

CONSOLIDATED FINANCIAL STATEMENTS

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

DECEMBER 31, 2018

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, 2018 and 2017, 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, 2018 and 2017, 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
March 28, 2019

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands of dollars)

December 31,

ASSETS	2018	2017
Current assets:		
Cash and cash equivalents	\$ 276,731	\$ 245,193
Patient/resident accounts receivable	119,441	131,788
Other receivables	10,571	7,815
Inventories	23,635	26,071
Prepaid expenses and other current assets	12,776	12,151
Total current assets	443,154	423,018
Assets limited as to use	57,002	47,937
Investments	185,013	196,082
Property and equipment, net	375,471	364,784
Other assets	114,675	109,010
Total assets	\$ 1,175,315	\$ 1,140,831
LIABILITIES AND NET ASSETS		
Current liabilities:		
Current portion of long-term obligations	\$ 20,029	\$ 18,157
Accounts payable	60,728	55,395
Accrued expenses	83,952	83,400
Due to third-party payors	43,236	40,862
Total current liabilities	207,945	197,814
Long-term obligations, net	198,812	192,703
Other long-term obligations	504,516	517,354
Total liabilities	911,273	907,871
Net assets:		
Without donor restrictions	256,336	224,896
With donor restrictions	7,706	8,064
Total net assets	264,042	232,960
Total liabilities and net assets	\$ 1,175,315	\$ 1,140,831

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>2018</u>	<u>2017</u>
Revenues and other support without donor restrictions:		
Net patient/resident service revenue before provision for bad debts	\$ -	\$ 1,136,549
Provision for bad debts	-	(25,616)
Net patient/resident service revenue	<u>1,157,052</u>	<u>1,110,933</u>
Other revenue	26,829	21,278
Net assets released from restrictions	<u>540</u>	<u>595</u>
Total revenues and other support without donor restrictions	<u>1,184,421</u>	<u>1,132,806</u>
Expenses:		
Salaries and wages	533,955	519,969
Employee benefits	149,195	138,122
Medical and professional fees	51,582	48,404
Purchased services	111,010	106,415
Supplies	214,885	199,110
Depreciation and amortization	47,021	47,947
Interest	12,661	10,174
Insurance	12,601	15,686
Other expenses	<u>31,367</u>	<u>30,702</u>
Total expenses	<u>1,164,277</u>	<u>1,116,529</u>
Income from operations	20,144	16,277
Nonoperating revenues and expenses:		
Investment income (loss)	(7,281)	20,120
Other components of net periodic pension cost	(12,751)	(11,760)
Other revenues and gains, net	<u>541</u>	<u>631</u>
Total nonoperating revenues and expenses	<u>(19,491)</u>	<u>8,991</u>
Excess of revenues over expenses	<u>\$ 653</u>	<u>\$ 25,268</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>2018</u>	<u>2017</u>
Net assets without donor restrictions:		
Excess of revenues over expenses	\$ 653	\$ 25,268
Change in unrealized gain on interest rate swaps	828	313
Change in pension obligation, other than net periodic cost	22,228	(28,257)
Net assets released from restrictions used for capital	1,653	1,609
Amortization of terminated interest rate swaps	1,833	783
Capital grants	3,927	8
Contributions	94	80
Other	(98)	(43)
Increase (decrease) in net assets without donor restrictions before effects of discontinued operations	31,118	(239)
Gain from discontinued operations	322	13
Increase (decrease) in net assets without donor restrictions	31,440	(226)
Net assets with donor restrictions:		
Contributions	1,890	1,434
Investment income (loss)	(23)	37
Special events revenue, net	83	438
Change in interest in related Foundation	(267)	(55)
Net assets released from restrictions	(2,193)	(2,204)
Other	152	(4)
Increase (decrease) in net assets with donor restrictions	(358)	(354)
Increase (decrease) in net assets	31,082	(580)
Net assets, beginning of year	232,960	233,540
Net assets, end of year	<u>\$ 264,042</u>	<u>\$ 232,960</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,

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities:		
Increase (decrease) in net assets	\$ 31,082	\$ (580)
Gain in net assets from discontinued operations	(322)	(13)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities		
Depreciation and amortization	47,021	47,947
Change in minimum pension liability adjustment	(22,228)	28,257
Undistributed earnings in equity investees	316	(267)
Amortization of discount on debt issuance	61	61
Amortization of premium on debt issuance	(571)	(574)
Amortization of debt issuance costs	1,283	466
Loss (gain) on sale of property and equipment	24	(160)
Change in unrealized loss (gain) on investments	11,242	(16,726)
Realized gain on investments	(1,315)	(941)
Realized gain on interest rate swaps	(846)	(319)
Other	(175)	(137)
Decrease (increase) in assets:		
Patient/resident accounts receivables	12,347	(6,571)
Other receivables	(2,756)	1,660
Inventories	2,436	(2,471)
Prepaid expenses and other current assets	(1,141)	256
Other assets	(4)	13
Increase (decrease) in liabilities:		
Accounts payable	5,033	8,716
Accrued expenses	570	4,243
Due to third-party payors	2,376	(4,881)
Other liabilities	9,069	4,573
Total from continuing operations	<u>93,502</u>	<u>62,552</u>
Total used in discontinued operations	<u>(2,542)</u>	<u>(3,204)</u>
Net cash provided by operating activities	<u>90,960</u>	<u>59,348</u>
Cash flows from investing activities:		
Purchase of property and equipment	(54,715)	(38,518)
Proceeds from sale of property and equipment	21	305
Purchase of assets limited as to use	(25,430)	(33)
Proceeds from sale of assets limited as to use	16,690	3,146
Purchase of investments	(5,115)	(8,382)
Proceeds from sale of investments	6,304	9,028
Purchase of equity investments	(2,270)	(1,351)
Net cash used in investing activities	<u>(64,515)</u>	<u>(35,805)</u>
Cash flows from financing activities:		
Proceeds from issuance of long-term obligations, net	21,519	12,937
Repayments of current and long-term obligations	(16,426)	(18,518)
Net cash provided by (used in) financing activities	<u>5,093</u>	<u>(5,581)</u>
Increase in cash and cash equivalents	31,538	17,962
Cash and cash equivalents - beginning of year	<u>245,193</u>	<u>227,231</u>
Cash and cash equivalents - end of year	<u>\$ 276,731</u>	<u>\$ 245,193</u>

See accompanying notes.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE 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 are the corporate members of CHS, with equal ownership interest.

Catholic Health System, Inc. and Subsidiaries 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 of Niagara Falls (MSM).

Home and Community Based Subsidiaries: The Home and Community Based Subsidiaries include Western New York Catholic Long-Term Care, Inc. d/b/a Father Baker Manor (FBM), St. Francis Geriatric and Healthcare Services, Inc. (SFG), Niagara Homemakers Services, Inc. d/b/a Mercy Home Care (MHC), McAuley Seton Home Care Corporation (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 (CCF), 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), 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.

Recently Adopted Accounting Pronouncements: In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, "Revenue from Contracts with Customers (Topic 606)" (ASU 2014-09), using a modified retrospective method of application to all contracts existing on January 1, 2018. The ASU outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance, and requires expanded disclosures about revenue recognition. The core principle of the revenue model is that the System recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the System expects to be entitled in exchange for those goods or services.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The System's process for implementation began with a preliminary evaluation of ASU 2014-09 and consideration of subsequent interpretations by the FASB Transition Resource Group for Revenue Recognition and the American Institute of Certified Public Accountants. The System performed an analysis of revenue streams and transactions under ASU 2014-09. In particular, for net patient/resident service revenue, the System performed an analysis into the application of the portfolio approach as a practical expedient to group patient contracts with similar characteristics, such that revenue for a given portfolio would not be materially different than if it were evaluated on a contract-by-contract basis. Upon adoption, the majority of what was previously classified as provision for bad debts and presented as a reduction to net patient/resident service revenue on the consolidated statements of operations and changes in net assets is treated as an implicit price concession that reduces the transaction price, which is reported as net patient/resident service revenue. The new standard also requires enhanced disclosures related to the disaggregation of revenue and significant judgments made in measurement and recognition. The impact of adopting ASU 2014-09 is not material to total revenues and other support without donor restrictions, excess of revenues over expenses or net assets without donor restrictions.

In August 2016, the FASB issued ASU 2016-14, "Presentation of Financial Statements for Not-for-Profit Entities" (ASU 2016-14). This standard intends to make certain improvements to the current reporting requirements for not-for-profit entities. The System implemented ASU 2016-14 in 2018 and applied the changes retrospectively. The new standard changes the following aspects of the consolidated financial statements: Temporarily restricted and permanently restricted net asset classes have been combined into a single net asset class now called net assets with donor restrictions; Unrestricted net asset class has been renamed net assets without donor restrictions; and the consolidated financial statements include a disclosure about liquidity and availability of resources (Note 3) and certain categories of expenses that are attributable to more than one program or supporting function (Note 17).

In March 2017, the FASB issued ASU 2017-07, "Compensation - Retirement Benefits (Topic 715) Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost" (ASU 2017-07). This ASU requires the service cost component of net periodic benefit cost related to defined benefit pension and postretirement benefit plans to be reported in the same financial statement line as other compensation costs arising from services rendered during the period. Other components of net periodic pension cost are required to be presented separately from service costs and outside of income from operations in the consolidated statements of operations and changes in net assets. Further, only the service cost component of net periodic pension cost will be eligible for capitalization in assets. The System adopted ASU 2017-07 in 2018 and applied the changes retrospectively. The adoption of ASU 2017-07 had no impact on excess of revenues over expenses.

The following table presents the impact of the ASU 2017-07 adoption on the System's consolidated statements of operations and changes in net assets:

	Year ended December 31, 2017		
	Previously Reported	Impact of Adoption	As Reported
Employee benefits	\$ 149,882	\$ (11,760)	\$ 138,122
Income from operations	\$ 4,517	\$ 11,760	\$ 16,277
Other components of net periodic pension cost	\$ -	\$ (11,760)	\$ (11,760)
Total nonoperating expenses and revenues	\$ 20,751	\$ (11,760)	\$ 8,991
Excess of revenues over expenses	\$ 25,268	\$ -	\$ 25,268

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

New Accounting Pronouncements: In January 2016, the FASB issued ASU 2016-01, “Financial Instruments – Overall (Subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities” (ASU 2016-01), which requires entities to measure equity investments that do not result in consolidation and are not accounted for under the equity method at fair value and recognize any changes in fair value in excess of revenues over expenses unless the investments qualify for the new practicability exception. The amendments in ASU 2016-01 are effective for the System beginning in 2019.

In February 2016, the FASB issued ASU 2016-02, “Leases (Topic 842)” (ASU 2016-02), which affects any entity that enters into a lease (as that term is defined in ASU 2016-02), with some specified scope exceptions. The main difference between the guidance in ASU 2016-02 and current accounting principles generally accepted in the United States of America (US GAAP) is the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under current US GAAP. Under ASU 2016-02, lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach, which includes a number of optional practical expedients. In July 2018, the FASB issued ASU 2018-11, “Leases (Topic 842) Targeted Improvements”, which allows lessees and lessors to recognize and measure leases at the beginning of the period of adoption without modifying the comparative period financial statements. This guidance will be effective for the System beginning in 2019.

In June 2018, the FASB issued ASU 2018-08, “Not-for-Profit Entities (Topic 958) Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made” (ASU 2018-08). This standard clarifies the definition of an exchange transaction. As a result, not-for-profit entities will account for most federal and/or state and local government grants as donor-restricted conditional contributions, rather than as exchange transactions. The amendments in ASU 2018-08 are effective for interim and annual periods beginning after December 15, 2018. The amendment should be applied on a modified prospective basis, and early adoption is permitted. In the first set of financial statements following the effective date, the amendments should be applied to agreements that are either not completed as of the effective date, or entered into after the effective date.

In August 2018, the FASB issued ASU 2018-14, “Compensation – Retirement Benefits – Defined Benefit Plans – General (Subtopic 715-20) Disclosure Framework – Changes to the Disclosure Requirements for Defined Benefit Plans” (ASU 2018-14), which applies to all employers that sponsor defined benefit pension or other postretirement plans. The amendments in ASU 2018-14, which remove, modify or add certain disclosure requirements as part of the FASB’s disclosure framework project to improve the effectiveness of the notes to the financial statements, are effective for the System beginning in 2021.

