



CONSOLIDATED FINANCIAL STATEMENTS,
SUPPLEMENTARY INFORMATION AND AUDIT
REPORTS AND SCHEDULES RELATED TO
OFFICE OF MANAGEMENT AND BUDGET
CIRCULAR A-133

North Shore-Long Island Jewish Health System, Inc.
Year Ended December 31, 2012
With Reports of Independent Auditors

Ernst & Young LLP

 **ERNST & YOUNG**

North Shore-Long Island Jewish Health System, Inc.

Consolidated Financial Statements, Supplementary Information and Audit Reports
and Schedules Related to Office of Management and Budget Circular A-133

Year Ended December 31, 2012

Contents

Consolidated Financial Statements

| | |
|---|---|
| Report of Independent Auditors..... | 1 |
| Consolidated Statements of Financial Position..... | 4 |
| Consolidated Statements of Operations..... | 5 |
| Consolidated Statements of Changes in Net Assets..... | 6 |
| Consolidated Statements of Cash Flows..... | 7 |
| Notes to Consolidated Financial Statements..... | 8 |

**Supplementary Information and Audit Reports and Schedules Related to Office
of Management and Budget Circular A-133**

| | |
|---|----|
| Schedule of Expenditures of Federal Awards..... | 68 |
| Notes to Schedule of Expenditures of Federal Awards..... | 80 |
| Report of Independent Auditors 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> | 82 |
| Report of Independent Auditors on Compliance for Each Major Federal Program and on Internal Control Over Compliance Required by OMB Circular A-133..... | 84 |
| Schedule of Findings and Questioned Costs..... | 87 |

Report of Independent Auditors

The Board of Trustees
North Shore-Long Island Jewish Health System, Inc.

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of North Shore-Long Island Jewish Health System, Inc. and its member corporations and other affiliated entities (collectively, the “System”), which comprise the consolidated statements of financial position as of December 31, 2012 and 2011, and the related consolidated statements of operations, changes in net assets and cash flows for the years then ended and the related notes to the consolidated financial statements.

Management’s Responsibility for the Financial Statements

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

Auditor’s Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States 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 of material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the North Shore-Long Island Jewish Health System, Inc. and its member corporations and other affiliated entities at December 31, 2012 and 2011, and the consolidated results of their operations, changes in their net assets and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Change in the Presentation of the Provision for Bad Debts

As discussed in Note 2 to the consolidated financial statements, in 2012 the System adopted the provisions of Accounting Standards Update No. 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*, which resulted in a change to the presentation of the provision for bad debts on the consolidated statements of operations effective January 1, 2011. Our opinion is not modified with respect to this matter.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The Schedule of Expenditures of Federal Awards for the year ended December 31, 2012 as required by US 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 information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the 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. In our opinion, the 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 also have issued our report dated April 15, 2013 on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant

agreements and other matters. 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 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 System's internal control over financial reporting and compliance.

Ernst + Young LLP

April 15, 2013, except for the schedule of expenditures of federal awards for which the date is September 30, 2013.

North Shore-Long Island Jewish Health System, Inc.

Consolidated Statements of Financial Position

(In Thousands)

| | December 31 | |
|---|--------------|--------------|
| | 2012 | 2011 |
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 283,258 | \$ 474,738 |
| Marketable securities and other investments | 1,496,070 | 1,116,810 |
| Accounts receivable for services to patients, net of allowance for doubtful accounts of \$109,790 in 2012 and \$108,837 in 2011 | 697,216 | 620,543 |
| Accounts receivable for physician activities, net | 60,151 | 53,428 |
| Assets limited as to use, current portion | 119,166 | 76,017 |
| Pledges receivable, current portion | 35,426 | 48,939 |
| Insurance claims receivable, current portion | 103,621 | 97,346 |
| Other current assets | 159,829 | 212,114 |
| Total current assets | 2,954,737 | 2,699,935 |
| Assets limited as to use, net of current portion | 840,463 | 805,632 |
| Pledges receivable, net of current portion | 120,880 | 111,866 |
| Property, plant and equipment, net | 3,372,151 | 3,104,120 |
| Insurance claims receivable, net of current portion | 357,061 | 372,243 |
| Other assets | 158,373 | 169,617 |
| Total assets | \$ 7,803,665 | \$ 7,263,413 |
| Liabilities and net assets | | |
| Current liabilities: | | |
| Short-term borrowings | \$ 110,540 | \$ 90,540 |
| Accounts payable and accrued expenses | 493,994 | 592,634 |
| Accrued salaries and related benefits | 527,832 | 466,667 |
| Current portion of capital lease obligations | 5,000 | 4,208 |
| Current portion of long-term debt | 50,934 | 46,656 |
| Current portion of insurance claims liability | 103,621 | 97,346 |
| Current portion of malpractice and other insurance liabilities | 60,413 | 47,130 |
| Current portion of third-party payer structured liabilities | 5,438 | 5,438 |
| Current portion of estimated payable to third-party payers | 352,995 | 288,029 |
| Total current liabilities | 1,710,767 | 1,638,648 |
| Accrued retirement benefits, net of current portion | 660,356 | 558,785 |
| Capital lease obligations, net of current portion | 80,913 | 81,790 |
| Long-term debt, net of current portion | 1,470,728 | 1,366,719 |
| Insurance claims liability, net of current portion | 357,061 | 372,243 |
| Malpractice and other insurance liabilities, net of current portion | 652,337 | 580,965 |
| Third-party payer structured liabilities, net of current portion | 23,951 | 29,248 |
| Other long-term liabilities | 417,471 | 445,055 |
| Total liabilities | 5,373,584 | 5,073,453 |
| Commitments and contingencies | | |
| Net assets: | | |
| Unrestricted | 1,959,501 | 1,735,798 |
| Temporarily restricted | 341,669 | 328,463 |
| Permanently restricted | 128,911 | 125,699 |
| Total net assets | 2,430,081 | 2,189,960 |
| Total liabilities and net assets | \$ 7,803,665 | \$ 7,263,413 |

See accompanying notes.

North Shore-Long Island Jewish Health System, Inc.

Consolidated Statements of Operations

(In Thousands)

| | Year Ended December 31 | |
|--|-------------------------------|--------------|
| | 2012 | 2011 |
| Operating revenue: | | |
| Net patient service revenue | \$ 5,693,546 | \$ 5,354,818 |
| Physician practice revenue | 758,409 | 671,917 |
| Provision for bad debts | (97,994) | (99,111) |
| Total patient revenue, net of provision for bad debts | 6,353,961 | 5,927,624 |
| Other operating revenue | 302,691 | 245,585 |
| Net assets released from restrictions used for operations | 45,330 | 49,937 |
| Total operating revenue | 6,701,982 | 6,223,146 |
| Operating expenses: | | |
| Salaries | 3,315,368 | 3,013,834 |
| Employee benefits | 957,616 | 861,052 |
| Supplies and expenses | 1,984,936 | 1,888,927 |
| Depreciation and amortization | 275,601 | 264,128 |
| Interest | 70,594 | 61,007 |
| Total operating expenses | 6,604,115 | 6,088,948 |
| Excess of operating revenue over operating expenses | 97,867 | 134,198 |
| Non-operating gains and losses: | | |
| Investment income | 42,636 | 42,933 |
| Change in net unrealized gains and losses and change in value of equity method investments | 123,549 | (24,307) |
| Change in fair value of interest rate swap agreements designated as derivative instruments | (4,495) | (14,909) |
| Loss on refunding and refinancing of long-term debt | (4,590) | (12,589) |
| Contribution received in the acquisition of The Long Island Home | 12,823 | – |
| Medical resident tax recovery | – | 1,794 |
| Other non-operating gains and losses | (5,510) | 12,011 |
| Total non-operating gains and losses | 164,413 | 4,933 |
| Excess of revenue and gains and losses over expenses | 262,280 | 139,131 |
| Net assets released from restrictions for capital asset acquisitions | 38,590 | 15,847 |
| Contributions of long-lived assets | – | 54,000 |
| Change in fair value of interest rate swap agreements designated as cash flow hedges | 677 | (793) |
| Recovery (loss) of fair value of endowment corpus | 696 | (194) |
| Pension and other postretirement liability adjustments | (78,540) | (149,267) |
| Increase in unrestricted net assets | \$ 223,703 | \$ 58,724 |

See accompanying notes.

North Shore-Long Island Jewish Health System, Inc.

Consolidated Statements of Changes in Net Assets
(In Thousands)

Years Ended December 31, 2012 and 2011

| | Total | Unrestricted | Temporarily Restricted | Permanently Restricted |
|---|----------------------------|----------------------------|-----------------------------------|-----------------------------------|
| Net assets, January 1, 2011 | \$ 2,104,845 | \$ 1,677,074 | \$ 306,053 | \$ 121,718 |
| Contributions and grants | 105,408 | – | 101,427 | 3,981 |
| Investment income | 7,869 | – | 7,869 | – |
| Change in net unrealized gains and losses and change in value of equity method investments | (6,656) | – | (6,656) | – |
| Excess of revenue and gains and losses over expenses | 139,131 | 139,131 | – | – |
| Net assets released from restrictions for: | | | | |
| Capital asset acquisitions | – | 15,847 | (15,847) | – |
| Operations | (49,937) | – | (49,937) | – |
| Non-operating activities | (14,640) | – | (14,640) | – |
| Contributions of long-lived assets | 54,000 | 54,000 | – | – |
| Change in fair value of interest rate swap agreements designated as cash flow hedges | (793) | (793) | – | – |
| Loss of fair value of endowment corpus | – | (194) | 194 | – |
| Pension and other postretirement liability adjustments | (149,267) | (149,267) | – | – |
| Increase in net assets | <u>85,115</u> | <u>58,724</u> | <u>22,410</u> | <u>3,981</u> |
| Net assets, December 31, 2011 | 2,189,960 | 1,735,798 | 328,463 | 125,699 |
| Contributions and grants | 100,239 | – | 97,027 | 3,212 |
| Investment income | 2,728 | – | 2,728 | – |
| Change in net unrealized gains and losses and change in value of equity method investments | 12,900 | – | 12,900 | – |
| Excess of revenue and gains and losses over expenses | 262,280 | 262,280 | – | – |
| Net assets released from restrictions for: | | | | |
| Capital asset acquisitions | – | 38,590 | (38,590) | – |
| Operations | (45,330) | – | (45,330) | – |
| Non-operating activities | (14,833) | – | (14,833) | – |
| Change in fair value of interest rate swap agreements designated as cash flow hedges | 677 | 677 | – | – |
| Recovery of fair value of endowment corpus | – | 696 | (696) | – |
| Pension and other postretirement liability adjustments | (78,540) | (78,540) | – | – |
| Increase in net assets | <u>240,121</u> | <u>223,703</u> | <u>13,206</u> | <u>3,212</u> |
| Net assets, December 31, 2012 | <u>\$ 2,430,081</u> | <u>\$ 1,959,501</u> | <u>\$ 341,669</u> | <u>\$ 128,911</u> |

See accompanying notes.

North Shore-Long Island Jewish Health System, Inc.

Consolidated Statements of Cash Flows
(In Thousands)

| | Year Ended December 31 | |
|---|------------------------|-------------------|
| | 2012 | 2011 |
| Cash flows from operating activities | | |
| Increase in net assets | \$ 240,121 | \$ 85,115 |
| Adjustments to reconcile increase in net assets to net cash provided by operating activities: | | |
| Contribution received in the acquisition of The Long Island Home | (12,823) | – |
| Contributions of long-lived assets | – | (54,000) |
| Permanently restricted contributions | (3,212) | (3,981) |
| Depreciation and amortization | 275,601 | 264,128 |
| Net realized gains and losses, change in net unrealized gains and losses and change in value of equity method investments | (143,611) | 14,393 |
| Change in fair value of interest rate swap agreements | 3,818 | 15,702 |
| Loss on refunding and refinancing of long-term debt | 4,590 | 12,589 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable for services to patients, net | (65,854) | (50,183) |
| Accounts receivable for physician activities, net | (6,723) | (8,036) |
| Pledges receivable | 4,212 | 2,490 |
| Current portion of estimated payable to third-party payers | 63,171 | 33,529 |
| Accrued retirement benefits, net of current portion | 74,349 | 80,862 |
| Malpractice and other insurance liabilities | 81,452 | 85,917 |
| Net change in all other operating assets and liabilities | 38,582 | 224,154 |
| Net cash provided by operating activities | <u>553,673</u> | <u>702,679</u> |
| Cash flows from investing activities | | |
| Capital expenditures | (489,472) | (622,107) |
| Net cash invested in marketable securities and other investments and assets limited as to use | (318,296) | (109,159) |
| Cash received in the acquisition of The Long Island Home | 8,417 | – |
| Net cash used in investing activities | <u>(799,351)</u> | <u>(731,266)</u> |
| Cash flows from financing activities | | |
| Principal payments on long-term debt and capital lease obligations | (53,051) | (56,875) |
| Payments on refunded long-term debt | (71,292) | (306,177) |
| Payments on short-term borrowings | (83,485) | (77,380) |
| Payments on third-party payer structured liabilities | (5,297) | (6,630) |
| Proceeds from short-term borrowings | 103,485 | 152,380 |
| Proceeds from long-term debt, net of underwriter's discount | 197,915 | 395,428 |
| Payments for financing costs | (2,453) | (9,826) |
| Payment of termination costs related to interest rate swap agreements | (35,123) | – |
| Proceeds from permanently restricted contributions | 3,499 | 2,152 |
| Net cash provided by financing activities | <u>54,198</u> | <u>93,072</u> |
| Net (decrease) increase in cash and cash equivalents | <u>(191,480)</u> | <u>64,485</u> |
| Cash and cash equivalents, beginning of year | <u>474,738</u> | <u>410,253</u> |
| Cash and cash equivalents, end of year | <u>\$ 283,258</u> | <u>\$ 474,738</u> |
| Supplemental disclosure of cash flow information | | |
| Cash paid during the year for interest (exclusive of amounts capitalized) | <u>\$ 67,249</u> | <u>\$ 59,490</u> |
| Supplemental disclosure of noncash investing and financing activities | | |
| Capital leases incurred | <u>\$ –</u> | <u>\$ 726</u> |
| Contributions of long-lived assets | <u>\$ –</u> | <u>\$ 54,000</u> |

See accompanying notes.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements

(In Thousands)

December 31, 2012

1. Organization and Principles of Consolidation

North Shore-Long Island Jewish Health System, Inc. and its member corporations and other affiliated entities (collectively, the “System”) is an integrated health care delivery system in the New York metropolitan area. Various entities within the System are exempt from Federal income taxes under the provisions of Section 501(a) of the Internal Revenue Code (the “Code”) as organizations described in Section 501(c)(3), while other entities are not exempt from such income taxes. The exempt organizations also are exempt from New York State and local income taxes.

The accompanying consolidated financial statements include the accounts of the following principal operating organizations. All interorganization accounts and activities have been eliminated in consolidation.

