considered applicable for this revenue stream.

In certain instances, the Indiana University Health System does receive payment in advance of the services provided and would consider these amounts to represent contract liabilities. Contract liabilities at June 30, 2018 and 2017 were not significant.

The Indiana University Health System serves certain patients whose medical care costs are not paid at established rates. These patients include those under government programs, such as Medicare and Medicaid, and those that cannot afford health insurance because of inadequate resources or those who are uninsured or underinsured. Patient service revenue is reported at estimated net realizable amounts for services rendered. The Indiana University Health System recognizes patient service revenue associated with patients who have third-party payer coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, revenue is recognized on the basis of discounted rates in accordance with the financial assistance policy.

Patient service revenue recognized in the period from major payer sources is as follows:

	Six Months Ended	
	June 30	
	2018	2017
Third-party payers	\$ 2,799,242	\$ 2,553,750
Self-pay patients	19,508	26,113
Total payers	\$ 2,818,750	\$ 2,579,863

Subsequent Events

For the consolidated financial statements as of and for the six months ended June 30, 2018, management has evaluated subsequent events through August 3, 2018, the date that these financial statements were issued.

Other Recent Accounting Pronouncements Adopted

In March 2017, the FASB issued ASU 2017-07 requiring employers to report the service cost component of net periodic pension and post retirement cost within operating income. The other components are required to be presented separately from the service cost component and outside a subtotal of income from operations. Early adoption is permitted as of the beginning of an annual period for which financial statements have not yet been issued. Indiana University Health early adopted this guidance retrospectively, as

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2. Summary of Significant Accounting Policies (continued)

required, effective January 1, 2018. As the Indiana University Health pension plans no longer incur service costs due to their closed status, all net periodic pension costs are reported within nonoperating income within the consolidated statements of operations and changes in net assets.

New Accounting Guidance Not Yet Applicable

In June 2018, the FASB issued ASU 2018-08 related to contributions. The guidance clarifies how entities determine whether to account for a transfer of assets as an exchange transaction or a contribution, and provides more specific criteria to determine if contributions are conditional. The guidance is effective for recipients with fiscal years beginning after June 15, 2018, including interim periods, and resource providers with fiscal years beginning after December 15, 2018, including interim periods. Indiana University Health is evaluating the effect this guidance will have on its consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18 requiring a statement of cash flows to explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The updated guidance does not provide a definition of restricted cash. The amendments are effective for fiscal years beginning after December 15, 2018, an interim periods within fiscal years beginning after December 15, 2019. Amendments should be applied using a retrospective transition method to each period presented. Early adoption is permitted. Indiana University Health is still evaluating the impact of this guidance on its statement of cash flows.

In August 2016, the FASB issued ASU 2016-15 to clarify the classification of eight types of transactions in the statement of cash flows to reduce diversity in practices. The amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Amendments should be applied using a retrospective transition method to each period presented. Early adoption is permitted. Adoption of the guidance will result only in presentation changes reflected in the consolidated financial statements.

In August 2016, the FASB issued ASU 2016-14 for not-for-profit entities related to improving the usefulness of information provided to donors, grantors, creditors and other users of the financial statements by eliminating the distinction between resources with permanent restrictions and temporary restrictions from the face of the financial statements, as well as enhancing or providing additional information in the financial statements and notes related to liquidity, expense classifications, allocation methodology, underwater endowment funds and investment returns. The amendments in this update are effective for fiscal years beginning after December 15, 2017, and for interim periods

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2. Summary of Significant Accounting Policies (continued)

within fiscal years beginning after December 15, 2018. Application to interim financial statements is permitted, but not required in the initial year of adoption. Amendments should be applied retrospectively. Adoption of the guidance will result only in presentation changes reflected in the consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02 related to leases. One of the primary changes brought about by the new standard is the reporting of operating leases on the balance sheet. This new guidance dictates that the implementation of the new standard would recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. This new guidance is effective for fiscal years and interim periods within those fiscal years beginning after December 15, 2018. Indiana University Health is still evaluating the impact of this guidance on its consolidated financial statements.

3. Significant Transactions

MDwise

Indiana University Health held 50% membership interests in both MDwise, Inc. and MDwise Medicaid Network, Inc., with Health and Hospital Corporation of Marion County (HHC) holding the other 50% membership interest. On October 31, 2017, a sponsorship transfer agreement was entered into with Michigan-based McLaren Health Care (McLaren), whereby Indiana University Health and HHC would transfer their membership interests in MDwise, Inc. and MDwise Medicaid Network, Inc. to McLaren. The transaction closed on December 29, 2017, and resulted in the recognition of a gain of \$68,152 in other revenue on the consolidated statement of operations and changes in net assets.

Jay

On November 20, 2017, Indiana University Health entered into an Affiliation and Asset Transfer Agreement with Jay County Hospital, a 25-bed critical access hospital located in Portland, Indiana. Effective March 1, 2018, Jay County Hospital transferred substantially all of its assets and liabilities to Indiana University Health Jay, Inc., a newly created nonprofit organization, and Indiana University Health became the sole corporate member.