In August 2018, the FASB issued ASU 2018-15, “Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40) Customer’s accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract” (ASU 2018-15). This ASU aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal use software and hosting arrangements that include internal use software license. This update also requires the entity (customer) to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangements. Such expenses should be presented in the income statement in the same line as the expenses associated with the hosting arrangement and to classify payments for capitalized implementation costs in the statement of cash flows in the same manner as payment made for fees associated with the hosting element. The amendments in ASU 2018-15 are effective for annual reporting periods beginning after December 31, 2020, and should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. Early adoption is permitted.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Use of Estimates: The preparation of consolidated financial statements in conformity with US GAAP 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 consolidated 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, implicit price concessions, 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 obligations.

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.

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.

Supplemental disclosure of cash flow information and non-cash investing and financing transactions for the years ended December 31 are as follows:

	<u>2018</u>	<u>2017</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for interest	\$ 8,732	\$ 8,985
Non-cash investing and financing transactions:		
Assets acquired under capital lease obligations	\$ 2,115	\$ 652
Increase in construction related payables	\$ 300	\$ 1,890

Other Receivables and Other Assets: Other receivables consist primarily of managed care risk sharing receivables, physician loans, Foundation receivables, 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.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

	<u>2018</u>	<u>2017</u>
Current other receivables:		
Physician loans	\$ 1,618	\$ 3,107
Foundation receivables	1,625	1,352
Managed care risk receivables	980	417
Lease and rent receivables	1,135	1,057
Third-party receivables	3,421	987
Other	<u>1,792</u>	<u>895</u>
Other receivables	<u>\$ 10,571</u>	<u>\$ 7,815</u>
Non-current other assets:		
Insurance recoveries	\$ 106,735	\$ 102,846
Investments in healthcare ventures	4,782	3,007
Goodwill and other	<u>3,158</u>	<u>3,157</u>
Other assets	<u>\$ 114,675</u>	<u>\$ 109,010</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 net assets without donor restrictions 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 nonoperating revenues and expenses in the consolidated statements of operations and changes in net assets as the investments are trading securities.

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 statements of operations and changes in net assets

Gifts of long-lived assets such as land, building, or equipment are reported as support without donor restrictions 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 support with donor restrictions. Expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Debt Issuance Costs: Debt issuance costs are presented as a reduction of the carrying amount of debt rather than as an asset and amortized over the life of the related obligation. Amortization of debt issuance costs is reported as interest expense in the consolidated statements of operations and changes in net assets.

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 for the years ended December 31, 2018 and 2017.

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, 2018 and 2017 was \$623 and \$591, respectively, and is included in depreciation and amortization expense in the consolidated statements of operations and changes in net assets.

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

	<u>2018</u>	<u>2017</u>
Insurance liabilities	\$ 164,828	\$ 157,445
Long-term pension obligations	318,143	336,682
Asset retirement obligations	10,151	10,114
Interest rate swap	3,667	4,513
Contingent performance obligation	7,242	7,242
Other	<u>485</u>	<u>1,358</u>
Other long-term obligations	<u>\$ 504,516</u>	<u>\$ 517,354</u>

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 and is recognized as performance obligations are satisfied. Performance obligations are determined based on the nature of the services provided by the System. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected or actual charges. Management believes that this method provides a reasonable representation of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to inpatient services. The System measures the performance obligation from admission into the hospital to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge. Revenue for performance obligations satisfied at a point in time is recognized when goods or services are provided and management does not believe it is required to provide additional goods or services to the patient.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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. The System'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 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. The System estimates the transaction price for patients with deductibles and coinsurance from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient/resident service revenue in the period of the change and are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Adjustments arising from a change in the transaction price were not significant in the twelve months ended December 31, 2018 or 2017.

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/resident accounts receivable and the offset is in third-party liabilities. Surcharges are generally received and paid to the state within a few months. 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 consolidated 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 THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Amounts recognized for the years ended December 31, 2018 and 2017, related to prior years, including adjustments to prior year estimates, increased revenues by approximately \$3,650 and \$2,980, 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.

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.

Implicit Price Concessions: Implicit price concessions are 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 collectability of accounts not covered by insurance based on historical cash collections. The results of this review are then used to make modifications to the implicit price concessions recognized at time of service. 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 collection agencies, subject to terms of certain restrictions on collection efforts as determined by the System. Patient/resident accounts receivable are written off after collection efforts have been followed in accordance with the System's policies. The implicit price concession for the year ended December 31, 2018 amounted to \$23,477.

Patient/resident service revenue recognized in the period from these major payor sources is as follows for the years ended December 31:

	<u>2018</u>	<u>2017</u>
Medicare	42%	42%
Medicaid	13	12
Commercial	37	36
Self-pay/other	8	10
	<u>100%</u>	<u>100%</u>

The adoption of ASU 2014-09 has no impact on the System's patient/resident accounts receivable as it was historically recorded net of allowance for doubtful accounts on the consolidated balance sheets. The allowance for doubtful accounts for the year ended December 31, 2017 amounted to \$24,138.

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 and does not pursue collection of amounts. The System has determined it has provided an implicit price concession to uninsured patients/residents with other uninsured balances (for example, copays and deductibles). The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients/residents and the amounts the System expects to collect based on its collection history with those patients/residents. Those patients who meet the System's criteria for charity care are provided care without charge or at amounts less than established rates and the System has determined it has thus provided an implicit price concession. Price concessions, including charity care, are not reported as net patient service revenue.

In addition to charity care, the System provides 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.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Of the System's total expenses reported, an estimated \$10,630 and \$10,156 arose from providing services to charity patients for the years ended December 31, 2018 and 2017, respectively. 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.

Collective Bargaining Agreements: The System has approximately 42% of its employees working under thirteen collective bargaining agreements. The agreements are set to expire beginning April 30, 2019 through March 31, 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 activities.

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

	<u>2018</u>	<u>2017</u>
Cafeteria revenue	\$ 3,037	\$ 2,735
Parking revenue	1,103	1,253
Donor contributions to the Foundations without donor restrictions	2,125	2,021
Grant revenue	2,321	1,149
340(b) program revenue	5,016	1,936
Medicaid health home care coordination revenue	2,425	3,034
Shared services	5,042	3,458
Rental income	3,725	2,255
Other	<u>2,035</u>	<u>3,437</u>
Other revenue	<u>\$ 26,829</u>	<u>\$ 21,278</u>

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

	<u>2018</u>	<u>2017</u>
Rents and operating leases	\$ 10,482	\$ 9,544
Rental equipment	2,989	3,451
Dues	3,332	5,422
NYS DOH cash receipts assessment	6,983	6,023
Conferences, seminars and travel	2,171	2,276
Licenses and taxes	442	389
Sponsorships	391	-
Subscriptions	640	387
Other	<u>3,937</u>	<u>3,210</u>
Other expenses	<u>\$ 31,367</u>	<u>\$ 30,702</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Contributions: Contributions received are recorded as without donor restrictions or with donor restrictions 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 net assets without donor restrictions 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 net assets with donor restrictions, depending on the nature of the restrictions. When a restriction expires, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the consolidated 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 include excess of revenues over expenses, commonly referred to as the performance indicator. Changes in net assets without donor restrictions, 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, other than net periodic costs, and discontinued operations.

Net Assets without Donor Restrictions: Net assets without donor restrictions are available for the general operating purposes of the System and are not subject to any donor limitations.

Net Assets with Donor Restrictions: Net assets with donor restrictions include those which have been restricted by donors to be maintained in perpetuity as well as those whose use is limited by donors to a specific period or purpose and include the Hospitals' interest in the donor-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). Net assets with donor restrictions 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. Some donor-imposed restrictions are temporary in nature and when a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restriction and are reported on the consolidated statements of operations and changes in net assets as net assets released from restrictions used for capital. Net assets with donor restrictions are released to net assets without donor restrictions as restrictions are met, which can occur within the same period. Gifts whose restrictions are met within the same period in which they are received are recorded as an increase in net assets without donor restrictions. Other donor-imposed restrictions are perpetual in nature, consisting primarily of endowments, which require that the corpus be invested in perpetuity and only the income be made available for program operations in accordance with donor restrictions. Net assets with donor restrictions, which amounted to \$7,706 at December 31, 2018 (\$8,064 - 2017), consist primarily of contributions restricted for use towards various capital projects at the Hospitals. Proceeds from these contributions are included in the consolidated balance sheets under the captions of cash and cash equivalents and investments. Investment returns are included in net assets without donor restrictions unless the return is restricted by donor or law. Contributions receivable are included under the captions of other receivables within the consolidated balance sheets.

Endowments: For the years ended December 31, 2018 and 2017, the Mercy Hospital Foundation, Inc. and the Sisters Hospital Foundation Inc., had \$246 of net assets with donor restrictions to be maintained in perpetuity from the proceeds of a Charitable Remainder Unitrusts (CRUT). The CRUTs are included under the caption of investments within the balance sheets. The Foundations segregated these restricted funds that are to be maintained in perpetuity 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 \$50 of net assets with donor restrictions to be maintained in perpetuity, from the proceeds of a trust, as of December 31, 2018 (\$51 - 2017). The trust is included under the caption of investments within the consolidated balance sheets. Per the trust agreement, earnings shall be divided such that half of the earnings are to be used by the Foundation in line with donor-imposed stipulations and the other half is to be added to the principal and remain in perpetuity.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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. Tax-exempt organizations are subject to federal taxes on unrelated business income under section 511 of the Internal Revenue Code which are reported under the caption of other expenses in the consolidated statements of operations and changes in net assets.

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 are eliminated in the consolidated financial statements. The respective assets and liabilities are also eliminated in the consolidated financial statements.

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 and other external costs in the amount of \$2,377 and \$3,001 for the years ended December, 31 2018 and 2017, respectively. Capitalized project labor costs amounted to \$94 for the year ended December 31, 2017. There were no capitalized project labor costs for the year ended December 31, 2018.

Reclassifications: Certain prior year amounts were reclassified to conform to the 2018 consolidated financial statement presentation, primarily related to the adoption of ASU 2016-14 and ASU 2017-07.

Subsequent Events: The System evaluated subsequent events through March 28, 2019, which was the date the consolidated financial statements were available to be issued.

NOTE 3. LIQUIDITY AND AVAILABILITY

Financial assets available for general expenditure that is, without donor or other restrictions limiting their use, within one year of December 31, 2018 are:

Cash and cash equivalents	\$	276,731
Patient/resident accounts receivable and other receivables		128,271
Investments		177,770
Assets limited as to use		<u>44,092</u>
Financial assets available to meet general expenditures within one year	\$	<u>626,864</u>

The System has certain board-designated and donor-restricted assets limited as to use which are available for general expenditure within one year in the normal course of operations. Accordingly, these assets have been included in the quantitative information above. The System has other assets limited as to use for donor-restricted purposes and debt service. Additionally, certain other board-designated assets are designated for future capital expenditures. These assets limited as to use, which are more fully detailed in Note 4, are not available for general expenditure within the next year and are not reflected in the amounts above. However, the board-designated amounts could be made available, if necessary.

