

**CONSOLIDATED FINANCIAL STATEMENTS**

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

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**DECEMBER 31, 2014**

# CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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## **INDEPENDENT AUDITOR'S REPORT**

To the Board of Directors of the  
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 (together the System), which comprise the consolidated balance sheets as of December 31, 2014 and 2013, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended and the related notes to the consolidated financial statements.

### **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 opinions on the 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 our 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, we consider 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 reasonable basis for our audit opinions.

## Opinions

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, 2014 and 2013, 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 26, 2015

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

**CONSOLIDATED BALANCE SHEETS**

(in thousands of dollars)

December 31,

<b>ASSETS</b>	<b>2014</b>	<b>2013</b>
<b>Current assets:</b>		
Cash and cash equivalents	\$ 322,451	\$ 278,806
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$25,207 (2013 - \$26,379)	131,713	122,754
Other receivables	9,481	13,089
Inventories	22,548	20,129
Assets limited as to use	-	836
Prepaid expenses and other current assets	5,961	6,118
<b>Total current assets</b>	<b>492,154</b>	<b>441,732</b>
Interest in net assets of affiliated Foundation	2,852	4,616
Assets limited as to use	26,106	30,268
Investments	9,519	8,953
Property and equipment, net	336,679	271,620
Other assets	89,440	85,169
<b>Total assets</b>	<b>\$ 956,750</b>	<b>\$ 842,358</b>
<b>LIABILITIES AND NET ASSETS</b>		
<b>Current liabilities:</b>		
Current portion of long-term obligations	\$ 19,850	\$ 15,399
Line of credit payable	8,380	10,831
Accounts payable	44,891	45,638
Accrued expenses	59,736	64,852
Due to third-party payors	38,411	38,473
<b>Total current liabilities</b>	<b>171,268</b>	<b>175,193</b>
Long-term obligations, net	183,986	128,671
Other long-term obligations, net	455,276	346,097
<b>Total liabilities</b>	<b>810,530</b>	<b>649,961</b>
<b>Net assets:</b>		
Unrestricted	139,480	183,556
Temporarily restricted	6,494	8,595
Permanently restricted	246	246
<b>Total net assets</b>	<b>146,220</b>	<b>192,397</b>
<b>Total liabilities and net assets</b>	<b>\$ 956,750</b>	<b>\$ 842,358</b>

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>2014</u>	<u>2013</u>
<b>Unrestricted revenues and other support:</b>		
Net patient/resident service revenue	\$ 961,989	\$ 922,793
Provision for bad debts	<u>(21,292)</u>	<u>(20,712)</u>
Net patient/resident service revenue, less provision for bad debts	940,697	902,081
Other revenue	12,589	19,821
Net assets released from restrictions	<u>277</u>	<u>321</u>
<b>Total unrestricted revenues and other support</b>	<u>953,563</u>	<u>922,223</u>
<b>Expenses:</b>		
Salaries and wages	408,854	398,633
Employee benefits	124,052	131,141
Medical and professional fees	40,785	40,468
Purchased services	70,689	67,706
Supplies	178,105	170,557
Depreciation and amortization	41,141	36,743
Interest	8,379	6,937
Insurance	10,523	8,321
Other expenses	30,253	29,813
<b>Total expenses</b>	<u>912,781</u>	<u>890,319</u>
<b>Income from operations</b>	40,782	31,904
<b>Nonoperating revenues and losses:</b>		
Investment income	1,341	2,343
Other, net	<u>665</u>	<u>1,340</u>
<b>Total nonoperating revenues and losses</b>	<u>2,006</u>	<u>3,683</u>
<b>Excess of revenues over expenses</b>	<u><u>\$ 42,788</u></u>	<u><u>\$ 35,587</u></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>2014</u>	<u>2013</u>
<b>Unrestricted net assets:</b>		
Excess of revenues over expenses	\$ 42,788	\$ 35,587
Change in unrealized gain (loss) on interest rate swap	(2,807)	7,067
Change in pension obligation, other than net periodic cost	(90,373)	107,542
Net assets released from restrictions used for capital	1,197	1,236
Grant revenue for capital expenditures	168	390
Contributions	4,468	-
Other	2,455	147
(Decrease) increase in unrestricted net assets before effects of discontinued operations	(42,104)	151,969
Loss from discontinued operations	(1,972)	(1,302)
(Decrease) increase unrestricted net assets	(44,076)	150,667
<b>Temporarily restricted net assets:</b>		
Contributions and other	1,124	1,233
Investment income	3	19
Special events revenue, net	33	87
Change in temporarily restricted interest in related Foundation	(1,764)	701
Temporarily restricted net assets released from restrictions	(1,474)	(1,557)
Other	(23)	24
(Decrease) increase in temporarily restricted net assets	(2,101)	507
(Decrease) increase in net assets	(46,177)	151,174
Net assets, beginning of year	192,397	41,223
Net assets, end of year	<u>\$ 146,220</u>	<u>\$ 192,397</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,

	<b>2014</b>	<b>2013</b>
<b>Cash flows from operating activities:</b>		
(Decrease) increase in net assets	\$ (46,177)	\$ 151,174
Change in net assets from discontinued operations	1,972	1,302
Adjustments to reconcile (decrease) increase in net assets to net cash provided by operating activities		
Depreciation and amortization	41,141	36,743
Provision for bad debts	21,292	20,712
Change in undistributed net assets of related Foundation	1,764	(701)
Change in pension obligation, other than net periodic cost	90,373	(107,542)
Grant revenue for capital additions	(168)	(390)
Change in unrealized gain (loss) on interest rate swap	2,494	(7,176)
Realized loss on interest rate swap termination	534	-
Change in unrealized gain (loss) on investments	299	(621)
Undistributed earnings in equity investees	(427)	(7)
Other	(390)	(130)
(Increase) decrease in assets		
Patient accounts receivables	(30,699)	(21,463)
Other receivables	3,608	(5,175)
Inventories	(2,419)	(5,652)
Prepaid expenses and other current assets	157	(1,395)
Other assets	1,564	(1,063)
Increase (decrease) in liabilities:		
Accounts payable	453	(408)
Accrued expenses	(5,116)	2,243
Due to third-party payors	(62)	(2,500)
Other liabilities	15,294	21,837
Net cash used in operating activities of discontinued operations	(1,162)	(372)
<b>Net cash and cash equivalents provided by operating activities</b>	<b>94,325</b>	<b>79,416</b>
<b>Cash flows from investing activities:</b>		
Purchase of property and equipment	(48,267)	(42,522)
Proceeds from sale of property and equipment	43	-
Purchase of assets limited as to use	(207)	(2,772)
Proceeds from sale of assets limited as to use	5,159	12,654
Change in investments, net	(338)	(134)
<b>Net cash and cash equivalents used in investing activities</b>	<b>(43,610)</b>	<b>(32,774)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from issuance of long-term obligations	16,997	3,718
Proceeds of grant revenue for capital additions	168	390
Termination of interest rate swaps	(5,772)	-
Repayments of current and long-term obligations	(18,463)	(14,134)
<b>Net cash and cash equivalents used in financing activities</b>	<b>(7,070)</b>	<b>(10,026)</b>
<b>Increase in cash and cash equivalents</b>	<b>43,645</b>	<b>36,616</b>
Cash and cash equivalents - beginning of year	278,806	242,190
Cash and cash equivalents - end of year	<u>\$ 322,451</u>	<u>\$ 278,806</u>

See accompanying notes.



## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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#### 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, Ascension Health Ministries and Catholic Health Ministries. Ascension Health, Trinity Health, and the Diocese of Buffalo, New York are the corporate members of CHS, with equal ownership interest. CHS is 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) and Sisters of Charity Hospital of Buffalo, New York (SCH).

**Long-Term Care Subsidiaries:** The Long-term Care Subsidiaries include St. Francis Geriatric and Healthcare Services, Inc. (closed December 2009), St. Francis Home of Williamsville (SFHW), Western New York Catholic Long-Term Care, Inc. (Father Baker Manor), Nazareth Home of the Franciscan Sisters of the Immaculate Conception (closed 2007) and St. Elizabeth's Home (SEH) and St. Vincent's Home for the Aged (SVH).