Indiana University Health recognized the assets acquired and the liabilities assumed, measured at their fair values as of the date of acquisition, and recognized an inherent contribution as a result of the transaction in the amount of \$31,860.

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3. Significant Transactions (continued)

Dialysis Business

On June 1, 2017, Indiana University Health sold two outpatient hemodialysis in-center units in downtown Indianapolis and a home dialysis program to ISD Renal, Inc, a subsidiary of DaVita, Inc. Through the sale transaction, Indiana University Health sold substantially all of the assets owned and used by the dialysis business for \$25,763. Indiana University Health recognized a gain of \$25,285 related to the transaction. The gain is reflected in operating revenue on the consolidated statements of operations and changes in net assets.

Frankfort

On November 10, 2016, Indiana University Health entered into a lease agreement with Clinton County to lease the hospital building and other related property and equipment and to assume the operations of Frankfort Hospital, the Clinton County-owned hospital, effective June 1, 2017. As of the effective date, Indiana University Health began a five-year lease with renewal options for the 25-bed county-owned critical access hospital and affiliated medical offices. The annual minimum rental rate is \$1,000. Additional rent can be triggered if the hospital reaches certain net income targets, which is not expected to occur in 2018.

4. Assets Limited as to Use

Board-designated and donor-restricted investment funds are invested in accordance with Board-approved policies. The estimated fair value of the assets limited as to use is determined using market information and other appropriate valuation methodologies. The methods and assumptions used to estimate the fair value of assets limited as to use are as follows: (i) cash and cash equivalents: the carrying amounts reported in the consolidated balance sheets approximate fair value; (ii) marketable securities: the fair values are based on quoted market prices or, if quoted market prices are not available, quoted market prices of comparable instruments and other observable inputs; and (iii) other investments, including alternative investments. Certain alternative investments (such as hedged strategies and private investments) are accounted for using the equity method of accounting based upon the net asset values as are generally determined by third-party valuation firms and/or administrators of each fund in consultation with and approval of the fund investment managers.

The Indiana University Health System is a limited partner in funds that employ hedged investment strategies and private funds that employ investment strategies that require long holding periods to create value, both of which are designed to reduce overall portfolio volatility.

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4. Assets Limited as to Use (continued)

In the case of hedge funds, redemptions generally may be made quarterly with written notice ranging from 30 to 90 days; however, some funds employ lock-up periods that restrict redemptions or charge a redemption fee during the lock-up period. Lock-up periods range from one to three years with redemption charges of up to 5% of net asset value for redemptions made on or before the anniversary date of the initial investment or additional contribution. Upon complete redemption, many of the funds have “hold-back” provisions that allow the fund to retain up to 10% of the assets until the fund completes its audited financial statements for the redemption period. These investments are accounted for using the equity method of accounting, based on the fund’s financial information.

In the case of private funds, capital is returned as monetization events occur which may be infrequent in nature. Generally, capital is committed to a partnership for a period of five to ten years with the ability of the general partner to extend the life of the fund one to three additional years. During the first three to five years of a fund life, the general partner, in order to facilitate its funding of investments, will call capital from the limited partners up to the amount of its commitment. As of June 30, 2018 and June 30, 2017, there were \$346,754 and \$351,671 respectively of unfunded commitments relating to private fund investments, which are generally expected to be funded over the next five years.

Alternative investments include certain other risks that may not exist with other investments that are more widely traded. These include reliance on the skill of the fund managers, who often employ complex strategies utilizing various financial instruments, including futures contracts, foreign currency contracts, structured notes, interest rate, total return, and credit default swaps. Additionally, alternative investments may provide limited information on a fund’s underlying assets and have restrictive liquidity provisions. Management believes that the Indiana University Health System, in consultation with its investment consultants, has the capacity to analyze and interpret the risks associated with alternative investments and with this understanding, has determined that these investments represent a prudent approach for use in its portfolio management.

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4. Assets Limited as to Use (continued)

The composition of assets limited as to use is set forth in the following table.

	June 30	December 31
	2018	2017
Assets limited as to use:		
Cash and cash equivalents	\$ 151,954	\$ 130,530
Debt securities:		
Asset backed	142,040	107,600
Bank loans	246,129	238,242
Corporate debt	251,443	253,876
Government and agencies	207,885	152,561
Bond funds	414,811	376,148
Total debt securities	<u>1,262,308</u>	<u>1,128,427</u>
Equity securities:		
Domestic equities	59,251	58,232
Domestic equity funds	919,123	874,683
International equities	84,008	72,751
International equity funds	729,346	765,607
Total equity securities	<u>1,791,728</u>	<u>1,771,273</u>
Commodities	249,213	197,906
Alternatives:		
Hedge funds	1,407,053	1,422,190
Private	515,701	373,178
Total alternatives	<u>1,922,754</u>	<u>1,795,368</u>
Less current portion of assets limited to use	<u>(191,667)</u>	<u>(143,611)</u>
Total assets limited as to use	<u>\$ 5,186,290</u>	<u>\$ 4,879,893</u>