As part of the System's liquidity management plan, cash in excess of daily requirements are invested in short-term investments and money market funds. Additionally, the System maintains a \$20,000 line of credit as of December 31, 2018, as discussed in more detail in Note 7.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 4. ASSETS LIMITED AS TO USE

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

	<u>2018</u>	<u>2017</u>
By Board for capital improvements:		
Funded depreciation:		
Cash and cash equivalents	\$ 19,512	\$ 7,322
U.S. government obligations	3,472	3,929
Interest receivable	<u>16</u>	<u>21</u>
	23,000	11,272
Held by Trustee under Indenture Agreement:		
Cash and cash equivalents	7,584	13,670
U.S. government obligations	<u>964</u>	<u>962</u>
	8,548	14,632
Held by Trustee under Letter of Credit Agreement:		
Cash and cash equivalents	2,792	2,760
Board Designated for long-term care reinvestment:		
Cash and cash equivalents	2,602	2,601
Delivery System Reform Incentive Payment funds	19,074	15,836
Other	<u>986</u>	<u>836</u>
Assets limited as to use	<u>\$ 57,002</u>	<u>\$ 47,937</u>

NOTE 5. INVESTMENTS

Investments consisted of the following as of December 31:

	<u>2018</u>	<u>2017</u>
Investment in debt and equity securities:		
Fair value	\$ 185,013	\$ 196,082
Cost	<u>174,434</u>	<u>174,146</u>
Unrealized gain	<u>\$ 10,579</u>	<u>\$ 21,936</u>

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

	<u>2018</u>	<u>2017</u>
Interest and dividend income	\$ 2,646	\$ 2,453
Net unrealized and realized gains (losses) on investments	<u>(9,927)</u>	<u>17,667</u>
Investment income (loss)	<u>\$ (7,281)</u>	<u>\$ 20,120</u>

Included in investments is \$5,720 of restricted investments held by the Foundations due to donor restrictions (\$6,339 - 2017).

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 6. PROPERTY AND EQUIPMENT

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

	<u>2018</u>	<u>2017</u>
Land and land improvements	\$ 9,003	\$ 8,126
Buildings	285,598	270,223
Equipment	304,270	280,988
Capital leases	50,449	45,235
Leasehold improvements	<u>134,716</u>	<u>117,765</u>
	784,036	722,337
Accumulated depreciation	(383,261)	(341,007)
Accumulated amortization on capital leases	<u>(40,512)</u>	<u>(36,574)</u>
	360,263	344,756
Construction in progress	<u>15,208</u>	<u>20,028</u>
Property and equipment, net	<u>\$ 375,471</u>	<u>\$ 364,784</u>

Depreciation expense for the years ended December 31, 2018 and 2017 amounted to \$42,338 and \$42,249, respectively. Amortization expense on equipment under capital leases amounted to \$4,060 and \$5,107 for the years ended December 31, 2018 and 2017, respectively.

NOTE 7. LONG-TERM OBLIGATIONS

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

	<u>2018</u>	<u>2017</u>
Mercy Hospital of Buffalo		
Series 2006 Revenue Bonds (a)	\$ 5,781	\$ 6,549
Series 2008 Revenue Bonds (b)	18,597	19,400
Series 2012 Revenue Bonds (c)	2,683	2,764
Series 2015 Revenue Bonds (d)	10,751	11,001
2017 Bridge loan financing (f)	14,000	6,472
Cafeteria renovation loan with Aramark Healthcare, in monthly payments of \$3, matures August 2018	-	71
Capital lease obligations and other, at interest rates ranging from 2.73% to 4.25%, collateralized by equipment	<u>6,555</u>	<u>8,441</u>
	58,367	54,698
Kenmore Mercy Hospital		
Series 2006 Revenue Bonds (a)	5,059	6,240
Series 2012 Revenue Bonds (c)	12,287	12,657
Series 2015 Revenue Bonds (d)	3,771	3,860
2016 Bridge loan financing (e)	5,075	5,449
Term Loan for KMH Homes, Inc. (g)	3,193	3,752
Capital lease obligations and other, at various rates of interest ranging from 2.98% to 4.00%, collateralized by equipment	3,879	3,057
Other	<u>-</u>	<u>6</u>
	33,264	35,021

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

	<u>2018</u>	<u>2017</u>
Sisters of Charity Hospital		
Series 2006 Revenue Bonds (a)	16,564	18,761
Series 2015 Revenue Bonds (d)	5,069	5,188
2017 Bridge loan financing (f)	7,000	2,713
Capital lease obligations, at various rates of interest ranging from 3.13% to 4.87%, collateralized by equipment	<u>3,593</u>	<u>5,121</u>
	32,226	31,783
Mount St. Mary's Hospital and Health Center		
Capital lease obligations, at a 3.81% rate of interest, collateralized by equipment	-	15
Father Baker Manor		
Mortgage payable to Century Health Capital, Inc. (h)	4,060	4,592
McAuley Seton Home Health Care Corporation		
Term loan to bank (i)	-	40
Our Lady of Victory Renaissance Corporation		
Series 2007A Variable Rate Demand Bonds (j)	7,460	7,810
Series 2007B Variable Rate Demand Bonds (j)	<u>1,200</u>	<u>1,260</u>
	8,660	9,070
Trinity Medical WNY		
Capital lease obligations, at various rates of interest ranging from 3.15% to 5.79%, collateralized by equipment	130	304
Catholic Health System (Parent)		
Series 2015 Revenue Bonds (d)	77,203	80,825
Capital lease obligation for financing of VOIP telephone system, in monthly installments of \$22, including interest ranging from 2.92% to 2.97%, collateralized by equipment	<u>-</u>	<u>269</u>
	77,203	81,094
St. Francis Geriatric and Healthcare Services, Inc.		
Promissory Note (k)	<u>9,452</u>	<u>-</u>
Total long-term obligations	223,362	216,617
Less: Deferred financing costs	(4,521)	(5,757)
Less: Current portion of long-term obligations	<u>(20,029)</u>	<u>(18,157)</u>
Long-term obligations, net	<u>\$ 198,812</u>	<u>\$ 192,703</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:

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

- Series 2006A Bonds for \$13,360 were loaned to Mercy Hospital of Buffalo in order to finance the cost of Mercy Hospital of Buffalo'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 Sisters of Charity Hospital 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, which was merged into Sisters of Charity Hospital in 2009, to finance the cost of the St. Joseph Hospital's 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.

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 1.74% and 1.75% at December 31, 2018 and 2017, 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 day's 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, 2018 and 2017.

- 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.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of dollars)

NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

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, 2019 (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 8). The variable interest rate was 1.71% at December 31, 2018 and 2017.

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.
- Series 2012B Bonds for \$3,080 were loaned to Mercy Hospital of Buffalo for the purpose of funding the cost of improvements to Mercy Hospital of Buffalo'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, 2018 are as follows:

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		12,485
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><u>15,565</u></u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of dollars)

NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

- (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.

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, 2018 are as follows:

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>88,880</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of dollars)

NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

- 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. It is management's intention and ability to pay down these outstanding loans with the 2019 Series bond issue, expected to close in April 2019.
- 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. Promissory notes representing a borrowing under the 2017 loan agreements were signed December 14, 2018 at the full amount of the original loan agreements. Variable interest only payments are made monthly with the maturity date for the principal balance due May 31, 2019. It is management's intention and ability to pay down these outstanding loans with the 2019 Series bond issue, expected to close in April 2019.
- 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 began on 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 fixed 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. The term loan called for monthly principal payments of \$40 plus interest and matured on December 28, 2017. Outstanding borrowings were secured by substantially all the revenues and receipts of MSHC. The term loan contained various loan covenants, including a debt service coverage ratio. MSHC was in compliance with all covenants as of December 31, 2017. The term loan was paid in full in January 2018.
- 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 Skilled Nursing Facility (SNF) and Program of All-Inclusive Care for the Elderly (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 1.80% and 1.84% for the Series 2007A bonds and 2.60% and 1.59% for the Series 2007B bonds at December 31, 2018 and 2017, respectively. See Note 8 regarding the interest rate swap agreement OLV Renaissance entered into with respect to the Series 2007A Revenue Bonds.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

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 accounts receivable without donor restrictions 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, 2018 or 2017. 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.

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

Mercy Hospital of Buffalo was in compliance with this covenant as of December 31, 2018 and 2017. OLV Renaissance was in compliance with this covenant as of December 31, 2018 and 2017.

- k. On January 19, 2018, St. Francis Geriatric and Healthcare Services, Inc. entered into a promissory note with Five Star Bank in the amount of \$9,750. The loan calls for monthly payments of \$59, which includes principal and interest. Payments began on February 19, 2018 with the final payment due on January 19, 2028.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

Aggregate maturities of long-term obligations, including capital lease obligations, considering obligations subject to short-term remarketing as due according to their long-term amortization schedule, subsequent to December 31, 2018 are as follows:

	<u>Long-Term Debt</u>	<u>Capital Leases</u>	<u>Total</u>
2019	\$ 16,121	\$ 4,242	\$ 20,363
2020	14,722	3,224	17,946
2021	15,642	2,056	17,698
2022	18,791	1,575	20,366
2023	14,455	1,192	15,647
Thereafter	<u>129,474</u>	<u>3,619</u>	<u>133,093</u>
	209,205	15,908	225,113
Less: Deferred financing costs	(4,521)	-	(4,521)
Less: Interest	<u>-</u>	<u>(1,751)</u>	<u>(1,751)</u>
Long-term obligations	<u>\$ 204,684</u>	<u>\$ 14,157</u>	<u>\$ 218,841</u>

The System had a revolving line of credit of \$20,000 as of December 31, 2018 and 2017. There was no amount outstanding on the revolving line of credit as of December 31, 2018 or 2017.

Operating Leases: Future minimum lease payments under noncancelable operating leases for equipment and property (net of sublease rentals) are as follows at December 31, 2018:

2019	\$ 11,734
2020	10,616
2021	9,899
2022	8,102
2023	7,352
Thereafter	<u>11,775</u>
	59,478
Less: Minimum sublease rental	<u>(3,291)</u>
	<u>\$ 56,187</u>

Total expense for rents and operating type leases for equipment and property was \$13,471 and \$12,995 for the years ended December 31, 2018 and 2017, respectively.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 8. 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 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 \$1,833 and \$783 for the years ended December 31, 2018 and 2017, respectively.

The terms of the Series 2008 swap require the Hospitals to pay 3.785% on the notional amount of \$19,220 and \$20,020 at December 31, 2018 and 2017, 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 in 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 in net assets.

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

(in thousands of dollars)	2018		2017	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Interest rate contracts floating to fixed	Other long-term obligations	\$ <u>3,667</u>	Other long-term obligations	\$ <u>4,513</u>

The effects of derivative instruments on the consolidated statements of operations and changes in net assets at December 31 is as follows:

(in thousands of dollars)	Ineffective portion in Statement of Operations		Effective portion in Net Assets	
	2018	2017	2018	2017
Change in fair value of interest rate swaps	\$ <u>18</u>	\$ <u>6</u>	\$ <u>828</u>	\$ <u>313</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 II within the fair value hierarchy defined in Note 14.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of dollars)

NOTE 9. 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, 2018 and 2017 and statements of operations and changes in net assets, and cash flows for the years then ended December 31, 2018 and 2017.

