

CONSOLIDATED FINANCIAL STATEMENTS

**CATHOLIC HEALTH SYSTEM, INC.
AND SUBSIDIARIES**

DECEMBER 31, 2017

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Catholic Health System, Inc.
Buffalo, New York

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Catholic Health System, Inc. and its subsidiaries (collectively, the System), which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended and the related notes to the consolidated financial statements (collectively, the consolidated financial statements).

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the System'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 System'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 financial position of Catholic Health System, Inc. and its subsidiaries as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Freed Maxick CPAs, P.C.

Buffalo, New York
April 26, 2018

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands of dollars)

December 31,

ASSETS	2017	2016
Current assets:		
Cash and cash equivalents	\$ 245,193	\$ 227,231
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$24,138 (2016 - \$25,493)	131,788	125,202
Other receivables	7,815	9,293
Inventories	26,071	23,600
Prepaid expenses and other current assets	11,632	11,288
Total current assets	422,499	396,614
Assets limited as to use	47,937	38,059
Investments	196,082	179,045
Property and equipment, net	364,784	371,159
Other assets	109,529	111,489
Total assets	\$ 1,140,831	\$ 1,096,366
LIABILITIES AND NET ASSETS		
Current liabilities:		
Current portion of long-term obligations	\$ 18,157	\$ 15,312
Line of credit payable	-	4,310
Accounts payable	55,395	44,958
Accrued expenses	83,400	66,461
Due to third-party payors	40,862	47,881
Total current liabilities	197,814	178,922
Long-term obligations, net	192,703	195,760
Other long-term obligations, net	517,354	488,144
Total liabilities	907,871	862,826
Net assets:		
Unrestricted	224,896	225,122
Temporarily restricted	7,767	8,124
Permanently restricted	297	294
Total net assets	232,960	233,540
Total liabilities and net assets	\$ 1,140,831	\$ 1,096,366

See accompanying notes.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS

(in thousands of dollars)

For the Years Ended December 31,

	<u>2017</u>	<u>2016</u>
Unrestricted revenues and other support:		
Net patient/resident service revenue	\$ 1,136,549	\$ 1,087,220
Provision for bad debts	(25,616)	(19,568)
Net patient/resident service revenue, less provision for bad debts	1,110,933	1,067,652
Other revenue	21,278	20,955
Net assets released from restrictions	595	230
Total unrestricted revenues and other support	<u>1,132,806</u>	<u>1,088,837</u>
Expenses:		
Salaries and wages	519,969	481,803
Employee benefits	149,882	149,199
Medical and professional fees	48,404	41,465
Purchased services	106,415	106,314
Supplies	199,110	206,061
Depreciation and amortization	47,947	46,015
Interest	10,174	9,875
Insurance	15,686	13,239
Other expenses	30,702	32,521
Total expenses	<u>1,128,289</u>	<u>1,086,492</u>
Income from operations	4,517	2,345
Nonoperating revenues:		
Investment income	20,120	5,954
Other, net	631	2,316
Total nonoperating revenues	<u>20,751</u>	<u>8,270</u>
Excess of revenues over expenses	<u>\$ 25,268</u>	<u>\$ 10,615</u>

See accompanying notes.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS (CONTINUED)

(in thousands of dollars)

For the Years Ended December 31,

	<u>2017</u>	<u>2016</u>
Unrestricted net assets:		
Excess of revenues over expenses	\$ 25,268	\$ 10,615
Change in unrealized gain on interest rate swap	313	1,262
Change in pension obligation, other than net periodic cost	(28,257)	12,382
Net assets released from restrictions used for capital	1,609	2,044
Grant revenue for capital expenditures	-	125
Contributions	80	136
Other	748	614
(Decrease) increase in unrestricted net assets before effects of discontinued operations	(239)	27,178
Gain on sale of assets in discontinued operations	-	2,561
Gain (loss) from discontinued operations	13	(2,680)
(Decrease) increase unrestricted net assets	(226)	27,059
Temporarily restricted net assets:		
Contributions	1,431	2,403
Investment income	37	85
Special events revenue, net	438	278
Change in temporarily restricted interest in related Foundation	(55)	(22)
Temporarily restricted net assets released from restrictions	(2,204)	(2,274)
Other	(4)	224
(Decrease) increase in temporarily restricted net assets	(357)	694
Permanently restricted net assets:		
Contributions	3	1
Increase in permanently restricted net assets	3	1
(Decrease) increase in net assets	(580)	27,754
Net assets, beginning of year	233,540	205,786
Net assets, end of year	<u>\$ 232,960</u>	<u>\$ 233,540</u>

See accompanying notes.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands of dollars)

For the Years Ended December 31,

	2017	2016
Cash flows from operating activities:		
(Decrease) increase in net assets	\$ (580)	\$ 27,754
(Gain) loss in net assets from discontinued operations	(13)	2,680
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities		
Depreciation and amortization	47,947	46,015
Provision for bad debts	25,616	19,568
Gain on sale of LTC facilities	-	(2,561)
Change in minimum pension liability adjustment	28,257	(12,382)
Grant revenue for capital additions	-	(125)
Undistributed earnings in equity investees	(267)	(285)
Amortization of discount on debt issuance	61	62
Amortization of premium on debt issuance	(574)	(575)
Amortization of debt issuance costs	466	460
Gain on extinguishment of capital lease	-	(1,967)
(Gain) loss on sale of property and equipment	(160)	720
Change in unrealized gain on investments	(16,726)	(3,881)
Realized (gain) loss on investments	(941)	32
Realized gain on interest rate swap	(319)	(1,290)
Other	(137)	(108)
(Increase) decrease in assets		
Patient/resident accounts receivables	(32,187)	(2,428)
Other receivables	1,660	5,964
Inventories	(2,471)	2,505
Prepaid expenses and other current assets	256	(4,929)
Other assets	13	159
(Increase) decrease in liabilities:		
Accounts payable	8,716	(5,680)
Accrued expenses	4,243	(3,409)
Due to third-party payors	(4,881)	4,510
Other liabilities	4,573	15,695
Net cash used in discontinued operations	(3,204)	(2,661)
Net cash and cash equivalents provided by operating activities	59,348	83,843
Cash flows from investing activities:		
Purchase of property and equipment	(38,518)	(56,154)
Proceeds from sale of property and equipment	305	9
Proceeds from sale of assets in discontinued operations	-	3,012
Purchase of assets limited as to use	(33)	-
Proceeds from sale of assets limited as to use	3,146	58,720
Change in investments, net	(206)	(587)
Purchase of investments	(8,176)	(166,573)
Proceeds from sale of investments	9,028	-
Purchase of equity investments	(1,351)	-
Net cash and cash equivalents used in investing activities	(35,805)	(161,573)
Cash flows from financing activities:		
Proceeds from issuance of long-term obligations, net	12,937	5,786
Repayments of current and long-term obligations	(18,518)	(60,982)
Proceeds of grant revenue for capital additions	-	125
Net cash and cash equivalents used in financing activities	(5,581)	(55,071)
Increase (decrease) in cash and cash equivalents	17,962	(132,801)
Cash and cash equivalents - beginning of year	227,231	360,032
Cash and cash equivalents - end of year	<u>\$ 245,193</u>	<u>\$ 227,231</u>

See accompanying notes.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 1. ORGANIZATION

Catholic Health System, Inc. and Subsidiaries (CHS or the System) is an integrated healthcare delivery system in Western New York jointly sponsored by the Diocese of Buffalo, New York, and Catholic Health Ministries. Trinity Health and the Diocese of Buffalo, New York are the corporate members of CHS, with equal ownership interest.

CHS is the also the sole corporate member of the following subsidiaries:

Acute Care Subsidiaries: The Acute Care Subsidiaries (also collectively referred to as the Hospitals) include Mercy Hospital of Buffalo (MHB), Kenmore Mercy Hospital including KMH Homes Inc. and The McAuley Residence (KMH), Sisters of Charity Hospital of Buffalo, New York (SCH) and Mount St. Mary's Hospital and Health Center (MSM).

Home and Community Based Subsidiaries: The Home and Community Based Subsidiaries include Father Baker Manor, Mercy Home Care of Western New York, Inc. (MHC), McAuley Seton Home Care (MSHC) and Catholic Health Infusion Pharmacy (Infusion Pharmacy).

Other Subsidiaries: The Other Subsidiaries include, Our Lady of Victory Renaissance Corporation (OLV Renaissance), Continuing Care Foundation, Catholic Health System Program of All Inclusive Care for the Elderly, Inc. (LIFE) Trinity Medical WNY, P.C. (Trinity) and Niagara Medicine, P.C. (Niagara Medicine).

Discontinued Operations: The Discontinued Operations include St. Elizabeth's Home (SEH) and St. Vincent's Home for the Aged (SVH) (both sold 2016), St. Francis Home of Williamsville (sold 2015), St. Francis Geriatric and Healthcare Services, Inc. (closed 2009), and Nazareth Home of the Franciscan Sisters of the Immaculate Conception (closed 2007, sold 2015).

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies applied in preparing the accompanying consolidated financial statements are summarized below:

Principles of Consolidation: The consolidated financial statements of the System include the accounts of CHS (commonly referred to as the Parent) and each of its wholly-owned or controlled subsidiaries. All significant intercompany balances and transactions have been eliminated to reflect the consolidated amounts.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates made by the System include, but are not limited to, the reserves for asset retirement obligations, reserve for bad debts, reserve for third-party payor contractual adjustments and allowances, the provision for estimated receivables and payables for final settlements with those payors, the insurance reserves for workers' compensation, health insurance, professional and general liability, and actuarial assumptions used in determining pension expense.

Risks and Uncertainties: Investment securities are exposed to various risks, such as interest rate, market and credit. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the fair value of investment securities, it is at least possible that changes in risks in the near term could materially affect the net assets of the System.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates related to third-party payment matters will change by a material amount in the near term.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and Cash Equivalents: The System considers all highly liquid investments, generally with original maturities of three months or less when purchased, and short term investments, excluding amounts limited as to use, to be cash equivalents. The System maintains funds on deposit in excess of amounts insured by the Federal Depository Insurance limits.

	<u>2017</u>	<u>2016</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for interest	\$ 8,985	\$ 8,046
Non-cash investing and financing transactions:		
Assets acquired under capital lease obligations	\$ 652	\$ 3,890
Construction related payables	\$ 1,890	\$ (981)

Other Receivables and Other Assets: Other receivables consist primarily of managed care risk sharing receivables, physician loans, and other receivables. There is no allowance for doubtful accounts established against these receivables. Other non-current assets consist of insurance recoveries, investments in healthcare ventures, and other miscellaneous deferred charges.

The composition of current other receivables and other non-current assets is as follows at December 31:

	<u>2017</u>	<u>2016</u>
Current other receivables:		
Physician loans	\$ 3,111	\$ 4,148
Foundation receivables	1,352	1,499
Managed care risk receivable	411	-
Other	<u>2,941</u>	<u>3,646</u>
Other receivables	<u>\$ 7,815</u>	<u>\$ 9,293</u>
Non-current other assets:		
Insurance recoveries	\$ 103,365	\$ 106,930
Investments in healthcare ventures	3,007	1,402
Goodwill & other	<u>3,157</u>	<u>3,157</u>
Other assets	<u>\$ 109,529</u>	<u>\$ 111,489</u>

Inventories: Inventory consists primarily of drugs, medical supplies and food. These inventories are generally stated at the lower of cost (first-in, first-out) or net realizable value.

Investments: Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair values in the consolidated balance sheets.

Investment income and gains restricted by a donor are reported as increases in unrestricted net assets if the restrictions are met (either by passage of time or by use) in the reporting period in which the income and gains are recognized. Investment income or loss (including realized gains or losses on investments, interest, and dividends) is included in the excess of revenues over expenses, unless their use is restricted by donor stipulations or law. Unrealized gains and losses on investments are included in the performance indicator as the investments are trading securities.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Assets Limited as to Use: Assets limited as to use include assets set aside for debt service as required by trustee or indenture agreements, and assets set aside by the Board of Directors for specific future purposes. The Board retains control of these funds and may at its discretion subsequently use for other purposes.

Property and Equipment: Property and equipment are stated at cost if purchased, or if contributed, at the fair value on the date contributed. Depreciation is computed using the straight-line method over useful lives ranging from three to forty years. Equipment under capital lease is amortized on the straight-line method over the shorter of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the consolidated financial statements.

Gifts of long-lived assets such as land, building, or equipment are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Debt Issuance Costs: In accordance with ASU 2015-03, Simplifying the Presentation of Debt Issuances Costs, debt issuances costs are presented as a reduction of the carrying amount of debt rather than as an asset. Amortization of debt issuance costs is reported as interest expense in the statement of operations.

Impairment of Long-Lived Assets: The System evaluates its long-lived assets for financial impairment as events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable.

The System evaluates the recoverability of long-lived assets not held for sale by measuring the carrying amount of the assets against the estimated undiscounted future cash flows associated with them. If such evaluations indicate that the future undiscounted cash flows of certain long-lived assets are not sufficient to recover the carrying value of such assets, the assets are adjusted to their fair values. Based on these evaluations, there are no adjustments to the carrying value of long-lived assets in 2017 and 2016.

Asset Retirement Obligations: The System accrues for asset retirement obligations in the period in which they are incurred if sufficient information is available to reasonably estimate the fair value of the obligation. Over time, the liability is accreted to its settlement value. Upon settlement of the liability, the System will recognize a gain or loss for any difference between the settlement amount and liability recorded. Accretion expense for the years ended December 31, 2017 and 2016 was \$591 and \$556, respectively.

Other Long-Term Obligations: Other long-term obligations consist primarily of insurance liabilities, long-term pension obligations, asset retirement obligations, interest rate swap liabilities, and other long-term liabilities. The composition of other long-term liabilities is as follows at December 31:

	<u>2017</u>	<u>2016</u>
Insurance liabilities	\$ 157,445	\$ 156,194
Long-term pension obligations	336,682	307,867
Asset retirement obligations	10,114	9,929
Interest rate swap	4,513	4,832
Contingent performance obligation & other	<u>8,600</u>	<u>9,322</u>
Other long-term obligations	<u>\$ 517,354</u>	<u>\$ 488,144</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Net Patient/Resident Service Revenue: Net patient/resident service revenue is reported at the estimated net realizable amounts from patients/residents, third-party payors, and others for services rendered including estimated adjustments under various reimbursement agreements with third-party payors. The System has agreements with third-party payors that provide for payments to the System at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Third-party payors retain the right to review and propose adjustments to amounts recorded by the System. Such adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. CHS's Healthcare Assistance Program (HAP) provides discounts to patients based on need. In addition, the System will also assist patients with the application process for free or low-cost insurance. Those uninsured patients who do not qualify for the HAP or low-cost insurance and live in New York State, a state contiguous to New York State, or the state of Ohio, are provided an uninsured discount based on a service specific uninsured rate. This uninsured rate is similar in calculation method and amount to third party payor methods and rates.

Under the New York Health Care Reform Act (NYHCRA), hospitals are authorized to negotiate reimbursement rates with certain non-Medicare payors except for Medicaid, Workers' Compensation and No-Fault, which are regulated by New York State. These negotiated rates may take the form of rates per discharge, reimbursed costs, and discounted charges or as per diem payments. Reimbursement rates for non-Medicare payors regulated by New York State are determined on a prospective basis. These rates also vary according to a patient classification system defined by the Health Care Reform Act (HCRA) that is based on clinical, diagnostic and other factors.

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

- **Medicare:** Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. The System also receives reimbursement under a prospective payment system for certain medical outpatient services, based on service groups, called ambulatory payment classifications (APCs). Other services are based upon a fee schedule and other methodologies.
- **Medicaid and other:** Under the New York Health Care Reform Act (NYHCRA) hospitals are authorized to negotiate reimbursement rates for inpatient acute care services with all other non-Medicare payors except for Medicaid, Workers' Compensation and No-Fault, which are regulated by New York State. These negotiated rates may take the form of rates per discharge, reimbursed costs, and discounted charges or as per diem payments. Reimbursement rates for non-Medicare payors regulated by New York State are determined on a prospective basis. These rates also vary according to a patient classification system defined by NYHCRA that is based on clinical, diagnostic, and other factors.

Outpatient services are paid under various reimbursement methodologies, including prospective determined rates, cost reimbursement, fee schedules, and charges.