**Home Care Subsidiaries and Other Subsidiaries:** The Home Care and Other Subsidiaries include Mercy Home Care of Western New York, Inc. (MHC), McAuley Seton Home Care (MSHC), Our Lady of Victory Renaissance Corporation (OLV Renaissance), Catholic Health Infusion Pharmacy, Continuing Care Foundation, Catholic Health System Program of All Inclusive Care for the Elderly, Inc. (LIFE) and Trinity Medical WNY, PC.

#### 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.

As further described in Note 16, the System has entered into purchase agreements for the sale of certain assets of SFHW, SEH and SVH. As a result, at December 31, 2014 and 2013, certain assets and liabilities of SFHW, SEH, and SVH met the criteria for classifying those assets and liabilities as held for sale and accordingly, the operating results of these subsidiaries have been classified as discontinued within the statement of operations and changes in net assets.

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

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

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

**NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**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 (certificates of deposit), excluding amounts limited as to use, to be cash equivalents. The System maintains funds on deposit in excess of amounts insured by the Federal Depository Insurance limits.

	<u>2014</u>	<u>2013</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for interest	\$ 8,026	\$ 6,838
Non-cash investing and financing transactions:		
Assets acquired under capital lease obligations	\$ 57,537	\$ 3,198
Construction related payables	\$ -	\$ 836
Other non-cash transactions	\$ 1,200	\$ 1,591

**Other Receivables and Other Assets:** Other receivables consist primarily of managed care risk sharing receivables, physician loans, and other receivables. There is no allowance for doubtful accounts established against these receivables. Other non-current assets consist of deferred financing costs, insurance recoveries, investments in healthcare ventures, and other miscellaneous deferred charges. Amortization of the financing costs is provided on the effective interest method over the maturity of the bond issues.

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

<b>Current other receivables:</b>	<u>2014</u>	<u>2013</u>
Physician loans	\$ 3,388	\$ 4,088
Managed care risk receivable	1,007	4,612
Other	<u>5,086</u>	<u>4,389</u>
Other receivables	<u>\$ 9,481</u>	<u>\$ 13,089</u>
<b>Non-current other assets:</b>		
Insurance recoveries	\$ 80,647	\$ 74,877
Deferred financing costs, net	4,214	4,572
Investments in healthcare ventures	801	373
Other	<u>3,778</u>	<u>5,347</u>
Other assets	<u>\$ 89,440</u>	<u>\$ 85,169</u>

Amortization expense on debt issuance costs amounted to \$358 and \$360 for years ended December 31, 2014 and 2013, respectively. Accumulated amortization related to the debt issuance costs amounted to \$3,319 and \$2,961 at December 31, 2014 and 2013, respectively. Amortization expense is expected to be within approximately \$300 and \$400 for the years ended December 31, 2015 to 2019.

## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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#### NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

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

Investment income and gains restricted by a donor are reported as increases in unrestricted net assets if the restrictions are met (either by passage of time or by use) in the reporting period in which the income and gains are recognized. Investment income or loss (including realized gains or losses on investments, interest, and dividends) is included in the excess of revenues over expenses, unless their use is restricted by donor stipulations or law. Unrealized gains and losses on investments are included in the operating measure 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 period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the consolidated financial statements.

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

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

The System evaluates the recoverability of long-lived assets not held for sale by measuring the carrying amount of the assets against the estimated undiscounted future cash flows associated with them. If such evaluations indicate that the future undiscounted cash flows of certain long-lived assets are not sufficient to recover the carrying value of such assets, the assets are adjusted to their fair values. Based on these evaluations, there are no adjustments to the carrying value of long-lived assets in 2014 and 2013.

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

**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, 2014 and 2013 was \$484 and \$460, respectively.

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

	<u>2014</u>	<u>2013</u>
Insurance liabilities	\$ 123,329	\$ 111,297
Long-term pension obligations	314,971	215,715
Asset retirement obligations	10,064	9,556
Interest rate swap	5,853	8,596
Other	<u>1,059</u>	<u>933</u>
Other long-term liabilities	<u>\$ 455,276</u>	<u>\$ 346,097</u>

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

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

## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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#### NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

- **Medicare.** Inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. The System is reimbursed at a tentative rate with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicare Administrative Contractor. Cost reports have been audited and finalized by the Medicare Administrative Contractor through December 31, 2011. Disproportionate Share (DSH), Indirect Medical Education (IME), Graduate Medical Education (GME), Paramedical Education and Meaningful Use (MU) are all reconciled through settlement processes. During 2012, the system began participation with Catholic Medical Partners (CMP) as an Accountable Care Organization (ACO). The ACO places a global budget on all traditional Medicare claims (excluding e.g. DSH, IME, DME, MU) for patients associated with CMP Primary Care physicians. Claims are processed through fee for service billing and reconciled to the global budget along with quality measurement at the end of the period.
- **Non-Medicare.** The New York Health Care Reform Act of 1996, as updated, governs payments to hospitals in New York State. Under this system, hospitals and all non-Medicare payors, except Medicaid, Workers' Compensation and No-Fault insurance programs, negotiate hospitals' payment rates. If negotiated rates are not established, payors are billed at hospitals established charges. Medicaid, Workers' Compensation and No-Fault payors pay hospital rates promulgated by the New York State Department of Health (DOH) on a prospective basis. Adjustments to current and prior years' rates for these payors will continue to be made in the future. Effective December 1, 2009, NYS implemented inpatient reimbursement reform. The reform updated the data utilized to calculate the NYS DRG rates and service intensity weights (SIWs) in order to utilize refined data and more current information in DOH promulgated rates. Similar type outpatient reforms were implemented effective December 1, 2008.

Amounts recognized in 2014 and 2013 related to prior years, including adjustments to prior year estimates increased revenues approximately \$8,946 and \$7,788, respectively. These changes in estimates related to estimates for prior years cost report reopening, appeals, and tentative final cost reports, some of which are still subject to audit, additional reopening, and/or appeals.

Approximately 53% and 52% of net patient/resident service revenue was generated from services rendered to patients/residents under Medicare and Medicaid programs in 2014 and 2013, respectively. Approximately 36% and 37% of net patient/resident service revenue was generated from services rendered to patients under managed care programs in 2014 and 2013, respectively.

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

# CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

### NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

Patient and resident service revenue, net of contractual allowances and discounts, (but before the provision for bad debts), recognized in the period from these major payor sources, is as follows for the years ended December 31, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Patient/resident service revenue (net of contractual allowances and discounts):		
Medicare	\$ 392,049	\$ 373,277
Medicaid	120,647	102,503
Other third party payors	429,160	424,105
Patients/residents	<u>20,133</u>	<u>22,908</u>
Total net patient/resident service revenue	961,989	922,793
Provision for bad debts	<u>(21,292)</u>	<u>(20,712)</u>
Net patient/resident service revenue less provision for bad debts	<u>\$ 940,697</u>	<u>\$ 902,081</u>

**Charity Care:** The System provides services to all patients regardless of ability to pay. A patient is classified as a charity patient based on income eligibility criteria as established by the HAP which is determined by presentation for care without insurance, while using an estimator (PARO) of each guarantor's ability to pay. Free care is determined at 110% of Federal Poverty Guidelines (FPG), whereas discounted care is also provided at 500% FPG.

Of the System's total expenses reported, an estimated \$7,208 and \$7,970 arose from providing services to charity patients in 2014 and 2013, respectively. Costing is a full step down methodology of cost from non-revenue producing departments to revenue producing departments, with assignment of cost to individual charge items based on relative value units. Additional costs for the Hospitals include required payments for a gross receipts assessment to New York State which is used to fund the New York State Medicaid program and the HCRA. Revenues that offset the costs of Charity Care include payments from the New York State Uncompensated Care Pools.

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

# CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

### NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

**Collective Bargaining Agreements:** The System has approximately 40% of its employees working under thirteen collective bargaining agreements. The agreements are set to expire beginning April 30, 2015 through August 15, 2018.