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 9. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

Consolidating Balance Sheet
December 31, 2018

ASSETS	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Current assets:						
Cash and cash equivalents	\$ 44,880	\$ 73,603	\$ 56,435	\$ 48,139	\$ -	\$ 223,057
Patient/resident accounts receivable	-	44,896	31,311	18,050	-	94,257
Other receivables	1,265	2,121	2,673	1,829	-	7,888
Inventories	10	11,785	6,113	2,503	-	20,411
Prepaid expenses and other current assets	6,654	2,267	1,695	588	-	11,204
Due from affiliates	106,244	538	635	80	(103,286)	4,211
Total current assets	159,053	135,210	98,862	71,189	(103,286)	361,028
Assets limited as to use	20,842	968	19,552	2,420	-	43,782
Investments	-	30,842	91,654	22,008	-	144,504
Property and equipment, net	78,802	104,063	71,191	63,981	-	318,037
Other assets	13,256	45,762	35,922	14,155	-	109,095
Due from affiliates	5,210	-	10,304	1,456	(16,876)	94
Total assets	\$ 277,163	\$ 316,845	\$ 327,485	\$ 175,209	\$ (120,162)	\$ 976,540
LIABILITIES AND NET ASSETS						
Current liabilities:						
Current portion of long-term obligations	\$ 5,015	\$ 5,127	\$ 4,445	\$ 4,004	\$ -	\$ 18,591
Accounts payable	8,283	18,665	16,097	9,719	-	52,764
Accrued expenses	21,061	12,985	29,713	5,962	-	69,721
Due to third-party payors	33	16,788	10,922	5,892	-	33,635
Due to affiliates	1,069	21,005	23,399	21,924	(65,876)	1,521
Total current liabilities	35,461	74,570	84,576	47,501	(65,876)	176,232
Long-term obligations, net	70,216	52,399	27,391	28,384	-	178,390
Other long-term obligations	61,016	213,541	134,398	53,403	-	462,358
Due to affiliates	12,128	-	-	-	(11,760)	368
Total liabilities	178,821	340,510	246,365	129,288	(77,636)	817,348
Net assets (deficit):						
Without donor restrictions	98,342	(23,665)	81,120	45,921	(42,526)	159,192
Total net assets (deficit)	98,342	(23,665)	81,120	45,921	(42,526)	159,192
Total liabilities and net assets (deficit)	\$ 277,163	\$ 316,845	\$ 327,485	\$ 175,209	\$ (120,162)	\$ 976,540

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 9. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

Consolidating Statement of Operations
and Changes in Net Assets (Deficit)
For the Year Ended December 31, 2018

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Revenues and other support without donor restrictions:						
Net patient/resident service revenue	\$ -	\$ 437,494	\$ 321,415	\$ 181,936	\$ (113)	\$ 940,732
Other revenue	154,860	5,579	11,809	1,524	(138,727)	35,045
Total revenues and other support without donor restrictions	<u>154,860</u>	<u>443,073</u>	<u>333,224</u>	<u>183,460</u>	<u>(138,840)</u>	<u>975,777</u>
Expenses:						
Salaries and wages	73,246	180,778	152,257	74,135	(63,401)	417,015
Employee benefits	20,795	53,377	43,511	20,276	(18,227)	119,732
Medical and professional fees	9,764	18,820	15,630	4,979	(2,816)	46,377
Purchased services	32,275	38,624	33,463	15,078	(29,833)	89,607
Supplies	859	92,755	58,168	40,151	(727)	191,206
Depreciation and amortization	7,489	16,706	14,021	9,148	(7,187)	40,177
Interest	3,154	4,719	3,912	2,570	(2,789)	11,566
Insurance	499	4,841	3,582	1,805	(475)	10,252
Other expenses	5,501	16,885	11,134	5,518	(12,378)	26,660
Total expenses	<u>153,582</u>	<u>427,505</u>	<u>335,678</u>	<u>173,660</u>	<u>(137,833)</u>	<u>952,592</u>
Income (loss) from operations	1,278	15,568	(2,454)	9,800	(1,007)	23,185
Nonoperating revenues and expenses:						
Investment income (loss)	1,188	(391)	(4,050)	(589)	(1,021)	(4,863)
Other components of net periodic pension cost	(2,928)	(7,117)	(3,155)	(1,659)	2,568	(12,291)
Other revenues and gains, net	462	174	321	86	(540)	503
Total nonoperating revenues and expenses	<u>(1,278)</u>	<u>(7,334)</u>	<u>(6,884)</u>	<u>(2,162)</u>	<u>1,007</u>	<u>(16,651)</u>
Excess (deficiency) of revenues over expenses	<u>\$ -</u>	<u>\$ 8,234</u>	<u>\$ (9,338)</u>	<u>\$ 7,638</u>	<u>\$ -</u>	<u>\$ 6,534</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 9. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

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

For the Year Ended December 31, 2018

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Net assets without donor restrictions:						
Excess (deficiency) of revenues over expenses	\$ -	\$ 8,234	\$ (9,338)	\$ 7,638	\$ -	\$ 6,534
Change in unrealized gain on interest rate swaps	-	594	-	-	-	594
Change in pension obligation, other than net periodic cost	5,520	10,326	5,183	1,612	-	22,641
Amortization of terminated interest rate swaps	-	395	1,132	306	-	1,833
Transfers (to) from parent or affiliate	(3,735)	767	1,301	605	-	(1,062)
Capital grants	3,848	35	44	-	-	3,927
Contributions	94	210	1,122	261	-	1,687
Other	-	-	-	(87)	-	(87)
Valuation allowance on intercompany receivables	-	-	-	-	(10,165)	(10,165)
Increase (decrease) in net assets without donor restrictions	<u>5,727</u>	<u>20,561</u>	<u>(556)</u>	<u>10,335</u>	<u>(10,165)</u>	<u>25,902</u>
Increase (decrease) in net assets	5,727	20,561	(556)	10,335	(10,165)	25,902
Net assets (deficit), beginning 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>
Net assets (deficit), end of year	<u>\$ 98,342</u>	<u>\$ (23,665)</u>	<u>\$ 81,120</u>	<u>\$ 45,921</u>	<u>\$ (42,526)</u>	<u>\$ 159,192</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 9. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

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	-	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	2,199	1,877	532	-	10,237
Due from affiliates	100,247	354	770	67	(99,118)	2,320
Total current assets	162,218	123,222	99,905	61,493	(99,118)	347,720
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
Other assets	11,946	40,961	36,736	13,054	-	102,697
Due from affiliates	5,116	-	10,303	1,456	(16,875)	-
Total assets	\$ 276,636	\$ 298,980	\$ 330,852	\$ 167,599	\$ (115,993)	\$ 958,074
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	34,962	76,332	82,816	48,055	(71,872)	170,293
Long-term obligations, net	73,947	49,131	26,889	30,370	-	180,337
Other long-term obligations	75,112	217,743	139,471	53,588	(11,760)	474,154
Total liabilities	184,021	343,206	249,176	132,013	(83,632)	824,784
Net assets (deficit):						
Without donor restrictions	92,615	(44,226)	81,676	35,586	(32,361)	133,290
Total net assets (deficit)	92,615	(44,226)	81,676	35,586	(32,361)	133,290
Total liabilities and net assets (deficit)	\$ 276,636	\$ 298,980	\$ 330,852	\$ 167,599	\$ (115,993)	\$ 958,074

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 9. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

Consolidating Statement of Operations
and Changes in Net Assets (Deficit)
For the Year Ended December 31, 2017

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Revenues and other support without donor restrictions:						
Net patient/resident service revenue before provision for bad debts	\$ -	\$ 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	-	412,738	325,671	169,350	(97)	907,662
Other revenue	152,296	5,017	12,238	1,308	(136,805)	34,054
Total revenues and other support without donor restrictions	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	19,069	50,141	40,931	18,616	(16,874)	111,883
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	150,668	412,508	327,800	167,345	(135,448)	922,873
Income (loss) from operations	1,628	5,247	10,109	3,313	(1,454)	18,843
Nonoperating revenues and expenses:						
Investment income (loss)	312	3,772	8,880	2,145	-	15,109
Other components of net periodic pension costs	(2,693)	(6,734)	(2,686)	(1,664)	2,335	(11,442)
Other revenues and gains, net	538	360	317	131	(881)	465
Total nonoperating revenues and expenses	(1,843)	(2,602)	6,511	612	1,454	4,132
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 9. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

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

For the Year Ended December 31, 2017

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
Net assets without donor restrictions:						
Excess (deficiency) of revenues over expenses	\$ (215)	\$ 2,645	\$ 16,620	\$ 3,925	\$ -	\$ 22,975
Change in unrealized gain on interest rate swaps	-	191	-	-	-	191
Change in pension obligation, other than net periodic cost	(6,405)	(11,331)	(7,706)	(999)	-	(26,441)
Amortization of terminated interest rate swaps	-	155	446	182	-	783
Transfers (to) from parent or affiliate	26,010	(8,683)	(11,599)	(6,203)	-	(475)
Capital grants	-	-	-	8	-	8
Contributions	94	334	823	1,309	-	2,560
Other	-	-	-	99	-	99
Valuation allowance on intercompany receivables	-	-	-	-	(10,598)	(10,598)
Increase (decrease) in net assets without donor restrictions	<u>19,484</u>	<u>(16,689)</u>	<u>(1,416)</u>	<u>(1,679)</u>	<u>(10,598)</u>	<u>(10,898)</u>
Increase (decrease) in net assets	19,484	(16,689)	(1,416)	(1,679)	(10,598)	(10,898)
Net assets (deficit), 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 9. OBLIGATED GROUP FINANCIAL INFORMATION (CONTINUED)

Consolidating Statements of Cash Flows

For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities:		
Increase (decrease) in net assets	\$ 25,902	\$ (10,898)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities		
Depreciation and amortization	40,177	41,141
Change in minimum pension liability adjustment	(22,641)	26,441
Valuation allowance of intercompany receivables	10,165	10,598
Unrealized and realized loss (gain) on investments	7,647	(13,230)
Change in realized gain on interest rate swap	(605)	(194)
Realized gain on investments	(206)	-
Loss on sale of property and equipment	20	-
Undistributed earnings in equity investees	(73)	(267)
Amortization of discount on debt issuance	61	61
Amortization of premium on debt issuance	(572)	(574)
Amortization of debt issuance costs	1,217	403
Other	(1)	(140)
(Increase) decrease in assets		
Patient/resident accounts receivables	10,667	(3,372)
Other receivables	(1,511)	1,543
Inventories	2,719	(2,020)
Prepaid expenses and other current assets	(1,469)	269
Due from affiliates	(12,150)	(5,591)
Other assets	2	(16)
Increase (decrease) in liabilities:		
Accounts payable	4,834	7,230
Accrued expenses	(1,078)	1,438
Due to affiliate	420	914
Due to third-party payors	877	(3,149)
Other liabilities	7,120	1,416
Net cash provided by operating activities	<u>71,522</u>	<u>52,003</u>
Cash flows from investing activities:		
Purchase of property and equipment	(35,454)	(32,329)
Proceeds from sale of property and equipment	22	286
Purchase of assets limited as to use	(25,430)	(33)
Proceeds from sale of assets limited as to use	16,690	2,435
Purchase of investments	-	(434)
Purchase of equity investments	(2,270)	-
Proceeds from sale of investments	387	-
Net cash used in investing activities	<u>(46,055)</u>	<u>(30,075)</u>
Cash flows from financing activities:		
Proceeds from issuance of long-term obligations	11,815	12,937
Repayments of current and long-term obligations	(14,957)	(16,706)
Net cash used in financing activities	<u>(3,142)</u>	<u>(3,769)</u>
Increase in cash and cash equivalents	22,325	18,159
Cash and cash equivalents - beginning of year	<u>200,732</u>	<u>182,573</u>
Cash and cash equivalents - end of year	<u>\$ 223,057</u>	<u>\$ 200,732</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for interest	\$ 8,175	\$ 7,795
Non-cash transactions:		
Assets acquired under capital lease obligations	\$ 2,115	\$ 652
(Decrease) increase in construction related payables	\$ (372)	\$ 1,742

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 10. 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>2018</u>	<u>2017</u>
Projected Benefit Obligations		
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 725,508	\$ 636,377
Service cost	24,140	21,904
Interest cost	26,743	27,510
Expenses	(1,239)	(424)
Benefits paid	(23,497)	(21,093)
Actuarial (gain) loss	<u>(61,495)</u>	<u>61,234</u>
Projected benefit obligation at end of year	<u>\$ 690,160</u>	<u>\$ 725,508</u>
Accumulated benefit obligations at end of year	<u>\$ 634,520</u>	<u>\$ 658,757</u>
Plan Assets		
Change in plan assets:		
Fair value of assets at beginning of year	\$ 388,940	\$ 328,601
Actual return on plan assets	(25,273)	48,725
System contribution	33,131	33,131
Expenses	(1,284)	(538)
Benefits paid	<u>(23,497)</u>	<u>(21,093)</u>
Fair value of plan assets at end of year	<u>\$ 372,017</u>	<u>\$ 388,826</u>
Funded status at end of year	<u>\$ (318,143)</u>	<u>\$ (336,682)</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)

	<u>2018</u>	<u>2017</u>
Amounts recognized in the consolidated balance sheets:		
Non-current liabilities	\$ (318,143)	\$ (336,682)
Net amounts recognized	<u>\$ (318,143)</u>	<u>\$ (336,682)</u>
Amounts recognized in net assets without donor restrictions consists of:		
Actuarial net loss	\$ (178,372)	\$ (200,534)
Prior service cost	<u>(186)</u>	<u>(252)</u>
Total amount recognized	<u>\$ (178,558)</u>	<u>\$ (200,786)</u>
Other changes recognized in net assets without donor restrictions:		
Net (loss) gain arising during the period	\$ (8,402)	\$ 37,843
Amortization of prior service cost	(66)	(57)
Amortization of loss	<u>(13,860)</u>	<u>(9,430)</u>
Total amount recognized	<u>\$ (22,328)</u>	<u>\$ 28,356</u>
Components of net periodic benefit cost:		
Service cost	\$ 24,140	\$ 21,904
Interest cost	26,743	27,509
Expected return on plan assets	(27,911)	(25,244)
Amortization of prior service cost	66	57
Amortization of net loss	13,833	9,411
Recognized actuarial loss	<u>20</u>	<u>27</u>
Net periodic pension cost	<u>\$ 36,891</u>	<u>\$ 33,664</u>

The System's estimated prior service cost of \$178 and net loss of \$7,750 will be amortized from net assets without donor restrictions 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.