Hospitals

- North Shore University Hospital (“NSUH”), including the accounts of Syosset Hospital
- Long Island Jewish Medical Center (“LIJMC”), including Long Island Jewish Hospital, Steven and Alexandra Cohen Children’s Medical Center of New York and Zucker Hillside Hospital
- Staten Island University Hospital (“Staten Island”)
- Lenox Hill Hospital (“Lenox”)
- Southside Hospital (“Southside”)
- Forest Hills Hospital (“Forest Hills”)
- Franklin Hospital (“Franklin”), including the accounts of Orzac Center for Extended Care and Rehabilitation
- Glen Cove Hospital (“Glen Cove”)
- Huntington Hospital Association (“Huntington”)
- Plainview Hospital (“Plainview”)
- South Oaks Hospital (“South Oaks”)

Other Entities

- North Shore-Long Island Jewish Health System, Inc. and North Shore-Long Island Jewish Health Care, Inc. (“NSLIJ HCI”) – parent holding companies
- North Shore University Hospital Stern Family Center for Extended Care and Rehabilitation (“CECR”) – skilled nursing facility and rehabilitation center
- Broadlawn Manor Nursing and Rehabilitation Center (“Broadlawn”) – skilled nursing facility and rehabilitation center
- North Shore Health System Enterprises, Inc. and North Shore Health Enterprises, Inc. – holding companies for certain for-profit related entities
- North Shore-Long Island Jewish Health System Laboratories – laboratory services
- The Feinstein Institute for Medical Research – medical research
- North Shore-Long Island Jewish Health System Foundation, Inc. – fundraising
- Hospice Care Network, Inc. – hospice services
- Regional Insurance Company Ltd. (“Regional Insurance”) – captive insurance company providing excess professional and general liability insurance

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

1. Organization and Principles of Consolidation (continued)

Other Entities (continued)

- RegionCare, Inc. – infusion therapy, diagnostic laboratory, nurse staffing and licensed home health agency services
- North Shore Community Services, Inc. – real estate holdings and related services
- North Shore University Hospital Housing, Inc., North Shore University Hospital at Glen Cove Housing, Inc. and Hillside Hospital Houses, Inc. – housing and auxiliary facilities for staff members, students and employees
- Regional Claims Recovery Service – billing and collection services
- North Shore LIJ Physicians Insurance Company Risk Retention Group (“RRG”) – captive insurance company providing physician professional liability insurance
- Lenox Hill Physician Hospital Organization, Inc. and Lenox Hill consolidated professional corporations
- Staten Island consolidated professional corporations
- Huntington Hospital Dolan Family Health Center – community health center

The Long Island Home Acquisition

On July 1, 2012 (the “Acquisition Date”), the System acquired The Long Island Home, a New York not-for-profit corporation exempt from taxation, which consists of South Oaks, a behavioral health hospital, Broadlawn, a skilled nursing facility and rehabilitation center, and The Long Island Home Foundation (collectively, “The Long Island Home” or “LIH”). The System acquired The Long Island Home by means of an inherent contribution, where no consideration was transferred by the System. The System accounted for this business combination by applying the acquisition method and, accordingly, the inherent contribution received was valued as the excess of The Long Island Home’s assets over liabilities. In determining the inherent contribution received, all assets and liabilities were measured at fair value as of the Acquisition Date. The results of The Long Island Home’s operations have been included in the consolidated financial statements since the Acquisition Date.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

1. Organization and Principles of Consolidation (continued)

The following table summarizes the estimated fair values of LIH's assets and liabilities at the Acquisition Date:

| | July 1, 2012 |
|--|-------------------------|
| Assets | |
| Cash and cash equivalents | \$ 8,417 |
| Marketable securities and other investments | 5,049 |
| Accounts receivable for services to patients | 10,819 |
| Other current assets | 1,518 |
| Assets limited as to use | 114 |
| Property, plant and equipment | 54,160 |
| Insurance claims receivable | 3,540 |
| Other assets | 9,421 |
| Total assets | <u>93,038</u> |
| Liabilities | |
| Accounts payable and accrued expenses | 3,131 |
| Accrued salaries and related benefits | 5,833 |
| Estimated payable to third-party payers | 1,795 |
| Accrued retirement benefits | 27,222 |
| Capital lease obligations | 4,351 |
| Long-term debt | 28,333 |
| Insurance claims liability | 3,540 |
| Malpractice and other insurance liabilities | 3,203 |
| Other long-term liabilities | 2,807 |
| Total liabilities | <u>80,215</u> |
| Excess of assets over liabilities | <u>\$ 12,823</u> |
| Net assets acquired | |
| Unrestricted | \$ 12,823 |
| Temporarily restricted | - |
| Permanently restricted | - |
| | <u>\$ 12,823</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

1. Organization and Principles of Consolidation (continued)

The following table summarizes amounts attributable to The Long Island Home from the Acquisition Date through December 31, 2012, that are included in the accompanying 2012 consolidated statements of operations and consolidated statements of changes in net assets:

| | Period from July 1, 2012 to December 31, 2012 |
|---|--|
| | <hr/> |
| Total operating revenue | \$ 42,940 |
| Total operating expenses | <hr/> 46,212 |
| Deficiency of operating revenue over operating expenses | (3,272) |
| Total non-operating gains and losses | <hr/> 139 |
| Deficiency of revenue and gains and losses over expenses | (3,133) |
| Change in fair value of interest rate swap agreements designated as cash flow hedges | 120 |
| Pension and other postretirement liability adjustments | <hr/> 3,296 |
| Increase in unrestricted net assets | <hr/> <hr/> \$ 283 |
| Change in net assets: | |
| Unrestricted net assets | \$ 283 |
| Temporarily restricted net assets | — |
| Permanently restricted net assets | <hr/> — |
| Total change in net assets | <hr/> <hr/> \$ 283 |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

1. Organization and Principles of Consolidation (continued)

The following table represents unaudited pro forma financial information for the System, assuming the acquisition of The Long Island Home had taken place on January 1, 2011. The pro forma financial information is not necessarily indicative of the results of operations as they would have been had the transaction been effected on January 1, 2011.

| | Year Ended December 31 | |
|--|-------------------------------|--------------|
| | 2012 | 2011 |
| Total operating revenue | \$ 6,746,210 | \$ 6,309,948 |
| Total operating expenses | 6,652,026 | 6,178,192 |
| Excess of operating revenue over operating expenses | 94,184 | 131,756 |
| Total non-operating gains and losses | 151,854 | 5,063 |
| Excess of revenue and gains and losses over expenses | \$ 246,038 | \$ 136,819 |
| Change in net assets: | | |
| Unrestricted net assets | \$ 199,602 | \$ 46,780 |
| Temporarily restricted net assets | 13,206 | 22,410 |
| Permanently restricted net assets | 3,212 | 3,981 |
| Total change in net assets | \$ 216,020 | \$ 73,171 |

2. Summary of Significant Accounting Policies

Consolidated Statements of Operations

The accompanying consolidated statements of operations include the excess of revenue and gains and losses over expenses as the performance indicator. For purposes of display, transactions deemed by management to be ongoing, major or central to the provision of health care services are reported as operating revenue and operating expenses; peripheral or incidental transactions and unusual, nonrecurring items are reported as non-operating gains and losses.

Net assets released from restrictions for capital asset acquisitions, contributions of long-lived assets, the change in fair value of interest rate swap agreements designated as cash flow hedges, the recovery (loss) of fair value of endowment corpus and pension and other postretirement liability adjustments are excluded from the System's performance indicator.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Recent Accounting Standards

In July 2011, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities* (“ASU 2011-07”). Under ASU 2011-07, the provision for bad debts related to patient revenue is required to be presented as a deduction from patient revenue in the consolidated statements of operations rather than as an operating expense, with enhanced footnote disclosure on the policies for recognizing patient revenue and assessing bad debts. The guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2011. The System adopted the provisions of ASU 2011-07 in 2012 and retrospectively applied the presentation requirements.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, including accounts receivable for services to patients, and liabilities, including estimated payables to third-party payers, accrued retirement benefits and malpractice and other insurance liabilities, fair value determinations as of the Acquisition Date and disclosures of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

During 2012 and 2011, the System revised estimates made in prior years to reflect the passage of time and the availability of more recent information. Changes in estimates primarily relate to estimates made by management for third-party payer liabilities and malpractice and other insurance liabilities. For the years ended December 31, 2012 and 2011, the change in estimates for third-party payer liabilities related to prior years was not significant. For the year ended December 31, 2012, the change in estimates for malpractice and other insurance liabilities related to prior years was not significant. For the year ended December 31, 2011, the estimates for malpractice and other insurance liabilities related to prior years increased by approximately \$3,000.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Cash and Cash Equivalents

The System considers all highly liquid financial instruments purchased with a maturity of three months or less, other than those held in the investment portfolio and assets limited as to use, to be cash equivalents. The System maintains cash on deposit with major banks and invests in money market securities with financial institutions which exceed federally-insured limits. Management believes the credit risk related to these deposits is minimal.

Accounts Receivable and Patient Revenue

Net patient service revenue and physician practice revenue (collectively, “patient revenue”) are reported at estimated net realizable amounts due from patients, third-party payers and others for services rendered and include estimated retroactive revenue adjustments due to ongoing and future audits, reviews and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are provided and are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews and investigations.

The System recognizes accounts receivable and patient revenue associated with services provided to patients who have third-party payer coverage on the basis of contractual rates, governmental rates or established charges for the services rendered. For uninsured patients who are ineligible for any government assistance program, the System provides services without charge or at amounts less than its established rates for patients who meet the criteria of its charity care policy. Because the System does not pursue collection of amounts determined to qualify as charity care, such services are not reported as patient revenue. For patients who were determined by the System to have the ability to pay but do not, the estimated uncollectible amounts are recorded as the provision for bad debts. In distinguishing charity care from the provision for bad debts, a number of factors are considered, certain of which require a high degree of judgment.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Patient revenue for the year ended December 31, 2012, net of contractual and charity care allowances, but before the provision for bad debts, from insured and uninsured patients is approximately \$6,368,215 and \$83,740, respectively. Deductibles and copayments due from patients under third-party payment programs are included in the insured amount above.

The allowance for doubtful accounts represents the System's estimate of the uncollectible accounts receivable related to bad debts. Additions to the allowance for doubtful accounts result from the provision for bad debts. Accounts written off as uncollectible are deducted from the allowance for doubtful accounts. The allowance for doubtful accounts is based upon the System's assessment of historical and expected net collections, business and economic conditions, trends in health care coverage and other collection indicators.

For receivables associated with services provided to patients who have third-party payer coverage, the System analyzes amounts due from third-parties and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for third-party payers who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables associated with self-pay patients, which includes both patients without insurance and patients with deductible and copayment balances due after third-party coverage, the System records an allowance for doubtful accounts and a provision for bad debts in the period of service based on past experience. The allowance for doubtful accounts for self-pay patients was approximately 85% of the gross self-pay accounts receivable balance as of December 31, 2012.

The System's allowance for doubtful accounts relating to accounts receivable for services to patients and accounts receivable for physician activities totaled approximately \$124,709 at December 31, 2012.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Non-Medicare Reimbursement

In New York State, hospitals and all non-Medicare payers, except Medicaid, workers' compensation and no-fault insurance programs, negotiate hospitals' payment rates. If negotiated rates are not established, payers are billed at hospitals' established charges. Medicaid, workers' compensation and no-fault payers pay hospital rates promulgated by the New York State Department of Health ("NYSDOH"). Effective December 1, 2009, the New York State prospective payment methodology was updated such that payments to hospitals for Medicaid, workers' compensation and no-fault inpatient services are based on a statewide rate, with retroactive adjustments for certain rate components paid concurrently with the settlement of the final rate. Prior to December 1, 2009, the retroactive adjustments were paid in future years as a component of the hospital-specific rate. Outpatient services also are paid based on a statewide prospective system that was effective December 1, 2008. Medicaid rate methodologies are subject to approval at the Federal level by the Centers for Medicare and Medicaid Services ("CMS"), which may routinely request information about such methodologies prior to approval. Revenue related to specific rate components that have not been approved by CMS is not recognized until the System is reasonably assured that such amounts are realizable. Adjustments to the current and prior years' payment rates for those payers will continue to be made in future years.

Medicare Reimbursement

Hospitals are paid for most Medicare inpatient and outpatient services under the national prospective payment system and other methodologies of the Medicare program for certain other services. Federal regulations provide for certain adjustments to current and prior years' payment rates, based on industry-wide and System-specific data.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

The System has established estimates, based on information presently available, of amounts due to or from Medicare and non-Medicare payers for adjustments to current and prior years' payment rates, based on industry-wide and System-specific data. The current Medicaid, Medicare and other third-party payer programs are based upon extremely complex laws and regulations that are subject to interpretation. Noncompliance with such laws and regulations could result in fines, penalties and exclusion from such programs. The System is not aware of any allegations of noncompliance that could have a material adverse effect on the accompanying consolidated financial statements and believes that it is in compliance with all applicable laws and regulations. Medicare cost reports, which serve as the basis for final settlement with the Medicare program, have been audited by the Medicare fiscal intermediary and settled through years ranging from 2000 to 2011. Other years remain open for audit and settlement, as do numerous issues related to the New York State Medicaid program for prior years. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount when open years are settled and additional information is obtained.

There are various proposals at the Federal and State levels that could, among other things, significantly reduce payment rates or modify payment methods. The ultimate outcome of these proposals and other market changes, including the potential effects of health care reform that have been enacted by the Federal and State governments, cannot presently be determined. Future changes in the Medicare and Medicaid programs and any reduction of funding could have an adverse impact on the System. Additionally, certain payers' payment rates for various years have been appealed by certain members of the System. If the appeals are successful, additional income applicable to those years might be realized.

In April 2012, CMS settled a series of lawsuits filed in 2007 that challenged the calculation involving the use of the rural floor provision of the Balanced Budget Act of 1997. The System participated in this lawsuit and, as a result, received a cash settlement of approximately \$54,300 from Medicare for fiscal years 2000 through 2011, which increased net patient service revenue for the year ended December 31, 2012. Fees associated with participating in this lawsuit were approximately \$5,700 and increased supplies and expenses for the year ended December 31, 2012.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

The System grants credit without collateral to its patients, most of whom are insured under various third-party agreements. Government payer programs account for a significant portion of net patient service revenue. For the years ended December 31, 2012 and 2011, revenue from the Medicare and Medicaid programs, including Medicare and Medicaid managed care programs, accounted for approximately 50% and 52% of the System's net patient service revenue, respectively.

The significant concentrations of gross accounts receivable for services to patients from third-party payers and patients at December 31, 2012 and 2011, are as follows:

| | December 31 | |
|--------------------------|--------------------|-------------|
| | 2012 | 2011 |
| Medicare | 34% | 30% |
| Medicaid | 21 | 20 |
| Self-pay | 8 | 9 |
| Other third-party payers | 37 | 41 |
| | 100% | 100% |

Charity Care

Together, charity care and the provision for bad debts represent uncompensated care. The estimated cost of total uncompensated care is approximately \$169,957 and \$163,013 for the years ended December 31, 2012 and 2011, respectively. The estimated cost of uncompensated care is based on the ratio of cost to charges, as determined by System-specific data.

The estimated cost of charity care provided was \$135,078 and \$128,108 for the years ended December 31, 2012 and 2011, respectively. The estimated cost of charity care is based on the ratio of cost to charges, as determined by System-specific data.

For the years ended December 31, 2012 and 2011, the provision for bad debts, at charges, was \$97,994 and \$99,111, respectively. The provision for bad debts is multiplied by the ratio of cost to charges for purposes of inclusion in the total cost of uncompensated care amount identified above.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

The NYSDOH Hospital Indigent Care Pool (the “Pool”) was established to provide funds to hospitals for the provision of uncompensated care and is funded, in part, by a 1% assessment on hospital net inpatient service revenue. For the years ended December 31, 2012 and 2011, the System received \$66,983 and \$74,727, respectively, in Pool distributions, of which approximately \$54,000 and \$60,000 was related to charity care. The System made payments into the Pool of \$37,124 and \$36,557 for the years ended December 31, 2012 and 2011, respectively, for the 1% assessment.

See Note 8 for additional disclosure for charity care relating to Staten Island’s settlement with the New York State Attorney General.

Pledges Receivable

Pledges (promises to give), less an allowance for uncollectible amounts, are recorded as receivables in the year made at net present value and are recorded as temporarily or permanently restricted net assets. Pledges receivable that are due more than one year from the balance sheet date are discounted to reflect the present value of future cash flows.

Marketable Securities and Other Investments

Marketable securities are classified as trading securities. Investments in debt securities, equity securities and mutual funds with readily determinable fair values are reported at fair value, based on quoted market prices.

The System has invested in investment funds of hedge funds (“funds of hedge funds”), hedge funds, private equity funds and private real estate funds, which are included in marketable securities and other investments and assets limited as to use in the accompanying consolidated statements of financial position. These System investments are not readily marketable; they are reported under the equity method of accounting, which approximates fair value. The equity method reflects the System’s share of the net asset value of the respective funds.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Individual investment holdings of the funds of hedge funds, hedge funds, private equity funds and private real estate funds may include investments in both nonmarketable and market-traded securities. Valuations of these investments and, therefore, the System's holdings, may be determined by the investment managers or general partners. Values may be based on estimates that require varying degrees of judgment. Recorded estimates may change by a material amount in the near term. The investments may indirectly expose the System to securities lending, short sales of securities, and trading in futures and forwards contracts, options and other derivative products. However, the System's risk is limited to its amounts invested. The financial statements of the funds of hedge funds, hedge funds, private equity funds and private real estate funds are audited annually by independent auditors. At December 31, 2012, the System has future commitments of \$25,109 and \$4,606 to invest in private equity and private real estate funds for pension and restricted assets, respectively.

Other investments also include investments in commingled fixed income, equity and commodity funds. The individual investment holdings of these commingled funds are predominantly marketable securities. These investments are reported under the equity method of accounting, which approximates fair value. The equity method reflects the System's share of the net asset value of these investments. The financial statements of the commingled fixed income, equity and commodity funds are audited annually by independent auditors.

Investment income or loss (including realized gains and losses on investments, interest and dividends) and the change in net unrealized gains and losses and change in value of equity method investments are included in the performance indicator, unless the income or loss is restricted by donor or law.

Assets Limited as to Use

Assets limited as to use include funds held pursuant to debt financing arrangements, medical malpractice claims trust agreements, internally designated funds, including internally designated malpractice and other self-insurance assets and funds related to the medical resident tax recovery owed to the residents, deferred employee compensation plans and other temporarily and permanently restricted assets. Amounts required to meet current liabilities are reported as current assets.

