

CHE Trinity Inc.

Consolidated Financial Statements as of and for the
Year Ended June 30, 2014, Consolidated
Supplemental Schedule of Expenditures of Federal
Awards for the Year Ended June 30, 2014 and
Independent Auditors' Reports

CHE TRINITY INC.

TABLE OF CONTENTS

	Page
INDEPENDENT AUDITORS' REPORT	1-2
PART I - CONSOLIDATED FINANCIAL STATEMENTS	
CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2014:	
Balance Sheet	3-4
Statement of Operations and Changes in Net Assets	5-6
Statement of Cash Flows	7-8
Notes to Consolidated Financial Statements	9-46
PART II – CONSOLIDATED SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS AND INDEPENDENT AUDITORS' REPORTS ON INTERNAL CONTROL AND COMPLIANCE	
Consolidated Supplemental Schedule of Expenditures of Federal Awards for the Year Ended June 30, 2014	47-57
Notes to the Consolidated Supplemental Schedule of Expenditures of Federal Awards	58-59
INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>	60-61
INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE	62-64
Schedule of Findings and Questioned Costs for the year ended June 30, 2014	65-67
Summary Schedule of Prior-Year Audit Findings for the year ended June 30, 2013	68-69

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
CHE Trinity Inc.
Livonia, Michigan

We have audited the accompanying consolidated financial statements of CHE Trinity Inc. and its subsidiaries (the "Corporation"), which comprise the consolidated balance sheet as of June 30, 2014, and the related consolidated statement of operations and changes in net assets and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the consolidated financial statements of Baycare Health System, the Corporation's investment in which is accounted for by the use of the equity method. The accompanying consolidated financial statements of the Corporation include its investment in the net assets of Baycare Health System of \$1,770,927 as of June 30, 2014, respectively, and its equity method income from Baycare Health System of \$288,196 for the year then ended. The consolidated financial statements of Baycare Health System for the year ended December 31, 2013, were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Baycare Health System, is based on the report of the other auditors and the procedures that we considered necessary in the circumstances with respect to the inclusion of the Corporation's equity investment and equity method income in the accompanying consolidated financial statements taking into consideration the differences in fiscal years.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. The financial statements of Baycare Health System audited by other auditors were audited in accordance with auditing standards generally accepted in the United States of America.

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

whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Corporation's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, based on our audits and the report of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of CHE Trinity Inc. and subsidiaries as of June 30, 2014, and the results of their operations and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Supplemental Schedule

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying Consolidated Supplemental Schedule of Expenditures of Federal Awards for the year ended June 30, 2014 as required by the U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such supplementary information is the responsibility of the Corporation's management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. This supplementary information has been subjected to the auditing procedures applied in our audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, such information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 3, 2014, on our consideration of the Corporation's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters for the year ended June 30, 2014. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Corporation's internal control over financial reporting and compliance.

Deloitte & Touche LLP

October 3, 2014, except as it relates to Note 14 *Subsequent Events* and the Consolidated Supplemental Schedule of Expenditures of Federal Awards and related notes, as to which the date is March 19, 2015.

CHE TRINITY INC.

CONSOLIDATED BALANCE SHEET

JUNE 30, 2014

(In thousands)

ASSETS

CURRENT ASSETS:

Cash and cash equivalents	\$	901,282
Investments		3,231,318
Security lending collateral		187,882
Assets limited or restricted as to use - current portion		274,202
Patient accounts receivable, net of allowance for doubtful accounts of \$545.3 million		1,475,579
Estimated receivables from third-party payors		155,527
Other receivables		269,110
Inventories		206,226
Assets held for sale		207,989
Prepaid expenses and other current assets		140,359
Total current assets		<u>7,049,474</u>

ASSETS LIMITED OR RESTRICTED AS TO USE - Noncurrent portion:

Held by trustees under bond indenture agreements		53,652
Self-insurance, benefit plans and other		672,537
By Board		2,891,790
By donors		308,572
Total assets limited or restricted as to use - noncurrent portion		<u>3,926,551</u>

PROPERTY AND EQUIPMENT - Net 6,592,913

INVESTMENTS IN UNCONSOLIDATED AFFILIATES 2,257,555

GOODWILL 153,773

OTHER ASSETS 452,923

TOTAL ASSETS \$ 20,433,189

LIABILITIES AND NET ASSETS**CURRENT LIABILITIES:**

Commercial paper	\$	239,961
Short-term borrowings		1,123,620
Current portion of long-term debt		96,038
Accounts payable		685,748
Accrued expenses		275,960
Salaries, wages and related liabilities		656,467
Current portion of self-insurance reserves		197,040
Payable under security lending agreements		187,882
Liabilities held for sale		257,991
Estimated payables to third-party payors		323,546
		<hr/>
Total current liabilities		4,044,253

LONG-TERM DEBT - Net of current portion 3,619,237

SELF-INSURANCE RESERVES - Net of current portion 920,799

ACCRUED PENSION AND RETIREE HEALTH COSTS 727,873

OTHER LONG-TERM LIABILITIES

577,565

Total liabilities

9,889,727

NET ASSETS:

Unrestricted net assets	10,125,003
Noncontrolling ownership interest in subsidiaries	38,090
Total unrestricted net assets	<hr/> 10,163,093
Temporarily restricted net assets	293,306
Permanently restricted net assets	87,063
Total net assets	<hr/> 10,543,462

TOTAL LIABILITIES AND NET ASSETS

\$ 20,433,189

The accompanying notes are an integral part of the consolidated financial statements.

CHE TRINITY INC.

CONSOLIDATED STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS YEAR ENDED JUNE 30, 2014 (In thousands)

UNRESTRICTED REVENUE:	
Patient service revenue, net of contractual and other allowances	\$ 12,395,306
Provision for bad debts	(620,011)
Net patient service revenue less provision for bad debts	11,775,295
Capitation and premium revenue	689,053
Net assets released from restrictions	28,366
Other revenue	1,093,765
Total unrestricted revenue	<u>13,586,479</u>
EXPENSES:	
Salaries and wages	5,870,246
Employee benefits	1,202,093
Contract labor	102,504
Total labor expenses	<u>7,174,843</u>
Supplies	2,153,313
Purchased services	1,494,036
Depreciation and amortization	707,707
Occupancy	581,579
Medical claims	284,449
Interest	159,228
Other	649,186
Total expenses	<u>13,204,341</u>
OPERATING INCOME BEFORE OTHER ITEMS	382,138
Pension curtailment gain	149,734
Pension settlement loss	(195,987)
Asset impairment charges	(91,279)
Restructuring costs	(45,720)
Consolidation costs	(42,856)
Litigation accrual	(36,448)
OPERATING INCOME	119,582
NONOPERATING ITEMS:	
Investment income	609,010
Equity in earnings of unconsolidated affiliates	265,815
Change in market value and cash payments of interest rate swaps	(25,514)
Other, including income taxes	(17,488)
Total nonoperating items	<u>831,823</u>
EXCESS OF REVENUE OVER EXPENSES	951,405
EXCESS OF REVENUE OVER EXPENSES ATTRIBUTABLE TO NONCONTROLLING INTEREST	<u>(14,135)</u>
EXCESS OF REVENUE OVER EXPENSES, net of noncontrolling interest	<u>\$ 937,270</u>

	Controlling Interest	Noncontrolling Interest	Total
UNRESTRICTED NET ASSETS:			
Excess of revenue over expenses	\$ 937,270	\$ 14,135	\$ 951,405
Net assets released from restrictions for capital acquisitions	25,739	-	25,739
Net change in retirement plan related items - consolidated organizations	28,402	-	28,402
Net change in retirement plan related items - unconsolidated organizations	44,219	-	44,219
Other	13,934	(7,079)	6,855
Increase in unrestricted net assets before discontinued operations	1,049,564	7,056	1,056,620
Discontinued operations			
Loss from operations	(39,199)	-	(39,199)
Losses on substitutions of membership interests	(85,883)	-	(85,883)
Increase in unrestricted net assets	924,482	7,056	931,538
TEMPORARILY RESTRICTED NET ASSETS:			
Contributions	68,354	-	68,354
Net investment gain	15,757	-	15,757
Net assets released from restrictions	(54,105)	-	(54,105)
Other	(6,354)	-	(6,354)
Increase in temporarily restricted net assets	23,652	-	23,652
PERMANENTLY RESTRICTED NET ASSETS:			
Contributions for endowment funds	3,621	-	3,621
Net investment gain	2,858	-	2,858
Other	(12,094)	-	(12,094)
Increase in permanently restricted net assets	(5,615)	-	(5,615)
INCREASE IN NET ASSETS	942,519	7,056	949,575
NET ASSETS - July 1, 2013	9,562,853	31,034	9,593,887
NET ASSETS - June 30, 2014	\$ 10,505,372	\$ 38,090	\$ 10,543,462

The accompanying notes are an integral part of the consolidated financial statements.

CHE TRINITY INC.

CONSOLIDATED STATEMENT OF CASH FLOWS YEAR ENDED JUNE 30, 2014

(In thousands)

OPERATING ACTIVITIES:

Increase in net assets	\$	949,575
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization		707,707
Provision for bad debts		620,011
Asset impairment charges		91,279
Asset impairment charge and other non-cash items - discontinued operations		37,022
Restructuring costs		30,892
Litigation accrual		36,448
Losses on substitutions of membership interests		85,883
Equity in earnings of unconsolidated affiliates		(320,639)
Deferred retirement items - consolidated organizations		(28,402)
Deferred retirement items - unconsolidated organizations		(44,219)
Change in net unrealized and realized gains on investments		(571,787)
Change in market values of interest rate swaps		13,359
Restricted contributions and investment income received		(26,510)
Other adjustments		11,657
Changes in:		
Patient accounts receivable		(691,299)
Other assets		(59,010)
Accounts payable and accrued expenses		(30,734)
Estimated receivables from third-party payors		13,258
Estimated payables to third-party payors		(69,534)
Self-insurance reserves		73,341
Accrued pension and retiree health costs		(28,990)
Other liabilities		(600)
Net cash provided by operating activities of discontinued operations		(24,155)
Total adjustments		(175,022)
Net cash provided by operating activities		<u>774,553</u>

INVESTING ACTIVITIES:	
Purchases of investments	(3,107,406)
Proceeds from sales of investments	3,056,208
Purchases of property and equipment	(1,013,473)
Proceeds from disposal of property and equipment	14,047
Acquisitions	(3,768)
Dividends received from unconsolidated affiliates	39,551
Increase in assets limited as to use and other changes	(18,290)
Net cash used in investing activities of discontinued operations	<u>(12,961)</u>
Net cash used in investing activities	<u>(1,046,092)</u>
 FINANCING ACTIVITIES:	
Proceeds from issuance of debt	664,194
Repayments of debt	(379,241)
Net decrease in commercial paper	(128,961)
Increase in financing costs and other	(3,655)
Proceeds from restricted contributions and restricted investment income	26,510
Net cash used in investing activities of discontinued operations	<u>(4,395)</u>
Net cash provided by financing activities	<u>174,452</u>
 NET DECREASE IN CASH AND CASH EQUIVALENTS	 (97,087)
 CASH AND CASH EQUIVALENTS - Beginning of year	 <u>998,369</u>
 CASH AND CASH EQUIVALENTS - End of year	 <u>\$ 901,282</u>
 SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:	
Cash paid for interest (net of amounts capitalized)	\$ 155,268
New capital lease obligations for buildings and equipment	4,388
Accruals for purchases of property and equipment and other long-term assets	92,001
Unsettled investment trades, purchases	120,562
Unsettled investment trades, sales	135,756
Decrease in security lending collateral	34,299
Decrease in payable under security lending agreements	(34,299)

The accompanying notes are an integral part of the consolidated financial statements.

CHE TRINITY INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS YEAR ENDED JUNE 30, 2014

1. ORGANIZATION AND MISSION

Effective May 1, 2013, CHE Trinity Inc. (the “Corporation”) became the sole member of Catholic Health East, a Pennsylvania nonprofit corporation (“CHE”), and Trinity Health Corporation, an Indiana nonprofit corporation (“Trinity Health”) creating a unified Catholic national health system that enhances the mission of service to people and communities across the United States. This transaction was accounted for as a merger and thus the Corporation’s balance sheet was recorded at its historical basis under the carryover method. Transition and integration are ongoing with the Corporation incurring \$42.9 million of expenses for the year ended June 30, 2014, as a result of the transaction, which are included in consolidation costs in the statement of operations and changes in net assets.

The Corporation has adopted a fiscal year end of June 30. Effective July 1, 2013, CHE changed its fiscal year end from December 31 to June 30 in order to align CHE’s year end with the Corporation. These statements reflect the adoption of a June 30 fiscal year end.

The Corporation is sponsored by Catholic Health Ministries, a Public Juridic Person of the Holy Roman Catholic Church. The Corporation operates a comprehensive integrated network of health services including inpatient and outpatient services, physician services, managed care coverage, home health care, long-term care, assisted living care, and rehabilitation services located in 20 states. The operations are organized into Regional Health Ministries (“RHMs”). The mission statement for the Corporation is as follows:

We, CHE Trinity Inc., serve together in the spirit of the Gospel as a compassionate and transforming healing presence within our communities.

Community Benefit Ministry – Consistent with its mission, the Corporation provides medical care to all patients regardless of their ability to pay. In addition, the Corporation provides services intended to benefit the poor and underserved, including those persons who cannot afford health insurance or other payments such as copays and deductibles because of inadequate resources and/or are uninsured or underinsured, and to improve the health status of the communities in which it operates. The following summary has been prepared in accordance with the Catholic Health Association of the United States’, *A Guide for Planning and Reporting Community Benefit*, 2013 Edition.

The quantifiable costs of the Corporation's community benefit ministry for the year ended June 30, 2014 are as follows (in thousands):

Ministry for the poor and underserved:	
Charity care at cost	\$ 242,064
Unpaid cost of Medicaid and other public programs	325,575
Programs for the poor and the underserved:	
Community health services	21,345
Subsidized health services	46,962
Financial contributions	9,707
Community building activities	1,221
Community benefit operations	2,880
Total programs for the poor and underserved	<u>82,115</u>
Ministry for the poor and underserved	<u>649,754</u>
 Ministry for the broader community:	
Community health services	13,914
Health professions education	102,401
Subsidized health services	43,543
Research	4,407
Financial contributions	28,301
Community building activities	2,306
Community benefit operations	2,491
Ministry for the broader community	<u>197,363</u>
Community benefit ministry	<u>\$ 847,117</u>

The Corporation provides a significant amount of uncompensated care to its uninsured and underinsured patients, which is reported as bad debt at cost and not included in the amounts reported above. During the year ended June 30, 2014, the Corporation reported bad debt at cost (determined using a cost-to-charge ratio applied to the provision for bad debts) of \$196.1 million.

Ministry for the poor and underserved represents the financial commitment to seek out and serve those who need help the most, especially the poor, the uninsured and the indigent. This is done with the conviction that healthcare is a basic human right.

Ministry for the broader community represents the cost of services provided for the general benefit of the communities in which the Corporation operates. Many programs are targeted toward populations that may be poor, but also include those areas that may need special health services and support. These programs are not intended to be financially self-supporting.

Charity care at cost represents the cost of services provided to patients who cannot afford health care services due to inadequate resources and/or are uninsured or underinsured. A patient is classified as a charity patient in accordance with the Corporation's established policies as further described in Note 4. The cost of charity care is calculated using a cost-to-charge ratio methodology.

Unpaid cost of Medicaid and other public programs represents the cost (determined using a cost-to-charge ratio) of providing services to beneficiaries of public programs, including state Medicaid and indigent care programs, in excess of governmental and managed care contract payments.

Community health services are activities and services for which no patient bill exists. These services are not expected to be financially self-supporting, although some may be supported by outside grants or funding. Some examples include community health education, free immunization services, free or low cost prescription medications, and rural and urban outreach programs. The Corporation actively collaborates with community groups and agencies to assist those in need in providing such services.

Health professions education includes the unreimbursed cost of training health professionals such as medical residents, nursing students, technicians and students in allied health professions.

Subsidized health services are net costs for billed services that are subsidized by the Corporation. These include services offered despite a financial loss because they are needed in the community and either other providers are unwilling to provide the services or the services would otherwise not be available in sufficient amount. Examples of services include free-standing community clinics, hospice care, mobile units and behavioral health services.

Research includes unreimbursed clinical and community health research and studies on health care delivery.

Financial contributions are made by the Corporation on behalf of the poor and underserved to community agencies. These amounts include special system-wide funds used for charitable activities as well as resources contributed directly to programs, organizations, and foundations for efforts on behalf of the poor and underserved. Amounts included here also represent certain in-kind donations.

Community building activities include the costs of programs that improve the physical environment, promote economic development, enhance other community support systems, develop leadership skills training, and build community coalitions.

Community benefit operations include costs associated with dedicated staff, community health needs and/or asset assessments, and other costs associated with community benefit strategy and operations.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation – The consolidated financial statements include the accounts of the Corporation and all wholly owned, majority-owned, and controlled organizations. Investments where the Corporation holds less than 20% of the ownership interest are accounted for using the cost method. All other investments that are not controlled by the Corporation are accounted for using the equity method of accounting. The Corporation has included its equity share of income or losses from investments in unconsolidated affiliates in other revenue and in nonoperating equity gains in unconsolidated affiliates in the consolidated statement of operations and changes in net assets. All material intercompany transactions and account balances have been eliminated in consolidation.

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management of the Corporation to make assumptions, estimates and judgments that affect the amounts reported in the consolidated financial statements, including the notes thereto, and related disclosures of commitments and contingencies, if any. The Corporation considers critical accounting policies to be those that require more significant judgments and estimates in the preparation of its consolidated financial statements, including the following: recognition of net patient service revenue, which includes contractual allowances, provisions for bad debts and charity care; recorded values of investments, derivatives, and goodwill; reserves for losses and expenses related to health care professional and general liabilities; and risks and assumptions for measurement of pension and retiree medical liabilities. Management relies on historical experience and other assumptions believed to be reasonable in making its judgments and estimates. Actual results could differ materially from those estimates.

Cash and Cash Equivalents – For purposes of the consolidated statement of cash flows, cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less.

Investments – Investments, inclusive of assets limited or restricted as to use, include marketable debt and equity securities. Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value and are classified as trading securities. Investments also include investments in commingled funds, hedge funds and other investments structured as limited liability corporations or partnerships. Commingled funds and hedge funds that hold securities directly are stated at the fair value of the underlying securities, as determined by the administrator, based on readily determinable market values or based on net asset value, which is calculated using the most recent fund financial statements. Limited liability corporations and partnerships are accounted for under the equity method.