The Plan's target asset allocation and the actual asset allocation percentages for 2018 and 2017 are as follows at the respective measurement dates:

<u>Asset Category</u>	<u>Target</u>	<u>Actual</u>	
		<u>2018</u>	<u>2017</u>
Equities	70%	69%	71%
Fixed income	25	26	24
Other	<u>5</u>	<u>5</u>	<u>5</u>
	<u>100%</u>	<u>100%</u>	<u>100%</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)

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, 2018 and 2017.

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.

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.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)

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, 2018, measured at fair value on a recurring basis using the fair value hierarchy defined in Note 14.

At December 31, 2018	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Total</u>
Pension plans:				
Cash and cash equivalents	\$ 8,125	\$ -	\$ -	\$ 8,125
Equity securities	60,350	-	-	60,350
Debt securities:				
Government and government agency obligations	-	17,232	-	17,232
Corporate bonds	-	50,162	-	50,162
Asset backed securities	-	11,620	-	11,620
Mutual funds:				
Equity mutual funds	45,287	-	-	45,287
Fixed mutual funds	<u>20,185</u>	<u>-</u>	<u>-</u>	<u>20,185</u>
Subtotal	\$ 133,947	\$ 79,014	\$ -	212,961
Investment measured at net asset value:				
Commingled funds:				
Equity commingled funds				123,633
Fixed income commingled funds				17,591
Hedge funds				<u>17,876</u>
Total				<u><u>\$ 372,061</u></u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)

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	23,097	-	-	23,097
Subtotal	<u>\$ 151,222</u>	<u>\$ 74,109</u>	<u>\$ -</u>	<u>225,331</u>
 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><u>\$ 388,940</u></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 \$33,004 to the pension plan trust in 2019 to be allocated amongst participating entities.

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

2019	\$ 28,101
2020	\$ 30,481
2021	\$ 32,976
2022	\$ 35,575
2023	\$ 38,388
2024 - 2028	\$ 222,809

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)

	<u>2018</u>	<u>2017</u>
Weighted average assumptions used to determine end of the year benefit obligations:		
Discount rate	4.45%	3.75%
Rate of compensation increase	Age Based	Age Based
Weighted average assumptions used to determine net periodic pension cost:		
Discount rate	3.75%	4.40%
Expected long-term rate of return on plan assets	7.25%	7.25%
Rate of compensation increase	Age Based	Age Based
Measurement date	12/31/2018	12/31/2017

NOTE 11. 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, 2018 and 2017. 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% for the years ended December 31, 2018 and 2017. The System's reserve for unpaid and incurred but not reported claims at December 31, 2018 and 2017 is \$93,447 and \$89,640, respectively, and is included within other long-term obligations. The charges to expenses for professional and general liability for the years ended December 31, 2018 and 2017 were \$11,159 and \$13,558, 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 were \$80,953 and \$76,713 at December 31, 2018 and 2017, 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.

Workers' Compensation Arrangements

The System's insurance program for workers' compensation has a deductible of \$750 per occurrence in 2018 and 2017. 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 2018 and 2017, respectively. The System's current portion of liabilities for unpaid and incurred but not reported claims at December 31, 2018 and 2017 is \$8,949 and \$9,128, 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, 2018 and 2017 is \$71,381 and \$67,805, respectively, and is included in other long-term obligations.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 11. INSURANCE ARRANGEMENTS (CONTINUED)

The charges to expenses for workers' compensation costs approximated \$11,833 and \$10,524 for the years ended December 31, 2018 and 2017, 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. The System's current portion of insurance receivables related to the claims at December 31, 2018 and 2017 is \$677 and \$519, respectively, and is included in prepaid expenses and other current assets. The System's long-term portion of insurance receivables related to the claims at December 31, 2018 and 2017 is \$25,782 and \$26,132, 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, 2018 and 2017, was \$8,344 and \$7,310, respectively.

NOTE 12. 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, 2018, 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.

NOTE 13. 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>2018</u>	<u>2017</u>
Medicare	34%	35%
Medicaid	20	21
Blue Cross	8	7
Other third-party payors	26	27
Patients/residents	<u>12</u>	<u>10</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.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 14. 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, debt securities, exchange traded funds 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 I) and the lowest priority to unobservable inputs (level III). The three levels of the fair value hierarchy are described as follows:

- Level I: 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 II: Inputs other than quoted prices included within level I 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;
 - 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 II input must be observable for substantially the full term of the asset or liability.

- Level III: 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.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 14. FAIR VALUE MEASUREMENTS (CONTINUED)

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 isolation would result in a significantly different fair value measurement, respectively. The System classifies these securities as Level II 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, 2018 and 2017.

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 and Government Agency Obligations: Debt securities and government agency obligations 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.

Other: Other investments consist of life insurance policies which 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.

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.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 14. FAIR VALUE MEASUREMENTS (CONTINUED)

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 II 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, 2018 and 2017:

At December 31, 2018	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Total</u>
Assets limited as to use:				
Cash and cash equivalents	\$ 51,359	\$ -	\$ -	\$ 51,359
Equity securities	8	-	-	8
Government and government agency obligations	<u>3,472</u>	<u>2,147</u>	<u>-</u>	<u>5,619</u>
Subtotal	\$ 54,839	\$ 2,147	\$ -	56,986
Interest receivable				<u>16</u>
Total				<u>\$ 57,002</u>
Investments:				
Cash and cash equivalents	\$ 494	\$ -	\$ -	\$ 494
Equity securities	10,109	-	-	10,109
Debt securities	1,403	1,328	-	2,731
Exchange traded funds	3,810	-	-	3,810
Mutual funds	1,738	-	-	1,738
Other	<u>-</u>	<u>500</u>	<u>-</u>	<u>500</u>
Subtotal	\$ 17,554	\$ 1,828	\$ -	19,382
Investment measured at net asset value:				
Investment in Ascension Alpha Fund, LLC				<u>165,631</u>
Total				<u>\$ 185,013</u>
Interest rate swap liability	<u>\$ -</u>	<u>\$ 3,667</u>	<u>\$ -</u>	<u>\$ 3,667</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 14. FAIR VALUE MEASUREMENTS (CONTINUED)

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>5,916</u>
Subtotal	\$ 45,930	\$ 1,987	\$ -	47,917
Interest receivable				<u>20</u>
Total				<u>\$ 47,937</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>500</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>\$ 196,082</u>
Interest rate swap liability	\$ -	<u>4,513</u>	\$ -	<u>4,513</u>

NOTE 15. RELATED PARTY TRANSACTIONS

Trinity Health charged the System dues for participation in certain programs and governance matters. For the year ended December 31, 2017, amounts charged to expense related to these dues amounted to approximately \$2,100 and are included as a component of other expenses. Effective July 1, 2017, Trinity Health no longer charges the System dues for participation in certain programs and governance matters.

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 five of its executive staff on the Catholic Medical Partners’ Board of Directors.

As discussed in Note 11, 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 Mercy Hospital of Buffalo), and seven other joint venture limited partners. On April 10, 2018, EAMB refinanced its outstanding debt of \$2,200 at which time MHB became sole guarantor of principal and interest on the debt. For the year ended December 31, 2018, the outstanding balance of debt was \$2,170.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of dollars)

NOTE 15. RELATED PARTY TRANSACTIONS (CONTINUED)

Caritas Medical Arts Building L.L.C. is a joint venture between Sisters of Charity Hospital and Ciminelli Development Company. For the year ended December 31, 2018, there was \$1,579 (\$1,681 - 2017) of debt outstanding related to the Caritas Medical Arts Building L.L.C., of which Sisters of Charity Hospital has guaranteed \$526 (\$560 - 2017). Per the guaranty agreement, Sisters of Charity Hospital's obligation shall decrease on a dollar for dollar basis as the principal amount of the obligation is paid down.

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. For the year ended December 31, 2018, there was \$4,559 (\$4,700 - 2017) of debt outstanding related to the Marian Professional Center Associates, L.P., of which the Obligated Group has guaranteed \$2,280 (\$4,700 - 2017). 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.

NR Physician Group, P.L.L.C. is a joint venture between Niagara Medicine, P.C., Roswell Park Comprehensive Cancer Center and Buffalo Medical Group. NR Physician Group, P.L.L.C. provides radiation oncology services.

Niagara Falls Memorial Medical Center Cath Lab is a joint venture between Catholic Health System, Inc., Kaleida Health, Erie County Medical Center Corporation and Niagara Falls Memorial Medical Center. The joint operating agreement's purpose is to establish the joint operating responsibilities for the Cath Lab on the campus of Niagara Falls Memorial Medical Center and provide Cath Lab Services for the residents of Niagara County.

Catholic Health System, Inc. and Subsidiaries, through its wholly-owned subsidiary CH Emmaus, Inc., owns a 40% equity stake in Sterling Surgical Center, L.L.C. Sterling Surgical is a multi-specialty ambulatory surgery center.

NOTE 16. DISCONTINUED OPERATIONS

The following subsidiaries, which have been closed or sold as referenced, have been accounted for within discontinued operations: 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). During 2018, St. Francis Geriatric Healthcare Services, Inc., previously closed during 2009, resumed operations and is accounted for within home and community based subsidiaries.

The residual assets (net of inter-company receivables), liabilities, and net (deficit) assets of the discontinued operations were \$9,584, \$14,961 and (\$3,434), respectively, as of December 31, 2018 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 \$13,906, \$18,391 and (\$2,543), respectively, as of December 31, 2017.

The aggregate gain (loss) from discontinued operations for assets held for sale as well as the closed facilities was approximately \$322 and \$13 for the years ended December 31, 2018 and 2017, respectively.

NOTE 17. FUNCTIONAL EXPENSES

As discussed in Note 2, ASU No. 2016-14 requires the System to provide an analysis of expenses by both natural and functional classification. Expenses were allocated by function using a reasonable and consistent approach that was primarily based on personnel costs directly attributable by function.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars)

NOTE 17. FUNCTIONAL EXPENSES (CONTINUED)

	December 31, 2018		
	Healthcare Services	Management and General	Total
Salaries and wages	\$ 478,384	\$ 55,571	\$ 533,955
Employee benefits	133,695	15,500	149,195
Medical and professional fees	40,919	10,663	51,582
Purchased services	100,185	10,825	111,010
Supplies	212,452	2,433	214,885
Depreciation and amortization	44,111	2,910	47,021
Interest	10,685	1,976	12,661
Insurance	12,441	160	12,601
Other expenses	27,255	4,112	31,367
Total	\$ 1,060,127	\$ 104,150	\$ 1,164,277
	December 31, 2017		
	Healthcare Services	Management and General	Total
Salaries and wages	\$ 465,868	\$ 54,101	\$ 519,969
Employee benefits	123,776	14,346	138,122
Medical and professional fees	42,835	5,569	48,404
Purchased services	95,384	11,031	106,415
Supplies	196,900	2,210	199,110
Depreciation and amortization	44,929	3,018	47,947
Interest	7,375	2,799	10,174
Insurance	15,539	147	15,686
Other expenses	25,566	5,136	30,702
Total	\$ 1,018,172	\$ 98,357	\$ 1,116,529

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, 2018 and 2017 and for the years then ended and our report thereon appears on pages 1 - 2 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 - Unaudited) 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 - Unaudited).