Inventory of Supplies

Inventory, included in other current assets, is stated at the lower of cost (first-in, first-out method) or market.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Insurance Claims Receivable and Liability

For medical malpractice and similar contingent liabilities, the System does not net insurance recoveries against related claims liabilities and determines such claims liabilities without consideration of insurance recoveries. Accordingly, the System recognizes insurance receivables at the same time that it recognizes the liabilities, measured on the same basis as the liabilities, subject to the need for a valuation allowance for uncollectible amounts. The System recognized insurance claims receivable and insurance claims liability of \$460,682 (\$103,621 current and \$357,061 long-term) and \$469,589 (\$97,346 current and \$372,243 long-term) in the accompanying consolidated statements of financial position at December 31, 2012 and 2011, respectively. Such amounts represent the actuarially determined present value of medical malpractice and other insurance claims that are anticipated to be covered by insurance, discounted at a rate of 2.0%.

Property, Plant and Equipment

Property, plant and equipment is stated at cost or, in the case of gifts, at fair value at the date of the gift, less accumulated depreciation and amortization. Property, plant and equipment of The Long Island Home and Lenox that existed at their respective acquisition dates (July 1, 2012 and May 19, 2010, respectively) was recorded at fair value based upon an independent valuation. Depreciation and amortization of land improvements, buildings, fixed equipment and major movable equipment is computed by the straight-line method based upon the estimated useful lives of the assets ranging from three to forty years.

Equipment under capital lease obligations and leasehold improvements are amortized using the straight-line method over the lesser of the estimated useful life of the asset or the lease term. Such amortization is included in depreciation and amortization in the accompanying consolidated financial statements. During the period of construction of capital assets, interest costs are capitalized as a component of the cost of assets. When assets are disposed of, the carrying amounts of the assets and the related accumulated depreciation are removed from the accounts, and any resulting gain or loss on disposal is included in the performance indicator. When assets become fully depreciated, the carrying amounts of such assets and the related accumulated depreciation are removed from the accounts (see Note 6).

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Long-Lived Assets

Gifts of long-lived assets are reported at fair value established at the date of contribution as changes in unrestricted net assets, excluded from the performance indicator, unless explicit donor stipulations specify how the donated asset must be used.

During 2011, the System received a gift of land and a building in Manhattan. The land and building were recorded at their estimated fair value of \$54,000, based upon an independent valuation. The gift is recorded within contributions of long-lived assets in the accompanying consolidated statements of operations.

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If long-lived assets are deemed to be impaired, the impairment to be recognized is measured as the amount by which the carrying amount of the assets exceeds the fair value. Assets to be disposed of are reported at the lower of the carrying amount or the fair value, less costs to sell.

Intangible Assets

Upon acquisition of The Long Island Home in 2012 and Lenox in 2010, the System recorded intangible assets of \$8,700 and \$11,000, respectively, which are subject to impairment testing on an annual basis. At December 31, 2012, the System determined that there has been no impairment of these intangible assets.

In 2011, Staten Island purchased from Richmond University Medical Center (“RUMC”) the remainder interest in a joint venture between the hospitals for \$30,500. The purchase price was determined based upon an independent valuation, and as a result, an intangible asset was recorded for the purchase price which is being amortized over a five and one-half year useful life. At December 31, 2012 and 2011, the value of the intangible asset, net of accumulated amortization, is \$20,333 and \$25,879, respectively.

Intangible assets are included within other assets in the accompanying consolidated statements of financial position.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Deferred Financing Costs

Deferred financing costs, included in other assets, represent costs incurred to obtain financing for various System projects and initiatives. Amortization of these costs is provided over the term of the applicable indebtedness. Deferred financing costs, net of accumulated amortization, are \$33,173 and \$36,058 at December 31, 2012 and 2011, respectively. Amortization, included in interest expense in the accompanying consolidated statements of operations, is \$2,210 and \$1,880 for the years ended December 31, 2012 and 2011, respectively.

During 2012 and 2011, the System refunded certain long-term debt and issued new debt (see Note 7). Unamortized deferred financing costs of \$5,545 and \$2,515 were written off in connection with the 2012 and 2011 transactions, respectively, and are included within the loss on refunding and refinancing of long-term debt in the accompanying consolidated statements of operations. Additionally, new deferred financing costs of \$4,870 and \$13,003 were recorded as a result of the 2012 and 2011 transactions, respectively.

Interest Rate Swap Agreements

Interest rate swap agreements are reported at fair value. Fair value is estimated using discounted cash flow analyses based on current interest rates with consideration of the risk of non-performance. Changes in fair value of interest rate swap agreements designated as derivative instruments are recognized in the System's performance indicator. Changes in fair value of interest rate swap agreements designated as cash flow hedges are excluded from the performance indicator.

Other Long-Term Liabilities

Other long-term liabilities included in the accompanying consolidated statements of financial position primarily consist of the long-term portion of estimated payable to third-party payers, lease incentive obligations, deferred rent payable, asset retirement obligations, deferred revenue and the fair value of the interest rate swap agreements.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are restricted by donors or other external parties to be used for designated purposes or over specified time periods. When donor restrictions expire, that is, when a time restriction ends or a purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported as net assets released from restrictions.

Permanently restricted net assets have been restricted by donors to be maintained in perpetuity. Income from these net assets is available to support certain teaching, research and training programs.

Donor Gifts

Gifts of cash and other assets, including unconditional promises to give cash and other assets (pledges), are reported at fair value when the gift is received (or promise is made). Donor-restricted contributions whose restrictions are met within the same year as received are classified as unrestricted contributions in the accompanying consolidated financial statements.

The System receives conditional pledges, which are not reflected in the accompanying consolidated financial statements. The pledges primarily relate to the establishment of certain programs. As the conditions of the pledges are met, the pledges are recognized. At December 31, 2012 and 2011, \$4,025 and \$4,425, respectively, of conditional pledges have not been recognized in the consolidated statements of financial position. Contributions and pledges raised through fundraising efforts for the years ended December 31, 2012 and 2011 are summarized as follows:

| | 2012 | 2011 |
|-------------------------------|------------------|-------------------|
| Unrestricted | \$ 4,337 | \$ 22,614 |
| Unrestricted long-lived asset | – | 54,000 |
| Temporarily restricted | 68,001 | 65,727 |
| | \$ 72,338 | \$ 142,341 |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Medical Resident Tax Recovery

In March 2010, the Internal Revenue Service (“IRS”) announced that, for periods ending before April 1, 2005, medical residents would be eligible for the student exception of Federal Insurance Contributions Act (“FICA”) taxes. Under the student exception, FICA taxes do not apply to wages for services performed by students employed by a school, college or university where the student is pursuing a course of study. As a result, the IRS will allow refunds for institutions that filed timely FICA refund claims and provided certain information that met the requirements of perfection, established by the IRS, for their claims applicable to periods prior to April 1, 2005. Institutions are eligible for medical resident FICA refunds for both the employer and employee portions of FICA taxes paid, plus statutory interest.

For the year ended December 31, 2011, the System recorded revenue of \$1,794 related to FICA medical resident refund claims and related interest that are expected to meet the IRS requirements to be eligible for refunds. The System has recorded in the accompanying consolidated statements of financial position a receivable of \$7,247 and \$79,891, included in other current assets at December 31, 2012 and 2011, respectively. The System has recorded a liability related to the portion to be remitted to the medical residents of \$38,000 and \$37,230, included in accrued salaries and related benefits at December 31, 2012 and 2011, respectively. The System has established these estimates based on information presently available, which are subject to change as the IRS adjudicates the claims.

Functional Expenses

The System provides health care services to residents primarily within its geographic areas. Expenses related to providing these services pertain to the following functional categories for the years ended December 31, 2012 and 2011:

| | <u>2012</u> | <u>2011</u> |
|----------------------------|---------------------|---------------------|
| Health care services | \$ 5,763,206 | \$ 5,321,614 |
| General and administrative | 840,909 | 767,334 |
| Total operating expenses | <u>\$ 6,604,115</u> | <u>\$ 6,088,948</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

2. Summary of Significant Accounting Policies (continued)

Tax Status

Certain entities included in the System's consolidated financial statements are taxable entities under Federal or state laws. U.S. generally accepted accounting principles require that the asset and liability method of accounting for income taxes be utilized by these organizations. Under the asset and liability method, deferred income taxes are recognized for the tax consequences of temporary differences by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities.

The effect on deferred taxes of a change in tax rates is recognized in income in the period of enactment. At December 31, 2012 and 2011, the System has a deferred income tax asset which has been fully offset by a related valuation allowance. A valuation allowance is provided when it is more likely than not that some portion or all of the deferred tax asset will not be realized. Significant components of the deferred tax asset relate to the allowance for doubtful accounts receivable and net operating loss carryforwards. Certain entities have net operating loss carryforwards aggregating approximately \$149,000, which expire in varying amounts through 2032, and are available to offset future taxable income.

Reclassifications

Certain 2011 amounts in the accompanying consolidated financial statements have been reclassified from amounts previously reported to conform to the 2012 presentation. These reclassifications have no impact on the net assets previously reported.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

3. Marketable Securities and Other Investments

Marketable securities and other investments, stated at fair value and under the equity method of accounting, consist of the following at December 31, 2012 and 2011:

| | <u>2012</u> | <u>2011</u> |
|---------------------------------|---------------------|---------------------|
| Cash and short-term investments | \$ 45,700 | \$ 68,218 |
| U.S. Government obligations | 184,488 | 150,277 |
| Corporate and other bonds | 181,553 | 122,618 |
| Fixed income mutual funds | 404,814 | 303,551 |
| Equity securities | 192,103 | 98,943 |
| Equity mutual funds | 172,361 | 138,201 |
| Commingled equity funds | 161,092 | 115,639 |
| Funds of hedge funds | 153,566 | 116,892 |
| Interest and other receivables | 393 | 2,471 |
| | <u>\$ 1,496,070</u> | <u>\$ 1,116,810</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

3. Marketable Securities and Other Investments (continued)

Investment income and the change in net unrealized gains and losses and change in value of equity method investments are comprised of the following for the years ended December 31, 2012 and 2011:

| | 2012 | | |
|---|---------------------|-----------------------------------|--------------------|
| | Unrestricted | Temporarily Restricted | Total |
| Investment income: | | | |
| Interest and dividend income | \$ 36,215 | \$ 1,987 | \$ 38,202 |
| Net realized gains and losses | 6,421 | 741 | 7,162 |
| | <u>\$ 42,636</u> | <u>\$ 2,728</u> | <u>\$ 45,364</u> |
| Change in net unrealized gains and losses and change in value of equity method investments: | | | |
| Change in net unrealized gains and losses | \$ 75,715 | \$ 8,230 | \$ 83,945 |
| Equity method investment gains and losses | 38,004 | 4,670 | 42,674 |
| Equity method investment gains – other assets | 9,830 | – | 9,830 |
| | <u>\$ 123,549</u> | <u>\$ 12,900</u> | <u>\$ 136,449</u> |
| | | | |
| | 2011 | | |
| | Unrestricted | Temporarily Restricted | Total |
| Investment income: | | | |
| Interest and dividend income | \$ 32,515 | \$ 1,717 | \$ 34,232 |
| Net realized gains and losses | 10,418 | 6,152 | 16,570 |
| | <u>\$ 42,933</u> | <u>\$ 7,869</u> | <u>\$ 50,802</u> |
| Change in net unrealized gains and losses and change in value of equity method investments: | | | |
| Change in net unrealized gains and losses | \$ (33,869) | \$ (4,369) | \$ (38,238) |
| Equity method investment gains and losses | (15,306) | (2,287) | (17,593) |
| Equity method investment gains – other assets | 24,868 | – | 24,868 |
| | <u>\$ (24,307)</u> | <u>\$ (6,656)</u> | <u>\$ (30,963)</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

4. Assets Limited as to Use

Assets limited as to use, including marketable securities and other investments stated at fair value and under the equity method of accounting, consist of the following at December 31, 2012:

| | 2012 | | | |
|---------------------------------|---|--|--|-------------------|
| | Bond Indenture, Third-party Agreements and Other | Malpractice and Other Self-Insurance Assets | Temporarily and Permanently Restricted Assets (Including Investment Return) | Total |
| Cash and short-term investments | \$ 26,680 | \$ 34,909 | \$ 16,600 | \$ 78,189 |
| U.S. Government obligations | 257,666 | 39,254 | 4,994 | 301,914 |
| Corporate and other bonds | 29,374 | 28,551 | 4,313 | 62,238 |
| Fixed income mutual funds | 56,568 | 84,234 | 9,633 | 150,435 |
| Commingled fixed income funds | - | - | 5,084 | 5,084 |
| Equity securities | 15,702 | 27,529 | 27,812 | 71,043 |
| Equity mutual funds | 39,990 | 86,309 | 22,489 | 148,788 |
| Commingled equity funds | 10,761 | 16,448 | 24,587 | 51,796 |
| Target-age mutual funds | 8,955 | - | - | 8,955 |
| Commingled commodity funds | - | - | 3,428 | 3,428 |
| Funds of hedge funds | 12,210 | 36,403 | 23,758 | 72,371 |
| Hedge funds | - | - | 164 | 164 |
| Private equity funds | - | - | 2,095 | 2,095 |
| Private real estate funds | - | - | 2,326 | 2,326 |
| Interest and other receivables | 609 | 105 | 89 | 803 |
| | <u>\$ 458,515</u> | <u>\$ 353,742</u> | <u>\$ 147,372</u> | <u>959,629</u> |
| Less current portion | | | | <u>119,166</u> |
| | | | | <u>\$ 840,463</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

4. Assets Limited as to Use (continued)

Assets limited as to use, including marketable securities and other investments stated at fair value and under the equity method of accounting, consist of the following at December 31, 2011:

| | 2011 | | | |
|---------------------------------|---|--|--|-------------------|
| | Bond Indenture, Third-party Agreements and Other | Malpractice and Other Self-Insurance Assets | Temporarily and Permanently Restricted Assets (Including Investment Return) | Total |
| Cash and short-term investments | \$ 67,014 | \$ 25,696 | \$ 20,277 | \$ 112,987 |
| U.S. Government obligations | 348,060 | 39,508 | 5,232 | 392,800 |
| Corporate and other bonds | 2,221 | 33,370 | 3,807 | 39,398 |
| Fixed income mutual funds | 17,555 | 71,881 | 9,566 | 99,002 |
| Commingled fixed income funds | – | – | 3,384 | 3,384 |
| Equity securities | 238 | 25,155 | 18,649 | 44,042 |
| Equity mutual funds | 23,141 | 39,476 | 20,962 | 83,579 |
| Commingled equity funds | – | 19,616 | 20,901 | 40,517 |
| Target-age mutual funds | 5,629 | – | – | 5,629 |
| Commingled commodity funds | – | – | 1,202 | 1,202 |
| Funds of hedge funds | – | 30,876 | 22,224 | 53,100 |
| Hedge funds | – | – | 204 | 204 |
| Private equity funds | – | – | 2,137 | 2,137 |
| Private real estate funds | – | – | 1,718 | 1,718 |
| Interest and other receivables | 1,069 | 678 | 203 | 1,950 |
| | <u>\$ 464,927</u> | <u>\$ 286,256</u> | <u>\$ 130,466</u> | 881,649 |
| Less current portion | | | | 76,017 |
| | | | | <u>\$ 805,632</u> |

Included in the bond indenture, third-party agreements and other funds above are depreciation funds and other internally designated funds of approximately \$49,000 and \$46,000 at December 31, 2012 and 2011, respectively, which are included in the System's days cash on hand calculation (see Note 7).

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

5. Pledges Receivable

Pledges receivable at December 31, 2012 and 2011 consist of the following:

| | <u>2012</u> | <u>2011</u> |
|--|-------------------|-------------------|
| Amounts expected to be collected in: | | |
| Less than one year | \$ 53,806 | \$ 64,268 |
| One to five years | 103,900 | 101,154 |
| More than five years | 66,626 | 69,003 |
| | <u>224,332</u> | <u>234,425</u> |
| Less: | | |
| Discount to present value of future cash flows (discount rates ranging from 0.25% to 6.0%) | 14,917 | 15,324 |
| Allowance for uncollectible amounts | 53,109 | 58,296 |
| Current portion of pledges receivable | 35,426 | 48,939 |
| Pledges receivable, net of current portion | <u>\$ 120,880</u> | <u>\$ 111,866</u> |

6. Property, Plant and Equipment

Property, plant and equipment and accumulated depreciation and amortization at December 31, 2012 and 2011, are summarized as follows:

| | <u>2012</u> | <u>2011</u> |
|--|---------------------|---------------------|
| Land | \$ 601,437 | \$ 563,363 |
| Land improvements | 13,873 | 13,481 |
| Buildings and fixed equipment | 2,731,055 | 2,326,015 |
| Movable equipment | 965,858 | 864,730 |
| Leasehold improvements | 20,602 | 22,801 |
| | <u>4,332,825</u> | <u>3,790,390</u> |
| Less accumulated depreciation and amortization | 1,397,136 | 1,293,250 |
| | <u>2,935,689</u> | <u>2,497,140</u> |
| Construction-in-progress | 436,462 | 606,980 |
| | <u>\$ 3,372,151</u> | <u>\$ 3,104,120</u> |

The System wrote off approximately \$170,000 and \$103,000 of fully depreciated assets in 2012 and 2011, respectively.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

6. Property, Plant and Equipment (continued)

Net interest capitalized for the years ended December 31, 2012 and 2011 was approximately \$11,000 and \$19,300, respectively.