Investment Earnings – Investment earnings include interest, dividends, realized gains and losses on investments, holding gains and losses, and equity earnings. Investment earnings on assets held by trustees under bond indenture agreements, assets designated by the Board for debt redemption, assets held for borrowings under the intercompany loan program, assets held by grant-making foundations and assets deposited in trust funds by a captive insurance company for self-insurance purposes in accordance with industry practices are included in other revenue in the consolidated statement of operations and changes in net assets. Investment earnings from all other investments and board designated funds are included in nonoperating investment income unless the income or loss is restricted by donor or law.

Derivative Financial Instruments – The Corporation periodically utilizes various financial instruments (e.g., options and swaps) to hedge interest rates, equity downside risk and other exposures. The Corporation's policies prohibit trading in derivative financial instruments on a speculative basis. The Corporation recognizes all derivative instruments on the consolidated balance sheet at fair value.

Securities Lending – The Corporation participates in securities lending transactions whereby a portion of its investments are loaned, through its agent, to various parties in return for cash and securities from the parties as collateral for the securities loaned. Each business day the Corporation, through its agent, and the borrower determine the market value of the collateral and the borrowed securities. If on any business day the market value of the collateral is less than the required value, additional collateral is obtained as appropriate. The amount of cash collateral received under securities lending is reported as an asset and a corresponding payable in the consolidated balance sheet and is up to 105% of the market value of securities loaned. At June 30, 2014, the Corporation had securities loaned of \$207.1 million, and received collateral (cash and noncash) totaling \$212.7 million, relating to the securities loaned. The fees received for these transactions are recorded in investment income on the consolidated statement of operations and changes in net assets.

Assets Limited as to Use – Assets set aside by the Board for future capital improvements, future funding of retirement programs and insurance claims, retirement of debt, held for borrowings under the intercompany loan program, and other purposes over which the Board retains control and may at its discretion subsequently use for other purposes, assets held by trustees under bond indenture and certain other agreements, and self-insurance trust and benefit plan arrangements are included in assets limited as to use.

Donor-Restricted Gifts – Unconditional promises to give cash and other assets to the Corporation are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the

use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the consolidated statement of operations and changes in net assets.

Inventories – Inventories are stated at the lower of cost or market. The cost of inventories is determined principally by the weighted average cost method.

Assets and Liabilities Held for Sale – The Corporation has classified certain long-lived assets as assets held for sale in the consolidated balance sheet when the assets have met applicable criteria for this classification. The Corporation has also classified as held for sale those liabilities related to assets held for sale.

Property and Equipment – Property and equipment, including internal-use software, are recorded at cost, if purchased, or at fair value at the date of donation, if donated. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using either the straight-line or an accelerated method and includes capital lease and internal-use software amortization. The useful lives of these assets range from 2 to 50 years. Interest costs incurred during the period of construction of capital assets are capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support and are excluded from the excess of revenue over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support.

Goodwill – Goodwill represents the future economic benefits arising from assets acquired in a business combination that are not individually identified and separately recognized.

Asset Impairments –

Property and Equipment – The Corporation evaluates long-lived assets for possible impairment annually or whenever events or changes in circumstances indicate that the carrying amount of the asset, or related group of assets, may not be recoverable from estimated future undiscounted cash flows. If the estimated future undiscounted cash flows are less than the carrying value of the assets, the impairment recognized is calculated as the carrying value of the long-lived assets in excess of the fair value of the assets. The fair value of the assets is estimated based on appraisals, established market values of comparable assets or internal estimates of future net cash flows expected to result from the use and ultimate disposition of the asset.

Goodwill – Goodwill is tested for impairment on an annual basis or when an event or change in circumstance indicates the value of a reporting unit may have changed. Testing is conducted at the reporting unit level. If the carrying amount of the reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. Estimates of fair value are based on appraisals, established market prices for comparable assets or internal estimates of future net cash flows and presume stable, improving or, in some cases, declining results at our hospitals, depending on their circumstances.

As of July 1, 2013, the consolidated balance sheet included goodwill of \$151.6 million. Additional goodwill of \$2.2 million was recorded during the year ended June 30, 2014 related to acquisitions.

Other Assets – Other assets includes long-term notes receivable, reinsurance recovery receivables, definite and indefinite-lived intangible assets, deferred financing costs, and prepaid pension and retiree health costs. The majority of the net balances of definite-lived intangible assets include noncompete agreements and physician guarantees with finite lives amortized using the straight-line method over their estimated useful lives, which generally range from 5 to 22 years and 2 to 12 years, respectively. Indefinite-lived intangible assets primarily include trade names.

Short-Term Borrowings – Short-term borrowings include puttable variable rate demand bonds supported by self liquidity or liquidity facilities considered short-term in nature.

Other Long-Term Liabilities – Other long-term liabilities include deferred compensation, asset retirement obligations, interest rate swaps and deferred revenue from entrance fees. Deferred revenue from entrance fees are fees paid by residents of facilities for the elderly upon entering into continuing care contracts (net of the portion that is refundable to the resident) which are recorded as deferred revenue and amortized to income using the straight-line method over the estimated remaining life expectancy of the resident.

Temporarily and Permanently Restricted Net Assets – Temporarily restricted net assets are those whose use by the Corporation has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Corporation in perpetuity.

Patient Accounts Receivable, Estimated Receivables from and Payables to Third-Party Payors and Net Patient Service Revenue – The Corporation has agreements with third-party payors that provide for payments to the Corporation's RHMs at amounts different from established rates. Patient accounts receivable and net patient service revenue are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered. Estimated retroactive adjustments under reimbursement agreements with third-party payors and other changes in estimates are included in net patient service revenue and estimated receivables from and payables to third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined. Estimated receivables from third-party payors include amounts receivable from Medicare and state Medicaid meaningful use programs.

Self-Insured Employee Health Benefits – The Corporation administers self-insured employee health benefit plans for employees. The majority of the Corporation's employees participate in the programs. The provisions of the plans permit employees and their dependents to elect to receive medical care at either the Corporation's RHMs or other health care providers. Gross patient service revenue has been reduced by an allowance for self-insured employee health benefits which represents revenue attributable to medical services provided by the Corporation to its employees and dependents in such years.

Allowance for Doubtful Accounts – The Corporation recognizes a significant amount of patient service revenue at the time the services are rendered even though the Corporation does not assess the patient's ability to pay at that time. As a result, the provision for bad debts is presented as a deduction from patient service revenue (net of contractual provisions and discounts). For uninsured and underinsured patients that do not qualify for charity care, the Corporation establishes an allowance to reduce the carrying value of such receivables to their estimated net realizable value. This allowance is established based on the aging of accounts receivable and the historical collection experience by RHM and for each type of payor. A significant portion of the Corporation's provision for doubtful accounts relates to self-pay patients, as well as co-payments and deductibles owed to the Corporation by patients with insurance.

Premium and Capitation Revenue – The Corporation has certain RHMs that arrange for the delivery of health care services to enrollees through various contracts with providers and common provider entities. Enrollee contracts are negotiated on a yearly basis. Premiums are due monthly and are recognized as revenue during the period in which the Corporation is obligated to provide services to enrollees. Premiums received prior to the period of coverage are recorded as deferred revenue and included in accrued expenses in the consolidated balance sheet.

Certain of the Corporation’s RHMs have entered into capitation arrangements whereby they accept the risk for the provision of certain health care services to health plan members. Under these agreements, the Corporation’s RHMs are financially responsible for services provided to the health plan members by other institutional health care providers. Capitation revenue is recognized during the period for which the RHM is obligated to provide services to health plan enrollees under capitation contracts. Capitation receivables are included in other receivables in the consolidated balance sheet.

Reserves for incurred but not reported claims have been established to cover the unpaid costs of health care services covered under the premium and capitation arrangements. The premium and capitation arrangement reserves are classified with accrued expenses in the consolidated balance sheet. The liability is estimated based on actuarial studies, historical reporting, and payment trends. Subsequent actual claim experience will differ from the estimated liability due to variances in estimated and actual utilization of health care services, the amount of charges, and other factors. As settlements are made and estimates are revised, the differences are reflected in current operations.

Income Taxes – The Corporation and substantially all of its subsidiaries have been recognized as tax-exempt pursuant to Section 501(a) of the Internal Revenue Code. The Corporation also has taxable subsidiaries, which are included in the consolidated financial statements. Certain of the taxable subsidiaries have entered into tax sharing agreements and file consolidated federal income tax returns with other corporate taxable subsidiaries. The Corporation includes penalties and interest, if any, with its provision for income taxes in other nonoperating items in the consolidated statement of operations and changes in net assets.

Excess of Revenue Over Expenses – The consolidated statement of operations and changes in net assets includes excess of revenue over expenses. Changes in unrestricted net assets, which are excluded from excess of revenue over expenses, consistent with industry practice, include the effective portion of the change in market value of derivatives that meet hedge accounting requirements, permanent transfers of assets to and from affiliates for other than goods and services, contributions of long-lived assets received or gifted (including assets acquired using contributions, which by donor restriction were to be used for the purposes of acquiring such assets), net change in retirement plan related items, discontinued operations, extraordinary items and cumulative effects of changes in accounting principles.

Adopted Accounting Pronouncements –

On July 1, 2013, the Corporation adopted Accounting Standard Update (“ASU”) 2011-11, “*Disclosures About Offsetting Assets and Liabilities*.” This guidance contains new disclosure requirements regarding the nature of an entity’s rights of setoff and related arrangements associated with its financial instruments and derivative instruments. The adoption of this guidance had no impact on the Corporation’s consolidated financial statements.

On July 1, 2013, the Corporation adopted ASU 2012-02, “*Intangibles Goodwill and Other (Topic 350): Testing Indefinite-lived Intangible Assets for Impairment*.” This guidance provides entities the option of first assessing qualitative factors about the likelihood that an indefinite-lived intangible asset is impaired to determine whether further impairment assessment is necessary. It also enhances the consistency of the

impairment testing guidance among long-lived asset categories by permitting entities to assess qualitative factors to determine whether it is necessary to calculate the asset's fair value when testing an indefinite-lived intangible asset for impairment. The adoption of this guidance had no impact on the Corporation's consolidated financial statements.

On July 1, 2013, the Corporation adopted ASU 2012-05, "*Statement of Cash Flows (Topic 230): Not-for-Profit Entities: Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows.*" This guidance provides clarification on how entities classify cash receipts arising from the sale of certain donated financial assets in the statement of cash flows. The adoption of this guidance had no impact on the Corporation's consolidated statement of cash flows.

On July 1, 2013, the Financial Accounting Standards Board ("FASB") issued ASU 2013-01, "*Clarifying the Scope of Disclosures About Offsetting Assets and Liabilities.*" This guidance provides clarification on the scope of the offsetting disclosure requirements in ASU 2011-11. The adoption of this guidance did not have a material impact on the Corporation's consolidated financial statements.

Forthcoming Accounting Pronouncements –

In February 2013, the FASB issued ASU 2013-04, "*Obligations Resulting From Joint and Several Liability Arrangements for Which the Total Amount of the Obligation is Fixed at the Reporting Date,*" which requires entities to measure obligations within the scope of this guidance at the reporting date. This guidance is effective for the Corporation beginning July 1, 2014. The Corporation has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In July 2013, the FASB issued ASU 2013-11, "*Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists.*" This guidance requires entities to present an unrecognized tax benefit, or a portion of an unrecognized tax benefit, in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit, with some exceptions. This guidance is effective for the Corporation beginning July 1, 2014. The Corporation does not expect this guidance to have an impact on its consolidated financial statements.

In April 2014, the FASB issued ASU 2014-08, "*Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity.*" This guidance amends the definition of a discontinued operation and requires entities to provide additional disclosures about discontinued operations as well as disposal transactions that do not meet the discontinued operations criteria. This guidance is effective for the Corporation beginning July 1, 2015, with early adoption permitted. The Corporation has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09, "*Revenue From Contracts With Customers.*" This guidance outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. This guidance is effective for the Corporation beginning July 1, 2017. The Corporation has not yet evaluated the impact this guidance may have on its consolidated financial statements.

3. INVESTMENTS IN UNCONSOLIDATED AFFILIATES AND DISCONTINUED OPERATIONS

Investments in Unconsolidated Affiliates – The Corporation and certain of its RHM's have investments in entities that are recorded under the cost and equity methods of accounting. At June 30, 2014, the Corporation maintained investments in unconsolidated affiliates with ownership interests ranging from 0.7% to 51.0%. The Corporation's share of equity earnings from entities accounted for under the equity method was \$320.6 million for the year ended June 30, 2014, of which \$54.8 million is included in other revenue and \$265.8 million is included in nonoperating items in the consolidated statement of operations and changes in net assets. The most significant of these investments include the following:

BayCare Health System – The Corporation has a 50.4% interest in BayCare Health System Inc. and Affiliates (“BayCare”), a Florida not-for-profit corporation exempt from state and federal income taxes. BayCare was formed in 1997 pursuant to a Joint Operating Agreement (“JOA”) among the not-for-profit, tax-exempt members of the CHE BayCare Participants, Morton Plant Mease Health Care, Inc., and South Florida Baptist Hospital, Inc. (collectively, the “Members”). BayCare consists of three community health alliances located in the Tampa Bay area of Florida including St. Joseph's-Baptist Healthcare Hospital, St. Anthony's Health Care, and Morton Plant Mease Health Care. The Corporation has the right to appoint nine of the twenty-one voting members of the Board of Directors of BayCare, therefore the Corporation accounts for BayCare under the equity method of accounting. At June 30, 2014, the Corporation's investment in BayCare totaled \$1,770.9 million.

Gateway Health Plan – The Corporation has a 50.0% interest in Gateway Health Plan, L.P. and Subsidiaries (“GHP”), a Pennsylvania limited partnership. GHP has two general partners, Highmark Ventures Inc. formerly known as Alliance Ventures, Inc., and Mercy Health Plan, each owning 1%. In addition to the general partners, there are two limited partners, Highmark Inc. and Mercy Health Plan, each owning 49%. At June 30, 2014, the Corporation's investment in GHP totaled \$178.9 million.

Catholic Health System, Inc. – The Corporation has a one-third interest in Catholic Health System, Inc. and Subsidiaries (“CHS”). CHS, formed in 1998, is a not-for-profit integrated delivery healthcare system in western New York jointly sponsored by the Sisters of Mercy, Ascension Health System, the Franciscan Sisters of St. Joseph, and the Diocese of Buffalo. CHE, Ascension Health System, and the Diocese of Buffalo are the corporate members of CHS. CHS operates several organizations, the largest of which are four acute care hospitals located in Buffalo, New York: Mercy Hospital of Buffalo, Kenmore Mercy Hospital, Sisters of Charity Hospital, and St. Joseph Hospital. At June 30, 2014, the Corporation's investment in CHS totaled \$68.0 million.

Emory Healthcare/St. Joseph's Health System – The Corporation has a 49% interest in Emory Healthcare/St. Joseph's Health System (“EH/SJHS”). EH/SJHS operates several organizations, including two acute care hospitals, St. Joseph's Hospital of Atlanta and John's Creek Hospital. At June 30, 2014, the Corporation's investment in EH/SJHS totaled \$60.3 million.

Condensed consolidated balance sheets of BayCare, GHP, CHS and EH/SJHS as of June 30, 2014 are as follows (in thousands):

	<u>Baycare</u>	<u>GHP</u>	<u>CHS</u>	<u>EH/SJHS</u>
Total assets	\$5,390,589	\$643,593	\$872,106	\$430,434
Total liabilities	\$1,676,157	\$285,835	\$662,733	\$289,101

Condensed consolidated statements of operations of BayCare, GHP, CHS and EH/SJHS for the year ended June 30, 2014 are as follows (in thousands):

	<u>Baycare</u>	<u>GHP</u>	<u>CHS</u>	<u>EH/SJHS</u>
Revenue, net	\$2,591,325	\$1,849,055	\$939,581	\$368,190
Excess (deficiency) of revenue over expenses	\$576,392	\$32,377	\$42,821	(\$33,832)

The following amounts have been recognized in the accompanying consolidated statement of operations and changes in net assets related to the investments in BayCare, GHP, CHS and EH/SJHS for the year ended June 30, 2014 (in thousands):

	<u>Baycare</u>	<u>GHP</u>	<u>CHS</u>	<u>EH/SJHS</u>
Other revenue	\$ -	\$ 15,996	\$ -	\$ -
Equity in earnings of unconsolidated organizations	288,196	-	14,260	(26,446)
Other changes in unrestricted net assets	9,282	(3,948)	36,781	(7,382)
Changes in restricted net assets	462	-	-	-
	<u>\$ 297,940</u>	<u>\$ 12,048</u>	<u>\$ 51,041</u>	<u>\$ (33,828)</u>

The unaudited summarized financial position and results of operations for the entities accounted for under the equity method excluding BayCare, GHP, CHS and EH/SJHS as of and for the period ended June 30, 2014 are as follows (in thousands):

	<u>Medical Office Buildings</u>	<u>Outpatient and Diagnostic Services</u>	<u>Ambulatory Surgery Centers</u>	<u>Physician Hospital Organizations</u>	<u>Other Investees</u>	<u>Total</u>
Total assets	\$ 87,931	\$ 106,813	\$ 72,113	\$ 26,845	\$ 512,647	\$ 806,349
Total liabilities	\$ 69,872	\$ 38,732	\$ 42,502	\$ 21,609	\$ 280,263	\$ 452,978
Net assets	\$ 18,059	\$ 68,081	\$ 29,611	\$ 5,236	\$ 232,384	\$ 353,371
Revenue, net	\$ 18,103	\$ 145,907	\$ 134,207	\$ 35,474	\$ 682,900	\$ 1,016,591
Excess of revenue over expenses	\$ 3,454	\$ 16,245	\$ 40,508	\$ (421)	\$ 20,080	\$ 79,866

Discontinued Operations –

The Corporation has several entities that met the criteria for being presented as discontinued operations for the year ended June 30, 2014, the most significant of which include the following:

Mercy Health System of Maine (“Mercy Maine”) – Effective October 1, 2013, membership of Mercy Maine was assumed by Eastern Maine Health System (“EMHS”) via a membership substitution. Substantially all assets and liabilities transferred to EMHS on that date. As a result of the transfer, a loss on membership transfer of \$80.7 million was recorded in unrestricted net assets. The consolidated financial statements present the operations of Mercy Maine as a discontinued operation. For the year ended June 30, 2014, the Corporation reported revenue of \$55.5 million and loss on operations of \$0.4 million in discontinued operations in the consolidated statement of operations and changes in net assets.