In addition, under NYHCRA, all non-Medicare payors are required to make surcharge payments for the subsidization of indigent care and other health care initiatives. The percentage amount of the surcharge varies by payor and applies to a broad array of health care services. Surcharges are included in patient/residents receivables and the offset is in third party liabilities. Surcharges are generally received and paid to the state within a few months. Also, certain payors are required to fund a pool for graduate medical education expenses through surcharges on payments to hospitals for inpatient services or through voluntary election to pay a covered lives assessment directly to the New York State Department of Health. The System is required to prepare and file various reports on actual and allowable costs annually. Management believes that adequate provisions have been made in the financial statements for prior and current years' estimated settlements. The difference between the amount estimated and the actual final settlement is recorded as an adjustment to net patient/resident service revenue in the year the final settlement is determined.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Amounts recognized in 2017 and 2016 related to prior years, including adjustments to prior year estimates, increased revenues approximately \$2,979 and \$7,340, respectively. These changes in estimates related to estimates for prior years cost report reopening, appeals, and tentative final cost reports, some of which are still subject to audit, additional reopening, and/or appeals.

Approximately 54% and 57% of net patient/resident service revenue was generated from services rendered to patients/residents under Medicare and Medicaid programs in 2017 and 2016, respectively. Approximately 34% and 36% of net patient/resident service revenue was generated from services rendered to patients/residents under managed care programs in 2017 and 2016, respectively.

There are various proposals at the federal and state level that could, among other things, adjust payment rates. The outcome of these proposals, regulatory changes and other market conditions cannot presently be determined.

Provision for Bad Debts: The provision for bad debts is based upon management's assessment of expected net collections considering economic experience, trends in health care coverage, and other collection indicators. Periodically throughout the year, management assesses the adequacy of the allowance for uncollectible accounts based upon historical write-off experience by payor category, including those amounts not covered by insurance and history of cash collections. The results of this review are then used to make any modifications to the provision for bad debts expense to establish an appropriate allowance for uncollectible accounts. After satisfaction of amounts due from insurance and reasonable efforts to collect from the patient/resident have been exhausted, the System follows established guidelines for placing certain past-due patient/resident balances with the collection agencies, subject to terms of certain restrictions on collection efforts as determined by the System. Accounts receivable are written off after collection efforts have been followed in accordance with the System's policies.

Patient and resident service revenue, net of contractual allowances and discounts, recognized in the period from these major payor sources, is as follows for the years ended December 31, 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Patient/resident service revenue (net of contractual allowances and discounts):		
Medicare	\$ 478,127	\$ 455,548
Medicaid	145,422	159,487
Other third party payors	500,751	457,945
Patients/residents	<u>12,249</u>	<u>14,240</u>
Total net patient/resident service revenue	1,136,549	1,087,220
Provision for bad debts	<u>(25,616)</u>	<u>(19,568)</u>
Net patient/resident service revenue less provision for bad debts	<u>\$ 1,110,933</u>	<u>\$ 1,067,652</u>

Charity Care: The New York State Public Health Law requires all hospitals to implement financial aid policies and procedures for their patients. The law also requires hospitals to develop and make publicly available a summary of its financial aid policies and procedures. The System provides health care services to all patients on the basis of medical need, not on the ability to pay for services. For patients who meet certain criteria under the System's charity care policy, the System provides care to these patients without charge or at amounts less than its established rates. Because the System does not pursue collection of amounts determined to qualify for charity care, they are not reported as revenue. The System maintains records to identify and monitor the level of charity care it provides.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Of the System's total expenses reported, an estimated \$10,156 and \$9,299 arose from providing services to charity patients in 2017 and 2016, respectively. Costing is a full step down methodology of cost from non-revenue producing departments to revenue producing departments, with assignment of cost to individual charge items based on relative value units. Additional costs for the Hospitals include required payments for a gross receipts assessment to New York State which is used to fund the New York State Medicaid program and the HCRA. Revenues that offset the costs of Charity Care include payments from the New York State Uncompensated Care Pools.

The Hospitals provide care to patients at no charge or at discounted rates who meet eligibility requirements under its HAP (charity care). In addition to charity care, the Hospitals provide services to patients covered by Medicaid. The payments received for services provided to patients covered by Medicaid may be at or below costs in addition to the cost of care for patients without insurance. The Hospitals are also required to pay a gross receipts assessment to New York State which is used to fund the New York State Medicaid program and the HCRA.

Collective Bargaining Agreements: The System has approximately 41% of its employees working under thirteen collective bargaining agreements. The agreements are set to expire beginning June 1, 2018 through January 15, 2022.

Operating and Nonoperating Revenue and Losses: The System's primary mission is dedicated to meeting the health care needs in the regions in which it operates. The System is committed to providing a broad range of general and specialized health care services including inpatient, primary care, long-term care, outpatient services, and other health care related services. Only those activities directly associated with the furtherance of this mission are considered to be operating activities. Such activities include operation of cafeterias, parking lots, rental real estate and other ancillary activities. Other activities that result in gains or losses unrelated to the System's primary mission are considered to be nonoperating.

Electronic Health Record Incentive Payments: The American Recovery and Reinvestment Act of 2009 provides for Medicare and Medicaid incentive payments beginning in 2011 for eligible hospitals and professionals that adopt and meaningfully use certified electronic health record (EHR) technology. The System recognized income related to Medicare and Medicaid incentive payments using a gain contingency model that is based upon when the eligible hospitals have demonstrated meaningful use of certified EHR technology for the applicable period and the cost report information for the full cost report year that will determine the final calculation of the incentive payment is available.

Medicaid EHR incentive calculations and related payment amounts are based upon prior period cost report information available at the time our eligible hospitals adopt, implement or demonstrate meaningful use of certified EHR technology for the applicable period, and are not subject to revision for cost report data filed for a subsequent period. Thus, incentive income recognition occurs at the point the eligible hospitals adopt, implement or demonstrate meaningful use of certified EHR technology for the applicable period, as the cost report information for the full cost report year that will determine the final calculation of the incentive payment is known at that time. Medicare EHR incentive calculations and related initial payment amounts are based upon the most current filed cost report information available at the time the eligible hospitals demonstrate meaningful use of certified EHR technology for the applicable period. However, unlike Medicaid, this initial payment amount will be adjusted based upon an updated calculation using the annual cost report information for the cost report period that began during the applicable payment year. Thus, incentive income recognition occurs at the point the eligible hospitals demonstrate meaningful use of certified EHR technology for the applicable period and the cost report information for the full cost report year that will determine the final calculation of the incentive payment is available.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**
*(in thousands of dollars)***NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

The System recognized \$372 and \$804 of electronic health record incentive income related to Medicare and Medicaid incentive programs during the years ended December 31, 2017 and 2016, respectively, which is recorded in other revenue.

Other Revenue: The composition of other revenue for the years ended December 31, is set forth in the following table:

	<u>2017</u>	<u>2016</u>
Cafeteria revenue	\$ 2,735	\$ 2,768
Parking revenue	1,253	1,175
Unrestricted donor contributions to the Foundations	2,625	2,199
Medicare and Medicaid meaningful use	372	804
DSRIP grant revenue	-	605
340(b) program revenue	1,936	1,490
Medicaid health home care coordination revenue	3,034	2,944
Shared services	3,458	3,131
Other	<u>5,865</u>	<u>5,839</u>
Other revenue	<u>\$ 21,278</u>	<u>\$ 20,955</u>

Other Expenses: The composition of other expenses for the years ended December 31, is set forth in the following table:

	<u>2017</u>	<u>2016</u>
Rents and operating leases	\$ 9,271	\$ 9,237
Dues	3,572	5,469
NYS DOH cash receipt assessment	6,023	5,541
Taxes, travel and miscellaneous other	<u>11,836</u>	<u>12,274</u>
Other expenses	<u>\$ 30,702</u>	<u>\$ 32,521</u>

Contributions: Contributions received are recorded as unrestricted, temporary restricted or permanently restricted net assets depending on the existence and nature of any donor restrictions.

Contributions and pledges that are restricted by the donor are reported as an increase in unrestricted net assets if the restrictions expire, that is, when a stipulated time restriction ends or purpose restriction is accomplished in the reporting period in which the contribution is recognized. All other donor-restricted support is reported as increases in temporarily or permanently restricted net assets, depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of operations and changes in net assets released from restrictions.

Excess of Revenues over Expenses: The consolidated statements of operations and changes in net assets includes excess of revenues over expenses, commonly referred to as the performance indicator. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice include contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets), the effective portion of cash flow hedging derivatives, pension liability adjustments, and discontinued operations.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Net Assets: Unrestricted net assets are available for the general operating purposes of the System and are not subject to any donor limitations.

Temporarily restricted net assets are those whose use is limited by donors to a specific period or purpose and include the Hospitals' interest in the temporarily restricted net assets of the Mercy Hospital Foundation, Inc., Sisters Hospital Foundation, Inc., Kenmore Mercy Hospital Foundation, Inc., Mount St. Mary's Hospital Foundation, and Continuing Care Foundation, Inc. (collectively, the Foundations). Temporarily restricted net assets are released to unrestricted net assets as restrictions are met, which can occur in the same period. Gifts whose restrictions are met in the same period in which they are received are recorded as an increase in unrestricted net assets. Such restrictions include purpose restrictions where donors have specified the purpose for which the net assets are to be spent, or time restrictions imposed by donors or implied by the nature of the gift, pledges to be paid in future periods, or life income funds. Investment return is included in unrestricted net assets unless the return is restricted by donor or law.

Permanently restricted net assets have been restricted by donors to be maintained in perpetuity.

Temporarily Restricted Net Assets: Temporarily restricted net assets represent resources whose use is limited by donor-imposed stipulations that either expire by the passage of time or are met by specific-actions of the Foundations. Specific-actions most often involve completion of expenditures for purposes consistent with the donor's stipulations. When such donor-imposed stipulations are met, temporarily restricted net assets are reclassified to unrestricted net assets and reported on the statements of operations and changes in net assets as net assets released from restrictions used for capital. Temporarily restricted net assets, which amounted to \$7,767 at December 31, 2017 (\$8,124 – 2016), consist primarily of contributions restricted for use towards various capital projects at the Hospitals. Proceeds from these contributions are included in the balance sheets under the caption of cash and cash equivalents and investments. Contributions receivable are included under the caption of other receivables within the balance sheets.

Permanently Restricted Net Assets: Permanently restricted net assets include gifts which require, by donor restrictions, that the corpus be invested in perpetuity and only the income be made available for program operations in accordance with donor restrictions. Permanently restricted net assets, which amounted to \$297 at December 31, 2017 (\$294 – 2016), consist primarily of endowments.

Endowments: For the years ended December 31, 2017 and 2016, the Mercy Hospital Foundation, Inc. and the Sisters Hospital Foundation Inc., had \$246 of permanently restricted net assets from the proceeds of a Charitable Remainder Unitrusts (CRUT). The CRUTs are included under the caption of cash and cash equivalents within the balance sheets. The Foundations segregated these permanently restricted funds to enable preservation of purchasing power, as well as to ensure maintenance of the donor's intent. Mount St. Mary's Hospital Foundation, Inc. had \$51 of permanently restricted net assets, from the proceeds of a trust, as of December 31, 2017 (\$48 – 2016). The trust is included under the caption of cash and cash equivalents within the balance sheets. Per the trust agreement, earnings shall be divided such that half of the earnings are to be temporarily restricted to be used by the Foundation and the other half is to be added to the principal and remain permanently restricted.

Income Taxes: The consolidated financial statements do not include a provision for income taxes, as the System is a tax-exempt organization under Section 501(c) (3) of the Internal Revenue Code. The tax-exempt organizations are subject to federal taxes on unrelated business income under section 511 of the Internal Revenue Code which are reported as other expenses in these financial statements.

Transactions among Subsidiaries: Common costs incurred by CHS are allocated to the subsidiaries on a pro-rata cost basis formula. The allocation of these costs is recorded as other revenue by CHS and are recorded by the subsidiaries as a component of the natural account classification. The related income and expense is eliminated in the consolidated financial statements. The respective assets and liabilities are also eliminated in the consolidated financial statements.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Capitalized Software Costs: The System capitalizes certain costs that are incurred to purchase or to create and implement internal-use computer software, which includes software coding, installation, testing and certain data conversion from both internal and external providers in accordance with accounting guidance. These capitalized costs are amortized on a straight-line basis over ten years and reviewed for impairment on an annual basis. CHS capitalized software, computer equipment, and other external costs of \$6,811 during 2017 and \$3,089 during 2016. Capitalized project labor costs amounted to \$94 during 2017 and \$2,556 during 2016.

Reclassifications: Certain prior year amounts were reclassified to conform to the 2017 consolidated financial statement presentation.

Subsequent Events: The System evaluated subsequent events through April 26, 2018, which was the date the financial statements were available to be issued.

NOTE 3. ASSETS LIMITED AS TO USE

The composition of assets limited as to use is as follows at December 31:

	<u>2017</u>	<u>2016</u>
By Board for capital improvements:		
Funded depreciation:		
Cash and cash equivalents	\$ 7,322	\$ 7,184
U.S. government obligations	3,929	4,756
Interest receivable	21	22
	<u>11,272</u>	<u>11,962</u>
Held by Trustee under Indenture Agreement:		
Cash and cash equivalents	13,670	17,039
U.S. government obligations	962	-
	<u>14,632</u>	<u>17,039</u>
Held by Trustee under Letter of Credit Agreement:		
Cash and cash equivalents	<u>2,760</u>	<u>2,752</u>
Board Designated for long-term care reinvestment		
Cash and cash equivalents	<u>2,601</u>	<u>2,602</u>
Delivery System Reform Incentive Payment funds	<u>15,836</u>	<u>2,997</u>
Other	<u>836</u>	<u>707</u>
Assets limited as to use	<u>\$ 47,937</u>	<u>\$ 38,059</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**
*(in thousands of dollars)***NOTE 4. INVESTMENTS**

Investments consisted of the following as of December 31:

	<u>2017</u>	<u>2016</u>
Investment in debt and equity securities:		
Fair value	\$ 196,082	\$ 179,045
Cost	<u>174,146</u>	<u>174,103</u>
Unrealized gain	<u>\$ 21,936</u>	<u>\$ 4,942</u>

Investment income is summarized as follows for the years ended December 31:

	<u>2017</u>	<u>2016</u>
Interest and dividend income	\$ 2,453	\$ 2,105
Net unrealized and realized gains on investments	<u>17,667</u>	<u>3,849</u>
Investment income	<u>\$ 20,120</u>	<u>\$ 5,954</u>

NOTE 5. PROPERTY AND EQUIPMENT

Property and equipment, recorded at cost, consists of the following at December 31:

	<u>2017</u>	<u>2016</u>
Land and land improvements	\$ 8,126	\$ 7,802
Buildings	270,223	268,732
Equipment	280,988	258,494
Capital leases	45,235	44,600
Leasehold improvements	<u>117,765</u>	<u>113,344</u>
	722,337	692,972
Accumulated depreciation	(341,007)	(298,860)
Accumulated amortization on capital leases	<u>(36,574)</u>	<u>(31,831)</u>
	344,756	362,281
Construction in progress	<u>20,028</u>	<u>8,878</u>
Property and equipment, net	<u>\$ 364,784</u>	<u>\$ 371,159</u>

Depreciation expense in 2017 and 2016 amounted to approximately \$42,245 and \$39,880, respectively. Amortization expense on equipment under capital leases amounted to \$5,107 and \$5,591 in 2017 and 2016, respectively. There were no fully depreciated or amortized assets and capital leases written-off for the years ended December 31, 2017 and 2016.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 6. LONG-TERM OBLIGATIONS

Long-term obligations are comprised of the following at December 31:

	<u>2017</u>	<u>2016</u>
Mercy Hospital of Buffalo		
Series 2006 Revenue Bonds (a)	\$ 6,549	\$ 7,288
Series 2008 Revenue Bonds (b)	19,400	20,170
Series 2012 Revenue Bonds (c)	2,764	2,843
Series 2015 Revenue Bonds (d)	11,001	11,041
2017 Bridge loan financing (f)	6,472	-
Cafeteria renovation loan with Aramark Healthcare, in monthly payments of \$3, matures August 2018	71	176
Capital lease obligations and other, at interest rates ranging from 2.73% to 4.25%, collateralized by equipment	<u>8,441</u>	<u>10,335</u>
	<u>54,698</u>	<u>51,853</u>
Kenmore Mercy Hospital		
Series 2006 Revenue Bonds (a)	6,240	7,377
Series 2012 Revenue Bonds (c)	12,657	13,021
Series 2015 Revenue Bonds (d)	3,860	3,874
2016 Bridge loan financing (e)	5,449	5,822
Term Loan for KMH Homes, Inc. (g)	3,752	-
Capital lease obligations and other, at various rates of interest ranging from 2.98% to 4.00%, collateralized by equipment	3,057	4,057
Other	<u>6</u>	<u>17</u>
	<u>35,021</u>	<u>34,168</u>
Sisters of Charity Hospital		
Series 2006 Revenue Bonds (a)	18,761	20,873
Series 2015 Revenue Bonds (d)	5,188	5,206
2017 Bridge loan financing (f)	2,713	-
Capital lease obligations, at various rates of interest ranging from 3.13% to 4.87%, collateralized by equipment	<u>5,121</u>	<u>7,019</u>
	<u>31,783</u>	<u>33,098</u>
Mount St. Mary's Hospital and Health Center		
Capital lease obligations, at a 3.81% rate of interest, collateralized by equipment	<u>15</u>	<u>190</u>
Father Baker Manor		
Mortgage payable to Century Health Capital, Inc. (h)	<u>4,592</u>	<u>5,097</u>
McAuley Seton Home Health Care Corporation		
Term loan to bank (i)	<u>40</u>	<u>517</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 6. LONG-TERM OBLIGATIONS (CONTINUED)