Certain leases are considered to be the equivalent of installment purchases for purposes of accounting presentation. The liabilities relating to these assets are included in capital lease obligations. The cost, less accumulated amortization, of these assets is included in property, plant and equipment at December 31, 2012 and 2011 as follows:

| | <u>2012</u> | <u>2011</u> |
|-------------------------------|------------------|------------------|
| Buildings and fixed equipment | \$ 78,850 | \$ 78,000 |
| Movable equipment | 12,541 | 14,009 |
| | <u>91,391</u> | 92,009 |
| Less accumulated amortization | 28,859 | 26,843 |
| | <u>\$ 62,532</u> | <u>\$ 65,166</u> |

7. Debt

Long-Term Debt

Long-term debt at December 31, 2012 and 2011 consists of the following:

| | <u>2012</u> | <u>2011</u> |
|--|---------------------|---------------------|
| Bonds payable at varying dates through November 2042 at variable and fixed interest rates ranging from 1.03% to 5.75% | \$ 1,358,205 | \$ 1,273,775 |
| Other long-term debt payable at varying dates through December 2029 at fixed and floating interest rates ranging from 1.06% to 5.69% | 147,434 | 129,090 |
| Total long-term debt | <u>1,505,639</u> | 1,402,865 |
| Less current portion of bonds payable | 34,075 | 29,785 |
| Less current portion of other long-term debt | 16,859 | 16,871 |
| Add net unamortized bond premium | 16,023 | 10,510 |
| | <u>\$ 1,470,728</u> | <u>\$ 1,366,719</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

7. Debt (continued)

Annual aggregate principal payments applicable to long-term debt for years subsequent to December 31, 2012 are as follows:

| | Bonds Payable | Other Long-Term Debt | Total |
|-------------------------|--------------------------|-------------------------------------|---------------------|
| Year ended December 31: | | | |
| 2013 | \$ 34,075 | \$ 16,859 | \$ 50,934 |
| 2014 | 36,430 | 16,525 | 52,955 |
| 2015 | 37,775 | 17,582 | 55,357 |
| 2016 | 38,005 | 12,194 | 50,199 |
| 2017 | 39,650 | 12,445 | 52,095 |
| Thereafter | 1,172,270 | 71,829 | 1,244,099 |
| | <u>\$ 1,358,205</u> | <u>\$ 147,434</u> | <u>\$ 1,505,639</u> |

Most of the System's debt arrangements include security agreements of various types. The agreements may include the pledging as collateral of certain of the System's assets and revenues and limitations on the use of System assets, including restrictions on the transfer of assets to entities outside the System. At December 31, 2012 and 2011, substantially all of the System's assets were pledged as collateral under the terms of various debt agreements. In addition, certain debt agreements contain covenants related to the maintenance of financial ratios, including debt service coverage ratios and days cash on hand, and the maintenance of certain debt service and other reserve funds (assets limited as to use). At December 31, 2012 and 2011, except for The Long Island Home, the System was in compliance with the financial covenants. At December 31, 2012, The Long Island Home did not meet its debt service coverage ratio. Subsequent to December 31, 2012, The Long Island Home received a waiver from its lender through December 31, 2013.

North Shore-Long Island Jewish Health System, Inc.
Notes to Consolidated Financial Statements (continued)
(In Thousands)

7. Debt (continued)

Bonds Payable

Bonds payable consists of the following at December 31, 2012:

| | Interest Structure | Final Maturity | Outstanding Principal |
|---------------|-------------------------------|---------------------------|----------------------------------|
| Series 2012 A | Fixed | 2023 | \$ 48,930 |
| Series 2012 B | Fixed | 2042 | 135,000 |
| Series 2011 A | Fixed | 2041 | 386,385 |
| Series 2009 A | Fixed | 2037 | 235,615 |
| Series 2009 B | Fixed | 2039 | 50,000 |
| Series 2009 C | Fixed | 2039 | 37,500 |
| Series 2009 D | Fixed | 2039 | 37,500 |
| Series 2009 E | Fixed | 2033 | 60,890 |
| Series 2007 A | Fixed | 2037 | 147,445 |
| Series 2007 B | Floating Rate Notes | 2018 | 52,270 |
| Series 2005 A | Fixed | 2034 | 104,560 |
| Series 2005 B | Fixed | 2034 | 9,120 |
| Series 2003 | Fixed | 2018 | 26,585 |
| Series 1998 | Fixed | 2014 | 26,405 |
| | | | \$ 1,358,205 |

All of the System's bonds are tax-exempt and were issued through the Dormitory Authority of the State of New York ("DASNY"), except for the Series 2012 B bonds, which are taxable bonds.

In May 2012, certain members of the System (the "Obligated Group") issued \$48,930 of revenue bonds through the DASNY Series 2012A bonds. The Series 2012A bonds bear interest at fixed interest rates, payable semi-annually with a final maturity date of May 1, 2023. The proceeds of the Series 2012A bonds were used to refund a portion of the Obligated Group's Series 1998 bonds and pay the related costs of issuance. A non-cash loss on refunding of long-term debt of \$1,751 resulted from the transaction.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

7. Debt (continued)

In July 2012, the Obligated Group converted and remarketed \$125,000 of DASNY Series 2009B, C and D variable rate bonds to fixed rate bonds. Interest on the Series 2009B, C and D bonds is payable semi-annually and the bonds have a final maturity date of May 1, 2039. A non-cash loss on refinancing of long-term debt of \$2,839 resulted from the conversion and remarketing. In connection with this transaction, the Obligated Group paid \$35,123 to terminate the related interest rate swap agreements (“2009 Swaps”). The termination cost was based on the computed fair value of the 2009 Swaps at the termination date.

Prior to the conversion and remarketing of the Series 2009B, C and D bonds, the Obligated Group maintained approximately \$127,000 of irrevocable direct-pay letters of credit with three commercial banks which provided for the payment of the principal and interest of the Series 2009B, C and D bonds. The letters of credit were terminated with the conversion and remarketing of the Series 2009B, C and D bonds.

In September 2012, the Obligated Group issued \$135,000 of taxable bonds through the North Shore-Long Island Jewish Health System Series 2012B bonds. The Series 2012B bonds bear interest at fixed interest rates, payable semi-annually with a final maturity date of November 1, 2042. Part of the proceeds of the Series 2012B bonds were used to fund the termination cost of the 2009 Swaps and to pay the related costs of issuance. The remaining proceeds will be used to reimburse prior capital expenditures or fund future capital investments.

In October 2011, the Obligated Group issued \$392,200 of revenue bonds through the DASNY Series 2011A bonds. In conjunction with this issuance, the Obligated Group, which previously consisted of NSUH, LIJMC, Glen Cove, Plainview, Forest Hills and CECR, was expanded to include Franklin, Huntington, Lenox, Southside, Staten Island and NSLIJ HCI. The Series 2011A bonds bear interest at fixed interest rates, payable semi-annually with a final maturity date of May 1, 2041. The proceeds of the Series 2011A bonds were used to: (i) refund certain existing bonds of the new members of the Obligated Group, (ii) finance certain projects for the Obligated Group, (iii) fund the debt service reserve fund to secure the Series 2011A bonds, (iv) pay a portion of the interest on the Series 2011A bonds, and (v) pay costs of issuance incurred in connection with the issuance of the Series 2011A bonds. At the time of the issuance of the Series 2011A bonds, certain other bonds of the Obligated Group were cash defeased using sources other than the Series 2011A bond proceeds. A combined loss on refunding of long-term debt of \$12,589 resulted from the bond refunding and defeasance transactions.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

7. Debt (continued)

For certain existing bonds that were included in the System's refunding and defeasance transactions, funds were placed in escrow with a trustee to pay bondholders at future redemption dates. These funds and the liability for the corresponding bonds are excluded from the System's consolidated statement of financial position at December 31, 2012. Outstanding principal amounts to be paid from escrow to bondholders are comprised of the following at December 31, 2012:

| | Date of Final Redemption | Outstanding Principal |
|-----------------------------------|-------------------------------------|----------------------------------|
| Obligated Group Series 2003 Bonds | May 1, 2013 | \$ 36,300 |

Other Long-Term Debt

Other long-term debt consists of the following at December 31, 2012:

| | Interest Structure | Final Maturity | Outstanding Principal |
|--|-------------------------------|---------------------------|----------------------------------|
| Staten Island Term Loan | Variable | 2023* | \$ 42,000 |
| Lenox Mortgage | Variable | 2029 | 31,084 |
| The Long Island Home Mortgage | Variable | 2019 | 27,967 |
| Staten Island Note Payable | Variable | 2015 | 18,300 |
| LIJMC Tax-Exempt Lease Financing | Fixed | 2019 | 15,833 |
| Staten Island Tax-Exempt Lease Financing | Fixed | 2018 | 8,750 |
| NSUH Term Loan | Variable | 2014 | 3,500 |
| | | | <u>\$ 147,434</u> |

*A balloon payment of \$20,000 is due at maturity. Lender has an April 2018 call option.

In accordance with the terms of Staten Island's purchase of RUMC's remainder interest in its joint venture in 2011 (see Note 2), Staten Island recorded a note payable for the purchase price, to be paid through December 2015, with interest at the prime rate. At December 31, 2012, \$18,300 remained outstanding.

The long-term debt of The Long Island Home consists of a mortgage with interest payable monthly at a variable rate, with a balloon payment of \$22,727 due at maturity on January 1, 2019. The Long Island Home is not a member of the Obligated Group.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

7. Debt (continued)

Interest Rate Swap Agreements

In 2007, the Obligated Group entered into an interest rate swap agreement (“2007 Swap”) with a financial institution, matched to the term and rate of the Series 2007B bonds. Under the terms of the agreement, the Obligated Group receives variable interest payments and pays fixed interest payments on the notional value of the 2007 Swap. The notional value of the interest rate swap agreement amortizes. The swap agreement fixes the interest rate at a level viewed as acceptable by the Obligated Group. The terms of this swap agreement designate the 2007 Swap as a cash flow hedge under U.S. generally accepted accounting principles. Accordingly, changes in the fair value of the swap agreement are excluded from the performance indicator. The aggregate fair value of the 2007 Swap is a liability of \$5,414 and \$5,970 at December 31, 2012 and 2011, respectively, and is reflected in other long-term liabilities in the accompanying consolidated statements of financial position.

The Obligated Group entered into the 2009 Swaps with financial institutions related to the Series 2009B, C and D bonds. Under the terms of the agreements, and prior to the termination of the 2009 Swaps as previously described, the Obligated Group received variable interest payments and paid fixed interest payments on the notional value of the 2009 Swaps. The notional values of the interest rate swap agreements amortized. The swap agreements fixed the interest rate at a level viewed as acceptable by the Obligated Group. The terms of these swap agreements designated the 2009 Swaps as derivative instruments under U.S. generally accepted accounting principles. Accordingly, changes in the fair value of the swap agreements were recognized in the performance indicator. At December 31, 2011, the aggregate fair value of the 2009 Swaps was a liability of \$30,455, and is reflected in other long-term liabilities in the accompanying 2011 consolidated statement of financial position.

In 2008, Staten Island entered into interest rate swap agreements with financial institutions to fix the interest rate of its term loan at a level viewed as acceptable by Staten Island. Under the terms of the agreements, Staten Island will receive variable interest payments and pay fixed interest payments. The notional values of the interest rate swap agreements amortize. The System guarantees payments to the swap contract counterparties. The terms of these swap agreements designate them as derivative instruments under U.S. generally accepted accounting principles. Accordingly, changes in the fair value of the swap agreements are recognized in the performance indicator. The aggregate fair value of the swap agreements is a liability of \$2,952 and \$3,125 at December 31, 2012 and 2011, respectively, and is reflected in other long-term liabilities in the accompanying consolidated statements of financial position.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

7. Debt (continued)

The Long Island Home entered into interest rate swap agreements with a financial institution in 2008 to fix the interest rate of its variable rate mortgage at a level viewed as acceptable by The Long Island Home. Under the terms of the agreements, The Long Island Home will receive variable interest payments and pay fixed interest payments. The notional values of the interest rate swap agreements amortize. The terms of these swap agreements designate them as cash flow hedges under U.S. generally accepted accounting principles. Accordingly, changes in the fair value of the swap agreements are excluded from the performance indicator. The aggregate fair value of the swap agreements is a liability of \$2,686 and \$2,807 at December 31, 2012 and the Acquisition Date, respectively, and is reflected in other long-term liabilities in the accompanying 2012 consolidated statement of financial position.

Swap agreements expose the System to credit risk in the event of nonperformance by the counterparties. The System believes that the risk of material impact to its consolidated financial position arising from nonperformance by the counterparties is low.

Capital Lease Obligations

The System has entered into various capital lease agreements for buildings and equipment. Capital lease obligations at December 31, 2012 and 2011 consist of the following:

| | <u>2012</u> | <u>2011</u> |
|---|------------------|------------------|
| Minimum lease payments | \$ 251,469 | \$ 262,748 |
| Less executory costs | 100,593 | 105,629 |
| Less interest | 64,963 | 71,121 |
| Less current portion at net present value | 5,000 | 4,208 |
| Present value of net minimum long-term lease payments | <u>\$ 80,913</u> | <u>\$ 81,790</u> |

Future minimum lease payments under capital lease obligations as of December 31, 2012 are as follows:

| | | |
|------------------------------|--|-------------------|
| Year ending December 31: | | |
| 2013 | | \$ 15,978 |
| 2014 | | 15,823 |
| 2015 | | 14,516 |
| 2016 | | 13,250 |
| 2017 | | 12,769 |
| Thereafter | | 179,133 |
| Total minimum lease payments | | <u>\$ 251,469</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

7. Debt (continued)

Short-Term Borrowings

Certain members of the System have entered into several unsecured revolving credit facilities with commercial banks. Borrowings are primarily used to provide interim financing for capital improvement projects, with repayment to be provided from bond proceeds and the receipt of fundraising proceeds from capital campaigns. Additionally, amounts can be used to provide backup financing for the support of the certificate of need process as required by NYSDOH and short-term working capital to support the monthly operating cash conversion cycle. Interest options include prime-based rates, LIBOR-based rates and bank cost of funds rates. Total credit under such arrangements was \$312,000 and \$266,000 at December 31, 2012 and 2011, respectively. Balances outstanding from borrowings are \$110,540 and \$90,540 at December 31, 2012 and 2011, respectively.

8. Third-party Payer Structured Liabilities

In 1999, Staten Island agreed to settle an outstanding matter with the New York State Attorney General. This matter related to Staten Island receiving payments at various part-time clinics during the period January 1, 1994 through August 31, 1998 at an enhanced rate known as Products of Ambulatory Care. As a result of this matter, Staten Island agreed to remit to the State of New York (the "State") the gross sum of \$41,200, payable over an extended period. Payments commenced in November 1999 and are being made monthly, totaling \$2,000 per year for 20 years. Included in third-party payer structured liabilities is the present value of this agreement based upon a 6% discount factor. For 2012 and 2011, payments made under such arrangement totaled \$2,000 for each year, including \$733 and \$807 recorded as interest expense in the accompanying consolidated statements of operations for 2012 and 2011, respectively. Additionally, in accordance with Staten Island's mission and commitment to provide uncompensated care, Staten Island agreed to continue to provide uncompensated care and services to individuals unable to pay for such services. Such uncompensated care and services shall have value, as defined in the agreement, of not less than \$1,950 per year for 20 years. As the provision of uncompensated care is not considered incremental to those uncompensated services already provided by Staten Island, no liability was recorded for such amounts. Staten Island was in compliance with such provision in 2012 and 2011.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

8. Third-party Payer Structured Liabilities (continued)

In 2005, Staten Island agreed to settle an action commenced by the New York State Attorney General. The settlement related to the recovery of prior Medicaid payments to Chaps Community Health Center, Inc., a subsidiary of Staten Island. Pursuant to the settlement, Staten Island agreed to remit to the State \$76,500. This amount includes approximately \$8,000 of Medicaid reimbursement previously withheld in 2004 by the State, in connection with its investigation of this matter. The remaining amounts are payable to the State over a 13-year period which began in 2005. Payments for 2011 were \$5,000. The payments for years 2012 through 2014 are \$5,500 per year. In 2015 and 2016, payments are \$3,000 each year, and the required payment for 2017 is \$4,000. Staten Island has recorded the present value of these settlement payments based upon a 6% discount factor in the accompanying consolidated statements of financial position. Payments made under this settlement for 2012 and 2011 totaled \$5,500 and \$5,000, respectively, including approximately \$1,328 and \$1,536 recorded as interest expense in the accompanying consolidated statements of operations for the years ended December 31, 2012 and 2011, respectively. As part of the 2005 settlement agreement, Staten Island adopted a number of managerial and operational reforms that will govern the conduct of Staten Island officers, employees and Board members. The amounts payable under the 2005 settlement agreement are in addition to the amounts which continue to be payable under the 1999 settlement discussed previously.