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

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

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

The System recognized \$2,763 and \$5,845 of electronic health record incentive income related to Medicare and Medicaid incentive programs during the years ended December 31, 2014 and 2013, respectively, which is recorded in other revenue.

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

	<u>2014</u>	<u>2013</u>
Cafeteria revenue	\$ 2,618	\$ 2,634
Parking revenue	1,087	1,086
Unrestricted contributions to the Foundations	935	865
Legal settlements	-	4,000
Medicare and Medicaid meaningful use	2,763	5,845
Other	<u>5,186</u>	<u>5,391</u>
Total other revenue	\$ <u>12,589</u>	\$ <u>19,821</u>

## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

#### NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

	<u>2014</u>	<u>2013</u>
Rents and operating leases	\$ 9,984	\$ 10,264
Dues	5,197	4,973
Cash receipt assessment	5,201	5,442
Taxes, travel and miscellaneous other	<u>9,871</u>	<u>9,134</u>
Other expenses	<u>\$ 30,253</u>	<u>\$ 29,813</u>

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

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

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

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

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

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



## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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#### 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. The tax-exempt organizations are subject to federal taxes on unrelated business income under section 511 of the Internal Revenue Code which are reported as other expenses in these financial statements. The System's federal Exempt Organization Business Income Tax Returns for 2011, 2012, and 2013 remain subject to examination by the Internal Revenue Service.

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

**Capitalized Software Costs:** The System capitalizes certain costs that are incurred to purchase or to create and implement internal-use computer software, which includes software coding, installation, testing and certain data conversion from both internal and external providers in accordance with accounting guidance. These capitalized costs are amortized on a straight-line basis over ten years and reviewed for impairment on an annual basis. CHS capitalized software, computer equipment, and other external costs of \$5,553 during 2014 and \$6,496 during 2013. Capitalized project labor costs amounted to \$1,819 during 2014 and \$925 during 2013.

**Reclassifications:** Certain prior year amounts were reclassified to conform to the 2014 consolidated financial statement presentation.

**Subsequent Events:** The System evaluated subsequent events through March 26, 2015 which was the date the financial statements were available to be issued.

#### NOTE 3. INTEREST IN NET ASSETS OF AFFILIATED FOUNDATION

The System accounts for its interest in the Kenmore Mercy Hospital Foundation in accordance with the provisions of not-for-profit accounting guidance. This guidance establishes standards for transactions in which a not-for-profit organization (the recipient organization or the Foundation) accepts a contribution from a donor and agrees to transfer those assets, the return on investment of those assets, or both to another entity (the beneficiary) that is specified by the donor. This guidance further provides that when these organizations are financially interrelated, as defined in this guidance, the beneficiary is required to recognize its interest in the net assets of the recipient organization and adjust that interest for its share of the change in net assets.

The Foundation is a separate not-for-profit organization with its own board of directors and finances separate from that of the System and is not part of CHS's financial reporting entity.

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

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

**NOTE 3. INTEREST IN NET ASSETS OF AFFILIATED FOUNDATION (CONTINUED)**

A summary of the Foundation's aggregated assets, liabilities, net assets, and changes in net assets is as follows:

	<u>2014</u>	<u>2013</u>
Cash, investments and other assets	\$ 3,771	\$ 5,131
Total assets	<u>\$ 3,771</u>	<u>\$ 5,131</u>
Liabilities	\$ 919	\$ 515
Net assets:		
Unrestricted	2,393	3,897
Temporarily restricted	<u>459</u>	<u>719</u>
Total net assets	<u>2,852</u>	<u>4,616</u>
Total net assets and liabilities	<u>\$ 3,771</u>	<u>\$ 5,131</u>
Change in unrestricted net assets	\$ (1,504)	\$ 769
Change in temporarily restricted net assets	<u>(260)</u>	<u>(68)</u>
	<u>\$ (1,764)</u>	<u>\$ 701</u>

Distributions were made in the amount of \$2,127 and \$328 during 2014 and 2013, respectively.

The unrestricted net assets of the Foundation are classified as temporarily restricted net assets of Kenmore Mercy Hospital. This is consistent with accounting principles generally accepted in the United States of America, in that an implied time restriction exists upon such unrestricted net assets, as Kenmore Mercy Hospital does not control the Foundation.

**NOTE 4. ASSETS LIMITED AS TO USE**

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

	<u>2014</u>	<u>2013</u>
By Board for capital improvements:		
Funded depreciation:		
Cash and cash equivalents	\$ 9,518	\$ 2,418
U.S. government obligations	5,228	12,253
Interest receivable	<u>13</u>	<u>34</u>
	<u>14,759</u>	<u>14,705</u>
Held by Trustee under Indenture Agreement:		
Cash and cash equivalents	5,332	8,606
U.S. government obligations	<u>117</u>	<u>1,980</u>
	<u>5,449</u>	<u>10,586</u>
Held by Trustee under Letter of Credit Agreement:		
Cash and cash equivalents	<u>2,752</u>	<u>2,752</u>
Board Designated for long-term care reinvestment		
Cash and cash equivalents	<u>2,602</u>	<u>2,602</u>
Other	<u>544</u>	<u>459</u>
Assets limited as to use	<u>\$ 26,106</u>	<u>\$ 31,104</u>

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

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

**NOTE 5. INVESTMENTS**

Investments consisted of the following as of December 31:

	<u>2014</u>	<u>2013</u>
Investment in debt and equity securities:		
Fair value	\$ 9,519	\$ 8,953
Cost	<u>8,064</u>	<u>7,320</u>
Unrealized gain	<u>\$ 1,455</u>	<u>\$ 1,633</u>

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

	<u>2014</u>	<u>2013</u>
Interest and dividend income	\$ 1,130	\$ 1,235
Net unrealized and realized gains on investments	<u>211</u>	<u>1,108</u>
Total investment income	<u>\$ 1,341</u>	<u>\$ 2,343</u>

**NOTE 6. PROPERTY AND EQUIPMENT**

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

	<u>2014</u>	<u>2013</u>
Land and land improvements	\$ 7,532	\$ 7,431
Buildings	211,668	210,965
Equipment	194,889	164,762
Capital leases	84,339	39,502
Leasehold improvements	<u>89,956</u>	<u>70,650</u>
	588,384	493,310
Accumulated depreciation	(241,341)	(209,066)
Accumulated amortization on capital leases	<u>(25,924)</u>	<u>(18,544)</u>
	321,119	265,700
Construction in progress	<u>15,560</u>	<u>5,920</u>
Property and equipment, net	<u>\$ 336,679</u>	<u>\$ 271,620</u>

Depreciation expense in 2014 and 2013 amounted to approximately \$33,250 and \$29,848, respectively. Amortization expense on equipment under capital leases amounted to \$7,385 and \$6,445 in 2014 and 2013, respectively. Fully depreciated or amortized assets and capital leases of \$22 and \$21,670 were written-off for the years ended December 31, 2014 and 2013, respectively.