Saint Michael's Medical Center – On February 8, 2013, Saint Michael's Medical Center entered into an asset purchase agreement under which the hospital would be acquired by Prime Healthcare Services. The majority of assets and liabilities of Saint Michael's Medical Center have been classified as held for sale on the consolidated balance sheet. The transaction is pending subject to approval by the state of New Jersey. The consolidated financial statements present the operations of Saint Michael's Medical Center as a discontinued operation. For the year ended June 30, 2014, the Corporation reported revenue of \$194.2 million and losses on operations of \$15.0 million in discontinued operations in the consolidated statement of operations and changes in net assets. As of June 30, 2014, assets held for sale of \$127.9 million and liabilities held for sale of \$257.9 million and consisted of (in thousands):

Patient accounts receivable	\$ 21,475	Current portion of long-term debt	\$ 4,490
Other current assets	9,418	Accounts payable & accrued expenses	17,085
Property and equipment	81,465	Other current liabilities	8,546
Other assets	<u>15,559</u>	Long-term debt, net of current portion	<u>227,799</u>
Total assets	<u>\$ 127,917</u>	Total liabilities	<u>\$ 257,920</u>

Saint James Mercy Hospital ("SJM") – During December 2013, the Board of Directors of SJMH approved a plan to undergo a visioning plan and to transfer the majority of the operations of SJMH. Certain assets and liabilities of SJMH have been classified as held for sale on the consolidated balance sheet. The consolidated financial statements present the operations of SJMH as a discontinued operation. For the year ended June 30, 2014, the Corporation reported revenue of \$40.3 million and loss on operations of \$6.2 million in discontinued operations in the consolidated statement of operations and changes in net assets. As of June 30, 2014, assets held for sale were \$12.1 million. The majority of assets held for sale consist of property and equipment.

Mercy Health Partners, North ("North") – On May 8, 2014, the Corporation entered into a non-binding letter of intent with Munson Health under which substantially all of the healthcare operations located in Cadillac, Michigan and Grayling, Michigan would be acquired by Munson Healthcare. Discussions are subject to a definitive agreement. The letter of intent will remain in effect until the execution of a definitive agreement or the letter of intent is terminated by either party. Certain assets and liabilities of North have been classified as held for sale on the consolidated balance sheet. The consolidated financial statements present the hospital operations of North as a discontinued operation. For the year ended June 30, 2014, the Corporation reported revenue of \$150.2 million and loss on operations of \$13.4 million impairment, which includes a \$13.0 million asset impairment, in discontinued operations in the consolidated statement of operations and changes in net assets. As of June 30, 2014, assets held for sale of \$44.7 million consisted of (in thousands):

Inventories	\$ 3,369
Assets limited or restricted as to use Property and equipment	2,313
Investments in unconsolidated affiliates	<u>36,710</u>
Total assets	<u>\$ 44,706</u>

4. NET PATIENT SERVICE REVENUE

A summary of the payment arrangements with major third-party payors follows:

Medicare – Acute inpatient and outpatient services rendered to Medicare program beneficiaries are paid primarily at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Certain items are reimbursed at a tentative rate with final settlement determined after submission of annual cost reports and audits thereof by the Medicare fiscal intermediaries.

Medicaid – Reimbursement for services rendered to Medicaid program beneficiaries includes prospectively determined rates per discharge, per diem payments, discounts from established charges, fee schedules, and cost reimbursement methodologies with certain limitations. Cost reimbursable items are reimbursed at a tentative rate with final settlement determined after submission of annual cost reports and audits thereof by the Medicaid fiscal intermediaries.

Other – Reimbursement for services to certain patients is received from commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for reimbursement includes prospectively determined rates per discharge, per diem payments, and discounts from established charges.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

Charity Care – The Corporation provides services to all patients regardless of ability to pay. In accordance with the Corporation's policy, a patient is classified as a charity patient based on income eligibility criteria as established by the Federal Poverty Guidelines. Charges for services to patients who meet the Corporation's guidelines for charity care are not reflected in the accompanying consolidated financial statements.

Patient service revenues, net of contractual and other allowances (but before the provision for bad debts), recognized during the year ended June 30, 2014 is as follows (in thousands):

Medicare	\$	4,690,876
Blue Cross		2,538,707
Medicaid		1,609,374
Uninsured		489,355
Commercial and Other		<u>3,066,994</u>
Total	\$	<u>12,395,306</u>

A summary of net patient service revenue before provision for bad debts for the year ended June 30, 2014 is as follows (in thousands):

Gross charges:	
Acute inpatient	\$ 17,030,436
Outpatient, nonacute inpatient, and other	19,025,984
Gross patient service revenue	<u>36,056,420</u>
Less:	
Contractual and other allowances	(22,695,773)
Charity care charges	<u>(965,341)</u>
Net patient service revenue before provision for bad debts	<u><u>\$ 12,395,306</u></u>

5. PROPERTY AND EQUIPMENT

A summary of property and equipment at June 30, 2014 is as follows (in thousands):

Land	\$ 318,368
Buildings and improvements	7,655,128
Equipment	5,190,900
Capital leased assets	<u>192,754</u>
Total	13,357,150
Accumulated depreciation	(7,324,759)
Construction in progress	<u>560,522</u>
Property and equipment, net	<u><u>\$ 6,592,913</u></u>

At June 30, 2014, commitments to purchase property and equipment of approximately \$424 million were outstanding. Significant commitments are primarily for facility expansion at existing campuses and related infrastructures at the following RHMs: Holy Cross Hospital in Silver Spring, Maryland - \$153 million; Mercy Health System of Chicago (“MHSC”) in Chicago, Illinois - \$56 million; and Loyola University Health System (“LUHS”) in Chicago, Illinois - \$53 million. Costs of these projects are expected to be financed by proceeds from bond issuances, available funds, future operations of the hospitals and contributions.

As part of the acquisition of LUHS that occurred in fiscal year 2012, the Corporation has committed to spend at least \$300 million on capital projects for LUHS through fiscal year ending June 30, 2018. This amount may be increased to \$400 million if certain operating thresholds are met. Through June 30, 2014, approximately \$154 million of capital expenditures have been accrued on capital projects for LUHS. In addition, as part of the acquisition of MHSC that occurred in fiscal year 2012, the Corporation has committed to spend at least \$140 million for capital, information systems and equipment needs to support the operations of MHSC through the fiscal year ending June 30, 2017. This amount may be increased to \$150 million if certain operating thresholds are met. Through June 30, 2014, approximately \$65 million of capital expenditures have been accrued on such MHSC projects.

During the year ended June 30, 2014, the Corporation recorded total impairment charges of \$91 million included in asset impairment charges in the consolidated statement of operations and changes in net assets. Material adverse trends in the most recent estimates of future undiscounted cash flows of certain hospitals indicated that the carrying value of the long-lived assets was not recoverable from the estimated future cash flows. The Corporation believes the most significant factors contributing to the

continuing adverse financial trends include reductions in volumes of insured patients and shifts in payor mix. Fair value was determined using a third party valuation. Impairments were recorded at the following locations because fair value estimates were lower than carrying value: Mercy Suburban Hospital, Pennsylvania – \$32.7 million; Mount Carmel West, Columbus, Ohio – \$19.2 million; St. Francis, Wilmington, Delaware – \$15.5 million; St. Francis, Trenton, New Jersey – \$5.9 million; and other Southeast Michigan locations – \$17.2 million.

6. LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

A summary of short-term borrowings and long-term debt at June 30, 2014 is as follows (in thousands):

Short-term borrowings:

Variable rate demand bonds with contractual maturities through 2048. Interest payable monthly at rates ranging from 0.02% to 0.19% during 2014	<u>\$ 1,123,620</u>
------------------------------------------------------------------------------------------------------------------------------------------------	---------------------

Long-term debt:

Tax-exempt revenue bonds and refunding bonds:	
Fixed rate term and serial bonds, payable at various dates through 2048. Interest rate ranges from 2.0% to 7.62% during 2014	\$ 2,922,513
Variable rate term bonds, payable at various dates through 2048. Interest rate ranges from 0.48% to 4.1% during 2014	465,410
Notes payable to banks. Interest payable at rates ranging from 0.03% to 6.7%, fixed and variable, payable in varying monthly installments through 2032	11,675
Capital lease obligations (excluding imputed interest of \$64.6 million at June 30, 2014)	132,985
Mortgage obligations. Interest payable at rates ranging from 1.0% to 11.0% during 2014	111,161
Other	<u>35,299</u>
Total long-term debt	3,679,043
Less current portion, net of current discounts	(96,038)
Unamortized premiums, net	<u>36,232</u>
Long-term debt, net of current portion	<u>\$ 3,619,237</u>

Contractually obligated principal repayments on short-term borrowings and long-term debt are as follows (in thousands):

	<u>Short-Term Borrowings</u>	<u>Long-Term Debt</u>
Years ending June 30:		
2015	\$ 24,910	\$ 96,038
2016	26,215	102,434
2017	27,890	93,778
2018	30,200	95,081
2019	29,400	104,007
Thereafter	<u>985,005</u>	<u>3,187,705</u>
Total	<u>\$ 1,123,620</u>	<u>\$ 3,679,043</u>

A summary of interest costs on borrowed funds primarily under the revenue bond indentures during the year ended June 30, 2014 is as follows (in thousands):

Interest costs incurred	\$ 174,203
Less capitalized interest	<u>(14,975)</u>
Interest expense included in operations	<u>\$ 159,228</u>

Obligated Group and Other Requirements – The Corporation has debt outstanding under a Master Trust Indenture dated October 3, 2013, as amended and supplemented, the Amended and Restated Master Indenture (“ARMI”). The ARMI permits the Corporation to issue obligations to finance certain activities. Obligations issued under the ARMI are joint and several obligations of the Corporation, CHE and Trinity Health (the “Obligated Group”). Proceeds from tax-exempt bonds and refunding bonds are to be used to finance the construction, acquisition and equipping of capital improvements. Certain RHM’s of the Corporation constitute designated affiliates and the Corporation covenants to cause each designated affiliate to pay, loan or otherwise transfer to the Obligated Group such amounts necessary to pay the amounts due on all obligations issued under the ARMI. The Obligated Group and the designated affiliates are referred to as the Credit Group.

The Credit Group does not include certain Affiliates that borrow on their own or are members of a separate New York obligated group, but which are included in the Corporation’s consolidated financial statements. St. Peter’s Hospital of the City of Albany (“St. Peter’s”) currently is a member and the Obligated Group Agent of an obligated group created under that certain Master Trust Indenture dated as of January 1, 2008, between St. Peter’s and Manufacturers and Traders Trust Company, as Master Trustee. St. Peter’s received approval from the New York State Department of Health to permit the entry into that obligated group of additional entities within St. Peter’s Health Care Services, Northeast Health, Inc. and Seton Health System, Inc.

The Obligated Group agrees in the ARMI to cause Designated Affiliates to grant to the Master Trustee security interests in their Pledged Property in order to secure all Obligations issued under the Master Indenture. The Designated Affiliates when combined with the current Members of the Obligated Group represent no less than 85% of the consolidated net revenues of the Credit Group. The aggregate amount of obligations outstanding using the ARMI (other than obligations that have been advance refunded) were \$4,264 million at June 30, 2014.

There are several conditions and covenants required by the ARMI with which the Corporation must comply, including covenants that require the Corporation to maintain a minimum debt service coverage and limitations on liens or security interests in property, except for certain permitted encumbrances, affecting the property of the Corporation or any material designated affiliate (a designated affiliate whose total revenues for the most recent fiscal year exceed 5% of the combined total revenues of the Corporation for the most recent fiscal year). Long-term debt outstanding as of June 30, 2014, excluding amounts issued under the ARMI, is generally collateralized by certain property and equipment.

MHSC has obtained a mortgage loan in the amount of approximately \$66 million that is insured by the U.S. Department of Housing and Urban Development (“HUD”) under the Federal Housing Administration’s Section 242 Hospital Mortgage Insurance Program. Final closing of this HUD-insured loan occurred on June 30, 2014, at which time the remaining proceeds of this loan were disbursed to MHSC. At June 30, 2014, the unpaid principal balance of this loan was \$63.1 million. The loan collateral includes MHSC’s main hospital campus, two MHSC satellite facilities and personal property (including deposit accounts) of both MHSC and its affiliate Mercy Foundation, Inc. MHSC’s payment obligations under the two mortgage notes evidencing this loan are guaranteed by Trinity Health. The

mortgage loan agreements with HUD contain various covenants including: those relating to limitations on incurring additional debt; transactions with affiliates; transferring or disposing of designated property; use of funds and other assets of the mortgaged property; financial performance; required reserves; insurance coverage; timely submission of specified financial reports; and restrictions on prepayment of the mortgage loan. Mercy Health System of Chicago and Trinity Health provided covenants to HUD not to interfere in the performance of MHSC's obligations under the HUD-insured loan documents.

The Corporation issued \$627 million in tax-exempt variable rate hospital revenue bonds (the "Series 2013 Bonds") and remarketed \$89 million in CHE tax-exempt, variable rate hospital revenue bonds under the ARMI. Proceeds were used to retire \$44 million of CHE's then outstanding fixed rate hospital revenue bonds, \$120 million of CHE's then outstanding variable rate hospital revenue bonds and \$269 million of Trinity Health's then outstanding taxable commercial paper obligations. The remaining proceeds of the Series 2013 Bonds will be used to finance, refinance and reimburse a portion of the costs of acquisition, construction, renovation and equipping of health facilities, and to pay related costs of issuance. These transactions resulted in a loss from extinguishment of debt of \$1.6 million recorded in other nonoperating items in the consolidated statement of operations and changes in net assets.

Commercial Paper – The Corporation's commercial paper program is authorized for borrowings up to \$600 million. At June 30, 2014, the total amount of commercial paper outstanding was \$240 million. Proceeds from this program are to be used for general purposes of the Corporation. The notes are payable from the proceeds of subsequently issued notes and from other funds available to the Corporation, including funds derived from the liquidation of securities held by the Corporation in its investment portfolio. The interest rate charged on borrowings outstanding during the year ended June 30, 2014 ranged from 0.06% to 0.17%.

Liquidity Facilities – In July 2013, the Corporation renewed the Trinity Health credit agreements (collectively, the "Credit Agreements") previously entered into between Trinity Health and U.S. Bank National Association, which acts as an administrative agent for a group of lenders thereunder. The Credit Agreements establish a revolving credit facility for the Corporation, under which that group of lenders agree to lend to the Corporation amounts that may fluctuate from time to time. In October 2013, the Corporation exercised its option to increase by \$200 million the 2013 Credit Agreements from \$731 million to \$931 million. Amounts drawn under the 2013 Credit Agreements can only be used to support the Corporation's obligation to pay the purchase price of bonds which are subject to tender and that have not been successfully remarketed, and the maturing principal of and interest on commercial paper notes. Of the \$931 million available balance, \$150 million expires in July 2014, \$175 million expires in July 2015, \$321 million expires in July 2016 and \$285 million expires in July 2017. The Credit Agreements are secured by Obligations under the Master Indenture. As of June 30, 2014, there were no amounts outstanding on these credit agreements. In July 2014, the Corporation renewed and extended the Credit Agreements for an additional year through an amendment and restatement of the 2013 Credit Agreements.

The Corporation also maintains a CHE general purpose facility of \$300 million, of which \$42 million is related to letters of credit. At the Corporation's direction, this general purpose facility was reduced to \$45 million effective March 14, 2014. As of June 30, 2014, there were no draws on this general purpose credit facility.

In addition, in July 2013, the Corporation renewed a Trinity Health three year general purpose credit facility of \$200 million. As of June 30, 2014, there were no amounts outstanding under this credit facility.

Standby Letters of Credit – The Corporation entered into various standby letters of credit totaling approximately \$17.3 million at June 30, 2014. These standby letters of credit are renewed annually and are available to the Corporation as necessary under its insurance programs and for unemployment liabilities. There were no draws on these letters of credit during the year ended June 30, 2014.

7. PROFESSIONAL AND GENERAL LIABILITY PROGRAMS

The Corporation operates a wholly owned insurance company, Venzke Insurance Company, Ltd. (“Venzke”) that qualifies as a captive insurance company and provides certain insurance coverage to the Corporation’s RHM’s under a centralized program. The Corporation is self-insured for certain levels of general and professional liability, workers’ compensation and certain other claims. The Corporation has limited its liability by purchasing reinsurance and commercial coverage from unrelated third-party insurers.

Effective January 1, 2014, all assets and liabilities of Stella Maris Insurance Company, Ltd. (“Stella Maris”), which qualified as a captive insurance company, merged into Venzke. Policies issued and reinsurance purchased by Stella Maris prior to January 1, 2014 and all losses previous to January 1, 2014 have been assumed by Venzke.

The Corporation’s current self-insurance program includes \$20 million per occurrence for the first layers of professional liability, as well as \$10 million per occurrence for hospital government liability, \$5 million per occurrence for errors and omission liability, and \$1 million per occurrence for directors’ and officers’ liability. Additional layers of professional liability insurance are available with coverage provided through other insurance carriers and various reinsurance arrangements. The total amount available for these subsequent layers is \$100 million in aggregate. The Corporation self-insures \$750,000 per occurrence for workers’ compensation in most states, with commercial insurance providing coverage up to the statutory limits, and self-insures up to \$500,000 in property damage liability with commercial insurance providing coverage up to \$1 billion.

The liability for self-insurance reserves represents estimates of the ultimate net cost of all losses and loss adjustment expenses, which are incurred but unpaid at the consolidated balance sheet date. The reserves are based on the loss and loss adjustment expense factors inherent in the Corporation’s premium structure. Independent consulting actuaries determined these factors from estimates of the Corporation’s expenses and available industry-wide data. The Corporation discounts the reserves to their present value using a discount rate of 3.0%. The reserves include estimates of future trends in claim severity and frequency. Although considerable variability is inherent in such estimates, management believes that the liability for unpaid claims and related adjustment expenses is adequate based on the loss experience of the Corporation. The estimates are continually reviewed and adjusted as necessary.

Claims in excess of certain insurance coverage and the recorded self-insurance liability have been asserted against the Corporation by various claimants. The claims are in various stages of processing, and some may ultimately be brought to trial. There are known incidents occurring through June 30, 2014 that may result in the assertion of additional claims, and other claims may be asserted arising from services provided in the past. While it is possible that settlement of asserted claims and claims that may be asserted in the future could result in liabilities in excess of amounts for which the Corporation has provided, management, based upon the advice of Counsel, believes that the excess liability, if any, should not materially affect the consolidated financial position, operations or cash flows of the Corporation.