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5. Debt

Indiana University Health Obligated Group has executed direct-pay letter-of-credit agreements in support of all of its publicly remarketed variable-rate bond series, which require the credit provider to purchase bonds in the event the bonds are not remarketed. In addition, it has executed direct purchase agreements, whereby the credit provider purchases bonds for a predetermined period of time, after which the agreement must be extended or the bonds must be remarketed or reissued. In each of these two instances, the bonds have a longer nominal maturity than the agreement, but the existence and terms of these agreements allow for the long-term classification of the associated variable-rate bond series. When these letter of credit agreements have expiration dates within the succeeding twelve-month period, a greater portion of the associated debt is classified as current, because if not otherwise extended, the agreements with the credit providers would require the principal balance of the related bonds to be repaid over a shortened time frame. No such amounts were reclassified to current portion of long-term debt as of June 30, 2018 or December 31, 2017.

On April 17, 2018, Indiana University Health issued \$354,000 in par value of Series 2018A taxable, fixed-rate bonds. A portion of the proceeds was used to advance refund \$60,500 in par amount of the Indiana Finance Authority Hospital Revenue Bonds, Series 2011N (Indiana University Health Obligated Group), to refinance all of the Indiana Finance Authority Hospital Revenue Bonds, Series 2015C (Indiana University Health Obligated Group) in the amount of \$50,000, and to repay the balance on Indiana University Health's revolving commercial bank line of credit in the amount of \$50,000. Another portion of the proceeds was used to finance the termination payments related to certain interest rate swaps as further described in the Derivative Financial Instruments footnote. Remaining proceeds will be used for general corporate purposes.

On October 12, 2017, through the Indiana Finance Authority, Indiana University Health amended its Series 2011H and 2011I tax exempt, variable-rate, direct-purchase bonds changing both the variable rate and principal repayment schedule. Indiana University Health sold the bonds to a new direct purchaser with the expiration date of the direct-purchase agreement being the same date as the final maturity of the bonds.

As of June 30, 2018 and December 31, 2017, the Indiana University Health System maintained several lines of credit totaling \$230,000 and \$105,000, respectively. As of June 30, 2018 no amounts are drawn on the lines of credit. As of December 31, 2017, the total balance drawn on the lines of credit was \$50,000, which was included in the current portion of long-term debt as the line of credit associated with the drawn balance had an expiration date of June 30, 2018. The balance on the line was repaid in April 2018, in conjunction with the issuance of the Series 2018A bonds.

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6. Derivative Financial Instruments

Long-term interest rate swap arrangements have been entered into with the primary objective being to mitigate interest rate risk. The following fixed-pay swaps, stated at current notional amounts, remain in place as of June 30, 2018:

Notional Amount	Effective Date	Maturity Date	Rate Received	Rate Paid
54,075	6/23/2011	3/01/2036	62.30% LIBOR plus 0.24%	2.68%
63,950	11/15/2005	2/15/2030	62.30% LIBOR plus 0.24%	3.35%
64,225	6/20/2011	2/15/2030	62.30% LIBOR plus 0.24%	3.35%
17,098	6/16/2011	3/01/2033	LIBOR	4.92%
68,390	6/16/2011	3/01/2033	LIBOR	4.92%
4,900	1/27/2006	11/02/2020	Securities Industry and Financial Markets Association Municipal Swap Index (SIFMA)	3.98%

After giving effect to the above derivative transactions, the Indiana University Health System's variable-rate debt was approximately 22.6% and 24.4% of total debt outstanding as of June 30, 2018 and December 31, 2017, respectively.

In addition, long-term basis swap arrangements were entered into for the purpose of managing the effect of interest rates on cash flows and were in place as of June 30, 2018 as follows:

Notional Amount	Effective Date	Maturity Date	Swap Type	Rate Received	Rate Paid
\$ 140,446	3/10/2021	2/15/2033	Forward Starting Basis	75.00% three-month LIBOR minus 0.05%	SIFMA
309,200	3/10/2021	1/7/2033	Forward Starting Basis	75.00% three-month LIBOR minus 0.04%	SIFMA
309,200	1/07/2020	1/7/2033	Forward Starting Basis	75.00% one-month LIBOR	SIFMA

Guidance on fair value accounting stipulates that a credit valuation adjustment (CVA) should be applied to the mark-to-market valuation position of interest rate swaps to more closely capture the fair value of such instruments. Collateral arrangements reduce the credit exposure and are considered in determining the CVA. As of June 30, 2018, the fair value of interest rate swaps was a liability of \$43,718, which is net of CVA of \$2,385. As of December 31, 2017, the fair value of interest rate swaps was a liability of \$75,813, which is net of CVA of \$3,536. The fair values of the swaps have been included with noncurrent liabilities in the accompanying consolidated balance sheets.