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

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

**NOTE 7. LONG-TERM OBLIGATIONS**

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

	<u>2014</u>	<u>2013</u>
<b>Mercy Hospital of Buffalo</b>		
Series 2006 Revenue Bonds (a)	\$ 8,677	\$ 9,332
Series 2008 Revenue Bonds (b)	21,603	22,270
Series 2012 Revenue Bonds (c)	2,991	3,061
Bridge loan financing (d)	2,404	-
Mercy Comprehensive Care Center, monthly payments of \$9, including interest at 6.25%, matures November 2015	93	189
Cafeteria renovation loan with Aramark Healthcare, in monthly payments of \$3, matures August 2018	166	250
Capital lease obligations and other, at interest rates ranging from 2.87% to 4.63%, collateralized by equipment	<u>15,097</u>	<u>15,977</u>
	<u>51,031</u>	<u>51,079</u>
<b>Kenmore Mercy Hospital</b>		
Series 2006 Revenue Bonds (a)	9,512	10,520
Series 2012 Revenue Bonds (c)	13,726	14,066
Bridge loan financing (e)	3,990	-
Mortgage payable to Century Health Capital, Inc. for KMH Homes Inc. (f)	5,339	5,813
Capital lease obligations and other, at various rates of interest ranging from 2.9% to 5.0%, collateralized by equipment	3,018	2,528
Other	<u>35</u>	<u>44</u>
	<u>35,620</u>	<u>32,971</u>
<b>Sisters of Charity Hospital</b>		
Series 2006 Revenue Bonds (a)	24,857	26,737
Bridge loan financing (d)	4,844	-
Capital lease obligations, at various rates of interest ranging from 3.13% to 4.87%, collateralized by equipment	<u>8,505</u>	<u>8,258</u>
	<u>38,206</u>	<u>34,995</u>
<b>Father Baker Manor</b>		
Mortgage payable to Century Health Capital, Inc. (g)	<u>6,028</u>	<u>6,458</u>
<b>McAuley Seton Home Health Care Corporation</b>		
Loan payable to HSBC Bank (h)	<u>1,471</u>	<u>1,948</u>
<b>Our Lady of Victory Renaissance Corporation</b>		
Series 2007A Variable Rate Demand Bonds (i)	8,745	9,025
Series 2007B Variable Rate Demand Bonds (i)	1,420	1,470
Loan payable with HSBC Bank for Data Center (j)	<u>2,664</u>	<u>3,883</u>
	<u>12,829</u>	<u>14,378</u>

# CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

### NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

	<u>2014</u>	<u>2013</u>
<b>Catholic Health System (Parent)</b>		
Capital lease obligation for financing of VOIP telephone system, in monthly installments of \$22, including interest at 2.92%, collateralized by equipment	1,769	2,241
Bridge loan financing of Lawson ERP project (d)	5,758	-
Capital lease obligation for Administrative & Regional Training Center (ARTC) (k)	38,424	-
Capital lease obligations for ARTC leasehold improvements (l)	12,700	-
	<u>58,651</u>	<u>2,241</u>
Total long-term obligations	203,836	144,070
Less: Current maturities	<u>(19,850)</u>	<u>(15,399)</u>
Long-term obligations, net	<u>\$ 183,986</u>	<u>\$ 128,671</u>

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

- Series 2006A Bonds for \$13,360 was loaned to MHB in order to finance the cost of MHB's operating room expansion, other expansions and improvements at MHB's facility.
- Series 2006B Bonds for \$30,295 was loaned to SCH for the purpose of refunding DASNY's SCH Insured Revenue Bonds, Series 2003, which bonds were issued for the purpose of refunding a series of bonds issued in 1991, the proceeds of which were applied to finance the construction and renovation of the SCH facilities and to refinance outstanding indebtedness. Series 2006D for \$8,435 was loaned to the former St. Joseph Hospital (SJH), which was merged into SCH in 2009, to finance the cost of the SJH emergency room expansion project.
- Series 2006C Bonds for \$16,730 was loaned to KMH 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 KMH 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.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(in thousands of dollars)

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NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

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 0.04% and 0.06% at December 31, 2014 and 2013, respectively.

Certain financial covenants must be maintained by the Obligated Group. Failure to comply with these covenants requires a formal consultant's report and quarterly progress reports demonstrating how the facility is progressing towards compliance. The Loan Agreement requires the Obligated Group to comply with certain financial covenants, including maintenance of (i) a minimum number of days cash on hand; (ii) long-term debt service coverage; and (iii) a maximum leverage ratio. The Obligated Group was in compliance with these covenants at December 31, 2014 and 2013.

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

The Series 2008 Bonds were issued under the Master Trust Indenture that was created in 2006 pursuant to the formation of the Obligated Group. All material components of the Series 2008 issue mirror the Series 2006 issue. Among these items are the following: 1) a variable remarketed rate (determined by the Security Industry and Financial Markets Association (SIFMA)) collateralized by a letter of credit with HSBC Bank expiring November 18, 2018 (with the option of an initial term loan), 2) a security interest in and assignment of gross receipts of the Mercy Hospital of Buffalo, together with the Mercy Hospital of Buffalo's right to receive or collect the gross receipts, 3) consistent financial covenants, and 4) execution of an interest rate swap agreement (with HSBC Bank) consistent with the terms utilized in the 2006 swap agreement (see Note 8). The variable interest rate was 0.04% and 0.06% at December 31, 2014 and 2013, respectively.

- c. On July 12, 2012, \$17,315 of DASNY Catholic Health System Obligated Group Revenue Bonds, Series 2012 were issued. The Bonds consisted of the following:
- Series 2012A Bonds for \$14,235 were loaned to KMH 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 MHB for the purpose of funding the cost of improvements to MHB's existing approximately 381,000 square foot parking facility containing approximately 1,026 spaces. Proceeds of the Series 2012B Bonds were also applied to pay certain costs of issuing the Bonds. The discount and premium on the bonds of \$32 and \$46, respectively, are attributable to the difference between the stated interest rate on these bonds and will be amortized over the life of the bonds.

# CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

### NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

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, 2014 are as follows:

3.00% Serial Bonds Due July 1, 2015	\$	170
3.00% Serial Bonds Due July 1, 2016		350
3.00% Serial Bonds Due July 1, 2017		360
4.00% Serial Bonds Due July 1, 2018		370
3.50% Term Bonds Due July 1, 2022		1,610
4.00% Term Bonds Due July 1, 2027		2,385
5.00% Term Bonds Due July 1, 2032 (i)		2,960
4.75% Term Bonds Due July 1, 2039		<u>5,530</u>
Total Series 2012A Bonds		13,735
3.50% Term Bonds Due July 1, 2022	\$	605
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>2,975</u>
Total Series 2012 Bonds	\$	<u>16,710</u>

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

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

- d. In 2014, the System entered into a revolving line of credit agreement with a commercial bank that permits the System to borrow up to \$28,100 at the bank's adjusted one month LIBOR rate plus 1.25%. MHB used \$2,404 of the proceeds from the revolver to assist with the financing of MHB's cardiac holding unit and labor and delivery waiting projects. SCH used \$4,844 of the proceeds from the revolver to assist with the financing of an ambulatory surgery center. CHS Parent used \$5,758 of the proceeds from the revolver to assist with the financing of the System's Enterprise Resource Planning Project (ERP). Borrowings under the financing agreement mature at the earliest of the issuance of the System's planned fixed rate bond financing or July 1, 2016. The proceeds from the anticipated 2015 bond issuance will be used to repay all outstanding amounts under the revolving line of credit agreement.

## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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#### NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

- e. In 2014 KMH entered into a loan agreement with a commercial bank to borrow \$3,990 at an adjusted LIBOR rate. The loan agreement matures on May 31, 2015. The proceeds from the anticipated 2015 bond issuance will be used to repay all outstanding amounts under this loan agreement.
- f. Mortgage payable to Century Health Capital (an FHA - Insured Mortgage). The mortgage is payable in monthly installments of \$65 including interest of 5.51%. Monthly payments continue through maturity in July 2023. The mortgage is collateralized by the building and equipment.
- g. Mortgage payable to Century Health Capital (an FHA - Insured Mortgage). The mortgage is payable in monthly installments of \$64 including interest of 5.375%. Monthly payments continue through maturity in March 2025. The mortgage is collateralized by the building and equipment.
- h. MSHC entered into a term loan agreement with HSBC Bank. The agreement provided \$2,385. Outstanding borrowings under this agreement bear interest at a fixed rate of 2.62% at December 31, 2014. The term loan calls for monthly principal payments of \$40 plus interest and matures on December 28, 2017. Outstanding borrowings are secured by substantially all the revenues and receipts of MSHC. The term loan contains various loan covenants, including a debt service coverage ratio. MSHC was in compliance with all covenants as of December 31, 2014 and 2013.
- i. On April 1, 2007, OLV Renaissance entered into agreements with the Erie County Industrial Development Agency's (the Agency) for the purpose of obtaining revenue bonds used to finance construction of its SNF and PACE facilities. The agency took title to the facility through a lease agreement and simultaneously conveyed title back to OLV Renaissance through an installment sale of the lease interests. OLV Renaissance is obligated to make lease rental payments to the bond trustee, as the Agency's assignee, in amounts which correspond to the principal and interest payments on the bonds. At the expiration of the leases' term (April 2032), title fully reverts back to OLV Renaissance. On April 25, 2007, the Agency issued variable rate demand revenue bonds with an aggregate principal amount of \$11,860. The bond issue consists of two series of bonds: \$10,220 in variable rate demand Revenue Bonds Series 2007A (Series 2007A Bonds) and \$1,640 in variable rate demand Revenue Bonds Series 2007B (Series 2007B Bonds).