	<u>2017</u>	<u>2016</u>
Our Lady of Victory Renaissance Corporation		
Series 2007A Variable Rate Demand Bonds (j)	7,810	8,140
Series 2007B Variable Rate Demand Bonds (j)	1,260	1,315
Loan payable with bank for Data Center (k)	-	120
	<u>9,070</u>	<u>9,575</u>
Trinity Medical WNY		
Capital lease obligations, at various rates of interest ranging from 3.15% to 5.79%, collateralized by equipment	<u>304</u>	<u>-</u>
Catholic Health System (Parent)		
Series 2015 Revenue Bonds (d)	80,825	82,014
Capital lease obligation for financing of VOIP telephone system, in monthly installments of \$22, including interest at 2.92% to 2.97%, collateralized by equipment	<u>269</u>	<u>784</u>
	<u>81,094</u>	<u>82,798</u>
Total long-term obligations	216,617	217,296
Less: Deferred financing costs	(5,757)	(6,224)
Less: Current maturities	<u>(18,157)</u>	<u>(15,312)</u>
Long-term obligations, net	<u>\$ 192,703</u>	<u>\$ 195,760</u>

a. In November 2006, the System executed a restructuring transaction related to its outstanding debt. The System formed the Catholic Health System Obligated Group (the Obligated Group), consisting of its three primary hospitals (Mercy Hospital of Buffalo, Sisters of Charity Hospital, and Kenmore Mercy Hospital) and CHS. No subsidiaries of CHS other than the Members of the Obligated Group were included in this offering. On November 29, 2006, \$68,820 of Dormitory Authority of the State of New York (DASNY) Catholic Health System Obligated Group Revenue Bonds, Series 2006 were issued. The bonds consisted of the following:

- Series 2006A Bonds for \$13,360 were loaned to Mercy Hospital of Buffalo in order to finance the cost of MHB's operating room expansion, other expansions and improvements at Mercy Hospital of Buffalo's facility.
- Series 2006B Bonds for \$30,295 were loaned to Sisters of Charity Hospital for the purpose of refunding DASNY's SCH Insured Revenue Bonds, Series 2003, which bonds were issued for the purpose of refunding a series of bonds issued in 1991, the proceeds of which were applied to finance the construction and renovation of the Sisters of Charity Hospital facilities and to refinance outstanding indebtedness. Series 2006D for \$8,435 was loaned to the former St. Joseph Hospital (SJH), which was merged into Sisters of Charity Hospital in 2009, to finance the cost of the SJH emergency room expansion project.
- Series 2006C Bonds for \$16,730 were loaned to Kenmore Mercy Hospital for the purpose of refunding the NYS Medical Care Facilities Finance Agency FHA - Insured Mortgage Project Revenue Bonds, 1995 Series B which were applied to finance the construction of a three floor patient tower, certain renovations to the Kenmore Mercy Hospital facility and to refinance outstanding indebtedness.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 6. LONG-TERM OBLIGATIONS (CONTINUED)

In connection with the issuance of the Series 2006 Bonds, the Obligated Group entered into a Loan Agreement (the Loan Agreement) whereby the Obligated Group is required to pay funds sufficient in timing and amount to pay the principal and redemption price of the Series 2006 Bonds and related interest and administrative expenses as they come due. The Series 2006 Bonds pay interest at a variable remarketed rate and are collateralized by a letter of credit with HSBC Bank which expires on November 29, 2019. In the event the letter of credit is not renewed at expiration, and no event of default exists, then the outstanding Bonds, at the option of the members of the Obligated Group, would be subject to a mandatory tender and will convert to a five year (initial) Term Loan. Repayment of the principal of Initial Term Loan shall be identical to the scheduled principal payments on the Bonds with the remaining amount due at the end of the five year term.

The interest borne by the Series 2006 Bonds will be determined by the Remarketing Agent to be the lowest rate that, in the judgment of the Remarketing Agent, under prevailing financial market conditions, enables such Series 2006 Bonds to be sold at a price of par. The variable interest rate was 1.75% and 0.72% at December 31, 2017 and 2016, respectively.

Certain financial covenants must be maintained by the Obligated Group. Failure to comply with these covenants requires a formal consultant's report and quarterly progress reports demonstrating how the facility is progressing towards compliance. The Loan Agreement requires the Obligated Group to comply with certain financial covenants, including maintenance of (i) a minimum number of days cash on hand; (ii) long-term debt service coverage; and (iii) a maximum leverage ratio. The Obligated Group was in compliance with these covenants at December 31, 2017 and 2016.

- b. On November 19, 2008, \$24,700 of DASNY - Catholic Health System Obligated Group Revenue Bonds, Series 2008 was issued. Series 2008 was loaned to the Obligated Group for the purpose of financing the cost of an approximately 48,300 square foot addition (Mercy Hospital of Buffalo) for a new emergency department, new imaging facilities, construction of a new main entrance and lobby area, a new ambulance entrance, construction of a rooftop helipad, renovation of library space into conference rooms, other mechanical and electrical improvements and associated demolition and equipment costs. Proceeds of the Series 2008 Bonds were also applied to pay certain costs of issuing the Bonds. The discount on the bonds of \$322 will be accreted over the life of the bonds.

The Series 2008 Bonds were issued under the Master Trust Indenture that was created in 2006 pursuant to the formation of the Obligated Group. All material components of the Series 2008 issue mirror the Series 2006 issue. Among these items are the following: 1) a variable remarketed rate (determined by the Security Industry and Financial Markets Association (SIFMA)) collateralized by a letter of credit with HSBC Bank expiring November 18, 2018 (with the option of an initial term loan), 2) a security interest in and assignment of gross receipts of the Mercy Hospital of Buffalo, together with the Mercy Hospital of Buffalo's right to receive or collect the gross receipts, 3) consistent financial covenants, and 4) execution of an interest rate swap agreement (with HSBC Bank) consistent with the terms utilized in the 2006 swap agreement (see Note 7). The variable interest rate was 1.71% and 0.72% at December 31, 2017 and 2016, respectively.

- c. On July 12, 2012, \$17,315 of DASNY Catholic Health System Obligated Group Revenue Bonds, Series 2012 were issued. The Bonds consisted of the following:
- Series 2012A Bonds for \$14,235 were loaned to Kenmore Mercy Hospital for the purpose of financing the cost of a new two-story addition, which includes approximately 19,000 square feet on the first floor for a new emergency department, an approximately 14,794 square feet shell space on the second floor, and an approximately 16,000 square feet basement, as well as the cost of renovating existing space, expanding the existing parking lot and related demolition, and other mechanical and infrastructure improvements. Proceeds of the Series 2012A Bonds were also applied to pay certain costs of issuing the Bonds. The discount and premium on the bonds of \$157 and \$159, respectively, are attributable to the difference between the stated interest rate on these bonds and will be amortized over the life of the bonds.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 6. LONG-TERM OBLIGATIONS (CONTINUED)

- Series 2012B Bonds for \$3,080 were loaned to Mercy Hospital of Buffalo for the purpose of funding the cost of improvements to MHB's existing approximately 381,000 square foot parking facility containing approximately 1,026 spaces. Proceeds of the Series 2012B Bonds were also applied to pay certain costs of issuing the Bonds. The discount and premium on the bonds of \$32 and \$46, respectively, are attributable to the difference between the stated interest rate on these bonds and will be amortized over the life of the bonds.

The Series 2012 Bonds were issued under the Master Trust Indenture that was created in 2006 pursuant to the formation of the Obligated Group. In connection with the issuance of the Series 2012 Bonds, the Obligated Group entered into a Loan Agreement whereby the Obligated Group is required to make monthly payments sufficient to pay, among other things, the principal and Sinking Fund Installments of and interest on the Series 2012 Bonds as they become due. The Series 2012 Bonds bear interest at a fixed rate. The interest rates, maturities, and aggregate principal amounts outstanding at December 31, 2017 are as follows:

4.00% Serial Bonds Due July 1, 2018	\$ 370
3.50% Term Bonds Due July 1, 2022	1,610
4.00% Term Bonds Due July 1, 2027	2,385
5.00% Term Bonds Due July 1, 2032 (i)	2,960
4.75% Term Bonds Due July 1, 2039	<u>5,530</u>
Total Series 2012A Bonds	<u>12,855</u>
3.50% Term Bonds Due July 1, 2022	710
5.00% Term Bonds Due July 1, 2032 (i)	1,160
4.75% Term Bonds Due July 1, 2039	<u>1,210</u>
Total Series 2012B Bonds	<u>3,080</u>
Total Series 2012 Bonds	<u>\$ 15,935</u>

- (i) Optional redemption on July 1, 2022 at a redemption price of 100% of the principal amount of such Series 2012 Bonds or portions thereof to be redeemed, plus accrued interest to the redemption date.

The Series 2006, 2008 and 2012 Loan Agreements specifies that the Obligated Group shall continuously pledge, as security for the payment of all liabilities and the performance of all obligations of the Obligated Group pursuant to the Loan Agreement, a security interest in and assignment of the gross receipts of the Obligated Group, together with the Hospitals' right to receive or collect the gross receipts. Further, the Obligated Group delivered a mortgage to secure all obligations and liabilities of the Hospitals under the Loan Agreement. As further security to the Loan Agreement, the Obligated Group granted DASNY a security interest in such fixtures, furnishings and equipment as owned by the Obligated Group. In addition, a letter of credit in the amount of the bonds was entered into with HSBC Bank to provide security on the 2006 Bonds. The financial covenants required under the Loan Agreement are consistent with those of the Series 2006 Bonds and Series 2008 Bonds.

- d. On April 29, 2015, \$93,800 of Buffalo and Erie County Industrial Land Development Corporation Catholic Health System Obligated Group Revenue Bonds, Series 2015 were issued. Series 2015 was loaned to the Obligated Group for the purpose of financing the cost of improvements to the Labor & Delivery department, Pre/Post-Operative Holding areas, upgrading the electrical switchgear (Mercy Hospital of Buffalo), Ambulatory Surgery Center (Sisters Hospital, St. Joseph Campus), Operating Room Expansion (Kenmore Mercy Hospital), Enterprise Resource Planning software, leasehold improvements to the Administrative Regional Training Center, and purchase of the Administrative Regional Training Center (Catholic Health System). Proceeds of the Series 2015 Bonds were also applied to pay certain costs of issuing the Bonds. The premium on the bonds of \$9,968 is attributable to the difference between the stated interest rate on these bonds and will be amortized over the life of the bonds.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 6. LONG-TERM OBLIGATIONS (CONTINUED)

The Series 2015 Bonds were issued under the Master Trust Indenture that was created in 2006 pursuant to the formation of the Obligated Group. In connection with the issuance of the Series 2015 Bonds, the Obligated Group entered into a Loan Agreement whereby the Obligated Group is required to make monthly payments sufficient to pay, among other things, the principal and Sinking Fund Installments of and interest on the Series 2015 Bonds as they become due. The Series 2015 Bonds bear interest at a fixed rate. The interest rates, maturities, and aggregate principal amounts outstanding at December 31, 2017 are as follows:

5.00% Serial Bonds Due July 1, 2018	\$	3,520
5.00% Serial Bonds Due July 1, 2019		3,690
5.00% Serial Bonds Due July 1, 2020		3,870
5.00% Serial Bonds Due July 1, 2021		4,075
5.00% Serial Bonds Due July 1, 2022		4,265
5.00% Serial Bonds Due July 1, 2023		4,480
5.00% Serial Bonds Due July 1, 2024		4,705
5.00% Serial Bonds Due July 1, 2025		4,955
5.00% Serial Bonds Due July 1, 2026		1,900
5.00% Serial Bonds Due July 1, 2027		1,995
5.00% Serial Bonds Due July 1, 2028		2,095
5.00% Serial Bonds Due July 1, 2029		2,200
5.00% Serial Bonds Due July 1, 2030		2,305
5.25% Term Bonds Due July 1, 2035		13,440
5.00% Term Bonds Due July 1, 2040		17,275
4.00% Term Bonds Due July 1, 2045		<u>17,630</u>
Total Series 2015 Bonds	\$	<u>92,400</u>

- e. On December 30, 2016, Kenmore Mercy Hospital entered into a loan agreement with HSBC Bank in the amount of \$5,822. The term loan calls for monthly principal payments of \$45 plus interest (30-day LIBOR plus 200). The loan matures on December 30, 2021 with a balloon payment of the outstanding balance at that time.
- f. On April 7, 2017, Mercy Hospital of Buffalo and Sisters of Charity Hospital entered into two loan agreements with KeyBank in the amount of \$14,000 and \$7,000, respectively. The term loans are an interest only draw period through August 1, 2018. At that time, the term loan will be repaid over a term of up to 5 years amortized over 120 months. A balloon payment will be due at the end of the 5 year term. Principal payments will be determined based on amount drawn as of August 1, 2018.
- g. On December 20, 2017, KMH Homes, Inc. entered into a term note with M&T Bank in the amount of \$3,752. The loan calls for monthly payments of \$64, which includes principal and interest. Initial payment is expected to be paid February 1, 2018 with the final payment in July 2023. The debt is guaranteed by the Obligated Group.
- h. Mortgage payable to Century Health Capital (an FHA - Insured Mortgage). The mortgage is payable in monthly installments of \$64 including interest of 5.375%. Monthly payments continue through maturity in March 2025. The mortgage is collateralized by the building and equipment.
- i. MSHC entered into a term loan agreement with HSBC Bank in the amount of \$2,385. Outstanding borrowings under this agreement bear interest at a fixed rate of 2.62% at December 31, 2017 and 2016. The term loan calls for monthly principal payments of \$40 plus interest and matures on December 28, 2017. The term loan was paid in full subsequent to year end in January 2018. Outstanding borrowings are secured by substantially all the revenues and receipts of MSHC. The term loan contains various loan covenants, including a debt service coverage ratio. MSHC was in compliance with all covenants as of December 31, 2017 and 2016.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 6. LONG-TERM OBLIGATIONS (CONTINUED)

- j. On April 1, 2007, OLV Renaissance entered into agreements with the Erie County Industrial Development Agency (the Agency) for the purpose of obtaining revenue bonds used to finance construction of its SNF and PACE facilities. The agency took title to the facility through a lease agreement and simultaneously conveyed title back to OLV Renaissance through an installment sale of the lease interests. OLV Renaissance is obligated to make lease rental payments to the bond trustee, as the Agency's assignee, in amounts which correspond to the principal and interest payments on the bonds. At the expiration of the leases' term (April 2032), title fully reverts back to OLV Renaissance. On April 25, 2007, the Agency issued variable rate demand revenue bonds with an aggregate principal amount of \$11,860. The bond issue consists of two series of bonds: \$10,220 in variable rate demand Revenue Bonds Series 2007A (Series 2007A Bonds) and \$1,640 in variable rate demand Revenue Bonds Series 2007B (Series 2007B Bonds).

The Variable Interest Rate is determined by the remarketing agent based on (1) market interest rates for comparable securities; (2) other financial market rates and indices (including, but not limited to treasury bills, commercial paper, commercial bank prime rates, HUD project notes, federal fund rates and LIBOR); (3) general financial and credit market conditions; (4) credit rating and financial condition of OLV Renaissance; and (5) applicable tender provisions which may have bearing on the rate. The variable interest rate was 1.84% and 0.87% for the Series 2007A bonds and 1.59% and 1.40% for the Series 2007B bonds at December 31, 2017 and 2016, respectively. See Note 7 regarding the interest rate swap agreement OLV Renaissance entered into with respect to the Series 2007A Revenue Bonds.

The bonds are subject to conversion to a fixed interest rate at the written direction of OLV Renaissance. Upon conversion, the remarketing agent shall determine the fixed interest rate as the lowest rate of interest that would be necessary to sell the bonds in the secondary market at par plus accrued interest, based on prevailing market conditions and the yields at which comparable securities are being sold.

The Series 2007A Revenue Bonds are subject to mandatory sinking fund redemptions in years 2016 to 2032 in amounts ranging from \$310 to \$740 at variable interest rates. The Series 2007B Revenue Bonds are subject to mandatory sinking fund redemptions in years 2016 to 2032 in amounts ranging from \$55 to \$115.

Under the terms of the financing documents, OLV Renaissance has guaranteed payment of all amounts due under the Bonds. Additionally, the bonds are secured by first mortgage liens on all buildings, improvements and equipment now owned or subsequently acquired by OLV Renaissance, all unrestricted accounts receivable and a right of setoff against OLV Renaissance's funds held by the trustee.