The consolidating information for Catholic Health System, Inc. and its subsidiaries, presented on pages 51 through 63, and the consolidating information for Kenmore Mercy Hospital and subsidiaries, presented on pages 64 through 66, 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 2018 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
March 28, 2019

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, 2018 and 2017
(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, 2018 and 2017 are set forth in the following table:

	<u>2018</u>	<u>2017</u>
Charity care	\$ 10,630	\$ 10,156
Cost of community benefit programs	51,085	48,678
Unpaid cost of Medicaid programs	<u>64,716</u>	<u>70,409</u>
	<u>\$ 126,431</u>	<u>\$ 129,243</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2018

ASSETS	Parent	Acute Care Subsidiaries	Home and Community Based Subsidiaries	Other Subsidiaries	Discontinued Operations	Eliminations	Total
Current assets:							
Cash and cash equivalents	\$ 44,880	\$ 187,347	\$ 21,954	\$ 17,473	\$ 5,027	\$ 50	\$ 276,731
Patient/resident accounts receivable	-	103,345	12,923	3,173	-	-	119,441
Other receivables	1,265	8,510	203	593	-	-	10,571
Inventories	10	22,659	966	-	-	-	23,635
Prepaid expenses and other current assets	6,654	4,938	855	326	3	-	12,776
Due from affiliates	106,244	1,055	163	1,158	1,575	(110,195)	-
Total current assets	159,053	327,854	37,064	22,723	6,605	(110,145)	443,154
Interest in net assets of related Foundations	-	-	114	18	129	(261)	-
Assets limited as to use	20,842	22,941	10,828	1,300	1,091	-	57,002
Investments	-	163,887	21,126	-	-	-	185,013
Property and equipment, net	78,802	265,239	15,529	15,901	-	-	375,471
Other assets	30,281	97,509	9,669	913	3,334	(27,031)	114,675
Due from affiliates	5,210	11,759	1,058	-	368	(18,395)	-
Total assets	\$ 294,188	\$ 889,189	\$ 95,388	\$ 40,855	\$ 11,527	\$ (155,832)	\$ 1,175,315
LIABILITIES AND NET ASSETS (DEFICIT)							
Current liabilities:							
Current portion of long-term obligations	\$ 5,015	\$ 13,577	\$ 899	\$ 538	\$ -	\$ -	\$ 20,029
Accounts payable	8,283	47,914	614	3,917	-	-	60,728
Accrued expenses	21,061	53,727	4,687	4,210	267	-	83,952
Due to third-party payors	33	37,661	1,376	3,729	437	-	43,236
Due to affiliates	1,069	67,560	9,803	27,739	10,244	(116,415)	-
Total current liabilities	35,461	220,439	17,379	40,133	10,948	(116,415)	207,945
Long-term obligations, net	70,216	108,174	12,348	8,074	-	-	198,812
Due to affiliates, net	12,128	-	-	-	-	(12,128)	-
Other long-term obligations	61,016	416,115	21,318	2,054	4,013	-	504,516
Total liabilities	178,821	744,728	51,045	50,261	14,961	(128,543)	911,273
Net assets (deficit):							
Without donor restrictions	111,908	137,473	44,229	(9,894)	(3,434)	(23,946)	256,336
With donor restrictions	3,459	6,988	114	488	-	(3,343)	7,706
Total net assets (deficit)	115,367	144,461	44,343	(9,406)	(3,434)	(27,289)	264,042
Total liabilities and net assets (deficit)	\$ 294,188	\$ 889,189	\$ 95,388	\$ 40,855	\$ 11,527	\$ (155,832)	\$ 1,175,315

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, 2018

	Parent	Acute Care Subsidiaries	Home and Community Based Subsidiaries	Other Subsidiaries	Discontinued Operations	Eliminations	Total
Revenues and other support without donor restrictions:							
Net patient/resident service revenue	\$ -	\$ 1,035,244	\$ 84,253	\$ 47,392	\$ -	\$ (9,837)	\$ 1,157,052
Other revenue	154,860	26,030	2,205	8,989	-	(165,255)	26,829
Net assets released from restrictions	-	540	-	-	-	-	540
Total revenues and other support without donor restrictions	154,860	1,061,814	86,458	56,381	-	(175,092)	1,184,421
Expenses:							
Salaries and wages	73,246	458,663	46,299	29,049	-	(73,302)	533,955
Employee benefits	20,795	132,545	12,949	3,700	-	(20,794)	149,195
Medical and professional fees	9,764	43,852	1,129	3,288	-	(6,451)	51,582
Purchased services	32,275	98,810	3,352	19,161	-	(42,588)	111,010
Supplies	859	202,725	10,661	2,566	-	(1,926)	214,885
Depreciation and amortization	7,489	43,866	1,345	1,829	-	(7,508)	47,021
Interest	3,154	11,220	974	932	-	(3,619)	12,661
Insurance	499	11,215	770	616	-	(499)	12,601
Other expenses	5,501	37,769	3,162	2,679	-	(17,744)	31,367
Total expenses	153,582	1,040,665	80,641	63,820	-	(174,431)	1,164,277
Income (loss) from operations	1,278	21,149	5,817	(7,439)	-	(661)	20,144
Nonoperating revenues and expenses:							
Investment income (loss)	1,188	(6,029)	(792)	3	-	(1,651)	(7,281)
Other components of net periodic pension cost	(2,928)	(12,181)	(527)	(43)	-	2,928	(12,751)
Other revenues and gains, net	462	629	19	41	-	(610)	541
Total nonoperating revenues and expenses	(1,278)	(17,581)	(1,300)	1	-	667	(19,491)
Excess (deficiency) of revenues over expenses	\$ -	\$ 3,568	\$ 4,517	\$ (7,438)	\$ -	\$ 6	\$ 653

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, 2018

	Parent	Acute Care Subsidiaries	Home and Community Based Subsidiaries	Other Subsidiaries	Discontinued Operations	Eliminations	Total
Net assets without donor restrictions:							
Excess (deficiency) of revenues over expenses	\$ -	\$ 3,568	\$ 4,517	\$ (7,438)	\$ -	\$ 6	\$ 653
Change in unrealized gain on interest rate swaps	-	594	-	234	-	-	828
Change in pension obligation, other than net periodic cost	5,520	16,583	128	(3)	-	-	22,228
Net assets released from restrictions used for capital	-	1,653	-	-	-	-	1,653
Amortization of terminated interest rate swaps	-	1,833	-	-	-	-	1,833
Capital grants	3,848	79	-	-	-	-	3,927
Contributions	94	-	-	-	-	-	94
Other	(3,735)	3,170	304	156	389	(382)	(98)
Increase (decrease) in net assets without donor restrictions before effects of discontinued operations	5,727	27,480	4,949	(7,051)	389	(376)	31,118
Gain from discontinued operations	-	-	-	-	322	-	322
Increase (decrease) in net assets without donor restrictions	5,727	27,480	4,949	(7,051)	711	(376)	31,440
Net assets with donor restrictions:							
Contributions	-	1,673	-	217	-	-	1,890
Investment income (loss)	-	(23)	-	-	-	-	(23)
Special events revenue, net	-	83	-	-	-	-	83
Change in interest in related Foundation	-	-	9	(441)	-	165	(267)
Net assets released from restrictions	-	(2,193)	-	-	-	-	(2,193)
Other	-	(88)	-	-	(129)	369	152
Increase (decrease) in net assets with donor restrictions	-	(548)	9	(224)	(129)	534	(358)
Increase (decrease) in net assets	5,727	26,932	4,958	(7,275)	582	158	31,082
Net assets (deficit), beginning of year	109,640	117,529	39,385	(2,131)	(4,016)	(27,447)	232,960
Net assets (deficit), end of year	\$ 115,367	\$ 144,461	\$ 44,343	\$ (9,406)	\$ (3,434)	\$ (27,289)	\$ 264,042

CATHOLIC HEALTH SYSTEM - ACUTE CARE SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2018

ASSETS	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Mount St. Mary's Hospital	Total
Current assets:					
Cash and cash equivalents	\$ 74,224	\$ 57,213	\$ 48,219	\$ 7,691	\$ 187,347
Patient/resident accounts receivable	44,897	31,311	18,050	9,087	103,345
Other receivables	2,358	3,433	1,994	725	8,510
Inventories	11,832	6,113	2,503	2,211	22,659
Prepaid expenses and other current assets	2,268	1,705	588	377	4,938
Due from affiliates	485	481	87	2	1,055
Total current assets	<u>136,064</u>	<u>100,256</u>	<u>71,441</u>	<u>20,093</u>	<u>327,854</u>
Assets limited as to use	968	19,553	2,420	-	22,941
Investments	32,874	100,240	25,000	5,773	163,887
Property and equipment, net	104,064	71,191	63,983	26,001	265,239
Other assets	45,762	35,923	14,160	1,664	97,509
Due from affiliates	-	10,303	1,456	-	11,759
Total assets	<u>\$ 319,732</u>	<u>\$ 337,466</u>	<u>\$ 178,460</u>	<u>\$ 53,531</u>	<u>\$ 889,189</u>
LIABILITIES AND NET ASSETS (DEFICIT)					
Current liabilities:					
Current portion of long-term obligations	\$ 5,127	\$ 4,446	\$ 4,004	\$ -	\$ 13,577
Accounts payable	18,715	16,113	9,741	3,345	47,914
Accrued expenses	12,985	29,799	5,962	4,981	53,727
Due to third-party payors	16,788	10,921	5,892	4,060	37,661
Due to affiliates	21,024	23,426	21,921	1,189	67,560
Total current liabilities	<u>74,639</u>	<u>84,705</u>	<u>47,520</u>	<u>13,575</u>	<u>220,439</u>
Long-term obligations, net	52,399	27,391	28,384	-	108,174
Other long-term obligations	213,541	134,398	53,403	14,773	416,115
Total liabilities	340,579	246,494	129,307	28,348	744,728
Net assets (deficit):					
Without donor restrictions	(22,351)	87,727	48,976	23,121	137,473
With donor restrictions	1,504	3,245	177	2,062	6,988
Total net assets (deficit)	<u>(20,847)</u>	<u>90,972</u>	<u>49,153</u>	<u>25,183</u>	<u>144,461</u>
Total liabilities and net assets (deficit)	<u>\$ 319,732</u>	<u>\$ 337,466</u>	<u>\$ 178,460</u>	<u>\$ 53,531</u>	<u>\$ 889,189</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, 2018

	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Mount St. Mary's Hospital	Total
Revenues and other support without donor restrictions:					
Net patient/resident service revenue	\$ 437,489	\$ 321,413	\$ 181,936	\$ 94,406	\$ 1,035,244
Other revenue	6,212	12,362	1,940	5,516	26,030
Net assets released from restrictions	144	233	6	157	540
Total revenues and other support without donor restrictions	<u>443,845</u>	<u>334,008</u>	<u>183,882</u>	<u>100,079</u>	<u>1,061,814</u>
Expenses:					
Salaries and wages	181,046	152,467	74,335	50,815	458,663
Employee benefits	53,506	43,582	20,334	15,123	132,545
Medical and professional fees	18,840	15,647	4,989	4,376	43,852
Purchased services	38,756	33,676	15,163	11,215	98,810
Supplies	92,878	58,182	40,154	11,511	202,725
Depreciation and amortization	16,707	14,021	9,149	3,989	43,866
Interest	4,719	3,912	2,570	19	11,220
Insurance	4,841	3,583	1,805	986	11,215
Other expenses	17,015	11,371	5,637	3,746	37,769
Total expenses	<u>428,308</u>	<u>336,441</u>	<u>174,136</u>	<u>101,780</u>	<u>1,040,665</u>
Income (loss) from operations	15,537	(2,433)	9,746	(1,701)	21,149
Nonoperating revenues and expenses:					
Investment income (loss)	(478)	(4,631)	(779)	(141)	(6,029)
Other components of net periodic pension costs	(7,117)	(3,156)	(1,659)	(249)	(12,181)
Other revenues and gains, net	170	321	86	52	629
Total nonoperating revenues and expenses	<u>(7,425)</u>	<u>(7,466)</u>	<u>(2,352)</u>	<u>(338)</u>	<u>(17,581)</u>
Excess (deficiency) of revenues over expenses	<u>\$ 8,112</u>	<u>\$ (9,899)</u>	<u>\$ 7,394</u>	<u>\$ (2,039)</u>	<u>\$ 3,568</u>