The Variable Interest Rate is determined by the remarketing agent based on (1) market interest rates for comparable securities; (2) other financial market rates and indices (including, but not limited to treasury bills, commercial paper, commercial bank prime rates, HUD project notes, federal fund rates and LIBOR); (3) general financial and credit market conditions; (4) credit rating and financial condition of OLV Renaissance; and (5) applicable tender provisions which may have bearing on the rate. The variable interest rate was 0.04% for the Series 2007A bonds and 0.15% for the Series 2007B bonds at December 31, 2014. See Note 8 regarding the interest rate swap agreement OLV Renaissance entered into with respect to the Series 2007A Revenue Bonds.

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

The Series 2007A Revenue Bonds are subject to mandatory sinking fund redemptions in years 2012 to 2032 in amounts ranging from \$250 to \$740 at variable interest rates. The Series 2007B Revenue Bonds are subject to mandatory sinking fund redemptions in years 2012 to 2032 in amounts ranging from \$45 to \$115.



## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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#### NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

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

In accordance with the financing documents, at the option of the Issuer and upon notice given by OLV Renaissance, the Series 2007A Revenue Bonds are subject to optional redemption at 100%. In connection with the Bond financing, OLV Renaissance has executed an irrevocable direct pay letter of credit with a financial institution for a maximum amount of \$10,261. The parties have an agreement in principle to extend the letter of credit expiration date to at least May 1, 2018. There is no outstanding amount at December 31, 2014 or 2013. 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. The covenants were in effect during the years ended December 31, 2014 and 2013. OLV Renaissance's primary tenant, MHB is also required to comply with a covenant to maintain minimum long-term debt service coverage and a minimum days cash on hand as of any testing date.

MHB was in compliance with this covenant as of December 31, 2014 and 2013. OLV Renaissance failed the debt service coverage and debt to capitalization covenants for December 31, 2014 and 2013. OLV Renaissance obtained a waiver from HSBC Bank on March 10, 2015, for the December 31, 2014 and 2013 covenants.

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

Under the terms of the financing documents, OLV Renaissance has guaranteed payment of all amounts due under the loan. Additionally, the loan is secured by second mortgage liens on all buildings, improvements and equipment now owned or subsequently acquired by OLV Renaissance, all unrestricted accounts receivable and a right of setoff against OLV Renaissance's funds held by the trustee. The loan agreement requires certain covenants including debt service coverage to be maintained. OLV Renaissance was in compliance with the debt service coverage ratio for December 31, 2014 and 2013.

- k. During 2014, construction was completed on the Administrative and Regional Training Center (ARTC). At time of occupancy, a twenty-five year lease was entered into with the developer. The System has the option to purchase the building between the twelfth and fourteenth month of the lease, post occupancy. The System expects to exercise this option in 2015. The proceeds from the anticipated 2015 bond issuance will be used to finance this purchase. Once purchased, the current capital lease obligation will be terminated.
- l. During 2014, the System entered into multiple capital leases with a financial institution for funding of various leasehold improvements at the ARTC. The System is obligated to make payments each month until expiration in September 2024. The proceeds from the anticipated 2015 bond issuance will be used to repay all outstanding amounts under the capital lease obligations.

# CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

### NOTE 7. LONG-TERM OBLIGATIONS (CONTINUED)

Aggregate maturities of long-term debt, including capital lease obligations, considering obligations subject to short-term remarketing as due according to their long-term amortization schedule, subsequent to December 31, 2014 are as follows:

	<u>Long-Term Debt</u>	<u>Capital Leases</u>	<u>Total</u>
2015	\$ 11,998	\$ 8,173	\$ 20,171
2016	21,721	6,692	28,413
2017	7,828	5,904	13,732
2018	7,797	4,668	12,465
2019	7,236	3,251	10,487
Thereafter	<u>69,512</u>	<u>52,602</u>	<u>122,114</u>
	126,092	81,290	207,382
Less: Interest	<u>-</u>	<u>(3,546)</u>	<u>(3,546)</u>
Long-term obligations	<u>\$ 126,092</u>	<u>\$ 77,744</u>	<u>\$ 203,836</u>

Included in the amounts above are certain obligations expected to be refinanced by the System on a long-term basis in 2015. Within the "Long-Term Debt" caption are \$3,990 and \$13,006 of obligations due to mature in 2015 and 2016, respectively, included in the proposed refinancing amount. Similarly, in the "Capital Lease" caption are \$346, \$1,504, \$1,511, \$1,518, \$1,559 and \$44,686 of obligations due to mature in 2015 through 2019 and thereafter, respectively, included in the proposed refinancing amount.

At December 31, 2014 and 2013, the System had a revolving line of credit of \$20,000 of which \$8,380 and \$10,831 was outstanding as of December 31, 2014 and 2013. The variable interest rate was 2.16% and 2.17% at December 31, 2014 and 2013, respectively.

**Operating Leases:** Future minimum lease payments under noncancelable operating leases for equipment and property (net of sublease rentals) are as follows at December 31, 2014:

2015	\$ 10,243
2016	9,802
2017	6,341
2018	18,304
2019	3,739
Thereafter	<u>3,058</u>
	51,487
Less: Minimum sublease rental	<u>(1,197)</u>
	<u>\$ 50,290</u>

Total expense for rents and operating type leases for equipment and property was approximately \$9,574 and \$10,264 for 2014 and 2013, respectively.

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

**NOTES TO 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 USA, NA and JP Morgan Chase (the Financial Institutions) for purposes of mitigating risk posed by the Bonds accruing interest at a variable rate. Further, the Hospitals agreed not to take or omit to take any action that could reasonably be expected to result in the termination of the derivative agreement unless otherwise approved by the Financial Institutions, provided, however, that termination of the derivative agreement shall not constitute an event of default for purposes of the Loan Agreement, but upon any such termination of the derivative agreement, the Financial Institutions may require that the Hospitals direct the Series 2006 or Series 2008 Bonds be converted to bonds that bear a fixed rate of interest. The interest rate swap agreements outstanding on the Series 2006 Bonds as of December 31, 2013 was settled in 2014. Termination costs in the amount of \$5,772 will be amortized over the remaining life of the bonds. The net amount of termination costs are recorded in the financing activities on the statement of cash flows. Amortization expense related to the termination costs was \$80 for 2014 and \$0 in 2013.

The terms of the Series 2008 swap require the Hospitals to pay 3.785% on the notional amount (\$22,210 at December 31, 2014) and in exchange, the Hospitals will receive a variable rate payment based upon the SIFMA, calculated weekly. The 2008 swap agreement was executed on November 19, 2008 and expires on July 1, 2034. These dates correlate to the issue date and due date of the Bonds. The instrument qualifies for hedge treatment and is designated a cash flow hedge of future interest payments. The effective portion of the hedge has been excluded from excess of revenues over expenses and recorded within changes to net assets.

In connection with the issuance of the Series 2007 Bond and execution of the Loan Agreement, OLV Renaissance entered into an interest rate swap agreement with HSBC Bank USA, NA for the purpose of mitigating posed by the Bonds accruing interest at a variable rate. The terms of the Series 2006 swap require the Hospitals to pay a fixed rate of 4.143% on the notional amount (\$8,745 at December 31, 2014) and in exchange, OLV Renaissance will receive a variable rate payment based upon the SIFMA, calculated weekly. The notional amount of the swap is matched to the maturity schedule of the Series 2007 Bonds. The 2007 swap agreement was executed on May 25, 2007 and expires on April 1, 2032. These dates correlate to the issue date and due date of the Bonds. The instrument qualifies for hedge treatment and is designated a cash flow hedge of future interest payments. The effective portion of the hedge has been excluded from excess of revenues over expenses and recorded within changes to net assets.