8. PENSION AND OTHER BENEFIT PLANS

Deferred Compensation – The Corporation has nonqualified deferred compensation plans at certain RHM locations that permit eligible employees to defer a portion of their compensation. The deferred amounts are distributable in cash after retirement or termination of employment. As of June 30, 2014, the assets under these plans totaled \$137.8 million and liabilities totaled \$145.1 million.

Defined Contribution Benefits – The Corporation sponsors defined contribution pension plans covering substantially all of its employees. These programs vary by location and are funded by employee voluntary contributions, subject to legal limitations. Employer contributions to these plans include varying levels of matching and non-elective contributions. The employees direct their voluntary contributions and employer contributions among a variety of investment options. Trinity Health suspended the majority of employer matching contributions for the fiscal year 2014. Contribution expense under the plans totaled \$68.8 million for the year ended June 30, 2014.

Noncontributory Defined Benefit Pension Plans (“Pension Plans”) – Substantially all of the Corporation’s employees participate in qualified, noncontributory defined benefit pension plans. Certain non-qualified, supplemental plan arrangements also provide retirement benefits to specified groups of participants.

CHE maintains several defined benefit pension plans. One of the plans is subject to the provisions of the Employee Retirement Security Act of 1974 (“ERISA”). The remaining plans have Church Plan status as determined by the Internal Revenue Service and are not governed by ERISA. The majority of the CHE qualified defined benefit plans are frozen and participants are no longer accruing benefits in those plans. Funding for the ERISA plan is made in accordance with ERISA requirements. Funding for the Church Plans varies by plan but generally is based on plan liabilities with amortization of any under or over funding, over a seven year period.

Trinity Health maintains three defined benefit pension plans, two of which have frozen benefits and are subject to the provisions of ERISA. The third plan, the Trinity Health Pension Plan, has church plan status. For the majority of plan participants in the Trinity Health Pension Plan, prior to June 30, 2010, benefits were based on years of service and employees’ highest five years of compensation at which time an accrued frozen benefit was calculated for all active participants. As of July 1, 2010, participants accrue benefits based on a cash balance formula, which credits participants annually with a percentage of eligible compensation based on age and years of service, as well as an interest credit based on a benchmark interest rate. A transition adjustment was provided to participants who were vested as of June 30, 2010, whose age and service met certain requirements at that date. The transition adjustment applies to the pension benefit earned through June 30, 2010 and increased compensation under the final average pay formula over a five-year period. Effective June 2014, the Trinity Health Pension Plan was amended to freeze all future benefit accruals as of December 31, 2014. As a result of this amendment, the Trinity Health Pension Plan projected benefit obligation decreased \$49.5 million, and the Corporation recognized a curtailment gain of \$149.7 million in the consolidated statement of operations and changes in net assets. Because this plan has Church Plan status, funding in accordance with ERISA is not required. The Corporation’s adopted funding policy for its qualified plan, which is reviewed annually, is to fund the current normal cost based on the accumulated benefit obligation at the plans’ December 31 year-end, and amortization of any under or over funding over a ten-year period.

Effective December 2013, the majority of the CHE and Trinity Health Plans were amended to implement a voluntary lump sum distribution window. The amendments provided the opportunity for certain eligible participants to elect to receive a full distribution of their pension benefits as a lump sum during the program window period from March 24, 2014 to May 2, 2014. To be eligible a participant

must have terminated employment on or before December 31, 2013. As a result of this program, the Plans' projected benefit obligations decreased \$698.4 million for benefits paid, and the Corporation recognized a settlement loss of \$196 million in the consolidated statement of operations and consolidated statement of operations and changes in net assets.

Postretirement Health Care and Life Insurance Benefits (“Postretirement Plans”) – The Corporation sponsors both funded and unfunded contributory plans to provide health care benefits to certain of its retirees. All of the Postretirement Plans are closed to new participants. The plans cover certain hourly and salaried employees who retire from certain RHMs. Medical benefits for these retirees are subject to deductibles and co-payment provisions. Effective January 1, 2011, the funded plans provide benefits to certain retirees at fixed dollar amounts in Health Reimbursement Account arrangements for Medicare eligible participants.

The following table sets forth the changes in projected benefit obligations, accumulated postretirement obligations, and changes in plan assets and funded status of the plans for both the Pension and Postretirement Plans for the year ended June 30, 2014 (in thousands):

	<u>Pension Plans</u>	<u>Postretirement Plans</u>
Change in Benefit Obligation:		
Benefit obligation, beginning of year	\$ 6,244,763	\$ 107,865
Service cost	149,138	628
Interest cost	331,554	5,297
Actuarial loss (gain)	448,872	(302)
Benefits paid	(198,505)	(5,081)
Medicare Part D reimbursement	-	111
Curtailments	(49,449)	-
Settlements	(698,354)	-
Benefit obligation, end of year	<u>6,228,019</u>	<u>108,518</u>
Change in Plan Assets:		
Fair value of plan assets, beginning of year	5,491,447	84,523
Actual return on plan assets	699,893	15,338
Employer contributions	230,360	1,329
Benefits paid	(198,505)	(5,081)
Settlements	(698,354)	-
Fair value of plan assets, end of year	<u>5,524,841</u>	<u>96,109</u>
Unfunded amount recognized June 30	<u>\$ (703,178)</u>	<u>\$ (12,409)</u>
Recognized in other long-term assets	\$ 8,258	\$ 4,028
Recognized in accrued pension and retiree health costs	\$ (711,436)	\$ (16,437)

Actuarial losses incurred in the pension plans during the year ended June 30, 2014 are primarily related to changes in discount rates used to measure the plans' liabilities.

The accumulated benefit obligation and fair value of plan assets for the qualified defined benefit pension plans for the year ended June 30, 2014 are as follows (in thousands):

	<u>Pension Plans</u>
Accumulated benefit obligation	\$ 6,182,463
Fair value of plan assets	<u>5,524,841</u>
Funded status	<u><u>\$ (657,622)</u></u>

Components of net periodic benefit cost for the year ended June 30, 2014 consisted of the following (in thousands):

	<u>Pension Plans</u>	<u>Postretirement Plans</u>
Service cost	\$ 149,138	\$ 627
Interest cost	331,554	5,297
Expected return on assets	(398,683)	(6,008)
Amortization of prior service cost	(27,345)	(5,763)
Recognized net actuarial loss	<u>104,089</u>	<u>(167)</u>
Net periodic benefit cost (income) before curtailments/settlements	\$ 158,753	\$ (6,014)
Curtailment gain	(149,734)	-
Settlement loss	<u>195,987</u>	<u>-</u>
Net periodic benefit cost (income)	<u><u>\$ 205,006</u></u>	<u><u>\$ (6,014)</u></u>

The amounts in unrestricted net assets, including amounts arising during the year and amounts reclassified into net periodic benefit cost, are as follows (in thousands):

	Pension Plans			All Plans Grand Total
	Net Loss (Gain)	Prior Service Cost	Total	
Balance at July 1, 2013	\$ 1,813,218	\$ (221,844)	\$ 1,591,374	
Curtailements	100,285		100,285	
Settlements	(195,987)		(195,987)	
Reclassified into net periodic benefit cost	(104,089)	27,345	(76,744)	
Arising during the year	147,643	-	147,643	
Balance at June 30, 2014	<u>\$ 1,761,070</u>	<u>\$ (194,499)</u>	<u>\$ 1,566,571</u>	

	Postretirement Plans			All Plans Grand Total
	Net Loss (Gain)	Prior Service Credit	Total	
Balance at July 1, 2013	\$ 3,287	\$ (10,159)	\$ (6,872)	\$ 1,584,502
Curtailements	-	-	-	100,285
Settlements	-	-	-	(195,987)
Reclassified into net periodic benefit cost	167	5,763	5,930	(70,814)
Arising during the year	(9,529)	-	(9,529)	138,114
Balance at June 30, 2014	<u>\$ (6,075)</u>	<u>\$ (4,396)</u>	<u>\$ (10,471)</u>	<u>\$ 1,556,100</u>

The following are estimated amounts to be amortized from unrestricted net assets into net periodic benefit cost during fiscal year 2015 (in thousands):

	Pension Plans	Postretirement Plans
Amortization of prior service credit	\$ (5,877)	\$ (564)
Recognized net actuarial loss (gain)	31,580	(261)
Total	<u>\$ 25,703</u>	<u>\$ (825)</u>

Assumptions used to determine benefit obligations and net periodic benefit cost as of and for the year ended June 30, 2014 were as follows:

	Pension Plans	Postretirement Plans
Benefit Obligations:		
Discount rate	4.60% - 5.20%	4.00% - 4.75%
Rate of compensation increase in 2014		
Graduated to 4% by 2017	2.50%	N/A
Net Periodic Benefit Cost:		
Discount rate	4.95% - 5.70%	4.40% - 5.20%
Expected long-term return on plan assets	7.00% - 7.50%	7.50%
Rate of compensation	3.0%	N/A

Approximately 93% of the Corporation's pension plan liabilities are measured using the 4.90% discount rate at June 30, 2014.

The Corporation utilizes a pension liability driven investment strategy in determining its asset allocation and long-term rate of return for plan assets. This risk management strategy uses a glide path methodology based on funded status to initiate asset allocation changes across the efficient frontier. Efficient frontier analysis models the risk and return trade-offs among asset classes while taking into consideration the correlation among the asset classes. Historical market returns and risks are examined as part of this process, but risk-based adjustments are made to correspond with modern portfolio theory. Long-term historical correlations between asset classes are used, consistent with widely accepted capital markets principles. Current market factors, such as inflation and interest rates, are evaluated before long-term capital market assumptions are determined. The long-term rate of return is established using the efficient frontier analysis approach with proper consideration of asset class diversification and rebalancing. Peer data and historical returns are reviewed to check for reasonableness and appropriateness.

Health Care Cost Trend Rates – Assumed health care cost trend rates have a significant effect on the amounts reported for the postretirement plans. The postretirement benefit obligation includes assumed health care cost trend rates as of June 30, 2014 as follows:

Medical and drugs, pre-age 65	7.5%
Medical and drugs, post-age 65	7.5%
Ultimate trend rate	5.0%
Year rate reaches the ultimate rate	2023

A one-percentage point change in assumed health care cost trend rates would have the following effects at June 30, 2014 (in thousands):

	<u>One-Percentage- Point Increase</u>	<u>One-Percentage- Point Decrease</u>
Effect on postretirement benefit obligation	\$ 3,358	\$ (2,861)
Effect on total of service cost and interest cost components	\$ 209	\$ (176)

The Corporation's investment allocations at June 30, 2014 by investment category are as follows:

Investment Category:	Pension Plans	Postretirement Plans
Cash and cash equivalents	5%	1%
Marketable securities:		
U.S. and non-U.S equity securities	10%	-
Equity mutual funds	7%	-
Debt securities	33%	32%
Other investments:		
Commingled funds	14%	67%
Hedge funds	24%	-
Private equity funds	6%	-
Other	1%	-
Total	<u>100%</u>	<u>100%</u>

The Corporation employs a total return investment approach whereby a mix of equities and fixed income investments are used to maximize the long-term return of plan assets for a prudent level of risk. Risk tolerance is established through careful consideration of plan liabilities, plan funded status, and corporate financial condition. The investment portfolio contains a diversified blend of equity and fixed-income investments. Furthermore, equity investments are diversified across U.S. and non-U.S. stocks, as well as growth, value, and small and large capitalizations. Other investments, such as hedge funds, interest rate swaps, and private equity are used judiciously to enhance long-term returns while improving portfolio diversification. Derivatives may be used to gain market exposure in an efficient and timely manner; however, derivatives may not be used to leverage the portfolio beyond the market value of the underlying investments. Investment risk is measured and monitored on an ongoing basis through quarterly investment portfolio reviews, annual liability measurements, and periodic asset/liability studies. For the majority of the Corporation's pension plan investments, the combined target investment allocation at June 30, 2014 was global and traditional equity securities 30%; long/short equity 10%; fixed income obligations 40%; hedge funds 15%; and alternative debt 5%.

The following table summarizes the Pension and Postretirement Plans' assets measured at fair value at June 30, 2014 (in thousands). See Note 10 for definitions of Levels 1, 2 and 3 of the fair value hierarchy.

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Pension Plans:				
Cash and cash equivalents	\$ 294,057	\$ 602	\$ -	\$ 294,659
Equity securities	551,831	1,897	-	553,728
Debt securities				
Government and government agency obligations	-	538,138	-	538,138
Corporate bonds	-	1,132,025	-	1,132,025
Asset backed securities	-	69,621	2,467	72,088
Mutual funds				
Equity mutual funds	369,515	6,954	-	376,469
Fixed income mutual funds	107,318	-	-	107,318
Commingled funds				
Equity commingled funds	-	716,472	-	716,472
Fixed income commingled funds	-	66,950	-	66,950
Hedge funds	-	671,757	672,245	1,344,002
Private equity	-	-	309,163	309,163
Other	13,803	26	-	13,829
	<u>\$ 1,336,524</u>	<u>\$ 3,204,442</u>	<u>\$ 983,875</u>	<u>\$ 5,524,841</u>
Total pension plans' assets at fair value				
Postretirement Plans:				
Mutual funds				
Short term investment mutual funds	\$ 1,188	\$ -	\$ -	\$ 1,188
Fixed income mutual fund	30,862	-	-	30,862
Equity commingled fund	-	63,819	-	63,819
Other	240	-	-	240
	<u>\$ 32,290</u>	<u>\$ 63,819</u>	<u>\$ -</u>	<u>\$ 96,109</u>
Total postretirement plans' assets at fair value				

Unfunded capital commitments related to Level 3 private equity investments totaled \$119.5 million at June 30, 2014.

The Corporation's policy is to recognize transfers between all levels as of the beginning of the reporting period. There were no significant transfers to or from Levels 1 and 2 during the year ended June 30, 2014.

See Note 10 for the Corporation's methods and assumptions to estimate the fair value of equity and debt securities, mutual funds, commingled funds, and hedge funds.

Private Equity – These assets include several private equity funds that invest primarily in the United States, Asia and Europe, both directly and on the secondary market, pursuing distressed opportunities and natural resources, primarily energy. These funds are valued at net asset value, which is calculated using the most recent fund financial statements.

Other – Represents unsettled transactions relating primarily to purchases and sales of plan assets, accrued income, and derivatives. Due to the short maturity of these assets and liabilities, the fair value is equal to the carrying amounts. Concerning derivatives, the Pension Plans are party to certain agreements, which are designed to manage exposures to equities and interest rate risks. These instruments are used for the purpose of hedging changes in the fair value of assets and actuarial present value of accumulated plan benefits that result from interest rate changes, or as an efficient substitute for traditional securities. The fair value of the derivatives is estimated utilizing the terms of the derivative instruments and publicly available market yield curves. The Pension Plans’ investment policies specifically prohibit the use of derivatives for speculative purposes.

The following table summarizes the changes in Level 3 Pension Plan assets for the year ended June 30 (in thousands):

	<u>Asset Backed</u>			
	<u>Securities</u>	<u>Hedge Funds</u>	<u>Private Equity</u>	<u>Total</u>
Balance at July 1, 2013	\$ -	\$ 767,942	\$ 251,228	\$ 1,019,170
Realized gain	-	3,787	9,576	13,363
Unrealized (loss) gain	5	70,891	26,584	97,480
Purchases	2,462	-	78,006	80,468
Sales	-	(126,903)	(44,681)	(171,584)
Settlements	-	35,418	(11,550)	23,868
Transfers out to Level 2	-	(78,890)	-	(78,890)
Balance at June 30, 2014	<u>\$ 2,467</u>	<u>\$ 672,245</u>	<u>\$ 309,163</u>	<u>\$ 983,875</u>

Transfers out of Level 3 into Level 2 were made for direct hedge funds where initial lock-up periods expired during fiscal year 2014.

The preceding methods may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Corporation believes the valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Expected Contributions – The Corporation expects to contribute \$192.2 million to its Pension Plans and \$1.4 million to its Postretirement Plans during the year ended June 30, 2015 under the Corporation’s stated funding policy.

Expected Benefit Payments – The Corporation expects to pay the following for pension benefits, which reflect expected future service as appropriate, and expected postretirement benefits, before deducting the Medicare Part D subsidy (in thousands):

	<u>Pension Plans</u>	<u>Postretirement Plans</u>	<u>Postretirement Medicare Part D Subsidy</u>
2015	\$ 293,899	\$ 7,475	\$ 97
2016	296,896	7,549	93
2017	315,274	7,696	89
2018	334,068	7,789	83
2019	352,511	7,843	76
Years 2020 - 2024	1,959,666	38,456	296

9. COMMITMENTS AND CONTINGENCIES

Operating Leases – The Corporation leases various land, equipment and facilities under operating leases. Total rental expense, which includes provisions for maintenance in some cases, was \$202 million for the year ended June 30, 2014.

The following is a schedule of future minimum lease payments under operating leases as of June 30, 2014, that have initial or remaining lease terms in excess of one year (in thousands):

Years ending June 30:	
2015	\$ 141,356
2016	113,831
2017	97,093
2018	78,476
2019	61,978
Thereafter	<u>186,425</u>
Total	<u>\$ 679,159</u>

Litigation and Settlements –

Saint Alphonsus Regional Medical Center and its subsidiary Saint Alphonsus Diversified Care, Inc. (together, “Saint Alphonsus”) have been involved in litigation arising out of the withdrawal of Saint Alphonsus from an imaging center partnership. The matter first went to trial in 2007, was appealed and tried a second time in 2011. In the second trial, the jury held against Saint Alphonsus in the amount of \$52 million, which was offset by the value of Saint Alphonsus’ partnership interest, which, together with interest, was approximately \$6.6 million at the time of judgment. Saint Alphonsus appealed the second jury verdict to Idaho Supreme Court. On June 16, 2014, the Idaho Supreme Court affirmed the jury award, which, when combined with attorney fees, costs and interest, is a total judgment of approximately \$56 million. The Corporation recorded management’s estimation for damages of \$20 million in fiscal year 2007. As a result, an additional litigation accrual of \$36 million was recorded in the fiscal year 2014 consolidated statement of operations and statement of changes in net assets. The judgment was paid subsequent to year end.

CHE Trinity, Inc. as successor to CHE is the defendant in a purported class action lawsuit in New York state court brought by Emmet & Co, Inc., and First Manhattan Co, with respect to one series of bonds

issued for the benefit of CHE. Plaintiffs allege that CHE breached the Indenture relating to those bonds and violated the covenant of good faith and fair dealing in the exercise of its optional redemption rights for those bonds in connection with CHE's tender offer for those bonds. This lawsuit is similar to an earlier action by the plaintiffs against CHE and Merrill Lynch, Pierce, Fenner & Smith, one of the Corporation's underwriters, that was dismissed in 2013. The present lawsuit was preceded by plaintiff's unsuccessful 2014 request that the Trustee bring an action against CHE on the bonds in question. The Corporation believes that the tender and redemption process was properly conducted. The Corporation's management does not believe that this matter, if decided adversely, would have a material adverse effect on the financial condition of the Corporation. In June 2013, CHE received a notice from the IRS that these transactions were under audit, asking for information. CHE does not believe it has any direct exposure as these bonds are held by Merrill Lynch and is fully cooperating in the investigation.