In accordance with the financing documents, at the option of the Issuer and upon notice given by OLV Renaissance, the Series 2007A Revenue Bonds are subject to optional redemption at 100%. In connection with the Bond financing, OLV Renaissance has executed an irrevocable direct pay letter of credit with a financial institution for a maximum amount of \$10,261. The letter of credit expires May 1, 2020. There is no outstanding amount at December 31, 2017 or 2016. OLV Renaissance is required to pay an annual fee of 1.25% to maintain the letter of credit which is calculated on maximum amount available.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 6. LONG-TERM OBLIGATIONS (CONTINUED)

The bond agreements require certain covenants including debt service coverage and debt to capitalization to be maintained. OLV Renaissance's primary tenant, MHB is also required to comply with a covenant to maintain minimum long-term debt service coverage and a minimum days cash on hand as of any testing date.

MHB was in compliance with this covenant as of December 31, 2017 and 2016. OLV Renaissance was in compliance with this covenant as of December 31, 2017 and 2016.

- k. On December 28, 2011, OLV Renaissance entered into a term loan agreement with HSBC Bank, for the construction of a Data Center on the OLV Renaissance Campus. OLV Renaissance is obligated to make payments each month until expiration on December 31, 2016. The term loan bears interest at 3.05% repayable in monthly installments ranging from \$95 to \$110 plus interest beginning January 2012 through December 2016. The loan was paid off in full as of December 31, 2017.

Aggregate maturities of long-term debt, including capital lease obligations, considering obligations subject to short-term remarketing as due according to their long-term amortization schedule, subsequent to December 31, 2017 are as follows:

	<u>Long-Term Debt</u>	<u>Capital Leases</u>	<u>Total</u>
2018	\$ 13,202	\$ 5,167	\$ 18,369
2019	12,325	3,756	16,081
2020	12,867	2,736	15,603
2021	13,716	1,574	15,290
2022	16,496	1,098	17,594
Thereafter	<u>131,079</u>	<u>4,653</u>	<u>135,732</u>
	199,685	18,984	218,669
Less: Deferred financing costs	(5,757)	-	(5,757)
Less: Interest	<u>-</u>	<u>(2,052)</u>	<u>(2,052)</u>
Long-term obligations	<u>\$ 193,928</u>	<u>\$ 16,932</u>	<u>\$ 210,860</u>

The System had a revolving line of credit of \$20,000 of which \$4,310 was outstanding as of December 31, 2016 with a variable interest rate of 2.61%. At December 31, 2017, there was no amount outstanding on the revolving line of credit.

Operating Leases: Future minimum lease payments under noncancelable operating leases for equipment and property (net of sublease rentals) are as follows at December 31, 2017:

2018	\$ 10,509
2019	8,742
2020	8,194
2021	7,551
2022	5,570
Thereafter	<u>4,324</u>
	44,890
Less: Minimum sublease rental	<u>(2,159)</u>
	<u>\$ 42,731</u>

Total expense for rents and operating type leases for equipment and property was approximately \$13,012 and \$13,048 for 2017 and 2016, respectively.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 7. DERIVATIVE FINANCIAL INSTRUMENTS

In connection with the Series 2006 and 2008 Bonds and execution of the Loan Agreement, the Hospitals entered into interest rate swap agreements (derivative agreements) with HSBC Bank USA, NA and JP Morgan Chase (the Financial Institutions) for purposes of mitigating risk posed by the Bonds accruing interest at a variable rate. Further, the Hospitals agreed not to take or omit to take any action that could reasonably be expected to result in the termination of the derivative agreement unless otherwise approved by the Financial Institutions, provided, however, that termination of the derivative agreement shall not constitute an event of default for purposes of the Loan Agreement, but upon any such termination of the derivative agreement, the Financial Institutions may require that the Hospitals direct the Series 2006 or Series 2008 Bonds be converted to bonds that bear a fixed rate of interest. The interest rate swap agreements outstanding on the Series 2006 Bonds were settled in 2014. Termination costs in the amount of \$5,772 will be amortized over the remaining life of the bonds. Amortization expense related to the termination costs was \$783 and \$869 for 2017 and 2016, respectively.

The terms of the Series 2008 swap require the Hospitals to pay 3.785% on the notional amount of \$20,020 and \$20,785 at December 31, 2017 and 2016, respectively, and in exchange, the Hospitals will receive a variable rate payment based upon the SIFMA, calculated weekly. The 2008 swap agreement was executed on November 19, 2008 and expires on July 1, 2034. These dates correlate to the issue date and due date of the Bonds. The instrument qualifies for hedge treatment and is designated a cash flow hedge of future interest payments. The effective portion of the hedge has been excluded from excess of revenues over expenses and recorded within changes to net assets.

During 2007, OLV Renaissance entered into a hedging agreement with respect to interest rate exposure on the Series 2007A Revenue Bond. OLV Renaissance uses the interest rate swap agreement to reduce its exposure to interest rate changes. The interest rate swap fixes the interest rate paid by OLV Renaissance at 4.143% over the life of the bond, which matures in April 2032. The instrument qualifies for hedge treatment and is designated a cash flow hedge of future interest payments. The effective portion of the hedge has been excluded from excess of revenues over expenses and recorded within changes to net assets.

The fair value of derivative instruments at December 31 is as follows:

(in thousands of dollars)	2017		2016	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Interest rate contracts floating to fixed	Long-term liabilities	\$ <u>4,513</u>	Long-term liabilities	\$ <u>4,832</u>

The effects of derivative instruments on the consolidated statements of operations and changes in net assets for 2017 and 2016 are as follows:

(in thousands of dollars)	Ineffective portion in Statement of Operations		Effective portion in Net Assets	
	2017	2016	2017	2016
Change in fair value of interest rate swaps	\$ <u>6</u>	\$ <u>28</u>	\$ <u>313</u>	\$ <u>1,262</u>

The Hospitals measure their interest rate swaps at fair value on a recurring basis. The fair value of the interest rate swaps is determined based on financial models that consider current and future market interest rates and adjustments for nonperformance risk. The inputs utilized in the valuation process of the interest rate swaps are considered to be Level 2 within the fair value hierarchy defined in Note 13.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 8. OBLIGATED GROUP FINANCIAL INFORMATION

In November 2006, the System formed the Obligated Group, consisting of its three primary hospitals (MHB, SCH, which includes St. Joseph Hospital (SJH), and KMH) and the Parent. In 2006, the System issued \$68,820 of DASNY Catholic Health System Obligated Group Revenue Bonds, Series 2006. In 2008, the System issued \$24,700 of DASNY - Catholic Health System Obligated Group Revenue Bonds, Series 2008. In 2012, the System issued \$17,315 of DASNY – Catholic Health System Obligated Group Revenue Bonds, Series 2012. In 2015, the System issued \$93,800 of Buffalo and Erie County Industrial Land Development Corporation Revenue Bonds, Series 2015. These Revenue Bonds are joint and several obligations of the members of the Obligated Group. No affiliate of CHS, other than Members of the Obligated Group, is obligated for amounts due under the Series 2006, Series 2008, Series 2012, and Series 2015 Obligations. Management has determined that certain immaterial subsidiaries (Mercy Hospital Foundation, Inc., Sisters Hospital Foundation, Inc., Kenmore Mercy Hospital Foundation, Inc., and KMH Homes, Inc.) should be excluded from the Obligated Group financial information.

The following supplemental consolidating financial information for the Obligated Group presents the balance sheets as of December 31, 2017 and 2016 and statements of operations and changes in net assets, and cash flows for the years then ended December 31, 2017 and 2016.

These statements do not represent the results of the System.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 8. OBLIGATED GROUP FINANCIAL INFORMATION (CONSOLIDATED)

Consolidating Balance Sheet
December 31, 2017

ASSETS	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Current assets:						
Cash and cash equivalents	\$ 55,556	\$ 55,311	\$ 53,427	\$ 36,438	\$ -	\$ 200,732
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$16,694	-	49,200	34,783	20,941	-	104,924
Other receivables	778	2,641	2,268	690	-	6,377
Inventories	8	13,517	6,780	2,825	-	23,130
Prepaid expenses and other current assets	5,629	1,970	1,705	431	-	9,735
Due from affiliates	100,247	354	770	67	(99,118)	2,320
Total current assets	<u>162,218</u>	<u>122,993</u>	<u>99,733</u>	<u>61,392</u>	<u>(99,118)</u>	<u>347,218</u>
Assets limited as to use	13,202	2,683	16,315	2,776	-	34,976
Investments	-	32,488	96,545	23,183	-	152,216
Property and equipment, net	84,154	99,626	71,048	65,637	-	320,465
Due from affiliates	5,116	-	10,303	1,456	(16,875)	-
Other assets	11,946	41,190	36,908	13,155	-	103,199
Total Assets	<u>\$ 276,636</u>	<u>\$ 298,980</u>	<u>\$ 330,852</u>	<u>\$ 167,599</u>	<u>\$ (115,993)</u>	<u>\$ 958,074</u>
LIABILITIES AND NET ASSETS						
Current liabilities:						
Current portion of long-term obligations	\$ 5,049	\$ 4,181	\$ 4,134	\$ 3,601	\$ -	\$ 16,965
Accounts payable	7,401	17,762	14,201	8,938	-	48,302
Accrued expenses	21,728	14,614	27,899	6,558	-	70,799
Due to third-party payors	-	16,336	11,119	5,303	-	32,758
Due to affiliates	784	23,439	25,463	23,655	(71,872)	1,469
Total current liabilities	<u>34,962</u>	<u>76,332</u>	<u>82,816</u>	<u>48,055</u>	<u>(71,872)</u>	<u>170,293</u>
Long-term obligations, net	73,947	49,131	26,889	30,370	-	180,337
Other long-term obligations, net	75,112	217,743	139,471	53,588	(11,760)	474,154
Total liabilities	<u>184,021</u>	<u>343,206</u>	<u>249,176</u>	<u>132,013</u>	<u>(83,632)</u>	<u>824,784</u>
Net assets (deficit)						
Unrestricted	92,615	(44,226)	81,676	35,586	(32,361)	133,290
Total net assets (deficit)	<u>92,615</u>	<u>(44,226)</u>	<u>81,676</u>	<u>35,586</u>	<u>(32,361)</u>	<u>133,290</u>
Total Liabilities and net assets	<u>\$ 276,636</u>	<u>\$ 298,980</u>	<u>\$ 330,852</u>	<u>\$ 167,599</u>	<u>\$ (115,993)</u>	<u>\$ 958,074</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 8. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

Consolidating Statement of Operations
and Changes in Net Assets
Year Ended December 31, 2017

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Unrestricted revenues and other support:						
Net patient/resident service revenue	\$ -	420,858	\$ 333,222	\$ 173,005	\$ (97)	\$ 926,988
Provision for bad debts	-	(8,120)	(7,551)	(3,655)	-	(19,326)
Net patient/resident service revenue, less provision for bad debts	-	412,738	325,671	169,350	(97)	907,662
Other revenue	152,296	5,017	12,238	1,308	(136,805)	34,054
Total unrestricted revenues and other support	152,296	417,755	337,909	170,658	(136,902)	941,716
Expenses:						
Salaries and wages	75,709	180,004	149,842	71,498	(63,972)	413,081
Employee benefits	21,762	56,875	43,617	20,280	(19,209)	123,325
Medical and professional fees	4,375	22,888	15,241	4,882	(2,783)	44,603
Purchased services	32,050	35,661	32,284	15,513	(29,853)	85,655
Supplies	904	81,380	57,071	38,658	(745)	177,268
Depreciation and amortization	7,868	17,216	14,560	9,029	(7,532)	41,141
Interest	3,281	3,906	2,793	2,304	(2,898)	9,386
Insurance	518	6,228	4,836	2,146	(493)	13,235
Other expenses	6,894	15,084	10,242	4,699	(10,298)	26,621
Total expenses	153,361	419,242	330,486	169,009	(137,783)	934,315
Income (loss) from operations	(1,065)	(1,487)	7,423	1,649	881	7,401
Nonoperating revenues:						
Investment income	312	3,772	8,880	2,145	-	15,109
Other, net	538	360	317	131	(881)	465
Total nonoperating revenues	850	4,132	9,197	2,276	(881)	15,574
Excess (deficiency) of revenues over expenses	\$ (215)	\$ 2,645	\$ 16,620	\$ 3,925	\$ -	\$ 22,975

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 8. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

Consolidating Statement of Operations
and Changes in Net Assets (Continued)

Year Ended December 31, 2017

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Unrestricted net assets:						
Excess (deficiency) of revenues over expenses	\$ (215)	\$ 2,645	\$ 16,620	\$ 3,925	\$ -	\$ 22,975
Change in unrealized gain on interest rate swap	-	191	-	-	-	191
Change in pension obligation, other than net periodic cost	(6,405)	(11,331)	(7,706)	(999)	-	(26,441)
Transfers (to) from parent or affiliate	26,010	(8,683)	(11,599)	(6,203)	-	(475)
Contributions and other	94	489	1,269	1,598	-	3,450
Valuation allowance on intercompany receivables	-	-	-	-	(10,598)	(10,598)
(Decrease) increase in unrestricted net assets	<u>19,484</u>	<u>(16,689)</u>	<u>(1,416)</u>	<u>(1,679)</u>	<u>(10,598)</u>	<u>(10,898)</u>
(Decrease) increase in net assets	19,484	(16,689)	(1,416)	(1,679)	(10,598)	(10,898)
Net assets, beginning of year	<u>73,131</u>	<u>(27,537)</u>	<u>83,092</u>	<u>37,265</u>	<u>(21,763)</u>	<u>144,188</u>
Net assets (deficit), end of year	<u>\$ 92,615</u>	<u>\$ (44,226)</u>	<u>\$ 81,676</u>	<u>\$ 35,586</u>	<u>\$ (32,361)</u>	<u>\$ 133,290</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 8. OBLIGATED GROUP FINANCIAL INFORMATION (CONSOLIDATED)

Consolidating Balance Sheet
December 31, 2016

ASSETS	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Current assets:						
Cash and cash equivalents	\$ 40,750	\$ 48,531	\$ 57,712	\$ 35,580	\$ -	\$ 182,573
Patient/resident accounts receivable, net of estimated uncollectibles of \$21,427	-	46,269	35,114	20,169	-	101,552
Other receivables	690	2,685	3,928	617	-	7,920
Inventories	-	11,570	6,725	2,815	-	21,110
Prepaid expenses and other current assets	4,448	3,157	1,633	766	-	10,004
Due from affiliates	88,819	49	1,104	301	(84,466)	5,807
Total current assets	<u>134,707</u>	<u>112,261</u>	<u>106,216</u>	<u>60,248</u>	<u>(84,466)</u>	<u>328,966</u>
Assets limited as to use	15,630	2,682	3,476	2,740	-	24,528
Investments	-	29,667	88,160	21,170	-	138,997
Property and equipment, net	87,721	102,371	68,154	68,202	-	326,448
Due from affiliates	6,636	-	10,303	1,457	(16,876)	1,520
Other assets	11,328	45,684	37,177	15,987	-	110,176
Total Assets	<u>\$ 256,022</u>	<u>\$ 292,665</u>	<u>\$ 313,486</u>	<u>\$ 169,804</u>	<u>\$ (101,342)</u>	<u>\$ 930,635</u>
LIABILITIES AND NET ASSETS						
Current liabilities:						
Current portion of long-term obligations	\$ 2,783	\$ 4,070	\$ 4,260	\$ 2,536	\$ -	\$ 13,649
Line of credit payable	4,310	-	-	-	-	4,310
Accounts payable	6,649	14,593	10,680	7,408	-	39,330
Accrued expenses	20,502	14,485	14,681	6,854	-	56,522
Due to third-party payors	-	16,789	12,355	6,763	-	35,907
Due to affiliates	452	15,109	29,574	23,239	(67,819)	555
Total current liabilities	<u>34,696</u>	<u>65,046</u>	<u>71,550</u>	<u>46,800</u>	<u>(67,819)</u>	<u>150,273</u>
Long-term obligations, net	77,789	46,300	27,992	30,489	-	182,570
Other long-term liabilities	70,406	208,856	130,852	55,250	(11,760)	453,604
Total liabilities	<u>182,891</u>	<u>320,202</u>	<u>230,394</u>	<u>132,539</u>	<u>(79,579)</u>	<u>786,447</u>
Net assets (deficit)						
Unrestricted	73,131	(27,537)	83,092	37,265	(21,763)	144,188
Total net assets (deficit)	<u>73,131</u>	<u>(27,537)</u>	<u>83,092</u>	<u>37,265</u>	<u>(21,763)</u>	<u>144,188</u>
Total Liabilities and Net Assets	<u>\$ 256,022</u>	<u>\$ 292,665</u>	<u>\$ 313,486</u>	<u>\$ 169,804</u>	<u>\$ (101,342)</u>	<u>\$ 930,635</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 8. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