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

(in thousands of dollars)	<b>2014</b>		<b>2013</b>	
	<b>Balance Sheet Location</b>	<b>Fair Value</b>	<b>Balance Sheet Location</b>	<b>Fair Value</b>
Interest rate contracts floating to fixed	Long-term liabilities	\$ <u>5,853</u>	Long-term liabilities	\$ <u>8,596</u>

The effects of derivative instruments on the consolidated statements of operations and changes in net assets for 2014 and 2013 are as follows:

(in thousands of dollars)	<b>Ineffective portion in Statement of Operations</b>		<b>Effective portion in Net Assets</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Change in fair value of interest rate swaps	\$ <u>(72)</u>	\$ <u>184</u>	\$ <u>(2,807)</u>	\$ <u>7,067</u>

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

### **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** *(in thousands of dollars)*

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#### **NOTE 8. DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)**

The Hospitals measure their interest rate swaps at fair value on a recurring basis. The fair value of the interest rate swaps is determined based on financial models that consider current and future market interest rates and adjustments for nonperformance risk. The inputs utilized in the valuation process of the interest rate swaps are considered to be Level 2 within the fair value hierarchy defined in Note 14.

#### **NOTE 9. OBLIGATED GROUP FINANCIAL INFORMATION**

In November 2006, the System formed the Obligated Group, consisting of its four primary hospitals (MHB, SCH, 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, \$24,700 of DASNY - Catholic Health System Obligated Group Revenue Bonds, Series 2008. In 2012, the System issues \$17,315 of DASNY – Catholic Health System Obligated Group Revenue Bonds, Series 2012. 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 and Series 2012 Obligations. Management has determined that certain immaterial subsidiaries (Mercy Hospital Foundation, Inc., Sisters 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, 2014 and 2013 and statements of operations and changes in net assets, and cash flows for the years then ended December 31, 2014 and 2013.

**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, 2014

ASSETS	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
<b>Current assets:</b>						
Cash and cash equivalents	\$ 31,890	\$ 83,954	\$ 128,658	\$ 42,197	\$ -	\$ 286,699
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$23,200	-	53,406	42,153	21,401	-	116,960
Other receivables	1,462	4,244	2,873	2,327	-	10,906
Inventories	-	12,902	6,378	2,515	-	21,795
Assets limited as to use	-	-	-	-	-	-
Prepaid expenses and other current assets	4,144	674	524	298	-	5,640
Due from affiliates	64,218	-	654	-	(60,010)	4,862
<b>Total current assets</b>	<u>101,714</u>	<u>155,180</u>	<u>181,240</u>	<u>68,738</u>	<u>(60,010)</u>	<u>446,862</u>
Assets limited as to use	5,354	339	-	6,399	-	12,092
Property and equipment, net	77,225	98,193	76,257	61,555	-	313,230
Due from affiliates	2,802	22	10,303	1,479	(11,790)	2,816
Other assets	2,977	34,119	28,581	16,082	-	81,759
<b>Total Assets</b>	<u>\$ 190,072</u>	<u>\$ 287,853</u>	<u>\$ 296,381</u>	<u>\$ 154,253</u>	<u>\$ (71,800)</u>	<u>\$ 856,759</u>
<b>LIABILITIES AND NET ASSETS</b>						
<b>Current liabilities:</b>						
Current portion of long-term obligations	\$ 831	\$ 5,611	\$ 4,373	\$ 6,503	\$ -	\$ 17,318
Line of credit payable	8,380	-	-	-	-	8,380
Accounts payable	4,001	16,051	13,372	8,831	-	42,255
Accrued expenses	23,592	12,773	11,781	6,091	-	54,237
Due to third-party payors	-	17,482	11,344	6,042	-	34,868
Due to affiliates	554	13,805	19,838	11,103	(44,600)	700
<b>Total current liabilities</b>	<u>37,358</u>	<u>65,722</u>	<u>60,708</u>	<u>38,570</u>	<u>(44,600)</u>	<u>157,758</u>
Long-term obligations, net	57,820	45,421	33,833	29,117	-	166,191
Other long-term liabilities	71,380	195,234	123,740	54,037	(11,760)	432,631
<b>Total liabilities</b>	<u>166,558</u>	<u>306,377</u>	<u>218,281</u>	<u>121,724</u>	<u>(56,360)</u>	<u>756,580</u>
<b>Net assets</b>						
Unrestricted	23,514	(18,524)	78,100	32,529	(15,440)	100,179
Temporarily restricted	-	-	-	-	-	-
<b>Total net assets</b>	<u>23,514</u>	<u>(18,524)</u>	<u>78,100</u>	<u>32,529</u>	<u>(15,440)</u>	<u>100,179</u>
<b>Total Liabilities and Net Assets</b>	<u>\$ 190,072</u>	<u>\$ 287,853</u>	<u>\$ 296,381</u>	<u>\$ 154,253</u>	<u>\$ (71,800)</u>	<u>\$ 856,759</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

For the Year Ended December 31, 2014

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
<b>Unrestricted revenues, gains and other support:</b>						
Net patient/resident service revenue	\$ -	393,515	\$ 325,127	\$ 160,934	\$ -	\$ 879,576
Provision for bad debts	-	(10,070)	(7,307)	(2,496)	-	(19,873)
Net patient/resident service revenue less provision for bad debts	-	383,445	317,820	158,438	-	859,703
Other revenue	127,758	5,626	5,452	1,653	(123,025)	17,464
<b>Total unrestricted revenues, gains and other support</b>	<b>127,758</b>	<b>389,071</b>	<b>323,272</b>	<b>160,091</b>	<b>(123,025)</b>	<b>877,167</b>
<b>Expenses:</b>						
Salaries and wages	62,448	154,972	142,919	67,236	(57,782)	369,793
Employee benefits	16,868	50,458	44,854	19,655	(16,992)	114,843
Medical and professional fees	5,034	12,148	12,595	4,389	(3,818)	30,348
Purchased services	25,833	31,850	28,210	13,817	(26,033)	73,677
Supplies	601	80,341	55,855	33,567	(551)	169,813
Depreciation and amortization	4,659	16,187	14,856	7,445	(4,479)	38,668
Interest	1,451	3,018	2,345	1,917	(1,296)	7,435
Insurance	313	3,680	5,264	1,175	(303)	10,129
Other expenses	10,411	16,437	11,222	5,171	(12,572)	30,669
<b>Total expenses</b>	<b>127,618</b>	<b>369,091</b>	<b>318,120</b>	<b>154,372</b>	<b>(123,826)</b>	<b>845,375</b>
<b>Income (loss) from operations</b>	<b>140</b>	<b>19,980</b>	<b>5,152</b>	<b>5,719</b>	<b>801</b>	<b>31,792</b>
<b>Nonoperating revenues and losses:</b>						
Investment income	36	451	270	153	(34)	876
Other	478	48	936	46	(767)	741
<b>Total nonoperating revenues and losses</b>	<b>514</b>	<b>499</b>	<b>1,206</b>	<b>199</b>	<b>(801)</b>	<b>1,617</b>
<b>Excess of revenues over expenses</b>	<b>\$ 654</b>	<b>\$ 20,479</b>	<b>\$ 6,358</b>	<b>\$ 5,918</b>	<b>\$ -</b>	<b>\$ 33,409</b>

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 (Continued)