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6. Derivative Financial Instruments (continued)

As of June 30, 2018, interest rate swaps had a total notional amount of \$1,031,484, including \$272,638 of fixed-pay swaps and \$758,846 of basis swaps. Under agreements executed with counterparties, Indiana University Health is obligated to fund collateral amounts when the aggregate market value of swaps made with a given counterparty exceeds a threshold set forth in the related agreement. The aggregate fair value of all derivative instruments, consisting of fixed-pay and basis swaps, with credit-risk-related contingent features that are in a liability position on June 30, 2018 and December 31, 2017, was \$46,083 and \$63,996, respectively. No collateral was posted as of June 30, 2018 or December 31, 2017.

The Indiana University Health System recorded the following gains (losses), within nonoperating income, in the accompanying consolidated statements of operations and changes in net assets related to these derivative financial instruments:

	Six Months Ended	
	June 30	
	2018	2017
Gains (losses) on interest rate swaps, net:		
Unrealized gains on interest rate swaps	\$ 32,095	\$ 4,627
Realized losses on interest rate swaps	(16,952)	(5,678)
	\$ 15,143	\$ (1,051)

During April 2018, Indiana University Health terminated four fixed-pay interest rate swaps in the aggregate notional amount of \$103,850 for a one-time cash payment (outflow) of \$15,127, after which no payments or other amounts are owed to either party with respect to these swaps.

7. Fair Value Measurements

The accounting guidance for the application of fair value provides, among other matters, for the following: (i) defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and establishes a framework for measuring fair value; (ii) establishes a three-level hierarchy for fair value measurements based upon the observability of inputs to the valuation of an asset or liability as of the measurement date; (iii) requires consideration of nonperformance risk when valuing liabilities; and expands disclosures about instruments measured at fair value. The three-level hierarchy is based upon the nature of valuation techniques and whether such techniques are based upon observable or unobservable inputs, as defined.

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7. Fair Value Measurements (continued)

Observable inputs are intended to reflect market data obtained from independent sources, while unobservable inputs may reflect market assumptions made by management or measurements made by financial specialists generally associated with the financial asset or liability. These two types of inputs create the following fair value hierarchy:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities as of the reporting date. Includes debt issued by U.S. agencies.

Level 2 – Pricing inputs other than quoted prices included in Level 1 that are either directly observable or that can be derived or supported from observable data as of the reporting date. Includes all collective trusts and off-shore mutual funds.

Level 3 – Pricing inputs include those that are significant to the fair value of the financial asset or financial liability and are not observable from objective sources. In evaluating the significance of inputs, the Indiana University Health System generally classifies assets or liabilities as Level 3 when their fair value is determined using unobservable inputs that, individually or when aggregated with other unobservable inputs, represent more than 10% of the fair value of the assets or liabilities. These inputs may be used with internally developed methodologies that result in management's best estimate of fair value.

The following tables set forth, by level within the fair value hierarchy, the Indiana University Health System's financial assets and liabilities that were accounted for at fair value on a recurring basis as of June 30, 2018 and December 31, 2017. The financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The assessment of the significance of a particular input to the fair value measurement requires judgment, could be subject to change or variation, and may affect the valuation of fair value assets and liabilities and their classification within the fair value hierarchy levels.

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7. Fair Value Measurements (continued)

	Level 1	Level 2	Level 3	Net Asset Value	Fair Value	Equity Method	Carrying Value
June 30, 2018							
Assets							
Cash and cash equivalents	\$ 345,513	\$ -	\$ -	\$ -	\$ 345,513	\$ -	\$ 345,513
Short-term investments							
Debt securities							
Asset backed	-	2,809	-	-	2,809	-	2,809
Corporate debt	-	50,308	-	-	50,308	-	50,308
Government and agencies	24,519	-	-	-	24,519	-	24,519
Assets Limited to Use							
Cash and cash equivalents	151,954	-	-	-	151,954	-	151,954
Debt securities							
Asset backed	-	140,769	1,271	-	142,040	-	142,040
Bank loans	-	243,498	2,631	-	246,129	-	246,129
Corporate debt	-	251,062	381	-	251,443	-	251,443
Government and agencies	207,885	-	-	-	207,885	-	207,885
Bond funds	150,340	-	-	264,471	414,811	-	414,811
Equity securities							
Domestic equities	58,208	-	1,043	-	59,251	-	59,251
Domestic equity funds	191,328	-	-	727,795	919,123	-	919,123
International equities	84,008	-	-	-	84,008	-	84,008
International equity funds	182,525	-	-	546,821	729,346	-	729,346
Commodities	249,213	-	-	-	249,213	-	249,213
Alternatives							
Hedge Funds	-	-	-	-	-	1,407,053	1,407,053
Private Funds	-	-	-	-	-	515,701	515,701
Beneficial interests in charitable remainder and perpetual trusts	-	10,307	-	-	10,307	-	10,307
Total Cash and Investments	\$ 1,645,493	\$ 698,753	\$ 5,326	\$ 1,539,087	\$3,888,659	\$1,922,754	\$ 5,811,413
Liabilities							
Interest rate swaps	\$ -	\$ 43,718	\$ -	\$ -	\$ 43,718	\$ -	\$ 43,718
Total liabilities measured at fair value on a recurring basis	\$ -	\$ 43,718	\$ -	\$ -	\$ 43,718	\$ -	\$ 43,718