In 2008, Staten Island executed a settlement with the United States Department of Health and Human Services, Office of the Inspector General (the "HHS-OIG") and the New York State Attorney General's Office ("NYSAG") with respect to various issues. In settlement of the HHS-OIG claims, Staten Island has made a one-time payment of \$76,513. Staten Island funded the amount with a bank loan of \$60,000 (see Note 7) and the balance from operating cash. With respect to the NYSAG claim, Staten Island has agreed to make payments totaling \$12,400. Staten Island paid a lump-sum payment of \$6,200 and the remaining balance of \$6,200 was paid in equal amounts over a three-year period, which ended in 2011.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

8. Third-party Payer Structured Liabilities (continued)

In connection with the HHS-OIG and NYSAG settlement, Staten Island also entered into a five-year Corporate Integrity Agreement (“CIA”) with the HHS-OIG. This agreement obligates Staten Island to strengthen the current compliance program and implement certain management practices and initiatives. Such terms of this agreement include engaging an independent third party to act as an Independent Review Organization, enhancing the contract management policies and procedures, and expanding employee education. A material breach of the CIA could subject Staten Island to substantial monetary penalties and exclusion from participation in the Medicare and Medicaid programs. Management believes that Staten Island is in compliance with the terms and provisions of the CIA.

9. Fair Values of Financial Instruments

For assets and liabilities required to be measured at fair value, the System measures fair value based on 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. Fair value measurements are applied based on the unit of account from the System’s perspective. The unit of account determines what is being measured by reference to the level at which the asset or liability is aggregated (or disaggregated) for purposes of applying other accounting pronouncements.

The System follows a valuation hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

- Level 1:* Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets or liabilities.
- Level 2:* Observable inputs that are based on inputs not quoted in active markets, but corroborated by market data.
- Level 3:* Unobservable inputs are used when little or no market data is available.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

9. Fair Values of Financial Instruments (continued)

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. In determining fair value, the System uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible and considers nonperformance risk in its assessment of fair value.

A financial instrument's categorization within the three levels of the valuation hierarchy is not indicative of the investment risk associated with the underlying assets.

Financial assets and liabilities carried at fair value as of December 31, 2012 are classified in the following table in one of the three categories described previously:

| | 2012 | | | |
|---------------------------------|---------------------|-------------------|----------------|---------------------|
| | Level 1 | Level 2 | Level 3 | Total |
| Assets | | | | |
| Cash and short-term investments | \$ 407,147 | \$ — | \$ — | \$ 407,147 |
| Fixed income obligations: | | | | |
| U.S. Government obligations | 262,248 | 224,154 | — | 486,402 |
| Corporate and other bonds | — | 243,791 | — | 243,791 |
| Fixed income mutual funds | 555,249 | — | — | 555,249 |
| Equity securities: | | | | |
| Large cap | 145 | — | — | 145 |
| Small cap | 41,103 | — | — | 41,103 |
| International | 32,772 | — | — | 32,772 |
| Global | 189,126 | — | — | 189,126 |
| Equity mutual funds | 321,149 | — | — | 321,149 |
| Target-age mutual funds | 8,955 | — | — | 8,955 |
| Interest and other receivables | 1,196 | — | — | 1,196 |
| Liabilities | | | | |
| Interest rate swap agreements | — | (11,052) | — | (11,052) |
| | \$ 1,819,090 | \$ 456,893 | \$ — | \$ 2,275,983 |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

9. Fair Values of Financial Instruments (continued)

Financial assets and liabilities carried at fair value as of December 31, 2011 are classified in the following table in one of the three categories described previously:

| | 2011 | | | |
|---------------------------------|---------------------|-------------------|-------------|---------------------|
| | Level 1 | Level 2 | Level 3 | Total |
| Assets | | | | |
| Cash and short-term investments | \$ 655,943 | \$ – | \$ – | \$ 655,943 |
| Fixed income obligations: | | | | |
| U.S. Government obligations | 234,096 | 308,981 | – | 543,077 |
| Corporate and other bonds | – | 162,016 | – | 162,016 |
| Fixed income mutual funds | 402,553 | – | – | 402,553 |
| Equity securities: | | | | |
| Large cap | 1,040 | – | – | 1,040 |
| Small cap | 18,801 | – | – | 18,801 |
| International | 3 | – | – | 3 |
| Global | 123,141 | – | – | 123,141 |
| Equity mutual funds | 221,780 | – | – | 221,780 |
| Target-age mutual funds | 5,629 | – | – | 5,629 |
| Interest and other receivables | 4,421 | – | – | 4,421 |
| Liabilities | | | | |
| Interest rate swap agreements | – | (39,550) | – | (39,550) |
| | <u>\$ 1,667,407</u> | <u>\$ 431,447</u> | <u>\$ –</u> | <u>\$ 2,098,854</u> |

Fair value for Level 1 is based upon quoted market prices. Fair value for Level 2 is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets.

The amounts reported in the previous tables exclude investments reported under the equity method of accounting in the amounts of \$451,922 and \$334,793 at December 31, 2012 and 2011, respectively (see Note 2), and assets invested in the System's pension plans (see Note 10).

The fair values and carrying values of the System's financial instruments that are not required to be carried at fair value are as follows at December 31, 2012 and 2011:

| | 2012 | | 2011 | |
|--|--------------|----------------|--------------|----------------|
| | Fair Value | Carrying Value | Fair Value | Carrying Value |
| Debt (including short-term borrowings; excluding capital lease obligations) | \$ 1,745,358 | \$ 1,632,202 | \$ 1,546,039 | \$ 1,503,915 |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

9. Fair Values of Financial Instruments (continued)

The fair value of the System's bonds payable is based on quoted market prices for the related bonds. The fair value of other debt is based upon discounted cash flow analyses. Fair value of bonds payable at December 31, 2012 and 2011 is classified as Level 1 (\$1,487,384 and \$1,326,409, respectively), while fair value of other debt is classified as Level 2 (\$257,974 and \$219,630, respectively).

10. Pension Plans

The System maintains several pension plans for its employees. The following are descriptions of such plans and the respective pension expense for the years ended December 31, 2012 and 2011.

Certain members of the System provide pension and similar benefits to their employees through defined contribution plans. Contributions to the defined contribution plans are based on percentages of annual salaries. It is the policy of these members to fund accrued costs under these plans on a current basis. Pension expense for 2012 and 2011 related to the defined contribution plans amounted to \$88,049 and \$81,637, respectively.

Certain members of the System contribute to various multiemployer defined benefit pension plans under the terms of collective-bargaining agreements that cover union-represented employees. The risks of participating in these multiemployer plans are different from single-employer plans in the following aspects:

- a. Assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers.
- b. If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.
- c. If the System stops participating in any of its multiemployer plans, the System may be required to pay those plans an amount based on the underfunded status of the plan, referred to as a withdrawal liability.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The System’s significant participation in certain plans for the annual period ended December 31, 2012 is outlined in the following table. The following information for the 1199SEIU Health Care Employees Pension Fund (the “1199 Plan”) and the New York State Nurses Association Pension Plan (the “NYSNA Plan”) is included within the table:

- a. The “EIN/Pension Plan Number” column provides the plans’ Employee Identification Number (“EIN”) and the three-digit plan numbers.
- b. The “Pension Protection Act Zone Status” is based on information that the System received from the plans and is certified by the plans’ actuaries. Among other factors, plans in the red zone are generally less than 65% funded, plans in the yellow zone are less than 80% funded and plans in the green zone are at least 80% funded.
- c. The “FIP/RP Status Pending/Implemented” column indicates plans for which a financial improvement plan (“FIP”) or a rehabilitation plan (“RP”) is either pending or has been implemented.
- d. The last column lists the expiration dates of the collective bargaining agreements to which the plans are subject.

| Pension Fund | EIN/Pension Plan Number | Pension Protection Act Zone Status | | FIP/RP Status Pending/Implemented | Contributions of the System | | Surcharge Imposed | Expiration Date of Collective-Bargaining Agreements |
|----------------|-------------------------|------------------------------------|-------|-----------------------------------|-----------------------------|----------|-------------------|---|
| | | 2012 | 2011 | | 2012 | 2011 | | |
| 1199 Plan (a) | 13-3604862/ 001 | Green | Green | Implemented | \$46,781 | \$39,943 | No | 4/30/2015 |
| NYSNA Plan (b) | 13-6604799/ 001 | Green | Green | N/A | \$7,915 | \$7,887 | No | 10/13/2014, 12/31/2014 |

- (a) The 1199 Plan has implemented a rehabilitation plan for the period January 1, 2012 through December 31, 2024.
- (b) Retroactive to 2009, the NYSNA Plan changed its asset valuation method to amortize 2008 losses over ten years as allowed under the Pension Relief Act of 2010.
- (c) System 2011 contributions represent more than 5% of total contributions to the plans for the plan year ended December 31, 2011. Comparable plan-level contribution information for the plan year ended December 31, 2012 was not yet available at the time of financial statement issuance.

In addition to the plans noted in the table above, the System also participates in several other multiemployer plans. Contributions for these other plans totaled \$658 and \$555 for the years ended December 31, 2012 and 2011, respectively.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

Certain of the System's employees participate in deferred compensation plans. The liability for these plans totaled \$4,253 and \$3,904 at December 31, 2012 and 2011, respectively. In connection with these plans, the System deposits amounts with trustees on behalf of the participating employees. Under the terms of the plans, the System is not responsible for investment gains or losses incurred. The assets are restricted for payments under the plans, but may revert to the System under certain specified circumstances.

In addition, the System maintains various deferred compensation plans pursuant to Section 457(b) of the Code (the "457(b) Plans"). Eligible employees may defer compensation under a salary reduction agreement, subject to certain dollar limitations. Non-elective employer contributions may also be made for some of the 457(b) Plans. Payments upon retirement or termination of employment are based on amounts credited to the individual accounts. The assets and corresponding liability for the 457(b) Plans, included in assets limited as to use and accrued retirement benefits in the accompanying consolidated statements of financial position, totaled \$53,763 and \$41,763 at December 31, 2012 and 2011, respectively.

Certain employees, except for certain members of the medical staff and certain employees represented by collective bargaining agreements, are covered by noncontributory defined benefit plans (the "Plans"). Effective December 31, 2011, the Retirement Plan for Employees of Lenox Hill Hospital was merged into the System Cash Balance Plan. Effective August 31, 2012, the Doctor's Hospital of Staten Island Retirement Income Plan was merged into the System Cash Balance Plan. Effective December 31, 2012, the Huntington Hospital Pension Plan (the "Huntington Plan") was merged into the System Cash Balance Plan.

The System recognizes the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of the defined benefit plans in its consolidated statements of financial position.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The following tables provide a reconciliation of the changes in the Plans' projected benefit obligations and fair value of plan assets for the years ended December 31, 2012 and 2011 and statements of the funded status of the Plans as of December 31, 2012 and 2011:

| | <u>2012</u> | <u>2011</u> |
|---|---------------------|---------------------|
| Reconciliation of the projected benefit obligation | | |
| Obligation at January 1 | \$ 1,474,796 | \$ 1,302,959 |
| Inclusion of LIH obligation at Acquisition Date | 74,080 | — |
| Service cost | 53,732 | 47,449 |
| Interest cost | 78,707 | 75,762 |
| Plan amendments | 3,289 | 19,184 |
| Actuarial loss | 172,343 | 82,104 |
| Benefit payments | (64,622) | (52,662) |
| Obligation at December 31 | <u>\$ 1,792,325</u> | <u>\$ 1,474,796</u> |
| Reconciliation of fair value of plan assets | | |
| Fair value of plan assets at January 1 | \$ 1,035,695 | \$ 955,005 |
| Inclusion of LIH plan assets at Acquisition Date | 49,150 | — |
| Actual return on plan assets | 123,701 | 2,698 |
| Employer contributions | 92,849 | 130,654 |
| Benefit payments | (64,622) | (52,662) |
| Fair value of plan assets at December 31 | <u>\$ 1,236,773</u> | <u>\$ 1,035,695</u> |
| Funded status | | |
| Funded status at December 31 | <u>\$ (555,552)</u> | <u>\$ (439,101)</u> |
| Accumulated benefit obligation | <u>\$ 1,655,292</u> | <u>\$ 1,371,148</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The current portion of accrued retirement benefits related to the Plans, included in accrued salaries and related benefits in the accompanying consolidated statements of financial position, is \$4,047 and \$1,467 at December 31, 2012 and 2011, respectively.

As a result of the System's acquisition of The Long Island Home as disclosed in Note 1, the benefit obligation and plan assets of The Retirement Plan for Employees of The Long Island Home were included in the System's reporting as of the Acquisition Date.

Plan amendments in 2012 relate to new groups becoming eligible to accrue benefits under the System Cash Balance Plan.

Plan amendments in 2011 relate to the expansion of the System's Supplemental Executive Retirement Plans to cover additional employees.

The actuarial losses in 2012 and 2011 are primarily due to the decrease in the discount rate.

Included in unrestricted net assets at December 31, 2012 and 2011 are the following amounts that have not yet been recognized in net periodic benefit cost:

| | 2012 | | |
|--|--------------------------------------|---|---------------------|
| | Defined Benefit Plans | Postretirement Benefit Plans (see Note 11) | Total |
| Unrecognized actuarial (loss) gain | \$ (459,394) | \$ 30,844 | \$ (428,550) |
| Unrecognized prior service (cost) credit | (25,335) | 8,411 | (16,924) |
| | <u>\$ (484,729)</u> | <u>\$ 39,255</u> | <u>\$ (445,474)</u> |
| | 2011 | | |
| | Defined Benefit Plans | Postretirement Benefit Plans (see Note 11) | Total |
| Unrecognized actuarial loss | \$ (349,711) | \$ (1,674) | \$ (351,385) |
| Unrecognized prior service (cost) credit | (25,925) | 10,376 | (15,549) |
| | <u>\$ (375,636)</u> | <u>\$ 8,702</u> | <u>\$ (366,934)</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The following table provides the components of the net periodic benefit cost for the Plans for the years ended December 31, 2012 and 2011:

| | 2012 | 2011 |
|---|------------------|------------------|
| Service cost | \$ 53,732 | \$ 47,449 |
| Interest cost on projected benefit obligation | 78,707 | 75,762 |
| Expected return on plan assets | (83,232) | (79,857) |
| Amortization of net loss | 21,719 | 7,889 |
| Amortization of prior service cost | 3,880 | 3,328 |
| Settlement loss | 471 | - |
| Net periodic benefit cost | <u>\$ 75,277</u> | <u>\$ 54,571</u> |

The net loss (gain) and prior service cost (credit) included in unrestricted net assets expected to be recognized in net periodic benefit cost during the year ended December 31, 2013 are as follows:

| | Defined Benefit Plans | Postretirement Benefit Plans (see Note 11) | Total |
|--|--------------------------------------|---|------------------|
| Net loss (gain) | \$ 27,990 | \$ (1,638) | \$ 26,352 |
| Prior service cost (credit) | 3,686 | (1,732) | 1,954 |
| Increase (decrease) to net periodic benefit cost | <u>\$ 31,676</u> | <u>\$ (3,370)</u> | <u>\$ 28,306</u> |

Assumptions

Prior service costs are amortized over the average remaining service period of active participants. Gains and losses in excess of 10% of the greater of the projected benefit obligations and the market-related value of assets are amortized over the average remaining service period of active participants.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The range of weighted-average assumptions used in the measurement of the System's benefit obligations at December 31, 2012 and 2011 are shown in the following table:

| | <u>2012</u> | <u>2011</u> |
|-------------------------------|----------------------|---------------|
| Discount rate | 2.65% – 4.15% | 3.25% – 5.20% |
| Rate of compensation increase | 0.00% – 4.00% | 0.00% – 4.50% |

The range of weighted-average assumptions used in the measurement of the System's net periodic benefit cost for the years ended December 31, 2012 and 2011 are shown in the following table:

| | <u>2012</u> | <u>2011</u> |
|--|----------------------|---------------|
| Discount rate | 3.50% – 5.20% | 3.25% – 6.00% |
| Expected long-term rate of return on plan assets | 7.75% | 8.00% |
| Rate of compensation increase | 0.00% – 4.50% | 0.00% – 4.50% |

Estimated Future Benefit Payments

Benefit payments, which reflect expected future service, as appropriate, are expected to be paid as follows:

| | |
|--------------|-----------|
| 2013 | \$ 66,605 |
| 2014 | 80,405 |
| 2015 | 74,833 |
| 2016 | 84,247 |
| 2017 | 85,576 |
| 2018 to 2022 | 509,465 |