For the Year Ended December 31, 2014

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
<b>Unrestricted net assets:</b>						
Excess of revenues over expenses	\$ 654	\$ 20,479	\$ 6,358	\$ 5,918	\$ -	\$ 33,409
Change in unrealized gain on interest rate swap	-	(1,961)	(312)	52	-	(2,221)
Change in pension obligation, other than net periodic cost	(14,031)	(36,483)	(28,096)	(7,758)	-	(86,368)
Net assets released from restrictions	24	-	-	-	-	24
Grant revenue capital expenditures	-	168	314	-	-	482
Transfers to/from parent or affiliate	12,382	(8,198)	(5,648)	912	-	(552)
Contributions and other	4,444	608	886	2,219	-	8,157
Valuation allowance on intercompany receivables	-	-	-	-	(3,945)	(3,945)
Increase in unrestricted net assets	3,473	(25,387)	(26,498)	1,343	(3,945)	(51,014)
<b>Temporarily restricted net assets:</b>						
Temporarily restricted net assets released from restrictions	(24)	-	-	-	-	(24)
Contributions and other	-	-	-	-	-	-
Decrease in temporarily restricted net assets	(24)	-	-	-	-	(24)
Increase (decrease) in net assets	3,449	(25,387)	(26,498)	1,343	(3,945)	(51,038)
Net assets, beginning of year	20,065	6,863	104,598	31,186	(11,495)	151,217
Net assets, end of year	<u>\$ 23,514</u>	<u>\$ (18,524)</u>	<u>\$ 78,100</u>	<u>\$ 32,529</u>	<u>\$ (15,440)</u>	<u>\$ 100,179</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, 2013

ASSETS	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
<b>Current assets:</b>						
Cash and cash equivalents	\$ 27,961	\$ 63,904	\$ 129,694	\$ 31,914	\$ -	\$ 253,473
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$24,943	-	54,105	37,376	17,964	-	109,445
Other receivables	1,099	5,345	4,053	1,982	-	12,479
Inventories	-	11,113	6,013	2,181	-	19,307
Assets limited as to use	-	-	-	836	-	836
Prepaid expenses and other current assets	3,689	571	585	455	-	5,300
Due from affiliates	54,427	-	635	-	(50,389)	4,673
<b>Total current assets</b>	<u>87,176</u>	<u>135,038</u>	<u>178,356</u>	<u>55,332</u>	<u>(50,389)</u>	<u>405,513</u>
Assets limited as to use	5,379	1,324	211	9,483	-	16,397
Property and equipment, net	14,988	101,121	74,536	56,724	-	247,369
Due from affiliates	3,661	120	10,303	1,475	(12,008)	3,551
Other assets	1,020	28,270	26,197	16,249	-	71,736
<b>Total Assets</b>	<u>\$ 112,224</u>	<u>\$ 265,873</u>	<u>\$ 289,603</u>	<u>\$ 139,263</u>	<u>\$ (62,397)</u>	<u>\$ 744,566</u>
<b>LIABILITIES AND NET ASSETS</b>						
<b>Current liabilities:</b>						
Current portion of long-term obligations	\$ 452	\$ 5,518	\$ 4,473	\$ 2,499	\$ -	\$ 12,942
Line of credit payable	10,831	-	-	-	-	10,831
Accounts payable	3,182	17,785	15,087	7,983	(521)	43,516
Accrued expenses	22,294	15,682	13,582	7,399	-	58,957
Due to third-party payors	-	18,110	10,979	5,863	-	34,952
Due to affiliates	407	9,906	21,295	7,629	(38,621)	616
<b>Total current liabilities</b>	<u>37,166</u>	<u>67,001</u>	<u>65,416</u>	<u>31,373</u>	<u>(39,142)</u>	<u>161,814</u>
Long-term obligations, net	1,789	45,560	30,522	30,472	-	108,343
Other long-term liabilities	53,204	146,449	89,067	46,232	(11,760)	323,192
<b>Total liabilities</b>	<u>92,159</u>	<u>259,010</u>	<u>185,005</u>	<u>108,077</u>	<u>(50,902)</u>	<u>593,349</u>
<b>Net assets</b>						
Unrestricted	20,041	6,863	104,598	31,186	(11,495)	151,193
Temporarily restricted	24	-	-	-	-	24
<b>Total net assets</b>	<u>20,065</u>	<u>6,863</u>	<u>104,598</u>	<u>31,186</u>	<u>(11,495)</u>	<u>151,217</u>
<b>Total Liabilities and Net Assets</b>	<u>\$ 112,224</u>	<u>\$ 265,873</u>	<u>\$ 289,603</u>	<u>\$ 139,263</u>	<u>\$ (62,397)</u>	<u>\$ 744,566</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

For the Year Ended December 31, 2013

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
<b>Unrestricted revenues, gains and other support:</b>						
Net patient/resident service revenue	\$ -	371,395	\$ 322,669	\$ 154,244	\$ -	\$ 848,308
Provision for bad debts	-	(8,731)	(7,175)	(3,285)	-	(19,191)
Net patient/resident service revenue less provision for bad debts	-	362,664	315,494	150,959	-	829,117
Other revenue	123,375	10,143	6,776	2,655	(118,685)	24,264
<b>Total unrestricted revenues, gains and other support</b>	<b>123,375</b>	<b>372,807</b>	<b>322,270</b>	<b>153,614</b>	<b>(118,685)</b>	<b>853,381</b>
<b>Expenses:</b>						
Salaries and wages	62,267	147,687	143,089	65,965	(56,871)	362,137
Employee benefits	19,172	55,364	44,375	20,574	(17,962)	121,523
Medical and professional fees	4,855	12,030	14,848	4,595	(3,933)	32,395
Purchased services	23,205	28,818	28,434	12,649	(23,928)	69,178
Supplies	440	74,845	56,908	31,784	(397)	163,580
Depreciation and amortization	3,306	14,270	13,225	6,497	(3,306)	33,992
Interest	218	2,367	2,050	1,484	(218)	5,901
Insurance	269	3,123	3,226	1,377	(261)	7,734
Other expenses	9,872	15,928	11,363	4,898	(12,394)	29,667
<b>Total expenses</b>	<b>123,604</b>	<b>354,432</b>	<b>317,518</b>	<b>149,823</b>	<b>(119,270)</b>	<b>826,107</b>
<b>Income (loss) from operations</b>	<b>(229)</b>	<b>18,375</b>	<b>4,752</b>	<b>3,791</b>	<b>585</b>	<b>27,274</b>
<b>Nonoperating revenues and losses:</b>						
Investment income	21	598	263	81	(20)	943
Other	208	44	1,557	46	(565)	1,290
<b>Total nonoperating revenues and losses</b>	<b>229</b>	<b>642</b>	<b>1,820</b>	<b>127</b>	<b>(585)</b>	<b>2,233</b>
<b>Excess of revenues over expenses</b>	<b>\$ -</b>	<b>\$ 19,017</b>	<b>\$ 6,572</b>	<b>\$ 3,918</b>	<b>\$ -</b>	<b>\$ 29,507</b>

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 (Continued)

For the Year Ended December 31, 2013

	Parent	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Eliminations	Total
<b>Unrestricted net assets:</b>						
Excess of revenues over expenses	\$ -	\$ 19,017	\$ 6,572	\$ 3,918	\$ -	\$ 29,507
Change in unrealized loss on interest rate swap	-	3,413	1,994	643	-	6,050
Change in pension obligation, other than net periodic cost	16,080	45,520	31,530	10,804	-	103,934
Net assets released from restrictions	129	-	-	-	-	129
Grant revenue capital expenditures	390	1	19	-	-	410
Transfers to/from parent or affiliate	7,566	(7,311)	122	1,938	-	2,315
Contributions and other	-	988	1	328	-	1,317
Valuation allowance on intercompany receivables	-	-	-	-	17	17
Increase (decrease) in unrestricted net assets	24,165	61,628	40,238	17,631	17	143,679
<b>Temporarily restricted net assets:</b>						
Temporarily restricted net assets released from restrictions	(129)	-	-	-	-	(129)
Contributions and other	24	-	-	-	-	24
Decrease in temporarily restricted net assets	(105)	-	-	-	-	(105)
Increase (decrease) in net assets	24,060	61,628	40,238	17,631	17	143,574
Net assets, beginning of year	(3,995)	(54,765)	64,360	13,555	(11,512)	7,643
Net assets, end of year	<u>\$ 20,065</u>	<u>\$ 6,863</u>	<u>\$ 104,598</u>	<u>\$ 31,186</u>	<u>\$ (11,495)</u>	<u>\$ 151,217</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 Cash Flows**