On March 29, 2013, the CHE was notified that it is a defendant in a lawsuit which challenges the church plan status of the CHE Employee Pension Plan. In response thereto, CHE has filed a motion to dismiss the complaint which is now pending before the United States District Court for the Eastern District of Pennsylvania. At this point, it is not possible to assess the exposure, if any, related to these claims and no amount has been reserved at this time.

The Corporation is involved in other litigation and regulatory investigations arising in the course of doing business. After consultation with legal Counsel, management estimates that these matters will be resolved without material adverse effect on the Corporation's future consolidated financial position or results of operations.

Health Care Regulatory Environment

The health care industry is subject to numerous and complex laws and regulations of federal, state and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, privacy, government health care program participation requirements, government reimbursement for patient services, and fraud and abuse. Compliance with such laws and regulations is complex and can be subject to future government interpretation as well as regulatory enforcement actions, including fines, penalties and exclusion from government health care programs such as Medicare and Medicaid. The Corporation and its RHM's periodically receive notices from governmental agencies requesting information regarding billing, payment, or other reimbursement matters, or notices of the initiation of government investigations. The healthcare industry in general is experiencing an increase in these activities as federal and state governments increase their enforcement activities and institute new programs designed to identify potential irregularities in reimbursement or quality of patient care. Based on the information received to date, management does not believe the ultimate resolution of these matters will have a material adverse effect on the Corporation's future consolidated financial position or results of operations.

10. FAIR VALUE MEASUREMENTS

The Corporation's consolidated financial statements reflect certain assets and liabilities recorded at fair value. Assets and liabilities measured at fair value on a recurring basis in the Corporation's consolidated balance sheet include: cash; cash equivalents; equity securities; debt securities; mutual funds; commingled funds; hedge funds; securities lending collateral; and derivatives. Defined benefit retirement plan assets are measured at fair value on an annual basis. Liabilities measured at fair value on a recurring basis for disclosure only include debt.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value should be based on assumptions that market participants would use, including a consideration of non-performance risk.

To determine fair value, the Corporation uses various valuation methodologies based on market inputs. For many instruments, pricing inputs are readily observable in the market; the valuation methodology is widely accepted by market participants and involves little to no judgment. For other instruments, pricing inputs are less observable in the marketplace. These inputs can be subjective in nature and involve uncertainties and matters of considerable judgment. The use of different assumptions, judgments and/or estimation methodologies may have a material effect on the estimated fair value amounts.

The Corporation assesses the inputs used to measure fair value using a three level hierarchy based on the extent to which inputs used in measuring fair value are observable in the market. The fair value hierarchy is as follows:

Level 1 – Quoted (unadjusted) prices for identical instruments in active markets

Level 2 – Other observable inputs, either directly or indirectly, including:

- Quoted prices for similar instruments in active markets
- Quoted prices for identical or similar instruments in non-active markets (few transactions, limited information, non-current prices, high variability over time, etc.)
- Inputs other than quoted prices that are observable for the instrument (interest rates, yield curves, volatilities, default rates, etc.)

Inputs that are derived principally from or corroborated by other observable market data

Level 3 – Unobservable inputs that cannot be corroborated by observable market data

Valuation Methodologies – Exchange-traded securities whose fair value is derived using quoted prices in active markets are classified as Level 1. In instances where quoted market prices are not readily available, fair value is estimated using quoted market prices and/or other market data for the same or comparable instruments and transactions in establishing the prices, discounted cash flow models and other pricing models. These models are primarily industry-standard models that consider various assumptions, including time value and yield curve as well as other relevant economic measures. The inputs to these models depend on the type of security being priced but are typically benchmark yields, credit spreads, prepayment speeds, reported trades and broker-dealer quotes, all with reasonable levels of transparency. Generally, significant changes in any of those inputs in isolation would result in a significantly different fair value measurement. The Corporation classifies these securities as Level 2 within the fair value hierarchy.

The Corporation maintains policies and procedures to value instruments using the best and most relevant data available. The Corporation's Level 3 securities are primarily investments in hedge funds. The fair values of Level 3 investments in these securities are predominately valued using a net asset value per share, which is provided by third-party administrators; however, in some cases they are obtained directly from the investment fund manager. The Corporation did not adjust the prices obtained. Third-party administrators do not provide access to their proprietary valuation models, inputs, and assumptions. Accordingly, the Corporation reviews the independent reports of internal controls for these service providers. In addition, on a quarterly basis, the Corporation performs reviews of investment consultant

industry peer group benchmarking and supporting relevant market data. Finally, all of the fund managers of the Corporation's Level 3 securities have an annual independent audit performed by an accredited accounting firm. The Corporation reviews these audited financials for ongoing validation of pricing used. Based on the information available, we believe that the fair values provided by the third-party administrators and investment fund managers are representative of prices that would be received to sell the assets at June 30, 2014.

In instances where the inputs used to measure fair value fall into different levels of the fair value hierarchy, the fair value measurement has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Corporation's assessment of the significance of a particular item to the fair value measurement in its entirety requires judgment, including the consideration of inputs specific to the asset.

Following is a description of the valuation methodologies the Corporation used for instruments recorded at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy:

Cash and Cash Equivalents – The carrying amounts reported in the consolidated balance sheet approximate their fair value. Certain cash and cash equivalents are included in investments and assets limited or restricted as to use in the consolidated balance sheet.

Commercial Paper – The fair value of commercial paper is based on amortized cost. Commercial paper is designated as Level 2 investments with significant observable inputs including security cost, maturity and credit rating. Commercial paper is classified as either cash and cash equivalents or marketable securities in the consolidated balance sheet depending upon the length to maturity when purchased and are included in cash and cash equivalents or debt securities in the fair value table.

Security Lending Collateral – The security lending collateral is invested in a Northern Trust sponsored commingled collateral fund, which is comprised primarily of short-term securities. The fair value amounts of the commingled collateral fund are determined using the calculated net asset value per share (or its equivalent) for the fund with the underlying investments valued using techniques similar to those used for marketable securities noted below.

Equity Securities – Equity securities are valued at the closing price reported on the applicable exchange on which the security is traded, or are estimated using quoted market prices for similar securities.

Debt Securities – Debt securities are valued using quoted market prices and/or other market data for the same or comparable instruments and transactions in establishing the prices, discounted cash flow models and other pricing models. These models are primarily industry-standard models that consider various assumptions, including time value and yield curve as well as other relevant economic measures.

Mutual Funds – Mutual funds are valued using the net asset value based on the value of the underlying assets owned by the fund, minus liabilities, divided by the number of shares outstanding, and multiplied by the number of shares owned.

Commingled Funds – Commingled funds are developed for investment by institutional investors only and therefore do not require registration with the Securities and Exchange Commission. Commingled funds are recorded at fair value based on either the underlying investments that have a readily determinable market value or based on net asset value, which is calculated using the most recent fund financial statements. Commingled funds are categorized as Level 2 unless they have a redemption restriction greater than 95 days, in which case they are categorized as Level 3.

Hedge Funds – The Corporation invests in various hedge fund strategies. These funds utilize either a direct or a “fund-of-funds” approach resulting in diversified multi-strategy, multi-manager investments. Underlying investments in these funds may include equities, fixed income securities, commodities, currencies and derivatives. These funds are valued at net asset value, which is calculated using the most recent fund financial statements. Hedge funds are categorized as Level 2 unless they have a redemption restriction greater than 95 days, in which case they are categorized as Level 3.

The Corporation classifies its equity and debt securities, mutual funds, commingled funds and hedge funds as trading securities. The amount of holding gains for fiscal year 2014 included in the excess of revenue over expenses related to securities still held at June 30, 2014 were \$471.6 million.

Equity Method Investments – The Corporation accounts for certain other investments using the equity method. These investments are structured as limited liability corporations and partnerships and are designed to produce stable investment returns regardless of market activity. These investments utilize a combination of “fund-of-funds” and direct fund investment strategies resulting in a diversified multi-strategy, multi-manager investments approach. Some of these funds are developed by investment managers specifically for the Corporation’s use and are similar to mutual funds, but are not traded on a public exchange. Underlying investments in these funds may include other funds, equities, fixed income securities, commodities, currencies and derivatives. Audited information is only available annually based on the limited liability corporations, partnerships or funds’ year-end. Management’s estimates of the fair values of these investments are based on information provided by the third-party administrators and fund managers or the general partners. Management obtains and considers the audited financial statements of these investments when evaluating the overall reasonableness of the recorded value. In addition to a review of external information provided, management’s internal procedures include such things as review of returns against benchmarks and discussions with fund managers on performance, changes in personnel or process, along with evaluations of current market conditions for these investments. Investment managers meet with the Corporation’s Investment Subcommittee of the Finance and Stewardship Committee of the Board of Directors on a periodic basis. Because of the inherent uncertainty of valuations, values may differ materially from the values that would have been used had a ready market existed. The balance of these investments at June 30, 2014 was \$1,416 million. Unfunded capital commitments related to equity method investments totaled \$75.9 million at June 30, 2014.

Cash and cash equivalents, equity and debt securities, mutual funds, commingled funds, hedge funds, and equity method investments totaled \$8,427 million at June 30, 2014.

Interest Rate Swaps – The fair value of the Corporation’s derivatives, which are mainly interest rate swaps, are estimated utilizing the terms of the swaps and publicly available market yield curves along with the Corporation’s nonperformance risk as observed through the credit default swap market and bond market and based on prices for recent trades. These swap agreements are classified as Level 2 within the fair value hierarchy.

The following table presents information about the fair value of the Corporation's financial instruments measured at fair value on a recurring basis and recorded at June 30, 2014 (in thousands):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Assets:				
Cash and cash equivalents	\$ 1,585,907	\$ 38,630	\$ -	\$ 1,624,537
Security lending collateral	-	187,882	-	187,882
Equity securities	988,848	5,674	972	995,494
Debt securities:				
Government and government agency obligations	-	445,517	1,529	447,046
Corporate bonds	-	350,744	583	351,327
Asset backed securities	-	81,376	100	81,476
Bank loans	-	64,126	-	64,126
Other	-	10,599	-	10,599
Mutual funds:				
Equity mutual funds	847,924	-	-	847,924
Fixed income mutual funds	596,739	-	-	596,739
Real estate investment funds	10,682	-	-	10,682
Other	16,384	-	-	16,384
Commingled funds	-	774,926	-	774,926
Hedge funds	-	657,781	344,544	1,002,325
Interest rate swaps	-	32,258	-	32,258
Total assets	<u>\$ 4,046,484</u>	<u>\$ 2,649,513</u>	<u>\$ 347,728</u>	<u>\$ 7,043,725</u>
Liabilities:				
Interest rate swaps	<u>\$ -</u>	<u>\$ 148,885</u>	<u>\$ -</u>	<u>\$ 148,885</u>

The Corporation's policy is to recognize transfers between all levels as of the beginning of the reporting period. There were no significant transfers to or from Levels 1 and 2 during the year ended June 30, 2014.

The following table summarizes the changes in Level 3 assets for the year ended June 30, 2014 (in thousands):

	Equity Securities	Government and Government Agency Obligations	Corporate Bonds	Asset Backed Securities	Hedge Funds	Total
Balance at July 1, 2013	<u>\$ 1,449</u>	<u>\$ -</u>	<u>\$ 2,886</u>	<u>\$ -</u>	<u>\$ 376,807</u>	<u>\$ 381,142</u>
Realized gain	-	(2)	(99)	-	2,287	2,186
Unrealized (loss) gain	-	(609)	(96)	-	30,197	29,492
Purchases	-	2,140	1,230	100	14,170	17,640
Settlements	(3)	-	(4,638)	-	(17,243)	(21,884)
Transfers (to) from Level 2	(474)	-	1,300	-	(61,674)	(60,848)
Balance at June 30, 2014	<u>\$ 972</u>	<u>\$ 1,529</u>	<u>\$ 583</u>	<u>\$ 100</u>	<u>\$ 344,544</u>	<u>\$ 347,728</u>

Investments in Entities that Calculate Net Asset Value per Share – The Corporation holds shares or interests in investment companies at year-end, included in commingled funds and hedge funds, where the fair value of the investment held is estimated based on the net asset value per share (or its equivalent) of the investment company. There were no unfunded commitments as of June 30, 2014. The fair value and redemption rules of these investments are as follows as of June 30, 2014 (in thousands):

	<u>Fair Value</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>
Commingled funds	\$ 774,926	Daily - Monthly	0 - 60 days
Hedge funds	1,002,325	Monthly, quarterly, semi-annually	30 - 95 days
Total	<u>\$ 1,777,251</u>		

The hedge fund category includes equity long/short hedge funds, multi-strategy hedge funds and relative value hedge funds. Equity long/short hedge funds invest both long and short, primarily in U.S. common stocks. Management of the fund has the ability to shift investments from value to growth strategies, from small to large capitalization stocks, and from a net long position to a net short position. Multi-strategy hedge funds pursue multiple strategies to diversify risks and reduce volatility. Relative value hedge fund's strategy is to exploit structural and technical inefficiencies in the market by investing in financial instruments that are perceived to be inefficiently priced as a result of business, financial or legal uncertainties. Investments representing approximately 6.1% of the value of the investments in this category can only be redeemed bi-annually subsequent to the initial investment date. Investment representing 18.4% of the investments in this category can only be redeemed at the rate of 25% per quarter.

The commingled fund category primarily includes investments in funds that invest in financial instruments of U.S. and non-U.S. entities, primarily bonds, notes, bills, debentures, currencies, and interest rate and derivative products.

The composition of investment returns included in the consolidated statement of operations and changes in net assets for the year ended June 30, 2014 is as follows (in thousands):

Dividend, interest income and other	\$ 130,961
Realized gain, net	196,727
Realized equity gain, other investments	24,528
Change in net unrealized gain on investments	<u>350,532</u>
Total investment return	<u>\$ 702,748</u>
Included in:	
Operating income	\$ 75,123
Nonoperating items	609,010
Changes in restricted net assets	<u>18,615</u>
Total investment return	<u>\$ 702,748</u>

In addition to investments, assets restricted as to use include receivables for unconditional promises to give cash and other assets net of allowances for uncollectible promises to give. Unconditional promises to give consist of the following at June 30, 2014 (in thousands):

Amounts expected to be collected in:	
Less than one year	\$ 24,359
One to five years	34,761
More than five years	<u>5,840</u>
	64,960
Discount to present value of future cash flows	(2,819)
Allowance for uncollectible amounts	<u>(6,030)</u>
Total unconditional promises to give, net	<u><u>\$ 56,111</u></u>

Patient Accounts Receivable, Estimated Receivables from Third-Party Payors and Current Liabilities

– The carrying amounts reported in the consolidated balance sheet approximate their fair value.

Long-Term Debt – The carrying amounts of the Corporation’s variable rate debt approximate their fair values. The fair value of the Corporation’s fixed rate long-term debt is estimated using discounted cash flow analyses, based on current incremental borrowing rates for similar types of borrowing arrangements. The fair value of the fixed rate long-term revenue and refunding bonds was \$3,195 million at June 30, 2014. Under the fair value hierarchy, these financial instruments are valued primarily using Level 2 inputs. The related carrying value of the fixed rate long-term revenue and refunding bonds was \$2,923 million at June 30, 2014. The fair values of the remaining fixed rate capital leases, notes payable to banks, and mortgage loans are not materially different from their carrying values.

11. DERIVATIVE FINANCIAL INSTRUMENTS

Derivative Financial Instruments – In the normal course of business, the Corporation is exposed to market risks, including the effect of changes in interest rates and equity market volatility. To manage these risks the Corporation enters into various derivative contracts, primarily interest rate swaps. Interest rate swaps are used to manage the effect of interest rate fluctuations.

Management reviews the Corporation’s hedging program, derivative position, and overall risk management on a regular basis. The Corporation only enters into transactions it believes will be highly effective at offsetting the underlying risk.

Interest Rate Swaps – The Corporation utilizes interest rate swaps to manage interest rate risk related to the Corporation’s variable interest rate debt, variable rate leases and a fixed income investment portfolio. Cash payments on interest rate swaps totaled \$15.6 million for the year ended June 30, 2014 and are included in nonoperating income.

Certain of the Corporation’s interest rate swaps contain provisions that give certain counterparties the right to terminate the interest rate swap if a rating is downgraded below specified thresholds. If a ratings downgrade threshold is breached, the counterparties to the derivative instruments could demand immediate termination of the swaps. Such termination could result in a payment from the Corporation or a payment to the Corporation depending on the market value of the interest rate swap.

Effect of Derivative Instruments on Excess of Revenue over Expenses – The following table represents the effect derivative instruments had on the Corporation’s financial performance for the year ended June 30, 2014 (in thousands):

Derivatives Not Designated as Hedging Instruments	Location of Net Gain (Loss) Recognized in Excess of Revenue over Expenses or Unrestricted Net Assets	Amount of Net Gain (Loss) Recognized in Excess of Revenue over Expenses
Excess of Revenue over Expenses:		
Interest rate swaps	Change in market value and cash payment on interest rate swaps	\$ (25,514)
Interest rate swaps	Investment income	(593)
		<u>\$ (26,107)</u>

Balance Sheet Effect of Derivative Instruments - The following table summarizes the estimated fair value of the Corporation’s derivative financial instruments at June 30, 2014 (in thousands):

Derivatives Not Designated as Hedging Instruments	Consolidated Balance Sheet Location	Fair Value
Asset Derivatives:		
Interest rate swaps	Investments	\$ 5,855
Interest rate swaps	Other assets	26,403
Total asset derivatives		<u>\$ 32,258</u>
Liability Derivatives:		
Interest rate swaps	Other long-term liabilities	<u>\$ 148,885</u>

The counterparties to the interest rate swaps expose the Corporation to credit loss in the event of non-performance. At June 30, 2014, an adjustment for non-performance risk reduced derivative assets by \$1.0 million and derivatives liabilities by \$11.2 million.