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7. Fair Value Measurements (continued)

	Level 1	Level 2	Level 3	Net Asset Value	Fair Value	Equity Method	Carrying Value
December 31, 2017							
Assets							
Cash and cash equivalents	\$ 414,674	\$ -	\$ -	\$ -	\$ 414,674	\$ -	\$ 414,674
Short-term investments							
Corporate debt	-	5,081	-	-	5,081	-	5,081
Assets Limited to Use							
Cash and cash equivalents	130,530	-	-	-	130,530	-	130,530
Debt securities							
Asset backed	-	106,700	900	-	107,600	-	107,600
Bank loans	-	224,414	13,828	-	238,242	-	238,242
Corporate debt	-	253,852	24	-	253,876	-	253,876
Government and agencies	152,561	-	-	-	152,561	-	152,561
Bond funds	163,075	-	-	213,073	376,148	-	376,148
Equity securities							
Domestic equities	58,232	-	-	-	58,232	-	58,232
Domestic equity funds	215,690	-	-	658,993	874,683	-	874,683
International equities	72,751	-	-	-	72,751	-	72,751
International equity funds	210,022	-	-	555,585	765,607	-	765,607
Commodities	197,906	-	-	-	197,906	-	197,906
Alternatives							
Hedge Funds	-	-	-	-	-	1,422,190	1,422,190
Private Funds	-	-	-	-	-	373,178	373,178
Beneficial interests in charitable remainder and perpetual trusts							
	-	10,307	-	-	10,307	-	10,307
Total Cash and Investments	\$ 1,615,441	\$ 600,354	\$ 14,752	\$ 1,427,651	\$3,658,198	\$1,795,368	\$ 5,453,566
Liabilities							
Interest rate swaps	\$ -	\$ 75,813	\$ -	\$ -	\$ 75,813	\$ -	\$ 75,813
Total liabilities measured at fair value on a recurring basis	\$ -	\$ 75,813	\$ -	\$ -	\$ 75,813	\$ -	\$ 75,813

The fair value of cash and cash equivalents is based on quoted market prices and classified as Level 1. The fair value of Level 1 trading securities is based on quoted market prices from an active exchange or deemed to have similar liquidity characteristics. The fair value of Level 2 trading securities is based on third-party market quotes in an inactive market or similar securities in an active market and other observable inputs. The fair value of Level 3 trading securities is based on historical costs provided by a third-party valuation firm.

The fair value of interest rate swaps is based upon forward interest rate curves, as adjusted for CVA (see Note 6). The Indiana University Health System engages a third party to assist in valuing the CVA. The third party uses the income approach to present value the cash flows using the relevant rate of return for the corresponding swap contracts. Where observable, this return would be the observed market rate(s) of return associated with the swap counterparty in a liability position. Collateral amounts posted, if any, are also taken into consideration. The CVA depicts the difference in the mark-to-market absent any credit risk, and the fair value of the swap that incorporates the credit risk of the party holding the swap in a liability position at that point in time. For swaps for which Indiana University Health is in a liability position, this credit risk is measured by comparing the mark-to-market value derived using the LIBOR swap curve to the fair value derived using a published AA rated Municipal Healthcare curve (or the AA+ rated

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7. Fair Value Measurements (continued)

Municipal General Obligation curve for the swaps insured by Assured Guaranty Municipal Corporation), or comparable market data, adjusted to a taxable basis using the relevant SIFMA/LIBOR ratio.

The value of the CVA may vary depending upon the following factors:

- Whether the Indiana University Health System is required to post collateral under the swap agreements.
- To the extent that the credit rating of the Indiana University Health System increases or decreases, in which case the CVA would decrease and increase, respectively (assuming the swaps are in a liability position).
- To the extent that the spread between the swap curves discussed above expands or compresses.

Generally, swaps are transferred between Level 2 and Level 3 when the CVA exceeds 10% of the gross valuation of the swap. Transfers are generally recorded at the end of the reporting period.

8. Commitments and Contingencies

The Indiana University Health System is from time to time subject to various legal proceedings and claims arising in the ordinary course of business. The Indiana University Health System's management does not expect that the outcome in any of its currently ongoing legal proceedings or the outcome of any other claims, individually or collectively, will have a material adverse effect on the Indiana University Health System's consolidated financial condition, results of operations, or cash flow.

9. Retirement Plans

Defined Contribution Plans

Pension benefits are provided to substantially all employees of the Indiana University Health System, primarily through defined contribution plans.

Defined Benefit Plans

Defined-benefit pension plans sponsored by Indiana University Health, Ball Memorial, and Bloomington have been curtailed with benefits frozen and no new participants allowed. The defined benefit pension plans applicable to Indiana University Health were principally limited to current and former employees who elected not to participate in the

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9. Retirement Plans (continued)

defined-contribution plan established at the time of Indiana University Health's formation.