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, 2018

	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Mount St. Mary's Hospital	Total
Net assets without donor restrictions:					
Excess (deficiency) of revenues over expenses	\$ 8,112	\$ (9,899)	\$ 7,394	\$ (2,039)	\$ 3,568
Change in unrealized gain on interest rate swaps	594	-	-	-	594
Change in pension obligation, other than net periodic cost	10,326	5,183	1,612	(538)	16,583
Net assets released from restrictions used for capital	204	1,066	34	349	1,653
Amortization of terminated interest rate swaps	395	1,132	306	-	1,833
Capital grants	35	44	-	-	79
Other	779	1,301	610	480	3,170
Increase (decrease) in net assets without donor restrictions	20,445	(1,173)	9,956	(1,748)	27,480
Net assets with donor restrictions:					
Contributions	838	522	133	180	1,673
Investment income (loss)	(22)	2	-	(3)	(23)
Special events revenue, net	29	-	25	29	83
Net assets released from restrictions	(348)	(1,299)	(40)	(506)	(2,193)
Other	-	2	(90)	-	(88)
Increase (decrease) in net assets with donor restrictions	497	(773)	28	(300)	(548)
Increase (decrease) in net assets	20,942	(1,946)	9,984	(2,048)	26,932
Net assets (deficit), beginning of year	(41,789)	92,918	39,169	27,231	117,529
Net assets (deficit), end of year	\$ (20,847)	\$ 90,972	\$ 49,153	\$ 25,183	\$ 144,461

CATHOLIC HEALTH SYSTEM - HOME AND COMMUNITY BASED SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2018

ASSETS	Father Baker Manor	St. Francis Geriatric	Mercy Home Care	McAuley Seton Home Care	Infusion Pharmacy	Total
Current assets:						
Cash and cash equivalents	\$ 422	\$ 473	\$ 1,665	\$ 16,724	\$ 2,670	\$ 21,954
Patient/resident accounts receivable	3,102	-	225	8,201	1,395	12,923
Other receivables	14	8	104	72	5	203
Inventories	32	-	-	53	881	966
Prepaid expenses and other current assets	19	5	2	32	797	855
Due from affiliates	20	7	-	42	94	163
Total current assets	<u>3,609</u>	<u>493</u>	<u>1,996</u>	<u>25,124</u>	<u>5,842</u>	<u>37,064</u>
Interest in net assets of related Foundations	114	-	-	-	-	114
Assets limited as to use	10,828	-	-	-	-	10,828
Investments	-	-	-	21,126	-	21,126
Property and equipment, net	4,383	10,645	-	235	266	15,529
Other assets	4,306	507	693	3,650	513	9,669
Due from affiliates	-	-	1,058	-	-	1,058
Total assets	<u>\$ 23,240</u>	<u>\$ 11,645</u>	<u>\$ 3,747</u>	<u>\$ 50,135</u>	<u>\$ 6,621</u>	<u>\$ 95,388</u>
LIABILITIES AND NET ASSETS (DEFICIT)						
Current liabilities:						
Current portion of long-term obligations	\$ 562	\$ 337	\$ -	\$ -	\$ -	\$ 899
Accounts payable	244	10	1	146	213	614
Accrued expenses	1,312	41	454	2,309	571	4,687
Due to third-party payors	257	-	17	1,031	71	1,376
Due to affiliates	9,623	48	3	94	35	9,803
Total current liabilities	<u>11,998</u>	<u>436</u>	<u>475</u>	<u>3,580</u>	<u>890</u>	<u>17,379</u>
Long-term obligations, net	3,278	9,070	-	-	-	12,348
Other long-term obligations	7,984	522	2,421	9,796	595	21,318
Total liabilities	<u>23,260</u>	<u>10,028</u>	<u>2,896</u>	<u>13,376</u>	<u>1,485</u>	<u>51,045</u>
Net assets (deficit):						
Without donor restrictions	(134)	1,617	851	36,759	5,136	44,229
With donor restrictions	114	-	-	-	-	114
Total net assets (deficit)	<u>(20)</u>	<u>1,617</u>	<u>851</u>	<u>36,759</u>	<u>5,136</u>	<u>44,343</u>
Total liabilities and net assets (deficit)	<u>\$ 23,240</u>	<u>\$ 11,645</u>	<u>\$ 3,747</u>	<u>\$ 50,135</u>	<u>\$ 6,621</u>	<u>\$ 95,388</u>

CATHOLIC HEALTH SYSTEM - HOME AND COMMUNITY BASED SUBSIDIARIES

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

(in thousands of dollars)

For the Year Ended December 31, 2018

	Father Baker Manor	St. Francis Geriatric	Mercy Home Care	McAuley Seton Home Care	Infusion Pharmacy	Total
Revenues and other support without donor restrictions:						
Net patient/resident service revenue	\$ 18,502	\$ -	\$ 6,513	\$ 46,349	\$ 12,889	\$ 84,253
Other revenue	81	1,541	166	219	198	2,205
Total revenues and other support without donor restrictions	<u>18,583</u>	<u>1,541</u>	<u>6,679</u>	<u>46,568</u>	<u>13,087</u>	<u>86,458</u>
Expenses:						
Salaries and wages	11,672	317	4,587	26,926	2,797	46,299
Employee benefits	3,102	79	1,249	7,821	698	12,949
Medical and professional fees	165	-	28	913	23	1,129
Purchased services	1,096	454	353	1,223	226	3,352
Supplies	1,283	76	7	1,186	8,109	10,661
Depreciation and amortization	533	310	16	413	73	1,345
Interest	306	355	26	282	5	974
Insurance	561	42	43	93	31	770
Other expenses	837	13	221	1,576	515	3,162
Total expenses	<u>19,555</u>	<u>1,646</u>	<u>6,530</u>	<u>40,433</u>	<u>12,477</u>	<u>80,641</u>
Income (loss) from operations	(972)	(105)	149	6,135	610	5,817
Nonoperating revenues and expenses:						
Investment income (loss)	97	3	35	(930)	3	(792)
Other components of net periodic pension cost	(151)	-	(49)	(302)	(25)	(527)
Other revenues and gains, net	8	-	-	10	1	19
Total nonoperating revenues and expenses	<u>(46)</u>	<u>3</u>	<u>(14)</u>	<u>(1,222)</u>	<u>(21)</u>	<u>(1,300)</u>
Excess (deficiency) of revenue over expenses	<u>\$ (1,018)</u>	<u>\$ (102)</u>	<u>\$ 135</u>	<u>\$ 4,913</u>	<u>\$ 589</u>	<u>\$ 4,517</u>
Net assets without donor restrictions:						
Excess (deficiency) of revenue over expenses	\$ (1,018)	\$ (102)	\$ 135	\$ 4,913	\$ 589	\$ 4,517
Change in pension obligation, other than net periodic cost	9	-	7	127	(15)	128
Other	58	246	-	-	-	304
Increase (decrease) in net assets without donor restrictions	<u>(951)</u>	<u>144</u>	<u>142</u>	<u>5,040</u>	<u>574</u>	<u>4,949</u>
Net assets with donor restrictions:						
Change in interest in related Foundations	9	-	-	-	-	9
Increase (decrease) in net assets with donor restrictions	<u>9</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>9</u>
Increase (decrease) in net assets	<u>(942)</u>	<u>144</u>	<u>142</u>	<u>5,040</u>	<u>574</u>	<u>4,958</u>
Net asset (deficit), beginning of year	<u>922</u>	<u>1,473</u>	<u>709</u>	<u>31,719</u>	<u>4,562</u>	<u>39,385</u>
Net assets (deficit), end of year	<u>\$ (20)</u>	<u>\$ 1,617</u>	<u>\$ 851</u>	<u>\$ 36,759</u>	<u>\$ 5,136</u>	<u>\$ 44,343</u>

CATHOLIC HEALTH SYSTEM - OTHER SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2018

ASSETS	OLV Renaissance	Continuing Care Foundation	LIFE	Trinity	Niagara Medicine	Total
Current assets:						
Cash and cash equivalents	\$ 1,522	\$ 466	\$ 14,677	\$ 665	\$ 143	\$ 17,473
Patient accounts receivable	-	-	1,401	1,709	63	3,173
Other receivables	53	11	386	143	-	593
Prepaid expenses and other current assets	13	-	15	298	-	326
Due from affiliates	57	10	100	991	-	1,158
Total current assets	<u>1,645</u>	<u>487</u>	<u>16,579</u>	<u>3,806</u>	<u>206</u>	<u>22,723</u>
Interest in net assets of related Foundations	18	-	-	-	-	18
Assets limited as to use	322	-	978	-	-	1,300
Property and equipment, net	12,677	-	2,531	693	-	15,901
Other assets	300	-	16	-	597	913
Total assets	<u>\$ 14,962</u>	<u>\$ 487</u>	<u>\$ 20,104</u>	<u>\$ 4,499</u>	<u>\$ 803</u>	<u>\$ 40,855</u>
LIABILITIES AND NET ASSETS (DEFICIT)						
Current liabilities:						
Current portion of long-term obligations	\$ 425	\$ -	\$ -	\$ 113	\$ -	\$ 538
Accounts payable	183	-	3,174	557	3	3,917
Accrued expenses	349	-	1,041	2,820	-	4,210
Due to third-party payors	300	-	3,429	-	-	3,729
Due to affiliates	4,180	100	613	21,510	1,336	27,739
Total current liabilities	<u>5,437</u>	<u>100</u>	<u>8,257</u>	<u>25,000</u>	<u>1,339</u>	<u>40,133</u>
Long-term obligations, net	8,057	-	-	17	-	8,074
Other long-term obligations	1,216	-	788	-	50	2,054
Total liabilities	14,710	100	9,045	25,017	1,389	50,261
Net assets (deficit):						
Without donor restrictions	234	17	10,959	(20,518)	(586)	(9,894)
With donor restrictions	18	370	100	-	-	488
Total net assets (deficit)	<u>252</u>	<u>387</u>	<u>11,059</u>	<u>(20,518)</u>	<u>(586)</u>	<u>(9,406)</u>
Total liabilities and net assets (deficit)	<u>\$ 14,962</u>	<u>\$ 487</u>	<u>\$ 20,104</u>	<u>\$ 4,499</u>	<u>\$ 803</u>	<u>\$ 40,855</u>

CATHOLIC HEALTH SYSTEM - OTHER SUBSIDIARIES

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

(in thousands of dollars)

For the Year Ended December 31, 2018

	OLV Renaissance	Continuing Care Foundation	LIFE	Trinity	Niagara Medicine	Total
Revenues and other support without donor restrictions:						
Net patient service revenue	\$ -	\$ -	\$ 22,805	\$ 24,240	\$ 347	\$ 47,392
Other revenue	5,166	13	18	4,112	(320)	8,989
Total revenues and other support without donor restrictions	<u>5,166</u>	<u>13</u>	<u>22,823</u>	<u>28,352</u>	<u>27</u>	<u>56,381</u>
Expenses:						
Salaries and wages	293	-	2,276	26,480	-	29,049
Employee benefits	99	-	668	2,933	-	3,700
Medical and professional fees	22	-	56	2,830	380	3,288
Purchased services	1,714	9	16,057	1,354	27	19,161
Supplies	83	-	594	1,889	-	2,566
Depreciation and amortization	1,390	-	79	360	-	1,829
Interest	461	-	-	468	3	932
Insurance	54	-	9	553	-	616
Other expenses	67	1	500	2,111	-	2,679
Total expenses	<u>4,183</u>	<u>10</u>	<u>20,239</u>	<u>38,978</u>	<u>410</u>	<u>63,820</u>
Income (loss) from operations	983	3	2,584	(10,626)	(383)	(7,439)
Nonoperating revenues and expenses:						
Investment income (loss)	-	2	1	-	-	3
Other components of net periodic pension cost	-	-	(43)	-	-	(43)
Other revenues and gains, net	39	-	5	(3)	-	41
Total nonoperating revenues and expenses	<u>39</u>	<u>2</u>	<u>(37)</u>	<u>(3)</u>	<u>-</u>	<u>1</u>
Excess (deficiency) of revenues over expenses	<u>\$ 1,022</u>	<u>\$ 5</u>	<u>\$ 2,547</u>	<u>\$ (10,629)</u>	<u>\$ (383)</u>	<u>\$ (7,438)</u>