Consolidating Statement of Operations
and Changes in Net Assets
Year Ended December 31, 2016

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Unrestricted revenues, gains and other support:						
Net patient/resident service revenue	\$ -	406,659	\$ 328,488	\$ 170,876	\$ (80)	\$ 905,943
Provision for bad debts	-	(5,823)	(6,773)	(3,052)	-	(15,648)
Net patient/resident service revenue less provision for bad debts	-	400,836	321,715	167,824	(80)	890,295
Other revenue	150,353	4,901	11,383	1,406	(138,006)	30,037
Total unrestricted revenues, gains and other support	150,353	405,737	333,098	169,230	(138,086)	920,332
Expenses:						
Salaries and wages	70,905	169,673	145,760	70,113	(62,342)	394,109
Employee benefits	21,163	57,503	44,147	20,470	(19,071)	124,212
Medical and professional fees	4,613	18,279	13,272	4,744	(3,226)	37,682
Purchased services	34,568	39,629	31,822	15,232	(32,518)	88,733
Supplies	831	86,209	58,852	39,884	(667)	185,109
Depreciation and amortization	7,700	16,588	14,582	8,766	(7,641)	39,995
Interest	3,461	3,736	2,764	2,154	(2,987)	9,128
Insurance	527	5,121	4,580	2,303	(478)	12,053
Other expenses	9,148	17,145	10,136	5,187	(11,750)	29,866
Total expenses	152,916	413,883	325,915	168,853	(140,680)	920,887
Income (loss) from operations	(2,563)	(8,146)	7,183	377	2,594	(555)
Nonoperating revenues and losses:						
Investment income	51	875	462	213	-	1,601
Other	2,512	875	3,108	890	(2,594)	4,791
Total nonoperating revenues and losses:	2,563	1,750	3,570	1,103	(2,594)	6,392
Excess (deficiency) of revenues over expenses	\$ -	\$ (6,396)	\$ 10,753	\$ 1,480	\$ -	\$ 5,837

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 8. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

Consolidating Statement of Operations
and Changes in Net Assets (Continued)

Year Ended December 31, 2016

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Unrestricted net assets:						
Excess (deficiency) of revenues over expenses	\$ -	\$ (6,396)	\$ 10,753	\$ 1,480	\$ -	\$ 5,837
Change in unrealized gain on interest rate swap	-	887	-	-	-	887
Change in pension obligation, other than net periodic cost	1,122	3,839	3,941	1,439	-	10,341
Grant revenue for capital expenditures	-	125	-	-	-	125
Transfers (to) from parent or affiliate	25,433	(12,853)	(9,569)	(3,029)	-	(18)
Contributions and other	136	528	635	651	-	1,950
Valuation allowance on intercompany receivables	-	-	-	-	(3,571)	(3,571)
Increase (decrease) in unrestricted net assets	<u>26,691</u>	<u>(13,870)</u>	<u>5,760</u>	<u>541</u>	<u>(3,571)</u>	<u>15,551</u>
Increase (decrease) in net assets	26,691	(13,870)	5,760	541	(3,571)	15,551
Net assets, beginning of year	<u>46,440</u>	<u>(13,667)</u>	<u>77,332</u>	<u>36,724</u>	<u>(18,192)</u>	<u>128,637</u>
Net assets (deficit), end of year	<u>\$ 73,131</u>	<u>\$ (27,537)</u>	<u>\$ 83,092</u>	<u>\$ 37,265</u>	<u>\$ (21,763)</u>	<u>\$ 144,188</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

Consolidating Statements of Cash Flows

For the Years Ended December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities:		
(Decrease) increase in net assets	\$ (10,898)	\$ 15,551
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities		
Depreciation and amortization	41,141	39,995
Provision for bad debts	19,326	15,648
Change in minimum pension liability adjustment	26,441	(10,341)
Grant revenue for capital additions	-	(125)
Valuation allowance of intercompany receivables	10,598	3,571
Unrealized and realized loss on investments	(13,230)	(2,759)
Change in unrealized gain on interest rate swap	(194)	(904)
Gain on extinguishment of capital leases	-	(1,967)
Undistributed earnings in equity investees	(267)	(240)
Amortization of discount on debt issuance	61	62
Amortization of premium on debt issuance	(574)	(575)
Amortization of debt issuance costs	403	392
Other	(140)	729
(Increase) decrease in assets		
Patient accounts receivables	(22,698)	3,391
Other receivables	1,543	3,516
Inventories	(2,020)	2,585
Prepaid expenses and other current assets	269	(4,286)
Due from affiliates	(5,591)	(2,420)
Other assets	(16)	14
Increase (decrease) in liabilities:		
Accounts payable	7,230	(6,818)
Accrued expenses	1,438	(1,561)
Due to affiliate	914	(236)
Due to third-party payors	(3,149)	(590)
Other liabilities	1,416	13,851
Net cash and cash equivalents provided by operating activities	<u>52,003</u>	<u>66,483</u>
Cash flows from investing activities:		
Purchase of property and equipment	(32,329)	(50,647)
Proceeds from sale of property and equipment	286	9
Purchase of assets limited as to use	(33)	-
Proceeds from sale of assets limited as to use	2,435	50,067
Purchase of investments	(434)	(136,238)
Net cash and cash equivalents used in investing activities	<u>(30,075)</u>	<u>(136,809)</u>
Cash flows from financing activities:		
Proceeds from issuance of long-term obligations	12,937	5,786
Proceeds of grant revenue for capital additions	-	125
Repayments of current and long-term obligations	(16,706)	(58,178)
Net cash and cash equivalents used in financing activities	<u>(3,769)</u>	<u>(52,267)</u>
Increase (decrease) in cash and cash equivalents	<u>18,159</u>	<u>(122,593)</u>
Cash and cash equivalents - beginning of year	<u>182,573</u>	<u>305,166</u>
Cash and cash equivalents - end of year	<u>\$ 200,732</u>	<u>\$ 182,573</u>
Supplemental disclosures of cash flow information		
Cash paid during the year for interest	\$ 7,795	\$ 7,820
Non-cash transactions		
Assets acquired under capital lease obligations	\$ 652	\$ 1,990
Construction Related Payables	\$ 1,742	\$ (981)

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 8. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

The Obligated Group provides healthcare services to residents within its geographic region. Expenses related to providing these services for the year ended December 31, are as follows:

	<u>2017</u>	<u>2016</u>
Healthcare services	\$ 781,196	\$ 776,184
General and administrative	<u>153,119</u>	<u>144,703</u>
	<u>\$ 934,315</u>	<u>\$ 920,887</u>

NOTE 9. EMPLOYEE BENEFIT PLANS

Pension Arrangements: Effective January 1, 2001, the System began maintaining a qualified defined benefit pension plan covering substantially all of its employees at its constituent hospitals. As of that date, active participants in the KMH, MHB, and SCH plans who were employed at the Hospitals are covered under the Retirement Plan of the Catholic Health System (the Plan). Effective January 1, 2002, all other entities in the System, with the exception of the Nazareth Home, began participation in the Plan. Pension assets and liabilities from legacy plans, if any, were transferred to the Plan on September 25, 2002.

Effective January 1, 2001 or 2002, as applicable, all nonunion employees who had met the age and service requirements under their previous plan were given the option of choosing to participate in the cash balance feature of the Plan. Those who choose not to participate in the cash balance feature accrue benefits under the same formula as their previous plan. All nonunion employees who become participants after that date automatically participate under the cash balance formula.

The Plan bases benefits upon both years of service and earnings. Participants under the Hospitals formula earn benefits under a final average formula or a career average formula. The cash balance formula is a hypothetical account balance formula. A participant's benefit obligation is assigned to the location at which the person works. As participants transfer within the System to other CHS subsidiaries, the obligations and a proportional amount of the plan's assets transfer, accordingly.

Funded Status: The following tables summarize changes in the projected benefit obligation, the plan assets and the funded status of the CHS pension plan as well as the components of net periodic benefit costs, including key assumptions as of December 31.

	<u>2017</u>	<u>2016</u>
Projected Benefit Obligations		
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 636,377	\$ 605,150
Service cost	21,904	22,295
Interest cost	27,510	27,659
Expenses	(424)	(444)
Benefits paid	(21,093)	(18,698)
Actuarial loss	<u>61,234</u>	<u>415</u>
Projected benefit obligation at end of year	<u>\$ 725,508</u>	<u>\$ 636,377</u>
Accumulated benefit obligations at end of year	<u>\$ 658,757</u>	<u>\$ 576,683</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 9. EMPLOYEE BENEFIT PLANS (CONTINUED)

	<u>2017</u>	<u>2016</u>
Plan Assets		
Change in plan assets:		
Fair value of assets at beginning of year	\$ 328,601	\$ 298,106
Actual return on plan assets	48,725	25,294
System contribution	33,131	24,343
Expenses	(424)	(444)
Benefits paid	<u>(21,093)</u>	<u>(18,698)</u>
Fair value of plan assets at end of year	<u>\$ 388,940</u>	<u>\$ 328,601</u>
Funded status at end of year	<u>\$ (336,568)</u>	<u>\$ (307,776)</u>
Amounts recognized in the consolidated balance sheets:		
Non-current liabilities	<u>\$ (336,568)</u>	<u>\$ (307,776)</u>
Net amounts recognized	<u>\$ (336,568)</u>	<u>\$ (307,776)</u>
Amounts recognized in unrestricted net assets consists of:		
Actuarial net loss	\$ (200,534)	\$ (172,219)
Prior service cost	<u>(252)</u>	<u>(309)</u>
Total amount recognized	<u>\$ (200,786)</u>	<u>\$ (172,528)</u>
Other changes recognized in unrestricted net assets:		
Net loss arising during the period	\$ 37,746	\$ 28,374
Amortization of prior service cost	(57)	(129)
Amortization of loss	<u>(9,430)</u>	<u>(15,859)</u>
Total amount recognized	<u>\$ 28,257</u>	<u>\$ 12,382</u>
Components of net periodic benefit cost:		
Service cost	\$ 21,904	\$ 22,295
Interest cost	27,509	27,659
Expected return on plan assets	(25,244)	(23,830)
Amortization of prior service cost	57	59
Amortization of net loss	9,411	11,242
Recognized actuarial loss	<u>27</u>	<u>34</u>
Net periodic pension cost	<u>\$ 33,664</u>	<u>\$ 37,459</u>

The System's estimated prior service cost of \$66 and net loss of \$13,833 will be amortized from unrestricted net assets into net periodic pension cost over the next fiscal year.

The Plan's investment policies and strategies were used to develop the expected long-term rate of return on risk-free investment (primarily government bonds), the historical level of the risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns of each asset class. The expected return of each asset class was then weighted based on the target asset allocation to develop the expected long-term rate of return on assets assumption.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 9. EMPLOYEE BENEFIT PLANS (CONTINUED)

The Plan's target asset allocation and the actual asset allocation percentages for 2017 and 2016 are as follows at the respective measurement dates:

<u>Asset Category</u>	<u>Target</u>	<u>Actual</u>	
		<u>2017</u>	<u>2016</u>
Equities	70%	70%	70%
Fixed income	25	25	25
Other	<u>5</u>	<u>5</u>	<u>5</u>
	<u>100%</u>	<u>100%</u>	<u>100%</u>

The portfolio is diversified among a mix of assets including large and small cap, domestic and foreign equities, fixed income, alternatives (a fund of hedge funds), and cash. Asset mix is targeted to a specific allocation that is established by evaluating expected return, standard deviation, and correlation of various assets against the plan's long-term objectives. Asset performance is monitored quarterly and rebalanced if asset classes exceed explicit ranges. The Statement of Policy and Investment Objectives governs permitted types of investments, and outlines specific benchmarks and performance percentiles. The Catholic Health Benefit Plan Committee oversees the pension investment program and monitors investment performance. Risk is closely monitored through the evaluation of portfolio holdings and tracking the beta and standard deviation of the portfolio performance. The use of derivative financial instruments as an investment vehicle is specifically limited.

Accounting Standards Codification Topic 820 allows for the use of a practical expedient for the estimation of fair value of investments in investment companies for which the investment does not have a readily determinable fair value. For investments in non-unitized investments, the equivalent is the Plan's proportionate share of the partner's capital of the investment partnerships as reported by the general partners. Through its monitoring activities, the Plan believes that the carrying amounts of these financial instruments are reasonable estimates of fair value.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2017 and 2016.

Cash and Cash Equivalents: Include certain instruments in highly liquid debt instruments with original maturities of three months or less at date of purchase.

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

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

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

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 9. EMPLOYEE BENEFIT PLANS (CONTINUED)

Commingled Funds: Commingled funds are developed for investment by institutional investors only and therefore do not require registration with the Securities and Exchange Commission. Commingled funds are recorded at fair value based on either the underlying investments that have a readily determinable market value or based on net asset value, which is calculated using the most recent fund financial statements.

Hedge Funds: Hedge funds utilize either a direct or a “fund-of-funds” approach resulting in diversified multi-strategy, multi-manager investments. Underlying investments in these funds may include equities, fixed income securities, commodities, currencies and derivatives. These funds are valued at net asset value, which is calculated using the most recent fund financial statements.

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

The following table presents the Plan's financial instruments as of December 31, 2017, measured at fair value on a recurring basis using the fair value hierarchy defined in Note 13.

At December 31, 2017	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Total</u>
Pension plans:				
Cash and cash equivalents	\$ 17,728	\$ -	\$ -	\$ 17,728
Equity securities	65,583	-	-	65,583
Debt securities:				
Government and government agency obligations	-	11,971	-	11,971
Corporate bonds	-	53,697	-	53,697
Asset backed securities	-	8,441	-	8,441
Mutual funds:				
Equity mutual funds	44,814	-	-	44,814
Fixed mutual funds	<u>23,097</u>	<u>-</u>	<u>-</u>	<u>23,097</u>
Subtotal	151,222	74,109	-	225,331
Investment measured at net asset value:				
Commingled funds:				
Equity commingled funds				128,754
Fixed income commingled funds				17,388
Hedge funds				<u>17,467</u>
Total				\$ <u>388,940</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 9. EMPLOYEE BENEFIT PLANS (CONTINUED)

At December 31, 2016	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Total</u>
Pension plans:				
Cash and cash equivalents	\$ 12,507	\$ -	\$ -	\$ 12,507
Equity securities	31,909	-	-	31,909
Debt securities:				
Government and government agency obligations	-	17,246	-	17,246
Corporate bonds	-	49,964	-	49,964
Asset backed securities	-	6,025	-	6,025
Mutual funds:				
Equity mutual funds	36,273	-	-	36,273
Fixed mutual funds	<u>22,898</u>	<u>-</u>	<u>-</u>	<u>22,898</u>
Subtotal	103,587	73,235	-	176,822
Investment measured at net asset value:				
Commingled funds:				
Equity commingled funds				137,414
Fixed income commingled funds				591
Hedge funds				<u>13,774</u>
Total				\$ <u>328,601</u>

Contributions: Contributions to the Plan are made to make benefit payments to plan participants. The funding policy is to contribute amounts to the trusts sufficient to meet minimum funding requirements plus such additional amounts as may be determined to be appropriate. Contributions are made to benefit plans for the sole benefit of plan participants.

The System is expected to contribute an aggregate amount of approximately \$33,131 to the pension plan trust in 2018 to be allocated amongst participating entities.

Benefit Payments: Estimated future benefit payments by the System are as follows as of December 31:

2018	\$ 24,723
2019	\$ 27,413
2020	\$ 29,694
2021	\$ 32,181
2022	\$ 34,766
2023 - 2027	\$ 206,985

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 9. EMPLOYEE BENEFIT PLANS (CONTINUED)

	<u>2017</u>	<u>2016</u>
Weighted average assumptions used to determine end of the year benefit obligations:		
Discount rate	3.75%	4.40%
Rate of compensation increase	Age Based*	Age Based*
Weighted average assumptions used to determine net periodic pension cost:		
Discount rate	4.40%	4.65%
Expected long-term rate of return on plan assets	7.25%	7.50%
Rate of compensation increase	Age Based*	3.50%
Measurement date	12/31/2017	12/31/2016

*The System has updated the rate of compensation increase from 3.5% to an age based rate for all ages of benefit recipients during 2017, as expected salary increases ranged from 3.1% to 4.5%.

NOTE 10. INSURANCE ARRANGEMENTS

Professional and General Liability Arrangements

The System participates in the Trinity Health insurance program which provides coverage for healthcare professional (medical malpractice) and general liability exposures. The primary limits were \$20,000 per occurrence for healthcare professional liability and general liability for the years ending December 31 2017 and 2016. Professional and general liabilities are insured by Trinity Assurance, Ltd. (TAL), formerly Venzke Insurance Company, Ltd. (Venzke). TAL is a Cayman-domiciled insurer wholly-owned by Trinity Health. Excess coverage was also provided to the System, and this excess coverage is fully reinsured with nonaffiliated commercial insurance companies.