Pension benefits are based on years of service and compensation of employees (as defined) and are actuarially determined. Where applicable, the funding policy is to annually contribute the amount required to comply with applicable legislation and IRS regulations. Adjustments to pension liabilities to reflect funded status are charged or credited to unrestricted net assets.

The following summarizes the components of net periodic benefit cost for the curtailed defined benefit pension plans.

	Six Months Ended	
	June 30	
	2018	2017
Interest cost	\$ 6,793	\$ 8,002
Expected return on plan assets	(7,973)	(9,214)
Amortization of unrecognized net loss	1,736	1,744
Net periodic pension cost	<u>\$ 556</u>	<u>\$ 532</u>

The actuarial assumptions used to determine net periodic pension cost for the defined benefit pension plans are as follows:

	2018	2017
Discount rate	<u>4.12%</u>	4.49%
Expected rate of return on plan assets	<u>4.00%</u>	4.78%

Contributions to the defined benefit pension plans aggregated \$85,000 in 2017, of which \$70,000 was made as of June 30, 2017. There are no required contributions in 2018 and none were made in the first six months of 2018.

10. Health Care Legislation

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, participation requirements, reimbursement for patient services, Medicare and Medicaid fraud and abuse, and security, privacy, and standards of health information. Government activity has continued with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and noncompliance with regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together

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10. Health Care Legislation (continued)

with the imposition of significant fines and penalties, significant repayments for patient services previously billed, and disruptions or delays in processing administrative transactions, including the adjudication of claims and payment.

In the opinion of management, there are no known regulatory inquiries that are expected to have a material adverse effect on the consolidated financial statements of the Indiana University Health System; however, 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.

The Affordable Care Act and its associated legislation are designed, in part, to expand access to coverage to substantively all U.S. citizens through a combination of states' expansion of their Medicaid programs and the health insurance marketplace. For Indiana, the Centers for Medicare and Medicaid Services (CMS) approved the Healthy Indiana Plan 2.0, which was Indiana's response to expanding its Medicaid program. The state of Indiana's request for renewal of the Healthy Indiana Plan 2.0 waiver was recently approved by CMS for an additional three years, meaning that the state will continue to engage eligible adults in its signature health program through at least the year 2020. Changes to existing Medicare and Medicaid coverage and payments have also occurred as a result of this legislation. There is uncertainty regarding the future of the Affordable Care Act, but the specific impact of any changes or new legislation on the Indiana University Health System is not determinable at this time.

OTHER INFORMATION

As of June 30, 2018 and December 31, 2017 and for the six months ended June 30, 2018
and 2017

Indiana University Health, Inc. and Subsidiaries
Special Purpose Combined Balance Sheets - Obligated Group and Designated Affiliates
(Thousands of Dollars)

	June 30	December 31
	2018	2017
	(Unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 361,074	\$ 401,799
Short-term investments	77,636	5,081
Current portion of assets limited as to use	98,229	52,206
Patient accounts receivable	471,316	459,145
Other receivables	136,994	135,199
Prepaid expenses	52,903	33,167
Inventories	57,782	54,835
Total current assets	1,255,934	1,141,432
Assets limited as to use:		
Board-designated investment funds and other investments	4,734,074	4,405,934
Property and equipment:		
Cost of property and equipment in service	3,614,144	3,605,969
Less accumulated depreciation	(2,181,605)	(2,146,624)
	1,432,539	1,459,345
Construction-in-progress	41,001	36,341
Total property and equipment, net	1,473,540	1,495,686
Other assets:		
Equity interest in unconsolidated subsidiaries	310,507	308,677
Interest in net assets of foundations	9,020	8,319
Notes receivable and other (principally from related organizations)	662,222	695,341
Total other assets	981,749	1,012,337
Total assets	\$ 8,445,297	\$ 8,055,389

Continued on next page.

Indiana University Health, Inc. and Subsidiaries
Special Purpose Combined Balance Sheets - Obligated Group and Designated Affiliates (continued)
(Thousands of Dollars)

	June 30 2018	December 31 2017
	(Unaudited)	
Liabilities and net assets		
Current liabilities:		
Accounts payable and accrued expenses	\$ 1,760,579	\$ 1,646,938
Accrued salaries, wages, and related liabilities	110,491	123,862
Accrued health claims	69,132	72,056
Estimated third-party payer allowances	61,500	60,719
Current portion of long-term debt	53,062	98,405
Total current liabilities	<u>2,054,764</u>	<u>2,001,980</u>
Noncurrent liabilities:		
Long-term debt, less current portion	1,534,093	1,336,369
Interest rate swaps	43,550	75,562
Accrued pension obligations	672	570
Accrued medical malpractice claims	3,628	2,562
Other	27,288	24,069
Total noncurrent liabilities	<u>1,609,231</u>	<u>1,439,132</u>
Total liabilities	<u>3,663,995</u>	<u>3,441,112</u>
Net assets:		
Unrestricted	4,770,427	4,601,071
Temporarily restricted	2,944	2,257
Permanently restricted	7,931	10,949
Total net assets	<u>4,781,302</u>	<u>4,614,277</u>
Total liabilities and net assets	<u>\$ 8,445,297</u>	<u>\$ 8,055,389</u>