Cash Flows

The System expects to make contributions of approximately \$106,000 to the Plans in 2013.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The fair values of the Plans' assets at December 31, 2012, by asset category, are as follows:

| Asset Category | Level 1 | Level 2 | Level 3 | Total |
|---------------------------------|-------------------|-------------------|------------------|---------------------|
| Cash and short-term investments | \$ 32,600 | \$ - | \$ - | \$ 32,600 |
| Fixed income obligations: | | | | |
| U.S. Government obligations | 11,035 | 31,859 | - | 42,894 |
| Corporate and other bonds | - | 99,493 | - | 99,493 |
| Fixed income mutual funds | 165,153 | - | - | 165,153 |
| Commingled fixed income funds | - | 103,983 | - | 103,983 |
| Equity securities: | | | | |
| Large cap | 48,745 | - | - | 48,745 |
| Small cap | 28,054 | - | - | 28,054 |
| International | 45,187 | - | - | 45,187 |
| Global | 135,359 | - | - | 135,359 |
| Equity mutual funds | 139,622 | - | - | 139,622 |
| Commingled equity funds: | | | | |
| Large cap | - | 74,611 | - | 74,611 |
| Small cap | - | 24,058 | - | 24,058 |
| International | - | 52,373 | - | 52,373 |
| Commingled commodity funds | - | 26,961 | - | 26,961 |
| Alternative investments: | | | | |
| Funds of hedge funds | - | 186,173 | - | 186,173 |
| Hedge funds | - | 6,840 | - | 6,840 |
| Private equity funds | - | - | 9,667 | 9,667 |
| Private real estate funds | - | - | 13,145 | 13,145 |
| Interest and other receivables | 1,855 | - | - | 1,855 |
| | \$ 607,610 | \$ 606,351 | \$ 22,812 | \$ 1,236,773 |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The fair values of the Plans' assets at December 31, 2011, by asset category, are as follows:

| Asset Category | Level 1 | Level 2 | Level 3 | Total |
|---------------------------------|----------------|----------------|----------------|--------------|
| Cash and short-term investments | \$ 48,844 | \$ – | \$ – | \$ 48,844 |
| Fixed income obligations: | | | | |
| U.S. Government obligations | 89,085 | 46,523 | – | 135,608 |
| Corporate and other bonds | – | 87,584 | – | 87,584 |
| Fixed income mutual funds | 69,155 | – | – | 69,155 |
| Commingled fixed income funds | – | 77,101 | – | 77,101 |
| Equity securities: | | | | |
| Large cap | 47,542 | – | – | 47,542 |
| Small cap | 13,716 | – | – | 13,716 |
| International | 37,164 | – | – | 37,164 |
| Global | 86,522 | – | – | 86,522 |
| Equity mutual funds | 138,598 | – | – | 138,598 |
| Commingled equity funds: | | | | |
| Large cap | – | 42,949 | – | 42,949 |
| Small cap | – | 13,831 | – | 13,831 |
| International | – | 26,764 | – | 26,764 |
| Emerging markets | – | 14,701 | – | 14,701 |
| Commingled commodity funds | – | 12,091 | – | 12,091 |
| Alternative investments: | | | | |
| Funds of hedge funds | – | 151,430 | – | 151,430 |
| Hedge funds | – | 14,185 | – | 14,185 |
| Private equity funds | – | – | 8,645 | 8,645 |
| Private real estate funds | – | – | 5,658 | 5,658 |
| Interest and other receivables | 3,607 | – | – | 3,607 |
| | \$ 534,233 | \$ 487,159 | \$ 14,303 | \$ 1,035,695 |

Most investments classified in Levels 2 and 3 in the above tables consist of shares or units in investment funds, as opposed to direct interests in the funds' underlying holdings, which may be marketable. The classification of investments in the fair value hierarchy is not indicative of the investment risk associated with the underlying assets.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The following is a summary of assets in the Plans at December 31, 2012 (by asset category) with redemption restrictions:

| | Fair Value | Redemption Period (Including Notice Period) |
|-------------------------------|-------------------|--|
| Commingled fixed income funds | \$ 103,983 | 1 day to 5 days |
| Commingled equity funds | 151,042 | 3 days to 51 days |
| Commingled commodity funds | 26,961 | 11 days to 40 days |
| Funds of hedge funds | 186,173 | 110 days to 299 days |

Hedge fund investments of the Plans are in the process of being fully redeemed at December 31, 2012. Private equity and private real estate funds have long lifecycles with distributions not expected for several years. In the instance of certain redemptions, some investments noted above may require an extended waiting period to receive a remainder portion of the redemption.

The following table sets forth a summary of changes in the fair value of the Plans' Level 3 assets for the years ended December 31, 2012 and 2011:

| | 2012 | 2011 |
|---|------------------|------------------|
| Fair value at January 1 | \$ 14,303 | \$ 6,404 |
| Purchases | 5,533 | 8,979 |
| Sales | (2,655) | (1,226) |
| Net realized and unrealized gains and losses | 1,055 | 146 |
| Acquisition of The Long Island Home plan assets | 4,576 | - |
| Fair value at December 31 | <u>\$ 22,812</u> | <u>\$ 14,303</u> |

Basis Used to Determine the Expected Long-Term Rate of Return on Assets

The overall expected long-term rate of return on assets assumption is based upon a long-term building-block approach adjusted for current market conditions. First, return expectations for each asset class are developed with economic and fundamental drivers such as inflation, dividends and real earnings growth for stocks and real yields, defaults and recoveries for bonds. These expectations assume that market levels at the beginning of the forecast period are in a state of equilibrium. With the understanding that markets are more often than not in some state of disequilibrium, the "next ten year" return forecasts are adjusted to reflect the starting point for inflation expectations, interest rate levels and market risk premiums relative to historically normal market levels.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The fundamental building blocks used to develop the long-term equilibrium return expectations are based on a combination of consensus forecasts and long-term historical averages. The historical data is adjusted to reflect any fundamental changes that have occurred in the relative markets.

Once long-term equilibrium forecasts are developed, returns are adjusted for the next ten years to reflect the current environment as it relates to the key economic variables that influence returns across the capital markets. In doing so, the expected path for breakeven inflation, real interest rates and investment grade corporate bond spreads are modeled for the next ten years. In this framework, the investment grade corporate spreads are used as a proxy for the risk premium priced broadly into all asset classes within the capital markets.

While the precise expected return derived using the above approach will fluctuate somewhat from year to year, the Plans' policy is to hold this long-term assumption constant as long as it remains within a reasonable tolerance from the derived rate.

Description of Investment Policies and Strategies

The Plans' overall investment strategy is to achieve wide diversification of asset types, fund strategies, and fund managers. Equity securities include investments in domestic, international, global and emerging markets equities. Fixed income securities include corporate bonds of companies from diversified industries, mortgage-backed securities, emerging markets debt and U.S. Treasuries. Other types of investments include investments in commingled commodity funds and alternative investments that follow several different strategies.

There are specific guidelines and diversification standards for each investment manager. Eligible investments are specifically outlined. Each manager must disclose its strategies and report that it abides by the Employee Retirement Income Security Act of 1974 ("ERISA") rules, where applicable.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

10. Pension Plans (continued)

The Plans' weighted average asset allocations at December 31, 2012 and 2011, by asset category, are as follows:

| | 2012 | 2011 | Target Allocation |
|--|---------------|-------------|------------------------------|
| Cash and short-term investments | 2.8% | 5.4% | 1.0% |
| Fixed income obligations | 33.2 | 35.7 | 34.0 |
| Equity securities, including commingled equity funds | 44.3 | 36.7 | 40.0 |
| Commingled commodity funds | 2.2 | 1.4 | 3.0 |
| Alternative investments | 17.5 | 20.8 | 22.0 |
| | 100.0% | 100.0% | 100.0% |

Target allocations generally have permitted variances of plus/minus 5 points.

Subsequent to the Huntington Plan's merger into the System Cash Balance Plan, the System began the process of aligning the allocation of the assets from the Huntington Plan to the System's target allocations noted above. Assets from the Huntington Plan are in the process of being redeemed and reinvested to more closely attain the above noted target allocation.

11. Postretirement Benefits Other than Pensions

Certain employees are covered by the North Shore-Long Island Jewish Health System Retiree Medical and Life Insurance Plan (the "NS-LIJ Plan") and other postretirement benefit plans.

The NS-LIJ Plan is contributory with a 2% per year service subsidy up to 30 years (maximum 60%) for non-union employees hired prior to January 1, 2001. The subsidy for future retirees is as follows: for pre-65 retirees, a 2% per year service subsidy for years of service through 2000 and a 1% per year service subsidy for years of service for 2001 and thereafter, up to 30 years. For post-65 retirees, a 1% per year service subsidy for years of service through 2000 and a 0.5% per year service subsidy for years of service for 2001 and thereafter, up to 30 years. For non-union employees hired after January 1, 2001, the NS-LIJ Plan provides a defined dollar benefit subsidy of \$2,500 per year prior to age 65 and \$1,000 per year age 65 and later. To be eligible for the medical benefits, the employee must be at least 55 years old and be employed for at least fifteen years or after age 65, be employed for at least five years. Only pre-1994 retirees are eligible for the life insurance benefits. The life insurance benefit is not available to active employees. The NS-LIJ Plan is unfunded.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

11. Postretirement Benefits Other than Pensions (continued)

The following tables provide a reconciliation of the changes in the plans' benefit obligations and fair value of plan assets for the years ended December 31, 2012 and 2011 and a statement of the funded status of the plans as of December 31, 2012 and 2011:

| | <u>2012</u> | <u>2011</u> |
|--|--------------------|--------------------|
| Reconciliation of the benefit obligation | | |
| Obligation at January 1 | \$ 78,037 | \$ 90,513 |
| Inclusion of LIH obligation at Acquisition Date | 2,084 | – |
| Service cost | 2,179 | 2,423 |
| Interest cost | 4,040 | 5,048 |
| Plan participants' contributions | 2,233 | 2,488 |
| Plan amendments | 213 | 1,018 |
| Actuarial gain | (32,532) | (20,035) |
| Benefit payments | (3,782) | (3,806) |
| Federal subsidy on benefits paid | 388 | 388 |
| Obligation at December 31 | <u>\$ 52,860</u> | <u>\$ 78,037</u> |
| Reconciliation of fair value of plan assets | | |
| Fair value of plan assets at January 1 | \$ – | \$ – |
| Employer contributions | 1,549 | 1,318 |
| Plan participants' contributions | 2,233 | 2,488 |
| Benefit payments | (3,782) | (3,806) |
| Fair value of plan assets at December 31 | <u>\$ –</u> | <u>\$ –</u> |
| Funded status | | |
| Funded status at December 31 | <u>\$ (52,860)</u> | <u>\$ (78,037)</u> |

The current portion of accrued retirement benefits related to the plans, included in accrued salaries and related benefits in the accompanying consolidated statements of financial position, is \$2,025 and \$2,553 at December 31, 2012 and 2011, respectively.

The actuarial gains in 2012 and 2011 are primarily due to decreases in the actuarial assumption for the medical plan participation rate for future retirees, combined with favorable demographic and claims experience, partially offset by decreases in discount rates.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

11. Postretirement Benefits Other than Pensions (continued)

The following table provides the components of the net periodic benefit cost for the plans for the years ended December 31, 2012 and 2011:

| | <u>2012</u> | <u>2011</u> |
|--------------------------------------|-----------------|-----------------|
| Service cost | \$ 2,179 | \$ 2,423 |
| Interest cost on benefit obligation | 4,040 | 5,048 |
| Amortization of net (gain) loss | (11) | 758 |
| Amortization of prior service credit | (1,753) | (1,841) |
| Net periodic benefit cost | <u>\$ 4,455</u> | <u>\$ 6,388</u> |

Assumptions

The range of weighted-average discount rates used in the measurement of benefit obligations for the plans was 3.55% to 4.15% and 4.65% to 5.20% at December 31, 2012 and 2011, respectively. The range of weighted-average discount rates used in the measurement of net periodic benefit costs for the plans was 4.40% to 5.20% and 5.00% to 6.00% for 2012 and 2011, respectively.

Assumed Health Care Cost Trends

The assumed health care cost trend rates used in measuring the postretirement benefit obligation for the plans for 2012 and 2011 are as follows:

| | <u>2012</u> | <u>2011</u> |
|---|-------------|-------------|
| Health care cost trend rate assumed for next year | 7.50% | 8.00% |
| Rate to which the cost trend rate is assumed to decline (the ultimate trend rate) | 5.00% | 5.00% |
| Year that the rate reaches the ultimate trend rate | 2017 | 2018 |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

11. Postretirement Benefits Other than Pensions (continued)

Assumed health care cost trend rates have a significant effect on the amounts reported. A 1% change in assumed health care cost trend rates would have the following effects on the plans:

| | 2012 | | 2011 | |
|---|----------------|----------------|----------------|----------------|
| | 1% Increase | 1% Decrease | 1% Increase | 1% Decrease |
| Effect on total of service and interest cost components of net periodic postretirement health care benefit cost | \$ 486 | \$ (410) | \$ 466 | \$ (391) |
| Effect on the health care component of the postretirement benefit obligation | 4,371 | (3,653) | 6,928 | (5,822) |

Estimated Future Benefit Payments

Benefit payments, which reflect expected future service, as appropriate, are expected to be paid as follows:

| | |
|--------------|----------|
| 2013 | \$ 2,524 |
| 2014 | 2,629 |
| 2015 | 2,758 |
| 2016 | 2,864 |
| 2017 | 2,984 |
| 2018 to 2022 | 16,299 |

Prescription Drug Benefits

The Medicare Prescription Drug, Improvement and Modernization Act of 2003 provides for a prescription drug benefit under Medicare (“Medicare Part D”), as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. The expected subsidy reduced the accumulated postretirement benefit obligation at December 31, 2012 and 2011 by \$5,468 and \$5,103, respectively. The subsidy did not have a material impact on net periodic postretirement benefit cost for the 2012 and 2011 plan years.

North Shore-Long Island Jewish Health System, Inc.
Notes to Consolidated Financial Statements (continued)
(In Thousands)

11. Postretirement Benefits Other than Pensions (continued)

Expected federal subsidies to be received in future years for the plans are as follows:

| | | |
|--------------|----|-------|
| 2013 | \$ | 400 |
| 2014 | | 462 |
| 2015 | | 533 |
| 2016 | | 610 |
| 2017 | | 632 |
| 2018 to 2022 | | 2,368 |

12. Malpractice and Other Insurance Liabilities

Malpractice

The System's hospitals provide for potential medical malpractice losses through a combination of a self-insurance program and purchased primary and excess insurance, on both a claims-made and occurrence basis, as follows:

Primary Insurance Coverage

Effective January 1, 2003, the System purchases primary malpractice insurance on an occurrence basis. The policy provides coverage with limits of \$1,000 per claim and a \$50,000 annual policy in the aggregate through 2009. Effective 2010, the program retained \$750 of the primary coverage per indemnity claim, while aggregate limits increased to \$60,000.

From January 1, 1997 to December 31, 2002, the System's hospitals primarily participated in a combined insurance program, which provided coverage on a claims-made basis. In December 2002, the System purchased a tail insurance policy to cover unreported occurrences from these prior claims-made policy periods.

The estimated undiscounted liability for the retained primary coverage and losses in excess of the primary aggregate at December 31, 2012 and 2011 is \$330,146 and \$272,022, respectively. At December 31, 2012 and 2011, the liability is recorded at the actuarially determined present value of \$298,015 and \$244,992, respectively, based on a discount rate of 2.0%.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

12. Malpractice and Other Insurance Liabilities (continued)

Excess Insurance Coverage

Regional Insurance covers excess malpractice losses above the primary per claim limit, on a claims-made basis. Regional Insurance purchases reinsurance coverage for certain excess coverage layers. Reinsurance balances recoverable, included in other assets in the accompanying consolidated statements of financial position, are \$28,970 and \$39,394 at December 31, 2012 and 2011, respectively.

Regional Insurance's estimated undiscounted reserves for losses and loss expenses outstanding at December 31, 2012 and 2011 were \$338,592 and \$311,702, respectively, and are recorded at the actuarially determined present value of \$311,978 and \$289,658, respectively, based on a discount rate of 2.0%.

The estimated undiscounted incurred but not reported liability for claims in excess of primary layers at December 31, 2012 and 2011 was \$91,813 and \$85,442, respectively, and is recorded at the actuarially determined present value of \$79,097 and \$73,699, respectively, based on a discount rate of 2.0%.

Self-Insurance Coverage

For certain years, certain System hospitals were covered for malpractice claims under self-insured arrangements. For self-insured claims and incidents, the System has accrued \$1,100 at both December 31, 2012 and 2011, based on actuarial determinations and other analyses, as its best estimates of the ultimate cost of such losses.

RRG provides medical malpractice coverage to certain employed and voluntary physicians affiliated with the System. RRG's liability for insured losses and related expenses is \$9,109 and \$7,168 at December 31, 2012 and 2011, respectively. RRG purchases reinsurance for certain layers of coverage. Reinsurance balances recoverable, included in other assets in the accompanying consolidated statements of financial position, are \$3,366 and \$3,347 at December 31, 2012 and 2011, respectively.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

12. Malpractice and Other Insurance Liabilities (continued)

Certain coverage for LIJMC has been provided through participation in a pooled program with certain other health care facilities. This participation is with captive insurance companies and commercial insurance companies. LIJMC previously retained ownership in the captive insurance companies associated with this program. LIJMC accounted for its interest primarily using the equity method of accounting. In 2011, LIJMC sold its interest in these companies for approximately \$39,600, with approximately \$9,600 paid at the time of sale and the remaining amount to be paid in three equal, annual installments through June 2014, with interest at the prime rate. Amounts due to LIJMC, including accrued interest, are recorded within other current assets (\$10,325 and \$10,271) and other assets (\$10,000 and \$20,000) in the accompanying consolidated statements of financial position at December 31, 2012 and 2011, respectively.