The coverage provided is on a claims-made basis. The System therefore retains the liability for unasserted claims resulting from incidents that occurred on services provided prior to the consolidated financial statement date. The System has independent actuaries estimate the ultimate costs of such unasserted claims, which were discounted at 3% in 2017 and 2016. The System's reserve for unpaid and incurred but not reported claims at December 31, 2017 and 2016 is \$89,640 and \$86,250, respectively, and is included within other noncurrent liabilities. The charges to expenses for professional and general liability for 2017 and 2016 approximated \$13,558 and \$11,274, respectively, which has been included in insurance expense. The required claims liability and any anticipated insurance recoveries are to be reported on a gross basis. Amounts recognized as insurance receivables related to the claims approximated \$76,713 and \$74,921 at December 31, 2017 and 2016, respectively and is included in other non-current assets. Insurance recoveries are measured on the same basis as the liability subject to the need for a valuation allowance on uncollectible amounts.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 10. INSURANCE ARRANGEMENTS (CONTINUED)

Workers Compensation Arrangements

The System's insurance program for workers' compensation has a deductible of \$750 per occurrence in 2017 and 2016. Claims in excess of the deductible are fully insured. Losses from asserted claims and from unasserted claims identified under the System's incident reporting programs were accrued on a discounted basis based upon actuarial estimates of the settlement of such claims. The discount rate applied is 3% in 2017 and 2016, respectively. The System's current portion of liabilities for unpaid and incurred but not reported claims at December 31, 2017 and 2016 is \$9,128 and \$10,241, respectively, and is included in accrued expenses. The System's long term portion of liabilities for unpaid and incurred but not reported claims at December 31, 2017 and 2016 is \$67,805 and \$69,944, respectively, and is included in other long-term liabilities.

The charges to expenses for workers' compensation costs approximated \$10,524 and \$11,532 in 2017 and 2016, respectively, which has been included in employee benefits expense. The required claims liability and any anticipated insurance recoveries are to be reported on a gross basis. Amounts recognized as insurance receivables related to the claims approximated \$26,652 and \$30,009 at December 31, 2017 and 2016, respectively and is included in other non-current assets. Insurance recoveries are measured on the same basis as the liability subject to the need for a valuation allowance for uncollectible amounts.

Employee Health Arrangements

The System's insurance for employee health costs is self-insured up to \$375 per claim. Claims in excess of self-insurance levels are fully insured. Claims are accrued based upon the System's estimates of the aggregate liability for claims incurred using certain actuarial assumptions used in the insurance industry and based on the System's experience. The System's liability for unpaid health insurance claims, which has been included in accrued expenses at December 31, 2017 and 2016, was \$7,310 and \$7,280, respectively.

NOTE 11. LEGAL MATTERS

The System is involved in litigation and regulatory investigations arising in the course of business. The health care industry is subject to numerous laws and regulations of federal, state and local governments. Compliance with these laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at the time. Recently, government activity has increased with respect to investigations and allegations concerning possible violations by health care providers of fraud and abuse statutes and regulations, which could result in the imposition of significant fines and penalties as well as significant repayments for patient services previously billed under Medicare and Medicaid programs in the current and preceding years. While certain regulatory inquiries have been made at December 31, 2017, compliance with such laws and regulations is currently subject to government review and interpretation as well as regulatory actions unknown and/or unasserted at this time. Management believes it is in compliance with such laws and regulations and no unknown or unasserted claims were known at this time, which could have a material adverse affect on the System's future financial position, results from operations or cash flows.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 12. CONCENTRATIONS OF CREDIT RISK

The System grants credit without collateral to its patients, most of who are residents of Western New York and are insured under third-party agreements. The mix of receivables from patients and third-party payors at December 31 are as follows:

	<u>2017</u>	<u>2016</u>
Medicare	35%	30%
Medicaid	21	19
Blue Cross	7	9
Other third-party payors	27	30
Patients/residents	<u>10</u>	<u>12</u>
	<u>100%</u>	<u>100%</u>

The System maintains funds in excess of amounts insured by the Federal Depository Insurance limits. The System has diversified its deposit amounts in a variety of institutions to reduce the level of concentrated credit risk.

NOTE 13. FAIR VALUE MEASUREMENTS

The System's consolidated financial statements reflect certain assets and liabilities recorded at fair value. Assets and liabilities measured at fair value on a recurring basis on the System's consolidated balance sheets include cash and cash equivalents, equity securities, exchange traded funds, debt securities, mutual funds, commingled funds and interest rate swaps. Liabilities measured at fair value on a recurring basis for disclosure only include debt.

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

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

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1) and the lowest priority to unobservable inputs (level 3). The three levels of the fair value hierarchy are described as follows:

- Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Plan has the ability to access.
- Level 2: Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly such as:
 - Quoted prices for similar assets or liabilities in active markets;
 - Quoted prices for identical or similar assets or liabilities in inactive markets;
 - Inputs other than quoted prices that are observable for the asset or liability;

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 13. FAIR VALUE MEASUREMENTS (CONTINUED)

- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

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

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

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2017 and 2016.

Cash and Cash Equivalents: The carrying amounts reported in the consolidated balance sheets approximate their fair value. Certain cash and cash equivalents are included in investments and assets limited or restricted as to use in the consolidated balance sheets. The System considers all highly liquid investments, generally with original maturities of three months or less when purchased, and short term investments excluding amounts limited as to use, to be cash equivalents.

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

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

Exchange Traded Funds: Exchange traded funds are valued at the closing price reported on the applicable exchange on which the security traded is tracked.

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

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 13. FAIR VALUE MEASUREMENTS (CONTINUED)

Investment in Ascension Alpha Fund, LLC: This fund is wholly owned subsidiary of Ascension Health and includes pooled short term investment funds, equity securities, and fixed income securities. The fund's investments also include alternative investments and other investments, which are valued at the net asset value of the investments.

Interest Rate Swap Liability: The fair value of the interest rate swap is determined based on financial models that consider current and future market interest rates and adjustments for nonperformance risk. The fair value of these interest rate derivatives are based on quoted prices for similar instruments from a commercial bank, and therefore, the interest rate derivative is considered a Level 2 item in the fair value hierarchy.

The following tables set forth by level, within the fair value hierarchy, the Plan's assets at fair value as of December 31, 2017 and 2016:

At December 31, 2017	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Total</u>
Assets limited as to use:				
Cash and cash equivalents	\$ 41,993	\$ -	\$ -	\$ 41,993
Equity securities	8	-	-	8
Government and government agency obligations	<u>3,929</u>	<u>1,987</u>	<u>-</u>	<u>5,916</u>
Subtotal	45,930	1,987	-	47,917
Interest receivable				<u>20</u>
Total				<u><u>\$ 47,937</u></u>
Investments:				
Cash and cash equivalents	\$ 527	\$ -	\$ -	\$ 527
Equity securities	10,486	-	-	10,486
Debt securities	1,203	1,463	-	2,666
Exchange traded funds	4,423	-	-	4,423
Mutual funds	3,011	-	-	3,011
Other	<u>-</u>	<u>500</u>	<u>-</u>	<u>500</u>
Subtotal	19,650	1,963	-	21,613
Investment measured at net asset value:				
Investment in Ascension Alpha Fund, LLC				<u>174,469</u>
Total				<u><u>\$ 196,082</u></u>
Interest rate swap liability	<u>\$ -</u>	<u>\$ 4,513</u>	<u>\$ -</u>	<u>\$ 4,513</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 13. FAIR VALUE MEASUREMENTS (CONTINUED)

At December 31, 2016	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Total</u>
Assets limited as to use:				
Cash and cash equivalents	\$ 31,415	\$ -	\$ -	\$ 31,415
Equity securities	9	-	-	9
Government and government agency obligations	<u>5,714</u>	<u>899</u>	<u>-</u>	<u>6,613</u>
Subtotal	37,138	899	-	38,037
Interest receivable				<u>22</u>
Total				<u>\$ 38,059</u>
Investments:				
Cash and cash equivalents	\$ 633	\$ -	\$ -	\$ 633
Equity securities	11,503	-	-	11,503
Debt securities	895	1,262	-	2,157
Exchange traded funds	4,951	-	-	4,951
Other	<u>-</u>	<u>484</u>	<u>-</u>	<u>484</u>
Subtotal	17,982	1,746	-	19,728
Investment measured at net asset value:				
Investment in Ascension Alpha Fund, LLC				<u>159,317</u>
Total				<u>\$ 179,045</u>
Interest rate swap liability	<u>\$ -</u>	<u>\$ 4,832</u>	<u>\$ -</u>	<u>\$ 4,832</u>

NOTE 14. RELATED PARTY TRANSACTIONS

Trinity Health charged the System dues for participation in certain programs and governance matters. As of December 31, 2017 and 2016, amounts charged to expense related to these dues amounted to approximately \$2,100 and \$4,200, respectively, and are included as a component of other expenses.

CIPA WNY IPA d/b/a “Catholic Medical Partners” was incorporated in 1996 to establish managed care contracts that support clinical integration and provider accountability for cost and quality. The hospitals, long-term care, and home care subsidiaries are members of Catholic Medical Partners. The System has four of its executive staff on the Catholic Medical Partners’ Board of Directors.

As discussed in Note 10, the System obtains insurance coverage from Trinity Health.

East Aurora Medical Building, L.P. (EAMB) is a joint venture between Olean RE Property, LLC., Buffalo Family Group, Inc., Aurora Mercy Corporation (a wholly owned Corporation of MHB), and seven other joint venture limited partners. EAMB refinanced its outstanding debt of \$2,200 on April 10, 2018, at which time MHB became sole guarantor to payment of principal and interest on the debt.

Caritas Medical Arts Building L.L.C. is a joint venture between Sisters of Charity Hospital and Ciminelli Development Company. As of December 31, 2017, there was \$1,681 (\$1,762 – 2016) of debt outstanding related to the Caritas Medical Arts Building L.L.C., of which SCH has guaranteed \$560 (\$588 – 2016). Per the guaranty agreement, SCH’s obligation shall decrease on a dollar for dollar basis as the principal amount of the obligation is paid down.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 14. RELATED PARTY TRANSACTIONS (CONTINUED)

Marian Professional Center Associates, L.P. is a joint venture between Ciminelli Development Company, MHB, Alsace Abbott Corporation (a wholly owned Corporation of MHB), and three other joint venture partners. As of December 31, 2017, there was \$4,700 (\$4,193 – 2016) of debt outstanding related to the Marian Professional Center Associates, L.P., of which the Obligated Group has guaranteed \$4,700 (\$2,097 – 2016). Per the guaranty agreement, the Obligated Group's obligation shall decrease on a dollar for dollar basis as the principal amount of the obligation is paid down.

NOTE 15. DISCONTINUED OPERATIONS

The following subsidiaries, which have been closed or sold as referenced, have been accounted for within discontinued operations: St. Francis Geriatric Healthcare Services, Inc. (closed 2009), Nazareth Home of the Franciscan of the Immaculate Conception (closed 2007), St. Francis Home of Williamsville (sold 2015), St. Elizabeth's Home and St. Vincent's Home for the Aged (both sold 2016).

The residual assets (net of inter-company receivables), liabilities, and net (deficit) assets of the discontinued operations were \$13,906, \$18,391 and (\$2,543), respectively, as of December 31, 2017 and are included within their natural classifications in the accompanying consolidated balance sheets. The residual assets (net of inter-company receivables), liabilities, and net (deficit) assets of these discontinued operations were \$16,978, \$23,538 and (\$2,877), respectively, as of December 31, 2016.

In March 2016, the assets of SVH were sold to a third party. The sales price for the facility approximated \$635. After deducting asset value and other closing costs, the net gain from the sale was approximately \$640.

In March 2016, the assets of SEH were sold to a third party. The sales price for the facility approximated \$2,011. After deducting asset value and other closing costs, the net gain from the sale was approximately \$1,921.

The aggregate gain (loss) from discontinued operations for assets held for sale as well as the closed facilities was approximately \$13 and (\$2,680) in 2017 and 2016, respectively.

NOTE 16. FUNCTIONAL EXPENSES

The System provides general health care services to residents within its geographic region. Expenses related to providing these services for the years ended December 31 are as follows:

	<u>2017</u>	<u>2016</u>
Healthcare services	\$ 968,240	\$ 936,748
General and administrative	<u>160,049</u>	<u>149,744</u>
	<u>\$ 1,128,289</u>	<u>\$ 1,086,492</u>



INDEPENDENT AUDITOR'S REPORT ON ACCOMPANYING SUPPLEMENTARY INFORMATION

To the Board of Directors
Catholic Health System, Inc.
Buffalo, New York

We have audited the consolidated financial statements of Catholic Health System, Inc. and its subsidiaries (together the System) as of December 31, 2017 and 2016 and for the years then ended and our report thereon appears on page 1 of this document. These audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The Schedule of Net Cost of Providing Care of Persons Living in Poverty and Community Benefit Programs (Schedule of Social Accountability) is the responsibility of management and is provided for purposes of additional analysis of the consolidated financial statements. Such information is unaudited and therefore, we do not express an opinion on the Schedule of Net Cost of Providing Care of Persons Living in Poverty and Community Benefit Programs (Schedule of Social Accountability).

The consolidating information for Catholic Health System, Inc. and its subsidiaries, presented on pages 47 through 59, and the consolidating information for Kenmore Mercy Hospital and subsidiaries, presented on pages 60 through 62, is presented for purposes of additional analysis rather than to present the financial position, results of operations and cash flows of the individual companies 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 consolidating information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the 2017 information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Freed Maxick CPAs, P.C.

Buffalo, New York
April 26, 2018

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

**SCHEDULE OF NET COST OF PROVIDING CARE OF PERSONS LIVING IN POVERTY AND
COMMUNITY BENEFIT PROGRAMS (SCHEDULE OF SOCIAL ACCOUNTABILITY – UNAUDITED)
Years Ended December 31, 2017 and 2016
(in thousands of dollars)**

The total net costs related to the care of the poor and benefits for the broader community as of December 31 are set forth in the following table:

	<u>2017</u>	<u>2016</u>
Charity care	\$ 10,156	\$ 9,299
Cost of community benefit programs	48,678	42,174
Unpaid cost of Medicaid programs	<u>70,409</u>	<u>63,526</u>
	<u>\$ 129,243</u>	<u>\$ 114,999</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2017

ASSETS	Parent	Acute Care Subsidiaries	Home and Community Based Subsidiaries	Other Subsidiaries	Discontinued Operations	Eliminations	Total
Current assets:							
Cash and cash equivalents	\$ 55,556	\$ 154,343	\$ 13,793	\$ 13,137	\$ 8,364	\$ -	\$ 245,193
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$24,138	-	115,383	12,698	3,545	162	-	131,788
Other receivables	778	6,855	17	165	-	-	7,815
Inventories	8	25,024	1,039	-	-	-	26,071
Prepaid expenses and other current assets	5,629	4,542	653	208	600	-	11,632
Due from affiliates	100,247	1,097	161	1,063	1,574	(104,142)	-
Total current assets	<u>162,218</u>	<u>307,244</u>	<u>28,361</u>	<u>18,118</u>	<u>10,700</u>	<u>(104,142)</u>	<u>422,499</u>
Interest in net assets of related Foundations	-	-	105	183	129	(417)	-
Assets limited as to use	13,202	21,774	10,749	1,137	1,075	-	47,937
Investments	-	173,829	22,253	-	-	-	196,082
Property and equipment, net	84,154	260,699	5,517	14,414	-	-	364,784
Other assets	28,971	92,857	9,918	1,236	3,576	(27,029)	109,529
Due from affiliates	5,116	11,759	732	-	368	(17,975)	-
Total assets	<u>\$ 293,661</u>	<u>\$ 868,162</u>	<u>\$ 77,635</u>	<u>\$ 35,088</u>	<u>\$ 15,848</u>	<u>\$ (149,563)</u>	<u>\$ 1,140,831</u>
LIABILITIES AND NET ASSETS							
Current liabilities:							
Current portion of long-term obligations	\$ 5,049	\$ 11,931	\$ 572	\$ 605	\$ -	\$ -	\$ 18,157
Accounts payable	7,401	43,787	1,263	2,944	-	-	55,395
Accrued expenses	21,728	54,750	3,830	2,800	292	-	83,400
Due to third-party payors	-	35,992	1,735	2,696	439	-	40,862
Due to affiliates	784	73,679	7,973	12,808	10,327	(105,571)	-
Total current liabilities	<u>34,962</u>	<u>220,139</u>	<u>15,373</u>	<u>21,853</u>	<u>11,058</u>	<u>(105,571)</u>	<u>197,814</u>
Long-term obligations, net	73,947	106,390	3,800	8,566	-	-	192,703
Due to affiliates, net	12,128	-	-	4,157	260	(16,545)	-
Other long-term liabilities	62,984	424,104	20,550	2,643	7,073	-	517,354
Total liabilities	<u>184,021</u>	<u>750,633</u>	<u>39,723</u>	<u>37,219</u>	<u>18,391</u>	<u>(122,116)</u>	<u>907,871</u>
Net assets (deficit):							
Unrestricted	106,181	109,993	37,807	(2,843)	(2,672)	(23,570)	224,896
Temporarily restricted	3,413	7,239	105	712	129	(3,831)	7,767
Permanently restricted	46	297	-	-	-	(46)	297
Total net assets (deficit)	<u>109,640</u>	<u>117,529</u>	<u>37,912</u>	<u>(2,131)</u>	<u>(2,543)</u>	<u>(27,447)</u>	<u>232,960</u>
Total liabilities and net assets (deficit)	<u>\$ 293,661</u>	<u>\$ 868,162</u>	<u>\$ 77,635</u>	<u>\$ 35,088</u>	<u>\$ 15,848</u>	<u>\$ (149,563)</u>	<u>\$ 1,140,831</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (DEFICIT)