CATHOLIC HEALTH SYSTEM - OTHER SUBSIDIARIES

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

(in thousands of dollars)

For the Year Ended December 31, 2018

	<u>OLV Renaissance</u>	<u>Continuing Care Foundation</u>	<u>LIFE</u>	<u>Trinity</u>	<u>Niagara Medicine</u>	<u>Total</u>
Net assets without donor restrictions:						
Excess (deficiency) of revenues over expenses	\$ 1,022	\$ 5	\$ 2,547	\$ (10,629)	\$ (383)	\$ (7,438)
Change in unrealized gain on interest rate swaps	234	-	-	-	-	234
Change in pension obligation, other than net periodic cost	-	-	(3)	-	-	(3)
Other	158	-	(2)	-	-	156
Increase (decrease) in net assets without donor restrictions	<u>1,414</u>	<u>5</u>	<u>2,542</u>	<u>(10,629)</u>	<u>(383)</u>	<u>(7,051)</u>
Net assets with donor restrictions:						
Contributions	-	117	100	-	-	217
Change in interest in related Foundations	(164)	(277)	-	-	-	(441)
Increase (decrease) in net assets with donor restrictions	<u>(164)</u>	<u>(160)</u>	<u>100</u>	<u>-</u>	<u>-</u>	<u>(224)</u>
Increase (decrease) in net assets	<u>1,250</u>	<u>(155)</u>	<u>2,642</u>	<u>(10,629)</u>	<u>(383)</u>	<u>(7,275)</u>
Net assets (deficit), beginning of year	<u>(998)</u>	<u>542</u>	<u>8,417</u>	<u>(9,889)</u>	<u>(203)</u>	<u>(2,131)</u>
Net assets (deficit), end of year	<u>\$ 252</u>	<u>\$ 387</u>	<u>\$ 11,059</u>	<u>\$ (20,518)</u>	<u>\$ (586)</u>	<u>\$ (9,406)</u>

CATHOLIC HEALTH SYSTEM - DISCONTINUED OPERATIONS

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2018

ASSETS	Discontinued Operations				Total
	St. Francis Home	St. Elizabeth's Home	St. Vincent's Home	Nazareth Home	
Current assets:					
Cash and cash equivalents	\$ 2,565	\$ 658	\$ 426	\$ 1,378	\$ 5,027
Prepaid expenses and other current assets	3	-	-	-	3
Due from affiliates	2	-	-	1,573	1,575
Total current assets	<u>2,570</u>	<u>658</u>	<u>426</u>	<u>2,951</u>	<u>6,605</u>
Interest in net assets of related Foundations	68	60	1	-	129
Assets limited as to use	1,091	-	-	-	1,091
Other assets	3,289	24	21	-	3,334
Due from affiliates	-	368	-	-	368
Total assets	<u>\$ 7,018</u>	<u>\$ 1,110</u>	<u>\$ 448</u>	<u>\$ 2,951</u>	<u>\$ 11,527</u>
LIABILITIES AND NET ASSETS (DEFICIT)					
Current liabilities:					
Accrued expenses	\$ 232	\$ 33	\$ 2	\$ -	\$ 267
Due to third-party payors	434	3	-	-	437
Due to affiliates	7,427	1,342	1,475	-	10,244
Total current liabilities	<u>8,093</u>	<u>1,378</u>	<u>1,477</u>	<u>-</u>	<u>10,948</u>
Other long-term obligations	3,803	155	55	-	4,013
Total liabilities	<u>11,896</u>	<u>1,533</u>	<u>1,532</u>	<u>-</u>	<u>14,961</u>
Net assets (deficit):					
Without donor restrictions	(4,878)	(423)	(1,084)	2,951	(3,434)
Total net assets (deficit)	<u>(4,878)</u>	<u>(423)</u>	<u>(1,084)</u>	<u>2,951</u>	<u>(3,434)</u>
Total liabilities and net assets (deficit)	<u>\$ 7,018</u>	<u>\$ 1,110</u>	<u>\$ 448</u>	<u>\$ 2,951</u>	<u>\$ 11,527</u>

CATHOLIC HEALTH SYSTEM - DISCONTINUED OPERATIONS

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

(in thousands of dollars)

For the Year Ended December 31, 2018

	●————— Discontinued Operations —————●				
	St. Francis Home	St. Elizabeth's Home	St. Vincent's Home	Nazareth Home	Total
Net assets without donor restrictions:					
Other	\$ 68	\$ 60	\$ 1	\$ 260	\$ 389
Increase (decrease) in net assets without donor restrictions before effects of discontinued operations	68	60	1	260	389
Gain from discontinued operations	194	98	30	-	322
Increase (decrease) in net assets without donor restrictions	<u>262</u>	<u>158</u>	<u>31</u>	<u>260</u>	<u>711</u>
Net assets with donor restrictions:					
Other	(68)	(60)	(1)	-	(129)
Increase (decrease) in net assets with donor restrictions	<u>(68)</u>	<u>(60)</u>	<u>(1)</u>	<u>-</u>	<u>(129)</u>
Increase (decrease) in net assets	<u>194</u>	<u>98</u>	<u>30</u>	<u>260</u>	<u>582</u>
Net assets (deficit), beginning of year	<u>(5,072)</u>	<u>(521)</u>	<u>(1,114)</u>	<u>2,691</u>	<u>(4,016)</u>
Net assets (deficit), end of year	<u><u>\$ (4,878)</u></u>	<u><u>\$ (423)</u></u>	<u><u>\$ (1,084)</u></u>	<u><u>\$ 2,951</u></u>	<u><u>\$ (3,434)</u></u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

(KENMORE MERCY HOSPITAL AND SUBSIDIARIES)

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2018

ASSETS	Kenmore Mercy Hospital	The McAuley Residence	The Kenmore Mercy Foundation	Eliminations	Consolidated
Current assets:					
Cash and cash equivalents	\$ 43,071	\$ 5,068	\$ 80	\$ -	\$ 48,219
Patient/resident accounts receivable	14,617	3,433	-	-	18,050
Other receivables	471	1,358	165	-	1,994
Inventories	2,503	-	-	-	2,503
Prepaid expenses and other current assets	489	99	-	-	588
Due from affiliates	50	42	28	(33)	87
Total current assets	<u>61,201</u>	<u>10,000</u>	<u>273</u>	<u>(33)</u>	<u>71,441</u>
Interest in net assets of affiliated Foundation	3,227	-	-	(3,227)	-
Assets limited as to use	1,221	1,199	-	-	2,420
Investments	22,008	-	2,992	-	25,000
Property and equipment, net	55,198	8,783	2	-	63,983
Other assets	11,394	4,363	-	(1,597)	14,160
Due from affiliates	1,456	-	-	-	1,456
Total assets	<u>\$ 155,705</u>	<u>\$ 24,345</u>	<u>\$ 3,267</u>	<u>\$ (4,857)</u>	<u>\$ 178,460</u>
LIABILITIES AND NET ASSETS (DEFICIT)					
Current liabilities:					
Current portion of long-term obligations	\$ 3,363	\$ 641	\$ -	\$ -	\$ 4,004
Accounts payable	9,357	362	22	-	9,741
Accrued expenses	4,202	1,760	-	-	5,962
Due to third-party payors	5,268	624	-	-	5,892
Due to affiliates	8,193	13,743	18	(33)	21,921
Total current liabilities	<u>30,383</u>	<u>17,130</u>	<u>40</u>	<u>(33)</u>	<u>47,520</u>
Long-term obligations, net	25,832	2,552	-	-	28,384
Other long-term obligations	43,479	9,924	-	-	53,403
Total liabilities	<u>99,694</u>	<u>29,606</u>	<u>40</u>	<u>(33)</u>	<u>129,307</u>
Net assets (deficit):					
Without donor restrictions	55,834	(5,261)	3,050	(4,647)	48,976
With donor restrictions	177	-	177	(177)	177
Total net assets (deficit)	<u>56,011</u>	<u>(5,261)</u>	<u>3,227</u>	<u>(4,824)</u>	<u>49,153</u>
Total liabilities and net assets (deficit)	<u>\$ 155,705</u>	<u>\$ 24,345</u>	<u>\$ 3,267</u>	<u>\$ (4,857)</u>	<u>\$ 178,460</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

(KENMORE MERCY HOSPITAL AND SUBSIDIARIES)
 CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (DEFICIT)
 (in thousands of dollars)
 For the Year Ended December 31, 2018

	Kenmore Mercy Hospital	The McAuley Residence	The Kenmore Mercy Foundation	Eliminations	Consolidated
Revenue and other support without donor restrictions:					
Net patient/resident service revenue	\$ 160,957	\$ 20,979	\$ -	\$ -	\$ 181,936
Other revenue	1,410	114	416	-	1,940
Net assets released from restriction	-	-	6	-	6
Total revenue and other support without donor restrictions	<u>162,367</u>	<u>21,093</u>	<u>422</u>	<u>-</u>	<u>183,882</u>
Expenses:					
Salaries and wages	61,897	12,238	200	-	74,335
Employee benefits	16,911	3,365	58	-	20,334
Medical and professional fees	4,754	225	10	-	4,989
Purchased services	13,691	1,387	85	-	15,163
Supplies	38,711	1,440	3	-	40,154
Depreciation and amortization	8,408	740	1	-	9,149
Interest	2,388	182	-	-	2,570
Insurance	1,568	237	-	-	1,805
Other expenses	4,482	1,036	380	(261)	5,637
Total expenses	<u>152,810</u>	<u>20,850</u>	<u>737</u>	<u>(261)</u>	<u>174,136</u>
Income (loss) from operations	9,557	243	(315)	261	9,746
Nonoperating revenues and expenses:					
Investment income (loss)	(619)	30	(190)	-	(779)
Other components of net periodic pension cost	(1,445)	(214)	-	-	(1,659)
Other revenues and gains, net	65	21	-	-	86
Total nonoperating revenues and expenses	<u>(1,999)</u>	<u>(163)</u>	<u>(190)</u>	<u>-</u>	<u>(2,352)</u>
Excess (deficiency) of revenues over expenses	<u>\$ 7,558</u>	<u>\$ 80</u>	<u>\$ (505)</u>	<u>\$ 261</u>	<u>\$ 7,394</u>

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, 2018

	<u>Kenmore Mercy Hospital</u>	<u>The McAuley Residence</u>	<u>The Kenmore Mercy Foundation</u>	<u>Eliminations</u>	<u>Consolidated</u>
Net assets without donor restrictions:					
Excess (deficiency) of revenues over expenses	\$ 7,558	\$ 80	\$ (505)	\$ 261	\$ 7,394
Change in interest in affiliated Foundation	(473)	-	-	473	-
Change in pension obligation, other than net periodic cost	1,306	306	-	-	1,612
Net assets released from restrictions used for capital	-	3	31	-	34
Amortization of terminated interest rate swaps	306	-	-	-	306
Contributions	261	-	-	(261)	-
Other	563	47	-	-	610
Increase (decrease) in net assets without donor restrictions	<u>9,521</u>	<u>436</u>	<u>(474)</u>	<u>473</u>	<u>9,956</u>
Net assets with donor restrictions:					
Contributions	-	-	133	-	133
Special events revenue, net	-	-	25	-	25
Net assets released from restrictions	-	(3)	(37)	-	(40)
Change in interest in the KMH Foundation, Inc.	121	-	-	(121)	-
Other	-	(90)	-	-	(90)
Increase (decrease) in net assets with donor restrictions	<u>121</u>	<u>(93)</u>	<u>121</u>	<u>(121)</u>	<u>28</u>
Increase (decrease) in net assets	<u>9,642</u>	<u>343</u>	<u>(353)</u>	<u>352</u>	<u>9,984</u>
Net assets (deficit), beginning of year	<u>46,369</u>	<u>(5,604)</u>	<u>3,580</u>	<u>(5,176)</u>	<u>39,169</u>
Net assets (deficit), end of year	<u>\$ 56,011</u>	<u>\$ (5,261)</u>	<u>\$ 3,227</u>	<u>\$ (4,824)</u>	<u>\$ 49,153</u>