Malpractice claims have been asserted against System hospitals by various claimants. These claims are in various stages of processing, and some may ultimately be brought to trial. There are known incidents that have occurred through December 31, 2012 that may result in the assertion of additional claims, and other claims may be asserted arising from services provided to patients in the past. It is the opinion of the System's management that adequate insurance, including self-insurance, and malpractice reserves are being maintained to cover potential malpractice losses.

Workers' Compensation

Lenox has a self-insured program for workers' compensation claims since 1979 that includes excess insurance coverage for claims above certain amounts. At December 31, 2012 and 2011, the liability for the self-insured losses is recorded at the actuarially determined present value of \$11,857 and \$11,478, respectively, based on a discount rate of 2.0%.

The Long Island Home participated in a self-insurance trust (the "Trust") administered through the New York Association of Homes and Services for the Aging, along with other New York not-for-profit facilities to provide its workers' compensation insurance. The Trust provides a retrospectively rated insurance policy to its policy holders. The Long Island Home resigned from the Trust effective June 30, 2011. Effective December 31, 2011, the Trust ceased operations and is currently in a run-off phase. Under the terms of the Trust, the policy holders are responsible for the obligations of the Trust until all claims are fully matured. At December 31, 2012, a liability for retrospective premium adjustments is recorded at the actuarially determined present value of \$1,594.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

13. Other Operating Revenue

Other operating revenue consists of the following for the years ended December 31, 2012 and 2011:

| | <u>2012</u> | <u>2011</u> |
|---|-------------------|-------------------|
| Grants and contracts | \$ 87,711 | \$ 85,944 |
| Laboratory and other ancillary services | 109,281 | 89,878 |
| Electronic Health Record meaningful use revenue | 18,757 | — |
| Health plan risk pool distributions | 9,203 | 1,650 |
| Group purchasing rebates | 9,271 | 8,136 |
| Miscellaneous | 22,028 | 21,353 |
| Rental income | 15,063 | 14,945 |
| Cafeteria sales and vending machines | 12,524 | 14,000 |
| Insurance recoveries | 7,993 | — |
| Parking garage | 3,998 | 3,955 |
| Insurance premium revenue | 2,864 | 1,636 |
| Telephone and television | 1,482 | 1,987 |
| Resident rotation | 2,516 | 2,101 |
| | <u>\$ 302,691</u> | <u>\$ 245,585</u> |

14. Net Assets

Temporarily restricted net assets at December 31, 2012 and 2011 are available for the following health care services:

| | <u>2012</u> | <u>2011</u> |
|--|-------------------|-------------------|
| Teaching, research, training and other | \$ 184,652 | \$ 143,572 |
| Major modernization and purchases of equipment | 157,017 | 184,891 |
| | <u>\$ 341,669</u> | <u>\$ 328,463</u> |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

14. Net Assets (continued)

The System follows the requirements of the New York Prudent Management of Institutional Funds Act (“NYPMIFA”) passed into law effective September 2010 as they relate to its permanently restricted endowments. Prior to the enactment of the law, the System followed the requirements of the Uniform Management of Institutional Funds Act (“UMIFA”). The System has interpreted NYPMIFA, which did not have a significant effect on the System’s endowment policies that were in effect prior to the enactment, as requiring the preservation of the fair value of the original gift, as of the gift date, of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the System classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment funds.

The System’s endowments consist of donor-restricted funds established for a variety of purposes. As required by U.S. generally accepted accounting principles, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The System requires the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the System classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment funds that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure. The System considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the fund, (2) the purpose of the donor-restricted endowment fund, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments, and (6) the investment policies of the System.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

14. Net Assets (continued)

The System's investment and spending policies for endowment assets seek to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the System must hold in perpetuity or for a donor-specified term. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that expects to generate an average annual return in excess of 5.0%. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate-of-return objectives, the System relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The System targets a diversified asset allocation that consists of equities, fixed income and alternative investments.

The System has a policy of appropriating for distribution each year, no more than a 5% return on its endowment funds' corpus. In establishing this policy, the System considered the long-term expected return on its endowments.

For the year ended December 31, 2012, the System had the following endowment-related activities:

| | 2012 | | |
|--|-----------------------------------|-----------------------------------|--------------|
| | Temporarily Restricted | Permanently Restricted | Total |
| Endowment balance, beginning of year | \$ 5,339 | \$ 125,003 | \$ 130,342 |
| Investment return: | | | |
| Investment income | 2,728 | – | 2,728 |
| Net appreciation | 12,900 | – | 12,900 |
| Recovery of fair value of endowment corpus | – | 696 | 696 |
| Total investment return | 15,628 | 696 | 16,324 |
| Contributions | – | 3,212 | 3,212 |
| Amounts appropriated for expenditure | (4,443) | – | (4,443) |
| Net change in endowment funds | 11,185 | 3,908 | 15,093 |
| Endowment balance, end of year | \$ 16,524 | \$ 128,911 | \$ 145,435 |

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

14. Net Assets (continued)

For the year ended December 31, 2011, the System had the following endowment-related activities:

| | 2011 | | |
|--|-----------------------------------|-----------------------------------|--------------|
| | Temporarily Restricted | Permanently Restricted | Total |
| Endowment balance, beginning of year | \$ 9,724 | \$ 121,216 | \$ 130,940 |
| Investment return: | | | |
| Investment income | 2,068 | – | 2,068 |
| Net depreciation | (3,263) | – | (3,263) |
| Loss of fair value of endowment corpus | – | (194) | (194) |
| Total investment return | (1,195) | (194) | (1,389) |
| Contributions | – | 3,981 | 3,981 |
| Amounts appropriated for expenditure | (3,190) | – | (3,190) |
| Net change in endowment funds | (4,385) | 3,787 | (598) |
| Endowment balance, end of year | \$ 5,339 | \$ 125,003 | \$ 130,342 |

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the System to retain as a fund of perpetual duration. Deficiencies of this nature that are reported in unrestricted net assets were \$696 as of December 31, 2011. These deficiencies resulted from unfavorable market fluctuations. The individual donor-restricted endowment funds with deficiencies will retain future income and appreciation to restore the required fair value of the assets. There was no such deficiency as of December 31, 2012.

15. Commitments and Contingencies

Litigation, Claims and Settlements

In 2008, prior to the System’s acquisition of Lenox, Lenox received an administrative subpoena issued by the HHS-OIG, working in coordination with the Civil Division of the Office of the United States Attorney for the Southern District of New York (the “USAO/SDNY”). The subpoena requested documents and other information relating to Medicare outlier payments received by Lenox on Medicare claims submitted for the years 1997 to 2003. Lenox provided the information required by the subpoena, and in May 2012, the parties entered into a settlement agreement with no material impact on the consolidated financial statements.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

15. Commitments and Contingencies (continued)

In 2010, NSUH, the System and certain of their employees received Civil Investigative Demands issued by the USAO/SDNY relating to NSUH's clinical documentation improvement ("CDI") program for the period from 2003 to the present. The CDI program relates to the method by which NSUH and certain other System hospitals seek to ensure compilation of clear, complete, accurate and timely inpatient medical records. The System has produced documents and provided witnesses as required by the Civil Investigative Demands. The ultimate effect of this matter, if any, on the consolidated financial statements cannot currently be determined.

The System is involved in other litigation and claims which are not considered unusual to the System's business. While the ultimate outcome of these lawsuits cannot be determined at this time, it is the opinion of management that the ultimate resolution of these claims will not have a material adverse effect on the accompanying consolidated financial statements.

Operating Leases

The System leases certain office facility space, patient care facility space and equipment under operating leases that have initial or remaining noncancelable terms in excess of one year. Aggregate minimum operating lease payments are amortized on the straight-line basis over the terms of the respective leases. Rent expense under such leases is \$69,286 and \$68,351 for 2012 and 2011, respectively.

Future minimum lease payments under noncancelable operating leases with terms of one year or more are as follows:

| | |
|------------|-----------|
| 2013 | \$ 66,366 |
| 2014 | 57,378 |
| 2015 | 52,781 |
| 2016 | 48,359 |
| 2017 | 44,231 |
| Thereafter | 230,794 |

Collective Bargaining Agreements

At December 31, 2012, approximately 40% of the System's employees are union employees who are covered under the terms of various collective bargaining agreements. Certain collective bargaining agreements, which represent approximately 6% of union employees (3% of total employees), have expired, or will expire, within the next year and are currently being renegotiated.

North Shore-Long Island Jewish Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(In Thousands)

15. Commitments and Contingencies (continued)

Other Commitments

In March 2008, Hofstra University (the “University”) and the System entered into a joint academic agreement to work in close collaboration in the development of a medical school at the University (the “Medical School”), while remaining as separate corporations with separate governance. In June 2010, the Medical School, known as the Hofstra North Shore-LIJ School of Medicine, received preliminary accreditation from the Liaison Committee on Medical Education, as well as final approval of its education program from the New York State Education Department Division of Professional Education. The Medical School began accepting applications in 2010, and an initial class of 40 students began their studies in August 2011. Through June 30, 2017, the System shall provide up to \$50,000 to the University as reimbursement for a portion of the Medical School’s annual costs. Reimbursement payments after June 30, 2017 will be a minimum of \$5,000 for each academic year, with amounts indexed to the Medical School tuition. Reimbursement payments are contingent upon annual approval by the boards of the System and the University. The System shall not advance funds to the University that have not yet been spent in connection with the Medical School. To date, the System has recorded approximately \$27,500 of these costs related to the Medical School. The System also provides \$2,000 annually for funding of Medical School scholarships and up to \$2,000 annually for funding of student loans, with amounts indexed to the Medical School tuition.

In the normal course of business, the System enters into multi-year contracts with vendors, suppliers and service providers for goods or services to be provided to the System. Under the terms of such agreements, the System may be contingently liable for termination or other fees in the event of contract termination or default. The System does not believe that such contingent liabilities, should they become due, would have a material impact on the System’s consolidated financial position.

16. Subsequent Events

Management has evaluated the impact of subsequent events through April 15, 2013 representing the date at which the consolidated financial statements were issued. Except as disclosed in Note 7, no events have occurred that require disclosure in, or adjustment to, the consolidated financial statements.

Supplementary Information and Audit Reports
and Schedules Related to Office of Management
and Budget Circular A-133