Indiana University Health, Inc. and Subsidiaries
Special Purpose Combined Statements of Operations - Obligated Group and Designated Affiliates
(Thousands of Dollars)

	Six Months Ended June 30		Three Months Ended June 30	
	2018	2017	2018	2017
	(Unaudited)		(Unaudited)	
Revenues:				
Patient service revenue	1,365,252	1,266,281	697,451	628,474
Member premium revenue	150,675	189,363	75,625	95,135
Other revenue	292,396	270,325	144,162	157,557
Total operating revenues	<u>1,808,323</u>	<u>1,725,969</u>	<u>917,238</u>	<u>881,166</u>
Expenses:				
Salaries, wages, and benefits	593,214	563,122	301,557	286,852
Supplies, drugs, purchased services, and other	701,673	655,669	355,511	334,602
Hospital assessment fee	32,206	29,354	16,103	14,677
Health claims to providers	127,615	190,741	62,367	101,153
Depreciation and amortization	71,971	71,064	35,975	34,847
Interest	19,781	16,617	10,988	8,538
Total operating expenses	<u>1,546,460</u>	<u>1,526,567</u>	<u>782,501</u>	<u>780,669</u>
Operating income	<u>261,863</u>	<u>199,402</u>	<u>134,737</u>	<u>100,497</u>
Nonoperating income:				
Investment income, net	63,636	220,372	16,882	81,950
Gain (losses) on interest rate swaps, net	15,058	(1,122)	7,651	(657)
Debt extinguishment and other	(1,778)	5	(1,727)	-
Total nonoperating income	<u>76,916</u>	<u>219,255</u>	<u>22,806</u>	<u>81,293</u>
Excess of revenues over expenses	<u>\$ 338,779</u>	<u>\$ 418,657</u>	<u>\$ 157,543</u>	<u>\$ 181,790</u>

Indiana University Health, Inc. and Subsidiaries
Special Purpose Combined Balance Sheets - Obligated Group
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	June 30	December 31
	2018	2017
	(Unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 361,178	\$ 401,948
Short-term investments	77,636	5,081
Current portion of assets limited as to use	98,125	52,147
Patient accounts receivable	464,985	454,080
Other receivables	139,551	137,407
Prepaid expenses	52,663	32,978
Inventories	57,091	54,142
Total current assets	1,251,229	1,137,783
Assets limited as to use:		
Board-designated investment funds and other investments	4,729,254	4,401,110
Property and equipment:		
Cost of property and equipment in service	3,599,002	3,591,312
Less accumulated depreciation	(2,171,413)	(2,136,578)
	1,427,589	1,454,734
Construction-in-progress	40,822	36,306
Total property and equipment, net	1,468,411	1,491,040
Other assets:		
Equity interest in unconsolidated subsidiaries	310,706	308,875
Notes receivable and other (principally from related organizations)	666,933	700,735
Total other assets	977,639	1,009,610
Total assets	\$ 8,426,533	\$ 8,039,543

Continued on next page.

Indiana University Health, Inc. and Subsidiaries
Special Purpose Combined Balance Sheets - Obligated Group (continued)
(Thousands of Dollars)

	June 30	December 31
	2018	2017
	(Unaudited)	
Liabilities and net assets		
Current liabilities:		
Accounts payable and accrued expenses	\$ 1,780,492	\$ 1,667,856
Accrued salaries, wages, and related liabilities	109,522	122,736
Accrued health claims	69,132	72,056
Estimated third-party payer allowances	60,066	58,076
Current portion of long-term debt	53,062	98,405
Total current liabilities	2,072,274	2,019,129
Noncurrent liabilities:		
Long-term debt, less current portion	1,533,745	1,336,000
Interest rate swaps	43,550	75,562
Accrued pension obligations	672	570
Accrued medical malpractice claims	3,564	2,509
Other	27,288	24,069
Total noncurrent liabilities	1,608,819	1,438,710
Total liabilities	3,681,093	3,457,839
Net assets:		
Unrestricted	4,743,585	4,576,817
Permanently restricted	1,855	4,887
Total net assets	4,745,440	4,581,704
Total liabilities and net assets	\$ 8,426,533	\$ 8,039,543

Indiana University Health, Inc. and Subsidiaries
Special Purpose Combined Statements of Operations - Obligated Group
(Thousands of Dollars)