(in thousands of dollars)

For the Year Ended December 31, 2017

	Parent	Acute Care Subsidiaries	Home and Community Based Subsidiaries	Other Subsidiaries	Discontinued Operations	Eliminations	Total
Unrestricted revenues other support:							
Net patient/resident service revenue	\$ -	\$ 1,025,197	\$ 78,480	\$ 42,828	\$ -	\$ (9,956)	\$ 1,136,549
Provision for bad debts	-	(22,101)	(3,105)	(410)	-	-	(25,616)
Net patient/resident service revenue, less provision for bad debts	-	1,003,096	75,375	42,418	-	(9,956)	1,110,933
Other revenue	152,296	23,467	319	7,505	-	(162,309)	21,278
Net assets released from restrictions	-	595	-	-	-	-	595
Total unrestricted revenues and other support	152,296	1,027,158	75,694	49,923	-	(172,265)	1,132,806
Expenses:							
Salaries and wages	75,709	452,039	44,124	21,669	-	(73,572)	519,969
Employee benefits	21,762	135,259	11,636	2,976	-	(21,751)	149,882
Medical and professional fees	4,375	46,856	1,067	2,231	-	(6,125)	48,404
Purchased services	32,050	96,014	3,057	18,152	-	(42,858)	106,415
Supplies	904	189,075	8,756	2,330	-	(1,955)	199,110
Depreciation and amortization	7,868	45,027	1,153	1,792	-	(7,893)	47,947
Interest	3,281	9,026	672	651	-	(3,456)	10,174
Insurance	518	14,260	795	631	-	(518)	15,686
Other expenses	6,894	34,188	2,602	2,333	-	(15,315)	30,702
Total expenses	153,361	1,021,744	73,862	52,765	-	(173,443)	1,128,289
Income (loss) from operations	(1,065)	5,414	1,832	(2,842)	-	1,178	4,517
Nonoperating revenues:							
Investment income	312	17,771	2,037	-	-	-	20,120
Other, net	538	1,161	35	64	-	(1,167)	631
Total nonoperating revenues	850	18,932	2,072	64	-	(1,167)	20,751
Excess (deficiency) of revenues over expenses	\$ (215)	\$ 24,346	\$ 3,904	\$ (2,778)	\$ -	\$ 11	\$ 25,268

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (DEFICIT) (CONTINUED)

(in thousands of dollars)

For the Year Ended December 31, 2017

	Parent	Acute Care Subsidiaries	Home and Community Based Subsidiaries	Other Subsidiaries	Discontinued Operations	Eliminations	Total
Unrestricted net assets:							
Excess (deficiency) of revenues over expenses	\$ (215)	\$ 24,346	\$ 3,904	\$ (2,778)	\$ -	\$ 11	\$ 25,268
Change in unrealized gain on interest rate swap	-	191	-	122	-	-	313
Change in pension obligation, other than net periodic cost	(6,405)	(20,494)	(1,432)	(247)	321	-	(28,257)
Net assets released from restrictions	-	1,609	-	-	-	-	1,609
Contributions	94	-	-	-	-	(14)	80
Other	26,010	(25,180)	(39)	(43)	-	-	748
Increase (decrease) in unrestricted net assets before effects of discontinued operations	19,484	(19,528)	2,433	(2,946)	321	(3)	(239)
Gain from discontinued operations	-	-	-	-	13	-	13
(Decrease) increase in unrestricted net assets	19,484	(19,528)	2,433	(2,946)	334	(3)	(226)
Temporarily restricted net assets:							
Contributions and other	-	1,404	-	27	-	-	1,431
Investment income	-	37	-	-	-	-	37
Special events revenue, net	-	438	-	-	-	-	438
Change in temporarily restricted interest in related Foundation	-	-	6	(101)	-	40	(55)
Temporarily restricted net assets released from restrictions	-	(2,204)	-	-	-	-	(2,204)
Other	-	(4)	-	-	-	-	(4)
(Decrease) increase in temporarily restricted net assets	-	(329)	6	(74)	-	40	(357)
Permanently restricted net assets:							
Contributions	-	3	-	-	-	-	3
Increase in permanently restricted net assets	-	3	-	-	-	-	3
(Decrease) increase in net assets	19,484	(19,854)	2,439	(3,020)	334	37	(580)
Net assets (deficit), beginning of year	90,156	137,383	35,473	889	(2,877)	(27,484)	233,540
Net assets (deficit), end of year	\$ 109,640	\$ 117,529	\$ 37,912	\$ (2,131)	\$ (2,543)	\$ (27,447)	\$ 232,960

CATHOLIC HEALTH SYSTEM - ACUTE CARE SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2017

ASSETS	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Mount St. Mary's Hospital	Total
Current assets:					
Cash and cash equivalents	\$ 55,844	\$ 53,928	\$ 36,589	\$ 7,982	\$ 154,343
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$19,700	49,200	34,784	20,942	10,457	115,383
Other receivables	2,473	3,156	769	457	6,855
Inventories	13,559	6,780	2,825	1,860	25,024
Prepaid expenses and other current assets	1,971	1,718	431	422	4,542
Due from affiliates	324	723	43	7	1,097
Total current assets	<u>123,371</u>	<u>101,089</u>	<u>61,599</u>	<u>21,185</u>	<u>307,244</u>
Assets limited as to use	2,683	16,315	2,776	-	21,774
Investments	34,629	106,567	26,590	6,043	173,829
Property and equipment, net	99,627	71,049	65,639	24,384	260,699
Other assets	41,190	36,908	13,158	1,601	92,857
Due from affiliates	-	10,303	1,456	-	11,759
Total assets	<u>\$ 301,500</u>	<u>\$ 342,231</u>	<u>\$ 171,218</u>	<u>\$ 53,213</u>	<u>\$ 868,162</u>
LIABILITIES AND NET ASSETS					
Current liabilities:					
Current portion of long-term obligations	\$ 4,181	\$ 4,134	\$ 3,601	\$ 15	\$ 11,931
Accounts payable	17,800	14,222	8,953	2,812	43,787
Accrued expenses	14,630	27,978	6,565	5,577	54,750
Due to third-party payors	16,336	11,119	5,303	3,234	35,992
Due to affiliates	23,468	25,500	23,669	1,042	73,679
Total current liabilities	<u>76,415</u>	<u>82,953</u>	<u>48,091</u>	<u>12,680</u>	<u>220,139</u>
Long-term obligations, net	49,131	26,889	30,370	-	106,390
Other long-term liabilities	217,743	139,471	53,588	13,302	424,104
Total liabilities	<u>343,289</u>	<u>249,313</u>	<u>132,049</u>	<u>25,982</u>	<u>750,633</u>
Net assets (deficit):					
Unrestricted	(42,796)	88,900	39,020	24,869	109,993
Temporarily restricted	884	3,895	149	2,311	7,239
Permanently restricted	123	123	-	51	297
Total net assets (deficit)	<u>(41,789)</u>	<u>92,918</u>	<u>39,169</u>	<u>27,231</u>	<u>117,529</u>
Total liabilities and net assets	<u>\$ 301,500</u>	<u>\$ 342,231</u>	<u>\$ 171,218</u>	<u>\$ 53,213</u>	<u>\$ 868,162</u>

CATHOLIC HEALTH SYSTEM - ACUTE CARE SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (DEFICIT)

(in thousands of dollars)

For the Year Ended December 31, 2017

	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Mount St. Mary's Hospital	Total
Unrestricted revenues other support:					
Net patient/resident service revenue	\$ 420,858	\$ 333,222	\$ 173,005	\$ 98,112	\$ 1,025,197
Provision for bad debts	(8,123)	(7,565)	(3,674)	(2,739)	(22,101)
Net patient/resident service revenue, less provision for bad debts	412,735	325,657	169,331	95,373	1,003,096
Other revenue	5,649	12,678	1,759	3,381	23,467
Net assets released from restrictions	181	184	15	215	595
Total unrestricted revenues and other support	418,565	338,519	171,105	98,969	1,027,158
Expenses:					
Salaries and wages	180,407	150,066	71,700	49,866	452,039
Employee benefits	57,004	43,697	20,343	14,215	135,259
Medical and professional fees	22,909	15,261	4,893	3,793	46,856
Purchased services	35,759	32,500	15,602	12,153	96,014
Supplies	81,499	57,087	38,662	11,827	189,075
Depreciation and amortization	17,217	14,561	9,029	4,220	45,027
Interest	3,907	2,793	2,304	22	9,026
Insurance	6,228	4,836	2,146	1,050	14,260
Other expenses	15,166	10,419	4,790	3,813	34,188
Total expenses	420,096	331,220	169,469	100,959	1,021,744
Income (loss) from operations	(1,531)	7,299	1,636	(1,990)	5,414
Nonoperating revenues:					
Investment income	3,934	10,335	2,652	850	17,771
Other, net	356	587	132	86	1,161
Total nonoperating revenues	4,290	10,922	2,784	936	18,932
Excess (deficiency) of revenues over expenses	\$ 2,759	\$ 18,221	\$ 4,420	\$ (1,054)	\$ 24,346

CATHOLIC HEALTH SYSTEM - ACUTE CARE SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (DEFICIT) (CONTINUED)

(in thousands of dollars)

For the Year Ended December 31, 2017

	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Mount St. Mary's Hospital	Total
Unrestricted net assets:					
Excess (deficiency) of revenues over expenses	\$ 2,759	\$ 18,221	\$ 4,420	\$ (1,054)	\$ 24,346
Change in unrealized gain on interest rate swap	191	-	-	-	191
Change in pension obligation, other than net periodic cost	(11,331)	(7,706)	(999)	(458)	(20,494)
Net assets released from restrictions	210	807	37	555	1,609
Other	(8,505)	(11,153)	(5,997)	475	(25,180)
(Decrease) increase in unrestricted net assets	(16,676)	169	(2,539)	(482)	(19,528)
Temporarily restricted net assets:					
Contributions and other	417	678	120	189	1,404
Investment income	33	1	-	3	37
Special events revenue, net	63	167	21	187	438
Temporarily restricted net assets released from restrictions	(391)	(991)	(52)	(770)	(2,204)
Other	-	1	(5)	-	(4)
(Decrease) increase in temporarily restricted net assets	122	(144)	84	(391)	(329)
Permanently restricted net assets:					
Contributions	-	-	-	3	3
Increase in permanently restricted net assets	-	-	-	3	3
(Decrease) increase in net assets	(16,554)	25	(2,455)	(870)	(19,854)
Net assets (deficit), beginning of year	(25,235)	92,893	41,624	28,101	137,383
Net assets (deficit), end of year	<u>\$ (41,789)</u>	<u>\$ 92,918</u>	<u>\$ 39,169</u>	<u>\$ 27,231</u>	<u>\$ 117,529</u>

CATHOLIC HEALTH SYSTEM - DISCONTINUED OPERATIONS

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2017

ASSETS	Discontinued Operations					Total
	St. Francis Geriatric	St. Francis Home	St. Elizabeth's Home	St. Vincent's Home	Nazareth Home	
Current assets:						
Cash and cash equivalents	\$ 711	\$ 4,271	\$ 1,411	\$ 593	\$ 1,378	\$ 8,364
Resident accounts receivable, net of allowance for doubtful accounts of \$1,053	162	-	-	-	-	162
Prepaid expenses and other current assets	600	-	-	-	-	600
Due from affiliates	-	1	-	-	1,573	1,574
Total current assets	<u>1,473</u>	<u>4,272</u>	<u>1,411</u>	<u>593</u>	<u>2,951</u>	<u>10,700</u>
Interest in net assets of related Foundations	-	68	60	1	-	129
Assets limited as to use	-	1,075	-	-	-	1,075
Other assets	7	3,500	43	26	-	3,576
Due from affiliates	-	-	368	-	-	368
Total assets	<u>\$ 1,480</u>	<u>\$ 8,915</u>	<u>\$ 1,882</u>	<u>\$ 620</u>	<u>\$ 2,951</u>	<u>\$ 15,848</u>
LIABILITIES AND NET ASSETS						
Current liabilities:						
Accrued expenses	\$ 7	\$ 238	\$ 44	\$ 3	\$ -	\$ 292
Due to third-party payors	-	439	-	-	-	439
Due to affiliates	-	7,427	1,407	1,493	-	10,327
Total current liabilities	<u>7</u>	<u>8,104</u>	<u>1,451</u>	<u>1,496</u>	<u>-</u>	<u>11,058</u>
Due to affiliates, net	-	-	-	-	260	260
Other long-term liabilities	-	5,883	952	238	-	7,073
Total liabilities	<u>7</u>	<u>13,987</u>	<u>2,403</u>	<u>1,734</u>	<u>260</u>	<u>18,391</u>
Net (deficit) assets:						
Unrestricted	1,473	(5,140)	(581)	(1,115)	2,691	(2,672)
Temporarily restricted net assets	-	68	60	1	-	129
Total net (deficit) assets	<u>1,473</u>	<u>(5,072)</u>	<u>(521)</u>	<u>(1,114)</u>	<u>2,691</u>	<u>(2,543)</u>
Total liabilities and net assets	<u>\$ 1,480</u>	<u>\$ 8,915</u>	<u>\$ 1,882</u>	<u>\$ 620</u>	<u>\$ 2,951</u>	<u>\$ 15,848</u>

CATHOLIC HEALTH SYSTEM - DISCONTINUED OPERATIONS

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET (DEFICIT) ASSETS

(in thousands of dollars)

For the Year Ended December 31, 2017

	Discontinued Operations					
	St. Francis Geriatric	St. Francis Home	St. Elizabeth's Home	St. Vincent's Home	Nazareth Home	Total
Unrestricted net assets:						
Change in pension obligation, other than net periodic cost	\$ -	\$ 177	\$ 103	\$ 41	\$ -	\$ 321
Other	48	-	-	-	(48)	-
Increase (decrease) in unrestricted net assets before effects of discontinued operations	48	177	103	41	(48)	321
Gain (loss) from discontinued operations	5	188	(155)	(14)	(11)	13
Increase (decrease) unrestricted net assets	53	365	(52)	27	(59)	334
Increase (decrease) in net assets	53	365	(52)	27	(59)	334
Net (deficit) assets, beginning of year	1,420	(5,437)	(469)	(1,141)	2,750	(2,877)
Net (deficit) assets, end of year	<u>\$ 1,473</u>	<u>\$ (5,072)</u>	<u>\$ (521)</u>	<u>\$ (1,114)</u>	<u>\$ 2,691</u>	<u>\$ (2,543)</u>

CATHOLIC HEALTH SYSTEM - HOME AND COMMUNITY BASED SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2017

ASSETS	Father Baker Manor	Mercy Home Care	McAuley Seton Home Care	Infusion Pharmacy	Total
Current assets:					
Cash and cash equivalents	\$ 267	\$ 1,947	\$ 9,626	\$ 1,953	\$ 13,793
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$2,819	3,069	206	8,325	1,098	12,698
Other Receivables	8	-	-	9	17
Inventories	34	-	53	952	1,039
Prepaid expenses and other current assets	7	1	21	624	653
Due from affiliates	5	-	-	156	161
Total current assets	<u>3,390</u>	<u>2,154</u>	<u>18,025</u>	<u>4,792</u>	<u>28,361</u>
Interest in net assets of related Foundations	105	-	-	-	105
Investments	-	-	22,253	-	22,253
Assets limited as to use	10,749	-	-	-	10,749
Property and equipment, net	4,680	-	515	322	5,517
Other assets	5,150	349	3,843	576	9,918
Due from affiliates	-	640	92	-	732
Total assets	<u>\$ 24,074</u>	<u>\$ 3,143</u>	<u>\$ 44,728</u>	<u>\$ 5,690</u>	<u>\$ 77,635</u>
LIABILITIES AND NET ASSETS					
Current liabilities:					
Current portion of long-term obligations	\$ 532	\$ -	\$ 40	\$ -	\$ 572
Accounts payable	182	408	483	190	1,263
Accrued expenses	1,414	-	2,128	288	3,830
Due to third-party payors	548	17	1,099	71	1,735
Due to affiliates	7,874	20	17	62	7,973
Total current liabilities	<u>10,550</u>	<u>445</u>	<u>3,767</u>	<u>611</u>	<u>15,373</u>
Long-term obligations, net	3,800	-	-	-	3,800
Other long-term liabilities	8,802	1,989	9,242	517	20,550
Total liabilities	<u>23,152</u>	<u>2,434</u>	<u>13,009</u>	<u>1,128</u>	<u>39,723</u>
Net assets:					
Unrestricted	817	709	31,719	4,562	37,807
Temporarily restricted net assets	105	-	-	-	105
Total net assets	<u>922</u>	<u>709</u>	<u>31,719</u>	<u>4,562</u>	<u>37,912</u>
Total liabilities and net assets	<u>\$ 24,074</u>	<u>\$ 3,143</u>	<u>\$ 44,728</u>	<u>\$ 5,690</u>	<u>\$ 77,635</u>