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards

Year Ended December 31, 2012

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|--|---|---------------------------|-------------------------|
| Research and Development Cluster | | | |
| U.S. Department of Health and Human Services | | | |
| Direct grants and contracts: | | | |
| National Institutes of Health | 93.121, 93.173, 93.213, 93.226, 93.242, 93.262, 93.273, 93.279, 93.281, 93.351, 93.389, 93.393, 93.396, 93.399, 93.610, 93.HHSN-271-2009-00019C, 93.837 93.839, 93.846, 93.847, 93.853, 93.855, 93.859, 93.866 | | \$ 27,796,315 |
| ARRA – Trans-NIH Recovery Act Research Support | 93.701 | | <u>1,516,449</u> |
| Subtotal direct grants and contracts | | | <u>29,312,764</u> |
| Pass-through programs: | | | |
| Seattle Children’s Hospital: | | | |
| Food and Drug Administration Research | 93.103 | 1R01FD003526 | 6,745 |
| Duke University: | | | |
| Arthritis, Musculoskeletal and Skin Diseases Research | 93.846 | N01-AR-2-2265 | 32,004 |
| Case Western Reserve University: | | | |
| Best Pharmaceuticals for Children Act Pediatric Off-Patent Drug Study (PODS) | 93.HHSN275200503406C | HHSN275200503406C | 237,307 |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|---|------------------------|---------------------------|-------------------------|
| Research and Development Cluster (continued) | | | |
| U.S. Department of Health and Human Services (continued) | | | |
| Pass-through programs (continued): | | | |
| University of California San Francisco: Allergy, Immunology and Transplantation Research | 93.855 | N01-AI-15416 | \$ 109,866 |
| Cincinnati Children's Hospital: Arthritis, Musculoskeletal and Skin Diseases Research | 93.846 | N01AR042272 | 2,901 |
| Icahn School of Medicine at Mount Sinai: Maternal and Child Health Federal Consolidated Programs | 93.110 | 5H30MC00019-20-00/ | 85,437 |
| NYU School of Medicine: Environmental Health | 93.113 | 1R01ES014387-03 | 51,171 |
| University of Alabama: Oral Diseases And Disorders Research | 93.121 | N01-A1-30025 | 37,662 |
| Research Foundation for Mental Hygiene: Research Related To Deafness And Communication Disorders | 93.173 | 1R01DC007658 | 20,000 |
| Icahn School of Medicine at Mount Sinai: Research and Training in Complementary and Alternative Medicine | 93.213 | 1P01AT004511-01 | 126,213 |
| Research Foundation of the State University: Mental Health Research Grants | 93.242 | 1R01MH080050-02 | 197,996 |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|---|------------------------|---------------------------|-------------------------|
| Research and Development Cluster (continued) | | | |
| U.S. Department of Health and Human Services (continued) | | | |
| Pass-through programs (continued): | | | |
| Research Foundation for Mental Hygiene: Mental Health Research Grants | 93.242 | 1P50 MH086385-02 | \$ 201,515 |
| Research Foundation for Mental Hygiene: Drug Abuse and Addiction Research Programs | 93.279 | 2U10DA013035 | 12,122 |
| Albert Einstein College of Medicine: Minority Health and Health Disparities Research | 93.307 | P60MD000514 | 26,937 |
| Oklahoma Health Sciences Center: Cancer Treatment Research | 93.395 | U10 multiple | 17,652 |
| University of Virginia: Cancer Treatment Research | 93.395 | CA098543 5 U10-CA98543 | 134,034 |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|---|------------------------|--|-------------------------|
| Research and Development Cluster (continued) | | | |
| U.S. Department of Health and Human Services (continued) | | | |
| Pass-through programs (continued): | | | |
| University of California at San Diego: Cancer Treatment Research | 93.395 | P01CA081534 | \$ 58,625 |
| University of Florida: Cancer Control | 93.399 | U54CA136465 | 36,046 |
| University of Alabama: ARRA – Trans-NIH Recovery Act Research Support | 93.701 | 5RC2AR058964-02 | 90,279 |
| Duke University: ARRA – Trans-NIH Recovery Act Research Support | 93.701 | 5RC2AR058934 | 4,917 |
| Rhode Island Hospital: ARRA – Trans-NIH Recovery Act Research Support | 93.701 | 5R21HD058828 | 4,146 |
| New York University School of Medicine: ARRA – Trans-NIH Recovery Act Research Support | 93.701 | 5RC2AR058934 | 4,917 |
| Icahn School of Medicine at Mount Sinai: Cardiovascular Diseases Research | 93.837 93.837 | 1 U01 HL098123-01 5 U01 HL098123-04 | 108,065 63,796 |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|---|------------------------|------------------------------------|-------------------------|
| Research and Development Cluster (continued) | | | |
| U.S. Department of Health and Human Services (continued) | | | |
| Pass-through programs (continued): | | | |
| University of Michigan: | | | |
| Cardiovascular Diseases Research | 93.837 | 1R01HL093338-01A1 | \$ 52,027 |
| CureSearch: | | | |
| Blood Diseases and Resources Research | 93.839 | U01HL69254 | 1,976 |
| Baylor College: | | | |
| Blood Diseases and Resources Research | 93.839 | R01 HL095647-03 R01 HL095647-04 | 45,079 |
| Cincinnati Children's Hospital: | | | |
| Arthritis, Musculoskeletal and Skin Diseases Research | 93.846 | P 60AR047784 | 6,805 |
| University of Michigan: | | | |
| Arthritis, Musculoskeletal and Skin Diseases Research | 93.846 | 2U01AR052181 | 778 |
| Biomedical Research Models Inc.: | | | |
| Arthritis, Musculoskeletal and Skin Diseases Research | 93.846 | 1R41AR060620 | 172,515 |
| Arthritis, Musculoskeletal And Skin Diseases Research | 93.846 | 1R43AR062401-01AI | 20,702 |
| University of South Florida: | | | |
| Diabetes, Digestive, and Kidney Diseases Extramural Research | 93.847 | 1-U01-DK61055 | 1,930 |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|--|------------------------|---------------------------|-------------------------|
| Research and Development Cluster (continued) | | | |
| U.S. Department of Health and Human Services (continued) | | | |
| Pass-through programs (continued): | | | |
| Yale University: | | | |
| Diabetes, Digestive, and Kidney Diseases Extramural Research | 93.847 | U01 DK62429 | \$ 660,291 |
| University of Michigan: | | | |
| Diabetes, Digestive, and Kidney Diseases Extramural Research | 93.847 | U54DK083912 | 284 |
| Icahn School of Medicine at Mount Sinai: | | | |
| Diabetes, Digestive, and Kidney Diseases Extramural Research | 93.847 | U34DK084544 | 2,896 |
| University of California at San Francisco: | | | |
| Extramural Research Programs in the Neurosciences and Neurological Disorders | 93.853 | 2U01NS040024-06A1 | 37,516 |
| University of Texas Health Science Center: | | | |
| Extramural Research Programs in the Neurosciences and Neurological Disorders | 93.853 | 1R01 NS050627 | 3,438 |
| Massachusetts General Hospital: | | | |
| Extramural Research Programs in the Neurosciences and Neurological Disorders | 93.853 | 5U01 NS052592-03 | 35,388 |
| Columbia University: | | | |
| Extramural Research Programs in the Neurosciences and Neurological Disorders | 93.853 | 5U01 NS051483-04 | 464 |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|--|------------------------|---------------------------|-------------------------|
| Research and Development Cluster (continued) | | | |
| U.S. Department of Health and Human Services (continued) | | | |
| Pass-through programs (continued): | | | |
| Duke University: | | | |
| Allergy, Immunology and Transplantation Research | 93.855 | U19AI056363 | \$ 354,752 |
| Medical College of Wisconsin: | | | |
| Lung Diseases Research | 93.838 | 1RO1 HL095410-04 | 90 |
| University of Alabama Birmingham: | | | |
| A multiple Ascending Dose-Finding Pharmacokinetic & Pharmacodynamic Study of CMX-001 in Infants | 93.HHSN272201100038C | HHSN272201100038C | 1,490 |
| Adaptive sequential study evaluating prevention of neonatal HSV | 93.HHSN272201100034C | HHSN272201100034C | 1,490 |
| A Phase II 6 weeks oral valganciclovir versus placebo in infants | 93.HHSN272201100035C | HHSN272201100035C | 1,490 |
| A Pharmacokinetic/Pharmacodynamic & Resistance Evaluation of Intravenous Ganciclovir in Premature Infants | 93.HHSN272201100037C | HHSN272201100037C | 1,491 |
| New York University School of Medicine: | | | |
| ARRA – Recovery Act – Comparative Effectiveness Research – AHRQ | 93.715 | 10-00723 | 100,494 |
| Subtotal pass-through programs: | | | 3,173,739 |
| Total U.S. Department of Health and Human Services | | | 32,486,503 |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|---|------------------------|--|-------------------------|
| Research and Development Cluster (continued) | | | |
| U.S. Department of Defense | | | |
| Direct Programs: | | | |
| Military Medical Research and Development | 12.420 | W81XWH-09-1-0327 W81XWH-10-1-0305 W81XWH-10-1-0978 W81XWH-12-1-0084 | \$ 1,073,780 |
| Basic Scientific Research | 12.431 | W911NF-09-1-0125 | <u>190,200</u> |
| Total U.S. Department of Defense | | | <u>1,263,980</u> |
| National Science Foundation | | | |
| Direct Programs: | | | |
| Engineering Grants | 47.041 | CMMI-1151605 | <u>52,717</u> |
| Total National Science Foundation | | | <u>52,717</u> |
| Total Research and Development Cluster | | | <u>33,803,200</u> |
| Other Programs | | | |
| U.S. Department of Agriculture | | | |
| Pass-through program – New York State Department of Health: | | | |
| Special Supplemental Nutrition Program For Women, Infants, and Children | 10.557 | C025759/C019383 | <u>7,307,610</u> |
| Total U.S. Department of Agriculture | | | <u>7,307,610</u> |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|--|------------------------|---------------------------|-------------------------|
| Other Programs (continued) | | | |
| U.S. Department of Justice | | | |
| Pass-through program – New York State Crime Victims Board: | | | |
| Crime Victim Assistance | 16.575 | C501193 | \$ 100,830 |
| Pass-through program – Nassau County District Attorney: | | | |
| Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program | 16.580 | CQDA12000021 | 41,737 |
| Pass-through program – Suffolk County: | | | |
| ARRA – Edward Byrne Memorial Justice Assistance Grant (JAG) Program / Grants To Units Of Local Government | 16.804 | 2010-DJ-BX-1559 | 3,724 |
| Total U.S. Department of Justice | | | <u>146,291</u> |
| U.S. Department of Energy | | | |
| Pass-through program – New York State Energy Research and Development Authority: | | | |
| State Energy Program | 81.041 | 18963 | 17,908 |
| Total U.S. Department of Energy | | | <u>17,908</u> |
| U.S. Department of Education | | | |
| Pass-through programs – New York State Department of Education: | | | |
| Special Education Grants to States | 84.027 | C-010595 C010204 | 169,104 |
| Rehabilitation Services Vocational Rehabilitation Grants to States | 84.126 | C010205 | 153,070 |
| Total U.S. Department of Education | | | <u>322,174</u> |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|---|------------------------|------------------------------------|-------------------------|
| U.S. Department of Transportation | | | |
| Pass-through program – Town of North Hempstead: | | | |
| New Freedom Program | 20.521 | N/A | \$ 297,444 |
| Total U.S. Department of Transportation | | | <u>297,444</u> |
| U.S. Department of Health and Human Services | | | |
| Direct program – Health Resources and Services Administration: | | | |
| Coordinated Services and Access to Research for Women, Infants, Children, and Youth | 93.153 | H12HA10422A HI2HA24869 | 597,184 |
| Pass-through program – New York State Department of Health: | | | |
| Family Planning Services | 93.217 | C027029 C-016947 CO19951 | 442,571 |
| Pass-through program – City of New York Department of Health and Mental Hygiene: | | | |
| Immunization Cooperative Agreements | 93.268 | N/A | 132,099 |
| Direct program – Health Resources and Services Administration | | | |
| Nurse Education, Practice Quality and Retention Grants | 93.359 | D11HP22203-01-00 | 157,151 |
| Pass-through programs – New York State Department of Health: | | | |
| Hospital Acquired Infection Prevention Project | 93.C022818 | C022818 | 98,646 |
| Temporary Assistance for Needy Families | 93.558 | C019951 | 39,511 |
| Medical Assistance Program | 93.778 | C023912/C027002 C023911/C026020 | 143,428 |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|---|------------------------|---|-------------------------|
| Other Programs (continued) | | | |
| U.S. Department of Health and Human Services (continued) | | | |
| Pass-through program – Health Research Inc.: | | | |
| National Bioterrorism Hospital Preparedness Program | 93.889 | 1U3RHS0593401/15-0451-01 15-0451-03/1210NORTH008 11807545/1210State0009 | \$ 1,177,411 |
| Pass-through program – United Way: | | | |
| HIV Emergency Relief Project Grants | 93.914 | 10104/9802 11650/10 MAI 11 | 276,383 |
| Pass-through program – Suffolk County Department of Health: | | | |
| HIV Emergency Relief Project Grants | 93.914 | N/A | 2,411 |
| Pass-through program – New York State Department of Health: | | | |
| HIV Care Formula Grants | 93.917 | 003439-05/4004-03 | 382,395 |
| Pass-through program – Suffolk County Department of Health: | | | |
| Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease | 93.918 | N/A | 27,464 |
| Direct program – Health Resources and Services Administration: | | | |
| Ryan White HIV/AIDS Dental Reimbursement and Community Based Dental Partnership | 93.924 | T22HA22915/T22HA24890 T22HA22922/T22HA2489892 | 32,530 |
| Direct program – US Department of Health and Human Services / Centers for Disease Control and Prevention: | | | |
| HIV Prevention Activities–Health Department Based | 93.940 | 421-11 | 138,257 |

North Shore-Long Island Jewish Health System, Inc.

Schedule of Expenditures of Federal Awards (continued)

| Federal Grantor/Pass-Through Grantor/Program or Cluster Title/Project Title | Federal CFDA Number | Pass-Through ID Number | Federal Expenditures |
|--|------------------------|------------------------------------|-------------------------|
| Other Programs (continued) | | | |
| U.S. Department of Health and Human Services (continued) | | | |
| Pass-through program – Suffolk County Department of Health: | | | |
| HIV Prevention Activities–Health Department Based | 93.940 | N/A | \$ 2,683 |
| Pass-through program – New York State Office of Alcoholism and Substance Abuse Services: | | | |
| Block Grants For Prevention And Treatment Of Substance Abuse | 93.959 | CQBH11-0000-84/ 816 1214 904 BO | 263,823 |
| Pass-through program – New York State Department of Health: | | | |
| Preventive Health and Health Services Block Grant | 93.991 | C027002 816 0406 709 BO | 23,460 |
| Pass-through program – New York State Department of Health: | | | |
| Maternal And Child Health Services Block Grant To The States | 93.994 | C022458/C023853/C027029/C019951 | 390,830 |
| U.S. Center for Disease Control | | | |
| Queens World Trade Center Clinical Center of Excellence | 93.200-2011-39388 | 200-2011-39388 | 663,139 |
| Total U.S. Department of Health and Human Services | | | <u>4,991,376</u> |
| U.S. Department of Homeland Security | | | |
| Direct Program: | | | |
| Disaster Grants – Public Assistance (Presidentially Declared Disasters) | 97.036 | UD552G2 | 485,563 |
| Pass-through program – New York State Office of Homeland Security: | | | |
| Non-Profit Security Program | 97.008 | C167217 | 74,913 |
| Total U.S. Department of Health and Human Services | | | <u>560,476</u> |
| Total Other Programs | | | <u>13,643,279</u> |
| Total Expenditures of Federal Awards | | | <u>\$ 47,446,479</u> |

See accompanying notes to Schedule of Expenditures of Federal Awards.

North Shore-Long Island Jewish Health System, Inc.

Notes to Schedule of Expenditures of Federal Awards

Year Ended December 31, 2012

1. Basis of Presentation

The accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal grant activities of North Shore-Long Island Jewish Health System, Inc. and its member corporations and other affiliated entities (collectively, the "System") and is presented on the accrual basis of accounting. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this Schedule may differ from amounts presented in, or used in the preparation of, the consolidated financial statements.

Awards for reimbursable expenditures involving the U.S. Department of Homeland Security – Federal Emergency Management Agency ("FEMA") are reported by the System on the Schedule in the year that FEMA approves the applicable Award Worksheet, pursuant to guidance issued by the U.S. Department of Homeland Security (see Note 4).

2. Food and Nutrition Awards

During the year ended December 31, 2012, the System participated in the New York State Department of Health, Special Supplemental Nutrition Program for Women, Infants, and Children ("WIC") through the provision of nutritional counseling and the distribution of food vouchers. The United States Department of Agriculture, the federal agency that sponsors the WIC program under CFDA number 10.557, has determined that WIC food instruments are considered "property in lieu of money" and, therefore, should be reported as federal awards received by the System.

The total amount reported as federal awards on the Schedule represents the value of food vouchers redeemed in the amount of \$6,252,648 plus administrative costs of \$1,054,962 for the year ended December 31, 2012. As New York State funds are commingled with federal funds, federal funding percentages were applied to determine the total amount of federal funds to be reported above. These percentages were supplied by the New York State Department of Health as follows:

| | Federal Percentage | |
|------------------------|--|--|
| | October 1, 2012 to September 30, 2013 | October 1, 2011 to September 30, 2012 |
| Administrative costs | 84% | 84% |
| Food vouchers redeemed | 100 | 100 |

North Shore-Long Island Jewish Health System, Inc.

Notes to Schedule of Expenditures of Federal Awards (continued)

3. Subrecipients

Of the federal expenditures presented in the Schedule, the System provided federal awards to subrecipients as follows:

| Program Title | Federal CFDA Number | Amount Provided to Subrecipients |
|---|--------------------------------|---|
| Military Medical Research and Development | 12.420 | \$ 6,628 |
| Research Related to Deafness and Communication Disorders | 93.173 | 47,088 |
| Research on Healthcare Costs, Quality and Outcomes | 93.226 | 277,530 |
| Mental Health Research Grants | 93.242 | 119,003 |
| ARRA – Trans-NIH Recovery Act Research Support | 93.701 | 1,060,635 |
| Cardiovascular Diseases Research | 93.837 | 88,072 |
| Arthritis, Musculoskeletal and Skin Diseases Research | 93.846 | 78,095 |
| Diabetes, Digestive, and Kidney Diseases Extramural Research | 93.847 | 227,923 |
| Extramural Research Programs in the Neurosciences and Neurological Disorders | 93.853 | 411,557 |
| Allergy, Immunology and Transplantation Research | 93.855 | 119,030 |
| Total Research and Development Cluster | | <u>\$ 2,435,561</u> |

4. Federal Emergency Management Agency Awards (CFDA 97.036)

The System incurred certain costs in 2011 and 2012 which are or may be reimbursable by FEMA. Costs totaling \$485,563 incurred in 2011 were approved by FEMA in 2012 and are included on the accompanying Schedule for the year ended December 31, 2012 under CFDA number 97.036. The System also incurred certain costs in 2012 which may be reimbursable by FEMA; however, no awards for such costs were approved by FEMA in 2012 and, accordingly, no expenditures are included on the accompanying Schedule for the year ended December 31, 2012.

Report of Independent Auditors 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*

The Board of Trustees
North Shore-Long Island Jewish Health System, Inc.

We have audited, in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of North Shore-Long Island Jewish Health System, Inc. and its member corporations and other affiliated entities (collectively, the “System”), which comprise the consolidated statement of financial position as of December 31, 2012, and the related consolidated statements of operations, changes in net assets and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 15, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System’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 System’s internal control. Accordingly, we do not express an opinion on the effectiveness of the System’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 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 System's financial statements are free of 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 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.

Ernst + Young LLP

April 15, 2013

Report of Independent Auditors on Compliance for Each Major Federal Program and on Internal Control Over Compliance Required by OMB Circular A-133

The Board of Trustees
North Shore-Long Island Jewish Health System, Inc.

Report on Compliance for Each Major Federal Program

We have audited North Shore-Long Island Jewish Health System Inc. and its member corporations and other affiliated entities' (collectively, the "System") compliance with the types of compliance requirements described in the US Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the System's major federal programs for the year ended December 31, 2012. The System's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

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 System'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; 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 System'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 System's compliance.

Opinion on Each Major Federal Program

In our opinion, North Shore-Long Island Jewish Health System, Inc. and its member corporations and other affiliated entities 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 December 31, 2012.

Report on Internal Control Over Compliance

Management of North Shore-Long Island Jewish Health System Inc. and its member corporations and other affiliated entities 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 System'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 System'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.

Ernst & Young LLP

September 30, 2013

North Shore-Long Island Jewish Health System, Inc.

Schedule of Findings and Questioned Costs

Year Ended December 31, 2012

Part I—Summary of Auditor’s Results

Financial Statements Section

Type of auditor’s report issued: Unmodified, with an emphasis of matter paragraph for a change in accounting principle

Internal control over financial reporting:

| | | |
|---|--------------------------|-----------------------------------|
| Material weakness(es) identified? | <u> </u> Yes | <u> X </u> No |
| Significant deficiency(ies) identified? | <u> </u> Yes | <u> X </u> None reported |
| Noncompliance material to financial statements noted? | <u> </u> Yes | <u> X </u> No |

Federal Awards Section

Internal control over major programs:

| | | |
|---|--------------------------|-----------------------------------|
| Material weakness(es) identified? | <u> </u> Yes | <u> X </u> No |
| Significant deficiency(ies) identified? | <u> </u> Yes | <u> X </u> None reported |

Type of auditor’s 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** X **No**

North Shore-Long Island Jewish Health System, Inc.

Schedule of Findings and Questioned Costs (continued)

Part I—Summary of auditor’s results (continued)

Identification of major programs:

| <u>CFDA number(s)</u> | <u>Name of federal program or cluster</u> |
|---|--|
| 12.420, 12.431, 47.041, 93.103, 93.110, 93.113, 93.121, 93.173, 93.213, 93.226, 93.242, 93.262, 93.273, 93.279, 93.281, 93.307, 93.351, 93.389, 93.393, 93.395, 93.396, 93.399, 93.610, 93.701, 93.715, 93.837, 93.838, 93.839, 93.846, 93.847, 93.853, 93.855, 93.859, 93.866, 93.RD | Research and Development Cluster |
| 20.521 | New Freedom Program |
| 93.359 | Nurse Education, Practice Quality and Retention Grants |

Dollar threshold used to distinguish between Type A and Type B programs:

\$ 1,423,394

Auditee qualified as low-risk auditee?

 X **Yes** **No**

Part II—Financial statement findings section

This section identifies the significant deficiencies, material weaknesses, fraud, illegal acts, violations of provisions of contracts and grant agreements, and abuse related to the consolidated financial statements for which *Government Auditing Standards* require reporting in a Circular A-133 audit.

There are no matters that are required to be reported.

Part III—Federal award findings and questioned costs section

This section identifies the audit findings required to be reported by Circular A-133 section .510(a) (for example, material weaknesses, significant deficiencies and material instances of noncompliance, including questioned costs), as well as any abuse findings involving federal awards that are material to a major program.

There are no matters that are required to be reported.

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