	Six Months Ended June 30		Three Months Ended June 30	
	2018	2017	2018	2017
	(Unaudited)		(Unaudited)	
Revenues:				
Patient service revenue	1,346,109	1,249,595	686,587	620,117
Member premium revenue	150,675	189,363	75,625	95,134
Other revenue	295,451	273,447	145,705	159,094
Total operating revenues	<u>1,792,235</u>	<u>1,712,405</u>	<u>907,917</u>	<u>874,345</u>
Expenses:				
Salaries, wages, and benefits	586,454	556,423	298,060	283,460
Supplies, drugs, purchased services, and other	696,038	649,855	352,662	331,876
Hospital assessment fee	31,680	28,822	15,840	14,411
Health claims to providers	127,791	191,117	62,443	101,377
Depreciation and amortization	71,142	70,378	35,558	34,502
Interest	19,781	16,617	10,988	8,538
Total operating expenses	<u>1,532,886</u>	<u>1,513,212</u>	<u>775,551</u>	<u>774,164</u>
Operating income	<u>259,349</u>	<u>199,193</u>	<u>132,366</u>	<u>100,181</u>
Nonoperating income:				
Investment income, net	63,565	220,100	16,859	81,842
Gain (losses) on interest rate swaps, net	15,058	(1,122)	7,651	(657)
Debt extinguishment and other	(1,778)	5	(1,727)	-
Total nonoperating income	<u>76,845</u>	<u>218,983</u>	<u>22,783</u>	<u>81,185</u>
Excess of revenues over expenses	<u>\$ 336,194</u>	<u>\$ 418,176</u>	<u>\$ 155,149</u>	<u>\$ 181,366</u>

Indiana University Health, Inc. and subsidiaries
Statistical and Other Data
As of and for the Six and Three Months Ended June 30, 2018 and 2017
(Except as noted below)

Description	Six Months Ended June 30	
	2018	2017
Academic Health Center		
Active Members	1,287	1,315
Residents	693	652
Other Members	882	822
Total Medical Staff	2,862	2,789
Consolidated Number of Available Beds	2,608	2,550
Employees		
Consolidated FTE employees	29,629	28,349
Methodist/IU/Riley/Saxony/Morgan FTE employees	8,725	8,567
Credit Group coverage of Debt Service (dollars in thousands, annualized)		
Revenues over expenses (1)	652,711	447,076
Depreciation, amortization and interest (2)	190,974	187,596
Available to pay debt service	843,685	634,672
Actual debt service (2)	102,399	96,574
Historical debt service coverage ratio	8.24	6.57
Forecast maximum annual debt service (3)	114,219	106,775
Available to pay debt service	843,685	634,672
Forecast maximum annual debt service coverage ratio	7.39	5.94

Description	Six Months Ended June 30		Three Months Ended June 30	
	2018	2017	2018	2017
Consolidated Utilization and Operating Statistics				
Inpatient Days	323,316	311,564	158,084	154,380
Admissions	58,775	55,739	29,307	28,242
Occupancy Rate (based on available beds)	68.50%	67.52%	66.62%	66.54%
Average Length of Stay	5.50	5.59	5.39	5.47
Surgery Cases IP	15,375	15,133	7,847	7,773
Surgery Cases OP	38,600	38,771	19,878	19,678
Surgery Cases Total	53,975	53,904	27,725	27,451
Emergency Room Visits	222,693	228,642	110,786	113,407
Radiological Examinations	617,351	602,734	311,419	294,630
Gross Patient Service Revenue				
Medicare and Other Government	40.19%	40.07%	40.15%	39.99%
Medicaid	14.08%	13.81%	13.96%	13.88%
HIP	8.03%	8.15%	7.94%	8.21%
Medicaid and HIP	22.11%	21.96%	21.90%	22.09%
Wellpoint / Anthem	18.15%	18.24%	18.25%	18.40%
Other	16.57%	16.78%	16.62%	16.69%
Commercial / Managed Care	34.72%	35.02%	34.87%	35.09%
Self Pay and Other	2.98%	2.95%	3.08%	2.83%
Total Gross Patient Service Revenue:	100.00%	100.00%	100.00%	100.00%
Medicare Case Mix Index, Academic Health Center (4)	2.200	2.240	2.183	2.228

	June 30, 2018		June 30, 2017	
	Academic Health Center	Other System Hospitals	Academic Health Center	Other System Hospitals
Bed Complement: Available				
Medical Surgical	694	759	707	756
ICU / CCU	231	122	166	106
OB / Labor Delivery	54	139	28	143
Pediatrics	173	50	220	56
Psychiatric	26	46	28	42
High-Risk Nursery	104	87	104	69
Rehab and other	-	123	-	125
Total Bed Complement	1,282	1,326	1,253	1,297

(1) Adjusted for certain gains (losses) as defined in the IU Health Obligated Group Master Trust Indenture.
(2) Assumes all interest rate swaps are "Identified Financial Product Agreements" for all periods shown as defined in the IU Health Obligated Group Master Trust Indenture.
(3) Calculated in accordance with the definition of "Maximum Annual Debt Service" as defined in the IU Health Obligated Group Master Trust Indenture, but assumes an interest rate of 3.50% (which rate is inclusive of remarketing and credit facility costs) for all variable-rate debt and a one-month LIBOR rate of 3.63% for purposes of interest rate swap cash flows.
(4) Medicare system of classification for DRGs is annually revised effective October 1 of each year.