CATHOLIC HEALTH SYSTEM - HOME AND COMMUNITY BASED SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS

(in thousands of dollars)

For the Year Ended December 31, 2017

	Father Baker Manor	Mercy Home Care	McAuley Seton Home Care	Infusion Pharmacy	Total
Unrestricted revenues other support:					
Net patient/resident service revenue	\$ 17,400	\$ 6,550	\$ 43,251	\$ 11,279	\$ 78,480
Provision for bad debts	(1,245)	(30)	(1,528)	(302)	(3,105)
Net patient/resident service revenue, less provision for bad debts	16,155	6,520	41,723	10,977	75,375
Other revenue	119	10	-	190	319
Total unrestricted revenues and other support	<u>16,274</u>	<u>6,530</u>	<u>41,723</u>	<u>11,167</u>	<u>75,694</u>
Expenses:					
Salaries and wages	11,033	4,517	25,816	2,758	44,124
Employee benefits	3,218	1,138	6,594	686	11,636
Medical and professional fees	297	-	732	38	1,067
Purchased services	1,130	340	1,371	216	3,057
Supplies	1,232	13	1,207	6,304	8,756
Depreciation and amortization	530	19	559	45	1,153
Interest	334	27	306	5	672
Insurance	641	58	87	9	795
Other expenses	383	242	1,488	489	2,602
Total expenses	<u>18,798</u>	<u>6,354</u>	<u>38,160</u>	<u>10,550</u>	<u>73,862</u>
Income (loss) from operations	(2,524)	176	3,563	617	1,832
Nonoperating revenue and losses:					
Investment income	77	14	1,946	-	2,037
Other, net	9	3	20	3	35
Total nonoperating revenue and losses	<u>86</u>	<u>17</u>	<u>1,966</u>	<u>3</u>	<u>2,072</u>
Unrestricted net assets:					
Excess (deficiency) of revenue over expenses	(2,438)	193	5,529	620	3,904
Change in pension obligation, other than net periodic cost	(217)	(159)	(984)	(72)	(1,432)
Other	(39)	-	-	-	(39)
Increase (decrease) in unrestricted net assets	<u>(2,694)</u>	<u>34</u>	<u>4,545</u>	<u>548</u>	<u>2,433</u>
Temporarily restricted net assets:					
Change in temporarily restricted interest in related Foundations	6	-	-	-	6
Increase in temporarily restricted net assets	<u>6</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6</u>
Increase (decrease) in net assets	<u>(2,688)</u>	<u>34</u>	<u>4,545</u>	<u>548</u>	<u>2,439</u>
Net asset, beginning of year	<u>3,610</u>	<u>675</u>	<u>27,174</u>	<u>4,014</u>	<u>35,473</u>
Net assets, end of year	<u>\$ 922</u>	<u>\$ 709</u>	<u>\$ 31,719</u>	<u>\$ 4,562</u>	<u>\$ 37,912</u>

CATHOLIC HEALTH SYSTEM - OTHER SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2017

ASSETS	OLV Renaissance	Continuing Care Foundation	LIFE	Trinity	Niagara Medicine	Total
Current assets:						
Cash and cash equivalents	\$ 690	\$ 538	\$ 11,540	\$ 310	\$ 59	\$ 13,137
Patient accounts receivable, net of allowance for doubtful accounts of \$566	-	-	1,824	1,677	44	3,545
Other receivables	-	15	-	150	-	165
Prepaid expenses and other current assets	18	1	22	167	-	208
Due from affiliates	73	14	-	976	-	1,063
Total current assets	<u>781</u>	<u>568</u>	<u>13,386</u>	<u>3,280</u>	<u>103</u>	<u>18,118</u>
Interest in net assets of related Foundations	183	-	-	-	-	183
Assets limited as to use	308	-	829	-	-	1,137
Property and equipment, net	13,114	1	456	843	-	14,414
Other assets	300	-	19	-	917	1,236
Due from affiliates	-	-	-	-	-	-
Total assets	<u>\$ 14,686</u>	<u>\$ 569</u>	<u>\$ 14,690</u>	<u>\$ 4,123</u>	<u>\$ 1,020</u>	<u>\$ 35,088</u>
LIABILITIES AND NET ASSETS						
Current liabilities:						
Current portion of long-term obligations	\$ 410	\$ -	\$ -	\$ 195	\$ -	\$ 605
Accounts payable	-	-	2,430	509	5	2,944
Accrued expenses	779	1	-	2,004	16	2,800
Due to third-party payors	-	-	2,696	-	-	2,696
Due to affiliates	-	26	435	11,195	1,152	12,808
Total current liabilities	<u>1,189</u>	<u>27</u>	<u>5,561</u>	<u>13,903</u>	<u>1,173</u>	<u>21,853</u>
Long-term obligations, net	8,457	-	-	109	-	8,566
Due to affiliates, net	4,157	-	-	-	-	4,157
Other long-term liabilities	1,881	-	712	-	50	2,643
Total liabilities	<u>15,684</u>	<u>27</u>	<u>6,273</u>	<u>14,012</u>	<u>1,223</u>	<u>37,219</u>
Net (deficit) assets:						
Unrestricted	(1,180)	12	8,417	(9,889)	(203)	(2,843)
Temporarily restricted	182	530	-	-	-	712
Total net (deficit) assets	<u>(998)</u>	<u>542</u>	<u>8,417</u>	<u>(9,889)</u>	<u>(203)</u>	<u>(2,131)</u>
Total liabilities and net assets	<u>\$ 14,686</u>	<u>\$ 569</u>	<u>\$ 14,690</u>	<u>\$ 4,123</u>	<u>\$ 1,020</u>	<u>\$ 35,088</u>

CATHOLIC HEALTH SYSTEM - OTHER SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET (DEFICIT) ASSETS

(in thousands of dollars)

For the Year Ended December 31, 2017

	OLV Renaissance	Continuing Care Foundation	LIFE	Trinity	Niagara Medicine	Total
Unrestricted revenues other support:						
Net patient service revenue	\$ -	\$ -	\$ 23,705	\$ 18,719	\$ 404	\$ 42,828
Provision for bad debts	-	-	-	(410)	-	(410)
Net patient service revenue, less provision for bad debt	-	-	23,705	18,309	404	42,418
Other revenue	4,875	14	-	2,616	-	7,505
Total unrestricted revenues and other support	<u>4,875</u>	<u>14</u>	<u>23,705</u>	<u>20,925</u>	<u>404</u>	<u>49,923</u>
Expenses:						
Salaries and wages	281	-	2,115	19,273	-	21,669
Employee benefits	94	-	634	2,248	-	2,976
Medical and professional fees	22	-	112	1,635	462	2,231
Purchased services	1,752	-	15,158	1,210	32	18,152
Supplies	57	-	609	1,656	8	2,330
Depreciation and amortization	1,395	-	64	333	-	1,792
Interest	465	-	-	183	3	651
Insurance	59	-	12	541	19	631
Other expenses	60	7	436	1,812	18	2,333
Total expenses	<u>4,185</u>	<u>7</u>	<u>19,140</u>	<u>28,891</u>	<u>542</u>	<u>52,765</u>
(Loss) income from operations	690	7	4,565	(7,966)	(138)	(2,842)
Nonoperating revenue:						
Other, net	32	-	32	-	-	64
Total nonoperating revenue	<u>32</u>	<u>-</u>	<u>32</u>	<u>-</u>	<u>-</u>	<u>64</u>
(Deficiency) excess of revenues over expenses	<u>\$ 722</u>	<u>\$ 7</u>	<u>\$ 4,597</u>	<u>\$ (7,966)</u>	<u>\$ (138)</u>	<u>\$ (2,778)</u>

CATHOLIC HEALTH SYSTEM - OTHER SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET (DEFICIT) ASSETS (CONTINUED)

(in thousands of dollars)

For the Year Ended December 31, 2017

	OLV Renaissance	Continuing Care Foundation	LIFE	Trinity	Niagara Medicine	Total
Unrestricted net assets:						
(Deficiency) excess of revenues over expenses	\$ 722	\$ 7	\$ 4,597	\$ (7,966)	\$ (138)	\$ (2,778)
Change in unrealized gain on interest rate swap	122	-	-	-	-	122
Change in pension obligation, other than net periodic cost	-	-	(247)	-	-	(247)
Other	26	-	(4)	-	(65)	(43)
(Decrease) increase in unrestricted net assets	<u>870</u>	<u>7</u>	<u>4,346</u>	<u>(7,966)</u>	<u>(203)</u>	<u>(2,946)</u>
Temporarily restricted net assets:						
Contributions and other	-	27	-	-	-	27
Change in temporarily restricted interest in related Foundations	(40)	(61)	-	-	-	(101)
Decrease in temporarily restricted net assets	<u>(40)</u>	<u>(34)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(74)</u>
(Decrease) increase in net assets	<u>830</u>	<u>(27)</u>	<u>4,346</u>	<u>(7,966)</u>	<u>(203)</u>	<u>(3,020)</u>
Net assets (deficit), beginning of year	<u>(1,828)</u>	<u>569</u>	<u>4,071</u>	<u>(1,923)</u>	<u>-</u>	<u>889</u>
Net assets (deficit), end of year	<u>\$ (998)</u>	<u>\$ 542</u>	<u>\$ 8,417</u>	<u>\$ (9,889)</u>	<u>\$ (203)</u>	<u>\$ (2,131)</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

(KENMORE MERCY HOSPITAL AND SUBSIDIARIES)

CONSOLIDATING BALANCE SHEETS

(in thousands of dollars)

December 31, 2017

ASSETS	Kenmore Mercy Hospital	The McAuley Residence	The Kenmore Mercy Foundation	Eliminations	Consolidated
Current assets:					
Cash and cash equivalents	\$ 29,506	\$ 6,931	\$ 152	\$ -	\$ 36,589
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$3,131	17,479	3,463	-	-	20,942
Other receivables	684	6	79	-	769
Inventories	2,825	-	-	-	2,825
Prepaid expenses and other current assets	424	7	-	-	431
Due from affiliates	69	13	5	(44)	43
Total current assets	<u>50,987</u>	<u>10,420</u>	<u>236</u>	<u>(44)</u>	<u>61,599</u>
Interest in net assets of affiliated Foundation	3,580	-	-	(3,580)	-
Assets limited as to use	1,587	1,189	-	-	2,776
Investments	23,183	-	3,407	-	26,590
Property and equipment, net	56,346	9,290	3	-	65,639
Other assets	11,196	3,558	-	(1,596)	13,158
Due from affiliates	1,456	-	-	-	1,456
Total assets	<u>\$ 148,335</u>	<u>\$ 24,457</u>	<u>\$ 3,646</u>	<u>\$ (5,220)</u>	<u>\$ 171,218</u>
LIABILITIES AND NET ASSETS					
Current liabilities:					
Current portion of long-term obligations	\$ 3,026	\$ 575	\$ -	\$ -	\$ 3,601
Accounts payable	8,767	171	15	-	8,953
Accrued expenses	5,091	1,467	7	-	6,565
Due to third-party payors	4,582	721	-	-	5,303
Due to affiliates	8,828	14,841	44	(44)	23,669
Total current liabilities	<u>30,294</u>	<u>17,775</u>	<u>66</u>	<u>(44)</u>	<u>48,091</u>
Long-term obligations, net	27,194	3,176	-	-	30,370
Other long-term liabilities	44,478	9,110	-	-	53,588
Total liabilities	<u>101,966</u>	<u>30,061</u>	<u>66</u>	<u>(44)</u>	<u>132,049</u>
Net assets (deficit):					
Unrestricted	46,313	(5,697)	3,524	(5,120)	39,020
Temporarily restricted	56	93	56	(56)	149
Total net assets (deficit)	<u>46,369</u>	<u>(5,604)</u>	<u>3,580</u>	<u>(5,176)</u>	<u>39,169</u>
Total liabilities and net assets	<u>\$ 148,335</u>	<u>\$ 24,457</u>	<u>\$ 3,646</u>	<u>\$ (5,220)</u>	<u>\$ 171,218</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

(KENMORE MERCY HOSPITAL AND SUBSIDIARIES)
 CONSOLIDATING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS (DEFICIT)
 (in thousands of dollars)
 For the Year Ended December 31, 2017

	Kenmore Mercy Hospital	The McAuley Residence	The Kenmore Mercy Foundation	Eliminations	Consolidated
Unrestricted revenue and other support:					
Net patient/resident service revenue	\$ 153,654	\$ 19,351	\$ -	\$ -	\$ 173,005
Provision for bad debts	(2,873)	(782)	(19)	-	(3,674)
Net patient/resident service revenue, less provision for bad debts	150,781	18,569	(19)	-	169,331
Other revenue	1,256	52	451	-	1,759
Net assets released from restriction	-	-	15	-	15
Total unrestricted revenue and other support	152,037	18,621	447	-	171,105
Expenses:					
Salaries and wages	60,046	11,453	201	-	71,700
Employee benefits	17,020	3,261	62	-	20,343
Medical and professional fees	4,435	448	10	-	4,893
Purchased services	14,258	1,254	90	-	15,602
Supplies	37,279	1,379	4	-	38,662
Depreciation and amortization	8,277	751	1	-	9,029
Interest	2,136	168	-	-	2,304
Insurance	1,868	278	-	-	2,146
Other expenses (income)	4,262	436	1,393	(1,301)	4,790
Total expenses (income)	149,581	19,428	1,761	(1,301)	169,469
Income (loss) from operations	2,456	(807)	(1,314)	1,301	1,636
Nonoperating revenues:					
Investment income	2,131	13	508	-	2,652
Other, net	132	-	-	-	132
Total nonoperating revenues	2,263	13	508	-	2,784
Excess (deficiency) of revenues over expenses	\$ 4,719	\$ (794)	\$ (806)	\$ 1,301	\$ 4,420

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

(KENMORE MERCY HOSPITAL AND SUBSIDIARIES)

CONSOLIDATING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS (DEFICIT) (CONTINUED)

(in thousands of dollars)

For the Year Ended December 31, 2017

	<u>Kenmore Mercy Hospital</u>	<u>The McAuley Residence</u>	<u>The Kenmore Mercy Foundation</u>	<u>Eliminations</u>	<u>Consolidated</u>
Unrestricted net assets:					
Excess (deficiency) of revenues over expenses	\$ 4,719	\$ (794)	\$ (806)	\$ 1,301	\$ 4,420
Change in unrestricted interest in affiliated Foundation	(770)	-	-	770	-
Change in pension obligation, other than net periodic cost	(651)	(348)	-	-	(999)
Net assets released from restrictions	-	-	37	-	37
Other	(4,696)	-	-	(1,301)	(5,997)
(Decrease) increase in unrestricted net assets	<u>(1,398)</u>	<u>(1,142)</u>	<u>(769)</u>	<u>770</u>	<u>(2,539)</u>
Temporarily restricted net assets:					
Contributions	-	90	30	-	120
Special events revenue, net	-	-	21	-	21
Temporarily restricted net assets released from restrictions	-	-	(52)	-	(52)
Other	-	(6)	1	-	(5)
Increase in temporarily restricted net assets	<u>-</u>	<u>84</u>	<u>-</u>	<u>-</u>	<u>84</u>
(Decrease) increase in net assets	<u>(1,398)</u>	<u>(1,058)</u>	<u>(769)</u>	<u>770</u>	<u>(2,455)</u>
Net assets (deficit) - beginning of year	<u>47,767</u>	<u>(4,546)</u>	<u>4,349</u>	<u>(5,946)</u>	<u>41,624</u>
Net assets (deficit) - end of year	<u>\$ 46,369</u>	<u>\$ (5,604)</u>	<u>\$ 3,580</u>	<u>\$ (5,176)</u>	<u>\$ 39,169</u>