12. TEMPORARILY AND PERMANENTLY RESTRICTED NET ASSETS

Temporarily restricted net assets are those whose use by the Corporation has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained in perpetuity. Temporarily restricted net assets and permanently restricted net assets at June 30, 2014 are available for the following purposes (in thousands):

Temporarily Restricted Net Assets:	
Education and research	\$ 20,252
Building and equipment	103,683
Patient care	47,712
Cancer Center/research	14,753
Services for elderly care	33,767
Other	73,139
Total	<u>\$ 293,306</u>
 Permanently Restricted Net Assets:	
Hospital operations	\$ 25,844
Medical programs	7,465
Scholarship funds	5,033
Research funds	9,787
Community service funds	14,211
Other	24,723
Total	<u>\$ 87,063</u>

The Corporation's endowments consist of funds established for a variety of purposes. Endowments include both donor-restricted endowment funds and funds designated by the Board to function as endowments. Net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions. The Corporation considers various factors in making a determination to appropriate or accumulate donor-restricted endowment funds.

The Corporation employs a total return investment approach whereby a mix of equities and fixed income investments are used to maximize the long-term return of endowment funds for a prudent level of risk. The Corporation targets a diversified asset allocation to achieve its long-term return objectives within prudent risk constraints. The Corporation can appropriate each year all available earnings in accordance with donor restrictions. The endowment corpus is to be maintained in perpetuity. Certain donor-restricted endowments require a portion of annual earnings to be maintained in perpetuity along with the corpus. Only amounts exceeding the amounts required to be maintained in perpetuity are expended.

The following table summarizes net asset composition by type of fund at June 30, 2014 (in thousands):

	Unrestricted Net Assets	Temporarily Restricted Net Assets	Permanently Restricted Net Assets	Total
Donor-restricted endowment funds	\$ -	\$ 36,340	\$ 87,063	\$ 123,403
Board-designated endowment funds	90,942	-	-	90,942
Total endowment funds	<u>\$ 90,942</u>	<u>\$ 36,340</u>	<u>\$ 87,063</u>	<u>\$ 214,345</u>

Changes in endowment net assets for the year ended June 30, 2014 include (in thousands):

	Unrestricted Net Assets	Temporarily Restricted Net Assets	Permanently Restricted Net Assets	Total
Endowment net assets, July 1, 2013	\$ 78,848	\$ 31,598	\$ 92,678	\$ 203,124
Investment return:				
Investment gain	5,522	4,235	1,238	10,995
Change in net realized and unrealized gains	5,200	1,557	1,620	8,377
Total investment return	10,722	5,792	2,858	19,372
Contributions	38	131	3,621	3,790
Transfer to create a board designated endowment	1,161	-	-	1,161
Appropriation of endowment assets for expenditures	(5,601)	(1,606)	-	(7,207)
Other	5,774	425	(12,094)	(5,895)
Endowment net assets, June 30, 2014	<u>\$ 90,942</u>	<u>\$ 36,340</u>	<u>\$ 87,063</u>	<u>\$ 214,345</u>

The table below describes the restrictions for endowment amounts classified as temporarily restricted net assets and permanently restricted net assets as of June 30, 2014 (in thousands):

Temporarily Restricted Net Assets:

Term endowment funds	\$ 4,783
The portion of perpetual endowment funds subject a purpose restriction	31,557
Total endowment funds classified as temporarily restricted net assets	<u>\$ 36,340</u>

Permanently Restricted Net Assets:

Investment to be held in perpetuity, the income from which is expendable to support health care services	\$ 62,912
Endowments requiring income to be added to the original gift	13,939
Other	10,212
Total	<u>\$ 87,063</u>

Funds with Deficiencies – Periodically the fair value of assets associated with the individual donor-restricted endowment funds may fall below the level that the donor requires the Corporation to retain as a fund of perpetual duration. Deficiencies of this nature are reported in unrestricted net assets. These deficiencies result from unfavorable market fluctuations and/or continued appropriation for certain programs that was deemed prudent by the Corporation.

13. RESTRUCTURING CHARGES

During fiscal year 2014, management authorized and committed the Corporation to undertake a comprehensive performance improvement plan to realign its cost structure. The Corporation had a workforce reduction as part of the plan. As a result of these actions, restructuring charges of \$46 million have been included in the consolidated statement of operations and changes in net assets. The restructuring charges are primarily for severance and termination benefits. As of June 30, 2014, \$15 million in benefits have been paid.

14. SUBSEQUENT EVENTS

Management has evaluated subsequent events through March 19, 2015 the date the consolidated financial statements were issued. The following subsequent events were noted:

Merger of Entities – CHE Trinity Inc., CHE and Trinity Health were merged into one legal corporation, with Trinity Health being the surviving legal corporation on July 1, 2014.

Consolidation of Siouxland Surgery Center, LLP ("Siouxland") – Effective July 1, 2014, a joint venture was created between Mercy Health Services – Iowa, Corp. ("Mercy") and USP Health Ventures, LLC ("USP"), (collectively, "Mercy/USP"). Mercy owns a controlling interest of 55.71% and USP owns the remaining 44.29% interest of the joint venture. Mercy/USP then entered into a Securities Purchase Agreement with SSC Physician Investors, LLC ("Physician Investors"), whereby Mercy contributed 30.9% of their pre-existing ownership of Siouxland and USP contributed their newly acquired 24.6% ownership of Siouxland, resulting in Mercy/USP owning a controlling interest of 55.54% of Siouxland with the remaining 44.46% interest owned by Physician Investors. As a result of the transaction, Mercy reported a gain of \$40.3 million in the consolidated statement of operations and changes in net assets in July, 2014. Siouxland operates a surgical specialty hospital and medical facility in Dakota Dunes, South Dakota and has operating revenue of \$64 million annually. Summarized consolidated balance sheet information for Mercy/USP as of July 1, 2014 is as follows (in thousands):

Cash	\$ 4,178	Accounts payable and accrued expenses	\$ 9,409
Patient accounts receivable	11,191	Current portion of long-term debt	1,031
Other current assets	3,539	Long-term debt, net of current portion	12,075
Property and equipment	24,133	Total liabilities acquired	<u>\$ 22,515</u>
Goodwill	134,947		
Other assets	799	Unrestricted net assets	\$ 57,265
Total assets acquired	<u>\$ 178,787</u>	Unrestricted noncontrolling interest	99,007
		Total net assets	<u>\$ 156,272</u>

Litigation – On July 17, 2014, Trinity Health Corporation (now CHE Trinity Inc.) was notified that it is a defendant in a lawsuit filed in the United States District Court District of Maryland that challenges the church plan status of the Trinity Health Employee Pension Plan. This is similar to other purported class action cases that have been brought against large Catholic health care systems, including one making similar allegations with respect to the Catholic Health East employee pension plan. This is one of ten such challenges filed against Catholic health systems across the country. At this point, it is not possible to assess the exposure, if any, related to these claims and CHE Trinity Inc. has not reserved any amounts at this time related to either the

existing challenge with respect to the Catholic Health East employee pension plan or the recently filed lawsuit against Trinity Health Corporation.

Saint Francis Care ("SFC") - On December 17, 2014, the Corporation entered into a Definitive Agreement to become the sole corporate member of SFC, an integrated healthcare delivery system located in Hartford, Connecticut and the largest Catholic healthcare provider in New England with \$785 million of revenue reported for the fiscal year ended September 30, 2014. As part of the transaction, an investment of \$275 million in capital has been committed over a five year period by the Corporation. The transaction is subject to approval by the State of Connecticut.

Long-term Debt and Other Financing Arrangements:

Issuance of Commercial Paper – Between November 2014 and January 2015, the Corporation issued \$120 million of commercial paper, a portion of which was paid off as described below.

Issuance of Debt – During February and March 2015, the Credit Group issued \$1,013 million in tax-exempt fixed rate hospital revenue bonds, and \$100 million in tax-exempt variable rate hospital revenue bonds under the ARMI. Proceeds were used to retire \$548 million of then outstanding fixed rate hospital revenue bonds and \$260 million of then outstanding taxable commercial paper obligations. \$544 million of the bonds were advance refunded through net defeasance. The remaining \$4 million balance was currently refunded. The Corporation advance refunded the bonds by depositing funds in trustee-held escrow accounts exclusively for the payment of principal and interest. The trustees/escrow agents are solely responsible for the subsequent extinguishment of the bonds. The trustee held escrow accounts are invested in U.S. government securities. The remaining proceeds will be used to finance, refinance and reimburse a portion of the costs of acquisition, construction, renovation and equipping of health facilities, and to pay related costs of issuance. These transactions resulted in a loss from extinguishment of debt of \$95.5 million. During March 2015, the Credit Group issued \$350 million in taxable fixed rate hospital revenue bonds under the ARMI. Proceeds will be used to finance corporate purposes of the Corporation and its affiliates.

CHE TRINITY INC.

CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014

Federal Agency/Regional Health Ministry	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
RESEARCH AND DEVELOPMENT CLUSTER PROGRAMS:					
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES:					
<u>National Institutes of Health (NIH) Programs</u>					
Saint Alphonsus Regional Medical Center, Boise	Medical Library Assistance	93.879	Duke University	203-1070	\$ 35,090
Mount Carmel Health System, Columbus	Medical Library Assistance	93.879	University of Illinois at Chicago	HHSN-276-2011-00005C	4,357
Mount Carmel Health System, Columbus	Child Health and Human Development Extramural Research	93.865	The Ohio State University Research Foundation	60021133	2,904
Saint Joseph Mercy Health System, Michigan Heart, Ann Arbor	Extramural Research Programs in the Neurosciences and Neurological Disorders	93.853	University Medical Dentistry New Jersey	R01NS038384	8,400
St. Francis Medical Center, Trenton	Extramural Research Programs in the Neurosciences and Neurological Disorders	93.853	University of Maryland	1 U01 NS069208	35,817
Saint Joseph Mercy Health System, Michigan Heart, Ann Arbor	Diabetes, Digestive, and Kidney Diseases Extramural Research	93.847	University of Colorado Denver	7R18DK082377-05	19,204
Saint Joseph Mercy Health System, Michigan Heart, Ann Arbor	Arthritis, Musculoskeletal and Skin Diseases Research	93.846	University of North Carolina at Chapel Hill	5R01AR060852-03	18,245
Saint Joseph Mercy Health System, Michigan Heart, Ann Arbor	Cardiovascular Diseases Research	93.837	University of Rochester	U01 HL096607	15,077
Saint Alphonsus Regional Medical Center, Boise	Cardiovascular Diseases Research	93.837	Yale University	1R01HL115295-01	800
Saint Alphonsus Regional Medical Center, Boise	Cardiovascular Diseases Research	93.837	Brigham & Womens Hospital Inc	5U01HL101422	2,000
Saint Joseph Mercy Health System, Michigan Heart, Ann Arbor	Cardiovascular Diseases Research	93.837	New York University	1U01HL105907	11,020
Saint Joseph Mercy Health System, Michigan Heart, Ann Arbor	Cardiovascular Diseases Research	93.837	Partners, NHLBI	5R01HL091069	3,350
Mount Carmel Health System, Columbus	Cardiovascular Diseases Research	93.837	Brigham and Women's Hospital, Inc.	5U01HL101422	16,129
Saint Joseph Mercy Health System, Michigan Heart, Ann Arbor	Trans-NIH Recovery Act Research Support	93.701	Duke Corporation	R01HL098237	8,900
Mercy Medical Center-North Iowa, Mason City	Cancer Control	93.399	Iowa Oncology Research Association	5U10-CA035101-19	79,940
Saint Joseph Mercy Health System, Michigan Heart, Ann Arbor	Cancer Control	93.399	N/A	2U10-CA063848-20	1,536,231
Saint Joseph Mercy Health System, Michigan Heart, Ann Arbor	Cancer Control	93.399	N/A	U10-CA37377	60,100
Mercy Medical Center-North Iowa, Mason City	Cancer Treatment Research	93.395	Iowa Oncology Research Association	N/A	1,105
Saint Agnes Medical Center, Fresno	Cancer Treatment Research	93.395	Radiation Therapy Oncology Group	U10CA21661	3,039

(Continued)

CHE TRINITY INC.

CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014

Federal Agency/Regional Health Ministry	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
<u>National Institutes of Health (NIH) Programs (Continued)</u>					
St. Mary Mercy Hospital, Livonia	Cancer Treatment Research	93.395	Oregon Health & Science University	U10 CA032102	11,215
Mount Carmel Health System, Columbus	Cancer Cause and Prevention Research	93.393	Case Western Reserve University	RES507632	600
Saint Joseph Mercy Health System, Ann Arbor	National Center for Advancing Translational Sciences	93.350	University of North Carolina at Chapel Hill	8KL2TR00084-05	5,100
	Subtotal National Institutes of Health Programs				1,878,623
<u>Centers for Medicare and Medicaid Services</u>					
Saint Alphonsus Regional Medical Center, Boise	Prevention and Public Health Fund 2013 - Cooperative Agreement to Support Navigators in Federally-facilitated and State Partnership Exchanges	93.750	SAMG Federal Way Clinic	82020089569	67,250
<u>Agency for Healthcare Research and Quality</u>					
Saint Alphonsus Regional Medical Center, Boise	Research on Healthcare Costs, Quality and Outcomes	93.226	N/A	1R03HS021786-01	62,218
	Subtotal Agency for Healthcare Research and Quality				62,218
	Subtotal U.S. Department of Health and Human Services (Research)				2,008,091
U.S. DEPARTMENT OF DEFENSE:					
Saint Alphonsus Regional Medical Center, Boise	Military Medical Research and Development	12.420	N/A	W81XWH-07-2-0077	1,725
	Subtotal U.S. Department of Defense				1,725
	Total Research and Development Cluster Programs				2,009,816
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES (NON-RESEARCH):					
St. Joseph Mercy Oakland, Pontiac	Maternal and Child Health Services Block Grant to the States	93.994	State of Michigan	B04MC11171	7,494
Saint Joseph Regional Medical Center, South Bend	Maternal and Child Health Services Block Grant to the States	93.994	State of Indiana	6 B04 MC 00292-06	62,949
Muskegon Community Health Project, Muskegon	Preventive Health and Health Services Block Grant	93.991	MDCH	20140232	31,113
Samaritan Hospital, Albany	Preventive Health and Health Services Block Grant	93.991	NYS Department of Health	C026634	1,419
Hackley Life Counseling, Muskegon	Block Grants for Prevention and Treatment of Substance Abuse	93.959	Lakeshore Coordinating Council	N/A	212,134
Sisters of Providence Health System, Springfield	Block Grants for Prevention and Treatment of Substance Abuse	93.959	Commonwealth of Massachusetts Department of Public Health	SCDPH231853620180000	24,274
Sisters of Providence Health System, Springfield	Block Grants for Prevention and Treatment of Substance Abuse	93.959	Commonwealth of Massachusetts Department of Public Health	INTF2303MM3900617065	11,644
Sisters of Providence Health System, Springfield	Block Grants for Prevention and Treatment of Substance Abuse	93.959	Commonwealth of Massachusetts Department of Public Health	SCDPH230153581390000	18,621
Sisters of Providence Health System, Springfield	Block Grants for Prevention and Treatment of Substance Abuse	93.959	Commonwealth of Massachusetts Department of Public Health	2862861THEMERCYHAJS	7,022

(Continued)

CHE TRINITY INC.

**CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014**

Federal Agency/Regional Health Ministry U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES (NON-RESEARCH): (Continued)	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
Sisters of Providence Health System, Springfield	Block Grants for Prevention and Treatment of Substance Abuse	93.959	Commonwealth of Massachusetts Department of Public Health	INTF2324MM320042003	2,334
Pittsburgh Mercy Health System, Pittsburgh	Block Grants for Prevention and Treatment of Substance Abuse	93.959	PA Department of Health Bureau of Drug and Alcohol	153963	328,875
Mercy Health Partners, Hackley Campus, McClees Clinic	HIV Prevention Activities Health Department Based	93.94	Michigan Department of Community Health	U62 PS003671	108,000
Holy Cross Hospital, Ft. Lauderdale	HIV Prevention Activities Health Department Based	93.940	State of Florida	BW275	50,000
Holy Cross Hospital, Ft. Lauderdale	HIV Prevention Activities Health Department Based	93.940	State of Florida	BW275	50,000
Saint Josephs Health System, Atlanta	HIV Prevention Activities Health Department Based	93.940	Fulton County Health and Wellness	1U62PS003679	5,491
Saint Joseph's Health System, Atlanta	HIV Prevention Activities Non-Governmental Organization Based	93.939	N/A	5U65 PS002210	308,675
Saint Joseph's Health System, Atlanta	Cooperative Agreements for State-Based Comprehensive Breast and Cervical Cancer Early Detection Programs	93.919	State of Georgia Department of Human Services	N/A	123,575
Saint Mary's Health Care, Grand Rapids	Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	93.918	N/A	N/A	449,929
Saint Joseph's Health System, Atlanta	Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	93.918	N/A	6H76HA00090-21	721,779
St. Francis Medical Center, Trenton	Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	93.918	N/A	H76HA23468	245,558
Saint Mary's Health Care, Grand Rapids	HIV Care Formula Grants	93.917	Michigan Department of Community Health	X07HA00044	354,564
Mercy Health Partners, Hackley Campus, McClees Clinic	HIV Care Formula Grants	93.917	Michigan Department of Community Health	20141554-00	236,484
St. Francis Medical Center, Trenton	HIV Care Formula Grants	93.917	New Jersey Department of Health & Senior Services	AIDS13RWB004	53,316
Loyola University Health System, Chicago	HIV Emergency Relief Project Grants	93.914	The City of Chicago Department of Public Health	23782-3, 23782-4	332,702
Saint Joseph's Health System, Atlanta	HIV Emergency Relief Project Grants	93.914	Fulton County Board of Commissioners	PC-118-13SC88878-B-TR	508,659
Saint Josephs Health System, Atlanta	HIV Emergency Relief Project Grants	93.914	Fulton County Board of Commissioners	PC-118-14SC93991B-TR	117,275
Mount Carmel Health System, Columbus	National Bioterrorism Hospital Preparedness Program	93.889	Ohio Department of Health	02560112RP0512	72,962
Holy Cross Hospital, Silver Spring	National Bioterrorism Hospital Preparedness Program	93.889	Maryland Department of Health & Mental Hygiene	N/A	34,957

(Continued)

CHE TRINITY INC.

**CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014**

Federal Agency/Regional Health Ministry U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES (NON-RESEARCH): (Continued)	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
Saint Joseph Mercy Health System, Ann Arbor	National Bioterrorism Hospital Preparedness Program	93.889	Region 2 South DP. Def. Network	N/A	8,478
Saint Joseph Mercy Health System, Saline	National Bioterrorism Hospital Preparedness Program	93.889	Region 2 South DP. Def. Network	N/A	3,950
Saint Joseph Mercy Health System, Livonia	National Bioterrorism Hospital Preparedness Program	93.889	Region 2 South DP. Def. Network	N/A	1,259
Saint Joseph Regional Medical Center, South Bend	National Bioterrorism Hospital Preparedness Program	93.889	State of Indiana	N/A	41,251
Saint Joseph Regional Medical Center, Plymouth	National Bioterrorism Hospital Preparedness Program	93.889	State of Indiana	N/A	73,088
Mount Carmel Health System, Columbus	National Bioterrorism Hospital Preparedness Program	93.889	Ohio Department of Health	02560112RP0512	7,497
Mercy Medical Center, Dubuque	National Bioterrorism Hospital Preparedness Program	93.889	Black Hawk County Health Department	5883BHP109	3,505
Mercy Medical Center, Dubuque	National Bioterrorism Hospital Preparedness Program	93.889	Black Hawk County Health Department	5883BHP108	5,658
Mercy Medical Center, Clinton	National Bioterrorism Hospital Preparedness Program	93.889	Iowa Department of Public Health	5883BHP110	6,230
Mercy Medical Center, Clinton	National Bioterrorism Hospital Preparedness Program	93.889	Iowa Department of Public Health	5884BT70	20,564
Loyola University Health System, Chicago	National Bioterrorism Hospital Preparedness Program	93.889	Illinois Department of Public Health	47281061B	339,080
Loyola University Health System, Chicago	National Bioterrorism Hospital Preparedness Program	93.889	Illinois Department of Public Health	47281038	9,519
Saint Alphonsus Medical Center, Nampa	National Bioterrorism Hospital Preparedness Program	93.889	Idaho Healthcare System	820200896-03	35,904
Mercy Medical Center, Sioux City	National Bioterrorism Hospital Preparedness Program	93.889	State of Iowa	5883BHP39	3,472
Mercy Medical Center, Sioux City	National Bioterrorism Hospital Preparedness Program	93.889	State of Iowa	5883BHP50	21,251
Saint Alphonsus Regional Medical Center, Boise	National Bioterrorism Hospital Preparedness Program	93.889	Oregon Health Authority	-	5,707
Holy Cross Hospital, Ft. Lauderdale	National Bioterrorism Hospital Preparedness Program	93.889	State of Florida Department of Health	COP 2S-R2	41,271
St. Francis Medical Center, Trenton	Health Care and Other Facilities	93.887	N/A	C76HF19935	271,730
Hackley Life Counseling, Muskegon	Children's Health Insurance Program	93.767	Lakeshore Coordinating Counsel	N/A	220
Pittsburgh Mercy Health System, Pittsburgh	Social Services Block Grant	93.667	PA Department of Human Services	153963	161,521
Pittsburgh Mercy Health System, Pittsburgh	Foster Care Title IV-E	93.658	PA Department of Human Services	153963	255,362
Hackley Life Counseling, Muskegon	Health Care Innovation Awards	93.610	N/A	A-12007-115-504201	1,415,966
Holy Cross Hospital, Ft. Lauderdale	Community Transformation Grant	93.531	Broward Regional Health Planing Council	U558DP003661-01	88,249

(Continued)

CHE TRINITY INC.

**CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014**

Federal Agency/Regional Health Ministry U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES (NON-RESEARCH): (Continued)	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
Holy Cross Hospital, Ft. Lauderdale	Community Transformation Grant	93.531	Broward Regional Health Planing Council	U558DP003661-01	41,922
St. Peter's Health Partners, Albany	Affordable Care Act Grants for School-Based Health Center Capital Expenditures	93.501	N/A	N/A	21,859
Mercy Medical Center, New Hampton	Small Rural Hospital Improvement Grant Program	93.301	Iowa Department of Health	5884SH49	7,416
Mercy Hospital, Grayling	Small Rural Hospital Improvement Grant Program	93.301	State of Michigan Office of Rural Health	6H3HRH000400101	3,799
Baum Harmon Mercy Hospital, Primghar	Small Rural Hospital Improvement Grant Program	93.301	State of Iowa	5883SH05	260
Baum Harmon Mercy Hospital, Primghar	Small Rural Hospital Improvement Grant Program	93.301	State of Iowa	5884SH05	5,855
Oakland Mercy Hospital	Small Rural Hospital Improvement Grant Program	93.301	Nebraska Hospital Association	19451-Y3	3,660
Saint Joseph Mercy Health System, Ann Arbor	Centers for Disease Control and Prevention Investigations and Technical Assistance	93.283	Michigan Department of Community Health	IU58DP00379801	7,500
Saint Joseph Mercy Health System, Ann Arbor	Centers for Disease Control and Prevention Investigations and Technical Assistance	93.283	Michigan Department of Community Health	5U58DP0020 22 (12)	14,916
Saint Alphonsus Regional Medical Center, Boise	Centers for Disease Control and Prevention Investigations and Technical Assistance	93.283	N/A	HC539300	32,658
St. James Mercy Hospital, Hornell	Centers for Disease Control and Prevention Investigations and Technical Assistance	93.283	N/A	4701-01	34,574
St. Peter's Health Partners, Albany	Centers for Disease Control and Prevention Investigations and Technical Assistance	93.283	Health Research, Inc.	4707-01	114,641
Muskegon Community Health Project, Muskegon	Drug-Free Communities Support Program Grants	93.276	U.S. Department of Health and Human Services Substance Abuse and Mental Health Services Administration	5H79SP013090-08 REVISED	120,049
Saint Joseph Mercy Health System, Chelsea	Drug-Free Communities Support Program Grants	93.276	N/A	1H79SP018182-01	103,887
Saint Joseph Mercy Health System, Chelsea	Drug-Free Communities Support Program Grants	93.276	N/A	1H79SP020148-01	53,738
Muskegon Community Health Project, Muskegon	Substance Abuse and Mental Health Services Projects of Regional and National Significance	93.243	Lakeshore Coordinating Counsel	IU79SP019440-01	76,739
Pittsburgh Mercy Health System, Pittsburgh	Substance Abuse and Mental Health Services Projects of Regional and National Significance	93.243	N/A	N/A	347,037
St. Peter's Health Partners, Albany	Substance Abuse and Mental Health Services Projects of Regional and National Significance	93.243	St. Catherine's Center for Children	1H79T1021451-01	53,265

(Continued)

CHE TRINITY INC.

CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014

Federal Agency/Regional Health Ministry U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES (NON-RESEARCH): (Continued)	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
Oakland Mercy Hospital	State Rural Hospital Flexibility Program	93.241	Nebraska Department of Health & Human Services	20383-Y3	4,250
Saint Alphonsus Regional Medical Center, Boise	Telehealth Programs	93.211	N/A	H2AIT16611	27,601
Pittsburgh Mercy Health System, Pittsburgh	Projects for Assistance in Transition from Homelessness	93.150	PA Department of Human Services	153963	114,104
St. Peter's Health Partners, Albany	Injury Prevention and Control Research and State and Community Based Programs	93.136	NYS Department of Health	C026634	24,833
Our Lady of Lourdes Health Care Services, Camden	Nurse Anesthetist Traineeship	93.124	N/A	A22HP26002-01-01	11,791
Mercy Medical Center, Sioux City	Hospital Preparedness Program (HPP) and Public Health Emergency Preparedness (PHEP) Aligned Cooperative Agreements	93.074	Woodbury Coalition	5884BT63	10,003
Baum Harmon Mercy Hospital, Primghar	HPP and PHEP Aligned Cooperative Agreements	93.074	O'Brien County	5884BT76	16,110
Mercy Medical Center, Dubuque	HPP and PHEP Aligned Cooperative Agreements	93.074	Iowa Department of Public Health	5884BHP303	6,000
Mercy Medical Center, Dubuque	HPP and PHEP Aligned Cooperative Agreements	93.074	Black Hawk County Health Department	5884BT22	16,537
St. Peter's Health Partners, Albany	HPP and PHEP Aligned Cooperative Agreements	93.074	Health Research, Inc.	1864-09	40,000
St. Peter's Health Partners, Albany	HPP and PHEP Aligned Cooperative Agreements	93.074	Health Research, Inc.	1955-10	21,897
Seton Health System	HPP and PHEP Aligned Cooperative Agreements	93.074	Health Research, Inc	1866-09	35,000
Albany Memorial Hospital, Albany	HPP and PHEP Aligned Cooperative Agreements	93.074	Health Research, Inc	1953-10	24,000
Mercy Hospital, Grayling	Public Health Emergency Preparedness	93.069	N/A	CDC-RFA-TP09-902-H1N109	15,238
Saint Joseph's Health System, Atlanta	National Family Caregiver Support, Title III, Part E	93.052	Northwest Georgia Regional Commission	42700-373-0000012721	144,808
St. Francis Medical Center, Trenton	National Family Caregiver Support, Title III, Part E	93.052	New Jersey Department of Health & Senior Services	1150-13	54,841
St. Francis Medical Center, Trenton	National Family Caregiver Support, Title III, Part E	93.052	New Jersey Department of Health & Senior Services	1150-13	13,873
Mercy Health System of Southern Pennsylvania, Philadelphia	Public Health and Social Services Emergency Fund	93.003	PA Department of Health	4100062653	29,954
Mercy Health System of Southern Pennsylvania, Philadelphia	Public Health and Social Services Emergency Fund	93.003	PA Department of Health	4100062654	33,980
Mercy Health System of Southern Pennsylvania, Philadelphia	Public Health and Social Services Emergency Fund	93.003	PA Department of Health	4100062907	35,240
Mercy Health System of Southern Pennsylvania, Philadelphia	Public Health and Social Services Emergency Fund	93.003	PA Department of Health	4100062665	33,467
Total U. S. Department of Health and Human Services (Non-research)					9,059,839

(Continued)

CHE TRINITY INC.

CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014

Federal Agency/Regional Health Ministry	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
Medicaid Cluster:					
Hackley Life Counseling, Muskegon	Medical Assistance Program	93.778	Lakeshore Coordinating Counsel	610004	185,114
Pittsburgh Mercy Health System, Pittsburgh	Medical Assistance Program	93.778	PA Department of Human Services	N/A	5,977,874
St. Peter's Health Partners, Albany	Medical Assistance Program	93.778	NYS Department of Health	C026131	94,820
	Total Medicaid Cluster				6,257,808
CCDF Cluster:					
Saint Alphonsus Regional Medical Center, Boise	Child Care and Development Block Grant	93.575	N/A	EDK057-SB-002	430
	Total CCDF Cluster				430
Health Center Cluster:					
Saint Mary's Health Care, Grand Rapids	Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, and Public Housing Primary Care)	93.224	N/A	H80CS00031	649,280
Saint Joseph's Health System, Atlanta	Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, and Public Housing Primary Care)	93.224	N/A	5H80CS00022-12	3,651,652
Sisters of Providence Health System, Springfield	Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, and Public Housing Primary Care)	93.224	City of Springfield	20131040	142,101
Sisters of Providence Health System, Springfield	Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, and Public Housing Primary Care)	93.224	City of Springfield	20150053	284,201
Sisters of Providence Health System, Springfield	Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, and Public Housing Primary Care)	93.224	City of Springfield	20131039	24,715
	Total Health Center Cluster				4,751,949
Aging Cluster:					
Our Lady of Lourdes Health Care Services, Camden	Special Programs for the Aging Title III, Part B Grants for Supportive Services and Senior Centers	93.044	Camden County	04017	18,504
	Total Aging Cluster				18,504
	Total U. S. Department of Health and Human Services (Non-research)				20,088,530
DEPARTMENT OF VETERAN AFFAIRS:					
Saint Joseph's Health System, Atlanta	VA Supportive Services for Veteran Families Program	64.033	GA Department of Human Services	12-GA-544	38,375
	Total Department of Veteran Affairs				38,375
U.S. DEPARTMENT OF LABOR EMPLOYMENT TRAINING:					
Saint Joseph's Health System, Atlanta	Senior Community Service Employment Program	17.235	Georgia Department of Human Services	42700-373-0000012721	578,859
Workforce Investment Act (WIA) Cluster:					
Saint Joseph's Health System, Atlanta	WIA Adult Program	17.258	Georgia Department of Human Services	10921607	3,346
	Total WIA Cluster				3,346
	Total Department of Labor Employment Training				582,205

(Continued)

CHE TRINITY INC.

CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014

Federal Agency/Regional Health Ministry CORPORATION FOR NATIONAL AND COMMUNITY SERVICE	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
<u>Foster Grandparent/Senior Companion Center Cluster:</u>					
Our Lady of Lourdes Health Care Services, Camden	Senior Companion Program	94.016	N/A	14SX158202	346,715
Our Lady of Lourdes Health Care Services, Camden	Foster Grandparent Program	94.011	N/A	13GX147213	347,500
Our Lady of Lourdes Health Care Services, Camden	Foster Grandparent Program	94.011	N/A	13SF153893	138,572
Our Lady of Lourdes Health Care Services, Camden	Foster Grandparent Program	94.011	N/A	13SF153776	328,241
Total Foster Grandparent/Senior Companion Center Cluster:					1,161,028
Total Corporation For National and Community Service					1,161,028
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:					
Pittsburgh Mercy Health System, Pittsburgh	Continuum of Care Program	14.267	PA Department of Human Services	PA0404L3E001203 & PA0404L3E001304	148,940
Pittsburgh Mercy Health System, Pittsburgh	Continuum of Care Program	14.267	PA Department of Human Services	PA0259L3E001205	51,758
Pittsburgh Mercy Health System, Pittsburgh	Continuum of Care Program	14.267	PA Department of Human Services	PA0615L3E001201 & PA0615L3E001302	369,783
Pittsburgh Mercy Health System, Pittsburgh	Continuum of Care Program	14.267	PA Department of Human Services	PA0558L3E001202 & PA0558L3E001303	151,508
Pittsburgh Mercy Health System, Pittsburgh	Continuum of Care Program	14.267	PA Department of Human Services	PA 0399L3E001204	751,327
Pittsburgh Mercy Health System, Pittsburgh	Continuum of Care Program	14.267	PA Department of Human Services	PA 0399B3E001002	115,188
Hackley Hospital, Muskegon	Housing Opportunities for Persons with AIDS	14.241	Michigan Department of Community Health	MIH012-F999 & MIH13-F999	133,492
Saint Joseph's Health System, Atlanta	Housing Opportunities for Persons with AIDS	14.241	City of Atlanta	250131963	217,936
St. Peter's Health Partners, Albany	Shelter Plus Care	14.238	NYS Office of Alcoholism & Substance Abuse Services	C003960	175,013
St. Peter's Health Partners, Albany	Shelter Plus Care	14.238	NYS Office of Alcoholism & Substance Abuse Services	1513	250,202
Pittsburgh Mercy Health System, Pittsburgh	Supportive Housing Program	14.235	PA Department of Human Services	PA 0453B3E000900	254,236
Pittsburgh Mercy Health System, Pittsburgh	Supportive Housing Program	14.235	PA Department of Human Services	PA 0399B3E001103	60,566
Sisters of Providence Health System, Springfield	Supportive Housing Program	14.235	Mental Health Association Safe Haven Project	-	4,944
Sisters of Providence Health System, Springfield	Supportive Housing Program	14.235	Mental Health Association Project Reach	-	32,592
Saint Joseph's Health System, Atlanta	Supportive Housing Program	14.235	N/A	GA0024L4B001206	35,897
U. S. Department of Housing and Urban Development					2,753,382

(Continued)

CHE TRINITY INC.

CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014

Federal Agency/Regional Health Ministry	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
<u>Community Development Block Grant (CDBG) Entitlement Grants Cluster:</u>					
Our Lady of Lourdes Health Care Services, Camden	CDBG/Entitlement Grants	14.218	Camden County	5603-80-03	8,307
St. Peter's Health Partners, Albany	CDBG/Entitlement Grants	14.218	Albany County DSS	67915	220,998
St. Peter's Health Partners, Albany	CDBG/Entitlement Grants	14.218	NYS Office of Temporary & Disability Assistance	C021291	175,945
St. Peter's Health Partners, Albany	CDBG/Entitlement Grants	14.218	Albany Community Development Agency	4002-29	22,856
Saint Alphonsus Medical Center, Nampa	CDBG/Entitlement Grants	14.218	City of Nampa	826000231	20,000
	Total CDBG Entitlement Grants Cluster				448,106
	Total U. S. Department of Housing and Urban Development				3,201,488
STUDENT FINANCIAL AID CLUSTER PROGRAMS:					
U.S. DEPARTMENT OF EDUCATION:					
Mount Carmel College of Nursing, Columbus	Nursing Student Loans	93.364	N/A	N/A	70,000
Mount Carmel College of Nursing, Columbus	Federal Direct Student Loans	84.268	N/A	N/A	8,228,823
St. James Mercy Hospital, Hornell	Federal Direct Student Loans	84.268	N/A	N/A	111,943
St. Peter's Health Partners, Albany	Federal Direct Student Loans	84.268	N/A	N/A	405,562
St. Peter's Health Partners, Albany	Federal Direct Student Loans	84.268	N/A	N/A	453,666
St. Peter's Health Partners, Albany	Federal Direct Student Loans	84.268	N/A	N/A	263,613
St. Peter's Health Partners, Albany	Federal Direct Student Loans	84.268	N/A	N/A	250,518
Mount Carmel College of Nursing, Columbus	Federal Pell Grant Program	84.063	N/A	N/A	977,713
St. James Mercy Hospital, Hornell	Federal Pell Grant Program	84.063	N/A	N/A	70,143
St. Francis Medical Center, Trenton	Federal Pell Grant Program	84.063	N/A	N/A	14,980
St. Peter's Health Partners, Albany	Federal Pell Grant Program	84.063	N/A	N/A	209,485
St. Peter's Health Partners, Albany	Federal Pell Grant Program	84.063	N/A	N/A	108,242
Mount Carmel College of Nursing, Columbus	Federal Supplemental Educational Opportunity Grants	84.007	N/A	N/A	98,125
	Subtotal U.S. Department of Education				11,262,813
	Total Student Financial Aid Cluster Program				11,262,813
Mount Carmel Health System, Columbus	Special Education-Grants for Infants and Families	84.181	Franklin County Family and Children First Council	FCFC-13-025	602,600
	Total U. S. Department of Education				11,865,413

(Continued)

CHE TRINITY INC.

**CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014**

Federal Agency/Regional Health Ministry	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
U.S. DEPARTMENT OF JUSTICE					
<u>Justice Assistance Grant (JAG) Program Cluster:</u>					
Mount Carmel Health System, Columbus	Edward Byrne Memorial Justice Assistance Grant Program	16.738	Ohio Office of Criminal Justice Services	2011/2012 JG-D01-6331	40,110
Mount Carmel Health System, Columbus	Edward Byrne Memorial Justice Assistance Grant Program	16.738	Ohio Office of Criminal Justice Services	2012 JG-D01-6680	3,700
	Subtotal JAG Program Cluster				43,810
Mercy Medical Center, Sioux City	Improving the Investigation and Prosecution of Child Abuse and the Regional and Local Children's Advocacy Centers	16.758	Iowa Chapter Children's Advocacy	4-SIOU-IA-SA13	4,230
Mercy Medical Center, Sioux City	Improving the Investigation and Prosecution of Child Abuse and the Regional and Local Children's Advocacy Centers	16.758	Iowa Chapter Children's Advocacy	4-SIOU-IA-SA14	5,449
Mount Carmel Health System, Columbus	Violence Against Women Formula Grants	16.588	Ohio Office of Criminal Justice Services	2011/2012-WF-VA5-V521	37,621
St. Peter's Health Partners, Albany	Violence Against Women Formula Grants	16.588	NYS Division of Criminal Justice	TS40147	32,205
Mount Carmel Health System, Columbus	Crime Victim Assistance	16.575	State of Ohio Attorney General	2012/2013 VAGENE479	54,873
Pittsburgh Mercy Health System, Pittsburgh	Crime Victim Assistance	16.575	N/A	N/A	29,953
St. Peter's Health Partners, Albany	Crime Victim Assistance	16.575	NYS Exec Dept	C501144	329,026
	Total U.S. Department of Justice				537,167
U.S. DEPARTMENT OF AGRICULTURE:					
Muskegon Community Health Project, Muskegon	Supplemental Nutrition Assistance Program, Process and Technology Improvement Grants	10.580	Michigan Department of Human Services	ADMIN-12-99020-2	70,478
Sisters of Providence Health System, Springfield	Child and Adult Care Food Program	10.558	Mass. Dept. of Elementary & Secondary Education	SCDOE12758N70532117A	23,145
St. James Mercy Hospital, Hornell	Child and Adult Care Food Program	10.558	N/A	1440	25,540
St. Peter's Health Partners, Albany	Child and Adult Care Food Program	10.558	NYS Department of Health	2320	28,950
Samaritan Child Care Center	Child and Adult Care Food Program	10.558	NYS Department of Health	2205	27,416
Saint Mary's Health Care, Grand Rapids	Special Supplemental Nutrition Program for Women, Infants, and Children	10.557	Kent County Department of Community Health	XX4W1006	111,312
	Total U.S. Department of Agriculture				286,841
U.S. DEPARTMENT OF TRANSPORTATION:					
Mercy Medical Center, Sioux City	National Priority Safety Programs	20.616	State of Iowa	14-405b-M1CSS Task 01-00-00	1,098
<u>Highway Safety Cluster:</u>					
Mercy Medical Center, Sioux City	Alcohol Impaired Driving Countermeasures Incentive Grants I	20.601	State of Iowa	PAP 13-410, Task 37	1,346
Mercy Medical Center, Sioux City	State and Community Highway Safety	20.600	State of Iowa	14-402-MOTSP Task 03-00-00	7,059
	Total Highway Safety Cluster				8,405
	Total U.S. Department of Transportation				9,503

(Continued)

CHE TRINITY INC.

**CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014**

Federal Agency/Regional Health Ministry	Program Title	Federal CFDA Number	Pass-through Agency	Grantor Agency or Pass-through Identification Number	Expenditures
U.S. DEPARTMENT OF LABOR: St. Peter's Hospital, Albany	H-1B Job Training Grants	17.268	NYS Department of Labor	C014606	<u>45,641</u>
	Total U.S. Department of Labor				45,641
	TOTAL FEDERAL AWARDS				<u>\$ 39,826,007</u>

(Concluded)

CHE TRINITY INC.

NOTES TO THE CONSOLIDATED SUPPLEMENTAL SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS FOR THE YEAR ENDED JUNE 30, 2014

1. BASIS OF ACCOUNTING

The accompanying Consolidated Supplemental Schedule of Expenditures of Federal Awards is presented in accordance with the *U.S. Office of Management and Budget ("OMB") Circular A-133* and is prepared using the accrual basis of accounting.

Recent Regulatory Changes—In December 2013, the OMB issued comprehensive grant reform rules titled, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*. The new requirements consolidate what was previously in eight separate *OMB Circulars* into a single new document. This consolidation resulted in various areas of change to the previous requirements. The grant reform rules are intended to streamline the federal government's guidance on administrative requirements, cost principles, and audit requirements for federal awards. The final guidance supersedes *OMB Circulars A-21, A-50, A-87, A-89, A-102, A-110, A-122, and A-133*, and is effective for federal awards made after December 26, 2014. The Corporation is in the process of evaluating the impact of this guidance on its federal grant programs.

2. EXPENDITURES AND OTHER REPORTING

The Corporation's consolidated financial statements include, for the fiscal year ended June 30, 2014, the operations of Saint Joseph's Tower, Inc. ("Tower"), a wholly owned subsidiary of Trinity Continuing Care Services. The Tower reported total expenditures of federal awards of \$4,061,774 for the year ended June 30, 2014. Included in these total expenditures is \$3,435,778, which represents the outstanding mortgage balances insured under the Federal Housing Administration's ("FHA") Section 202 Supportive Housing for the Elderly. In addition, the Tower received \$625,996 of its revenues in the year ended June 30, 2014 from the U.S. Department of Housing and Urban Development under the terms of the Housing Assistance Payment contracts. The accompanying Consolidated Supplemental Schedule of Expenditures of Federal Awards does not include the federal grant activity of the Tower because the federal expenditures were included in a separate audit report in accordance with *OMB Circular A-133*.

The Corporation's consolidated financial statements include the operations of Mercy Health System of Chicago and Subsidiaries ("MHSC") for the year ended June 30, 2014. MHSC reported total expenditures of federal awards of \$59,839,413 for the year ended June 30, 2014. Included in these total expenditures is \$59,117,882, which represents the outstanding mortgage balances insured under FHA Section 242 Hospital Mortgage Insurance Program. The accompanying Consolidated Supplemental Schedule of Expenditures of Federal Awards does not include the federal grant activity of MHSC because the federal expenditures were included in a separate audit report in accordance with *OMB Circular A-133*.

The Corporation's consolidated financial statements include the operations of Saint Michael's Medical Center ("SMMC") for the year ended June 30, 2014. SMMC reported total expenditures of federal awards of \$1,452,003 for the year ended June 30, 2014. SMMC's fiscal year end is December 31 and the financial statements and Schedule of Federal Expenditures are audited separately for the year ended December 31, 2013. Accordingly, the federal expenditures were included in a separate audit report in accordance with *OMB Circular A-133*.

The Corporation's consolidated financial statements include, for the year ended June 30, 2014, the operations of Our Lady of Mercy Life Center ("OLMLC") and Villa Mary Immaculate ("Villa Mary"), which are subsidiaries of St. Peters Health Centers. OLMLC and Villa Mary reported total expenditures of federal

awards of \$5,665,809 and \$4,688,660, respectively, for the year ended June 30, 2014, which represents the outstanding mortgage balances insured under the FHA's Section 232 Mortgage Insurance for Residential Care Facilities. OLMLC and Villa Mary's fiscal year end is December 31 and the financial statements and Schedule of Federal Expenditures are audited separately for the year ended December 31, 2014. Accordingly, the federal expenditures were included in a separate audit report in accordance with *OMB Circular A-133*.

3. SUBRECIPIENTS

Of the federal expenditures included in the Consolidated Supplemental Schedule of Expenditures of Federal Awards, the Corporation provided federal awards to subrecipients for the year ended June 30, 2014, as follows:

Federal Grantor/Program Title	Regional Health Ministry	Federal CFDA Number	Amount
<i>U.S. Department of Health and Human Services:</i>			
Cancer Control	Saint Joseph Mercy Health System, Ann Arbor	93.399	\$ 549,003
Cancer Control	Saint Joseph Mercy Health System, Ann Arbor	93.399	31,260
State Rural Hospital Flexibility Program	Oakland Mercy Hospital, Sioux City	93.241	4,250
Total Amounts Provided to Subrecipients			<u>\$ 584,513</u>

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Directors of
CHE Trinity Inc.
Livonia, Michigan

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of CHE Trinity Inc. and its subsidiaries (the "Corporation") which comprise the consolidated balance sheet as of June 30, 2014, and the related consolidated statement of operations and changes in net assets and cash flows for the year then ended and the related notes to the consolidated financial statements, and have issued our report thereon dated October 3, 2014 (except as it relates to Note 14 Subsequent Events and the Consolidated Supplemental Schedules of Federal Awards and related notes, as to which the date is March 19, 2015). Our report includes a reference to other auditors who audited the financial statements of certain consolidated and unconsolidated entities, as described in our report on the Company's consolidated financial statements. The financial statements of the consolidated entities audited by other auditors were audited in accordance with auditing standards generally accepted in the United States of America.

Internal Control over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered the Corporation's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control. Accordingly, we do not express an opinion on the effectiveness of the Corporation's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Corporation's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Deloitte & Touche LLP

October 3, 2014

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE

To the Board of Directors of
CHE Trinity Inc.
Livonia, Michigan

Report on Compliance for Each Major Federal Program

We have audited CHE Trinity Inc. and its subsidiaries (the "Corporation") compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Corporation's major federal programs for the year ended June 30, 2014. The Corporation's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

The Corporation's consolidated financial statements include the operations of the Saint Joseph's Tower, Inc. (the "Tower"), a wholly owned subsidiary of Trinity Continuing Care Services, Mercy Health System of Chicago and Subsidiaries ("MHSC"), Our Lady of Mercy Life Center ("OLMLC"), Saint Michaels Medical Center ("SMMC"), and Villa Mary Immaculate ("Villa Mary") for the year ended June 30, 2014, each of which are wholly owned subsidiaries of the Corporation. The Federal Awards of \$4,061,774 for the Tower, \$59,839,413 for MHSC, \$1,452,003 for OLMLC, \$5,665,809 for SMMC, and \$4,688,660 for Villa Mary for the respective periods have been excluded from the Corporation's Consolidated Supplemental Schedule of Expenditures of Federal Awards. Our audit, described below, did not include the procedures relating to the Federal Awards of the Tower, or MHSC because the Corporation engaged other auditors to perform separate audits in accordance with OMB Circular A-133 and the Department of Housing and Urban Development requirements.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Corporation's major federal programs based on our audit of the types of compliance requirements referred to above.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect

on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Corporation's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Corporation's compliance.

Opinion on Each Major Federal Program

In our opinion, the Corporation complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2014.

Other Matters

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as Findings 2014-001 through 2014-002. Our opinion on each major federal program is not modified with respect to these matters.

The Corporation's responses to the noncompliance findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. The Corporation's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control over Compliance

Management of the Corporation is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Corporation's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Corporation's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Deloitte & Touche LLP

March 19, 2015

CHE TRINITY INC.

SCHEDULE OF FINDINGS AND QUESTIONED COSTS YEAR ENDED JUNE 30, 2014

SECTION I — SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued: Unmodified

Internal control over financial reporting:

- Material weakness(es) identified? yes no
- Significant deficiency(ies) identified that are not considered to be material weaknesses? yes none reported

Noncompliance material to the consolidated financial statements noted? yes no

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? yes no
- Significant deficiency(ies) identified that are not considered to be material weaknesses? yes none reported

Type of auditors' report issued on compliance for major programs: Unmodified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of *OMB Circular A-133*? yes no

The Corporation's major programs were:

Name of Federal Program or Cluster	CFDA Number
Continuum of Care Program	14.267
Student Financial Aid Cluster	84.007, 84.063, 84.268, 93.364
Consolidated Health Centers Cluster	93.224
Medical Assistance Program	93.778
Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	93.918

Dollar threshold used to distinguish between type A and type B programs \$1,194,780

Auditee qualified as a low-risk auditee? yes no

SECTION II — FINANCIAL STATEMENT FINDINGS SECTION

No matters were considered reportable.

SECTION III — FEDERAL AWARD FINDINGS AND QUESTIONED COSTS SECTION

FINDING 2014-001

FEDERAL PROGRAM INFORMATION

Name	CFDA	Contract Numbers
Grants to provide Outpatient Early Intervention Services with respect to HIV Disease - St. Francis Medical Center, Trenton	93.918	Various

Condition: Grant recipient failed to meet reporting deadlines for submission of required reports.

Criteria or specific requirement (including statutory, regulatory, or other citation): The *OMB Circular A-133 Compliance Supplement* requires recipients to follow the reporting requirements of the applicable grant agreements. Per the guidance provided in the grant agreements, various reports due to the United States Department of Health and Human Services Health Resources Service Administration were submitted subsequent to their due dates.

Effect: Consequences for failure to comply with these conditions may include a reduction of overall award and/or reduction in future awards.

Cause: Due to staff turnover, reports were not filed in a timely fashion. In addition, appropriate controls were not in place to ensure that program reporting requirements were met.

Questioned costs: None

Context: During the reporting compliance testing procedures at St. Francis Medical Center, Trenton ("Trenton"), the auditor made thirteen report submission selections. It was noted that five of the grant reporting submissions were not submitted to the grant agency by the reporting deadlines per the grant agreement.

Recommendation: Grant recipient should institute formal policies and procedures to ensure timely submissions of all required reports.

Views of Responsible Officials and Planned Corrective Action:

Timely submission of reports will be reemphasized to grant managers and accounting staff in the annual federal awards compliance training. In addition, Trenton finance staff will develop a checklist with all grant reporting deadlines and work with the grant managers to ensure reports are filed on a timely basis.

Contact Person: Charles Ott, Controller, St. Francis Medical Center, Trenton (609)599-6279

FINDING 2014-002

FEDERAL PROGRAM INFORMATION

Name	CFDA	Contract Numbers
Grants to provide Outpatient Early Intervention Services with respect to HIV Disease - St. Francis Medical Center, Trenton	93.918	Various

Condition: Grant recipient failed to meet earmarking requirements that require entities to spend fifty percent of funds awarded on early intervention services (EIS).

Criteria or specific requirement (including statutory, regulatory, or other citation): *Section 42 USC 300ff-51(b)(2), (e)(1) and (2), and (e)(3)(A) and (B) of the OMB Circular A-133 Compliance Supplement* states that a minimum of fifty percent of funds awarded must be spent on providing the following early intervention services (EIS) to individuals with HIV disease: testing, referrals, other clinical and diagnostic services, periodic medical evaluations, and therapeutic measures—directly and on-site or at sites where other primary care services are rendered.

Effect: Consequences for failure to comply with these conditions may include a reduction of overall award and/or a restriction or reduction in future awards.

Cause: At St. Francis Medical Center, Trenton ("Trenton") the cause for not meeting the 50% earmarking requirements for EIS is primarily due to the inability to fill positions. Physicians are resistant to the federally mandated compensation structure given the nature of the specialty. Similarly, the HIV case manager position has been a challenge to fill and has been vacant since April 2013. However, overall program objectives continue to be met in both specialist and primary care services provided by the program director; this position is considered maintenance of effort and therefore not funded by the Grant.

Questioned costs: None

Context: During the earmarking compliance testing procedures at Trenton, the auditor noted only thirty-nine percent of funds awarded were spent on providing early intervention services to individuals with HIV diseases during the calendar year ending December 31, 2013.

Recommendation: Grant recipient should institute formal policies and procedures to ensure earmarking requirements are properly tracked and complied with.

Views of Responsible Officials and Planned Corrective Action: Trenton will continue to seek and recruit for the unfilled positions. Any difficulty experienced in filling the open positions will continue to be communicated to the Federal Grant Officer and appropriately documented. In addition, the Earmarking Compliance calculation will be updated and monitored on a quarterly basis and communicated to the Grant Officer.

Contact Person: Charles Ott, Controller, St. Francis Medical Center, Trenton (609)599-6279

Summary Schedule of Prior-Year Audit Findings for the Year Ended June 30, 2013

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
2013	2013-1	Certain allowable expenditures were incurred and properly reported to the granting agency in FY2013. However, during allowable cost testing, the auditor noted that certain expenditures originally included in the Consolidated Supplemental Schedule of Expenditures of Federal Awards did not agree to grantor reimbursement reports. These amounts have been correctly removed from the FY2013 expenditures.	93.847, 93.750, 93.889	None	Corrective procedures were implemented.
2013	2013-2	During testing of the Columbus Nursing Student Loan (NSL) program, the auditor noted students with the incorrect student classification (i.e. current, repayment, grace period, deferment, forbearance). The Mount Carmel College of Nursing participates in the NSL program and is required to conduct an exit interview with the borrower before he or she leaves the institution. Furthermore, for a NSL loan, repayment of the loan must begin nine months after the student ceases to be a full-time or half-time student. The incorrect classification of students within the NSL program led to exit interviews not occurring and repayment periods not beginning for some borrowers after he or she left the institution.	93.364	None	Corrective procedures were implemented.
2013	2013-3	During cash management testing, the auditor noted that reimbursement requests were made relating to expenditures that were never incurred or purchased.	93.889	None	Corrective procedures were implemented.
2013	2013-4	Equipment purchased with fiscal 2013 grant funds by Mount Carmel Health System, Columbus could not be located. One of the current year grant expenditures was for the purchase of four pieces of equipment. During the auditor's physical inspection of the equipment, only three pieces of the equipment could be located.	93.889	None	Corrective procedures were implemented.

Summary Schedule of Prior-Year Audit Findings for the Year Ended June 30, 2013

2013	2013-5	Grant recipients failed to meet reporting deadlines for submission of required reports.	93.889	None	Corrective procedures were implemented.
*2013	*2013-001	Certain purchase order approval limits were not enforced properly, instances of accruals not being properly stated were identified, and vendor master file additions and maintenance activities were not properly documented or reviewed.	93.889	None	Corrective procedures were implemented.
**2013	**2013-001	For CFDA 14.235, out of a sample of 40 program income charges to the award, 7 client charges selected were not supported by the income verification documentation totaling \$605. Billing errors for 16 of the 40 client charges selected resulted in net over-charges totaling \$202. For CFDA 14.238, out of a sample of 40 program income charges to the award, 11 client charges selected were not supported by the income verification documentation totaling \$1,908. Billing errors for 19 of the 40 client charges selected resulted in net over-charges totaling \$334.	14.235, 14.238	\$3,049	Corrective procedures were implemented.

* Pertains to information disclosed in the Report on Federal Awards for Select Regional Health Ministries for Catholic Health East for the six-month period ended June 30, 2013.

** Pertains to information disclosed in the Report on Federal Awards and on Allegheny County Awards for Mercy Life Center Corporation for the year ended June 30, 2013.