For the Year Ended December 31, 2014 and 2013

	<b>2014</b>	<b>2013</b>
<b>Cash flows from operating activities:</b>		
Increase (decrease) in net assets	\$ (51,038)	\$ 143,574
Adjustments to reconcile (decrease) increase in net assets to net cash provided by operating activities		
Depreciation and amortization	38,668	33,992
Provision for bad debts	19,873	19,191
Change in pension obligation, other than periodic cost	86,368	(103,934)
Grant revenue for capital additions	(482)	(390)
Valuation allowance of intercompany receivables	3,945	(17)
Unrealized and realized loss (gain) on investments	10	41
Change in unrealized loss (gain) on interest rate swaps	1,890	(6,129)
Realized loss on termination of interest rate swaps	534	-
Gain on extinguishment of capital leases	-	(26)
Undistributed earnings in equity investees	(349)	34
Other	39	173
(Increase) decrease in assets:		
Patient accounts receivables	(27,388)	(17,456)
Other receivables	1,573	(5,348)
Inventories	(2,488)	(5,506)
Prepaid expenses and other current assets	(340)	(930)
Due from affiliates	(3,399)	2,613
Other assets	1,561	(1,034)
Increase (decrease) in liabilities:		
Accounts payable	(61)	(168)
Accrued expenses	(4,720)	1,989
Due to affiliate	84	(3,554)
Due to third-party payors	(84)	(3,310)
Other liabilities	14,431	19,765
<b>Net cash and cash equivalents provided by operating activities</b>	<b>78,627</b>	<b>73,570</b>
<b>Cash flows from investing activities:</b>		
Purchase of property and equipment	(46,276)	(40,709)
Proceeds from sale of property and equipment	42	-
Purchase of assets limited as to use	(28)	(2,523)
Proceeds from sale of assets limited as to use	5,159	12,654
<b>Net cash and cash equivalents used in investing activities</b>	<b>(41,103)</b>	<b>(30,578)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from issuance of long-term obligations	16,997	3,718
Termination of interest rate swaps	(5,772)	-
Proceeds of grant revenue for capital additions	482	390
Repayments of current and long-term obligations	(16,005)	(11,799)
<b>Net cash and cash equivalents used in financing activities</b>	<b>(4,298)</b>	<b>(7,691)</b>
<b>Increase in cash and cash equivalents</b>	<b>33,226</b>	<b>35,301</b>
Cash and cash equivalents - beginning of year	253,473	218,172
Cash and cash equivalents - end of year	<u>\$ 286,699</u>	<u>\$ 253,473</u>
<b>Supplemental disclosures of cash flow information</b>		
Cash paid during the year for interest	\$ 8,384	\$ 6,078
<b>Non-cash investing and financing transactions</b>		
Assets acquired under capital lease obligations	\$ 57,537	\$ 3,198
Construction related payables	\$ -	\$ 836
Other non-cash transactions	\$ 1,200	\$ 1,200

# CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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

	<u>2014</u>	<u>2013</u>
Healthcare services	\$ 625,105	\$ 606,172
General and administrative	<u>220,270</u>	<u>219,935</u>
	<u>\$ 845,375</u>	<u>\$ 826,107</u>

### 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>2014</u>	<u>2013</u>
<b>Projected Benefit Obligations</b>		
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 492,617	\$ 539,200
Service cost	18,024	20,805
Interest cost	24,445	20,997
Expenses	(406)	(247)
Benefits paid	(13,808)	(13,759)
Actuarial losses (gains)	<u>89,013</u>	<u>(74,379)</u>
Projected benefit obligation at end of year	<u>\$ 609,885</u>	<u>\$ 492,617</u>
<b>Accumulated benefit obligations at end of year</b>	<u>\$ 541,979</u>	<u>\$ 438,134</u>

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

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

**NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)**

	<u>2014</u>	<u>2013</u>
<b>Plan Assets</b>		
Change in plan assets:		
Fair value of assets at beginning of year	\$ 276,902	\$ 235,207
Actual return on plan assets	10,672	34,147
System contribution	21,554	21,554
Expenses	(406)	(247)
Benefits paid	<u>(13,808)</u>	<u>(13,759)</u>
Fair value of plan assets at end of year	<u>\$ 294,914</u>	<u>\$ 276,902</u>
<b>Funded status at end of year</b>	<u>\$ (314,971)</u>	<u>\$ (215,715)</u>
<b>Amounts recognized in the consolidated balance sheets:</b>		
Non-current liabilities	<u>\$ (314,971)</u>	<u>\$ (215,715)</u>
Net amounts recognized	<u>\$ (314,971)</u>	<u>\$ (215,715)</u>
<b>Amounts recognized in unrestricted net assets consists of:</b>		
Actuarial net loss	\$ (210,132)	\$ (119,529)
Prior service cost	<u>(482)</u>	<u>(712)</u>
Total amount recognized	<u>\$ (210,614)</u>	<u>\$ (120,241)</u>
<b>Other changes recognized in unrestricted net assets:</b>		
Net loss (gain) arising during the period	\$ 99,157	\$ (89,343)
Amortization of prior service cost	(229)	(229)
Amortization of loss	<u>(8,555)</u>	<u>(17,970)</u>
Total amount recognized	<u>\$ 90,373</u>	<u>\$ (107,542)</u>
<b>Components of net periodic benefit cost:</b>		
Service cost	\$ 18,024	\$ 20,805
Interest cost	24,445	20,997
Expected return on plan assets	(20,817)	(19,184)
Amortization of prior service cost or (credit)	229	229
Recognized actuarial loss	<u>8,555</u>	<u>17,970</u>
Net periodic pension cost	<u>\$ 30,436</u>	<u>\$ 40,817</u>

The estimated prior service cost and net loss that will be amortized from unrestricted net assets into net periodic pension cost over the next fiscal year for the System are \$129 and \$15,834, respectively.

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

**CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
*(in thousands of dollars)***NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)**

The Plan's target asset allocation and the actual asset allocation percentages for 2014 and 2013 are as follows at the respective measurement dates:

<u>Asset Category</u>	<u>Target</u>	<u>Actual</u>	
		<u>2014</u>	<u>2013</u>
Equities	75%	65%	61%
Fixed income	20	25	30
Other	<u>5</u>	<u>10</u>	<u>9</u>
	<u>100%</u>	<u>100%</u>	<u>100%</u>

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

Accounting Standards Codification Topic 820 allows for the use of a practical expedient for the estimation of fair value of investments in investment companies for which the investment does not have a readily determinable fair value. The practical expedient used by the Plan to value its investments in its Level 3 investments is the net asset value (NAV) per share, or its equivalent. 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 assets or liability's fair value measurement level with 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.

The 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, 2014 and 2013:

**Cash and cash equivalents** – Include certain instruments in highly liquid debt instruments with original maturities of three months or less at date of purchase.

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

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

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

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

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

**NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)**

**Commingled Funds** – Commingled funds are developed for investment by institutional investors only and therefore do not require registration with the Securities and Exchange Commission. Commingled funds are recorded at fair value based on either the underlying investments that have a readily determinable market value or based on net asset value, which is calculated using the most recent fund financial statements. Commingled funds are categorized as Level 2 unless they have a redemption restriction greater than 90 days, in which case they are categorized as Level 3.

**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. Hedge funds are categorized as Level 2 unless they have a redemption restriction greater than 90 days, in which case they are categorized as Level 3.

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, 2014, measured at fair value on a recurring basis using the fair value hierarchy defined in Note 14.

<b>At December 31, 2014</b>	<b><u>Level I</u></b>	<b><u>Level II</u></b>	<b><u>Level III</u></b>	<b><u>Total</u></b>
Cash and cash equivalents	\$ 14,058	\$ -	\$ -	\$ 14,058
Equity securities	31,992	-	-	31,992
Debt securities:				
Government and government agency obligations	-	7,935	-	7,935
Corporate bonds	-	49,708	-	48,708
Asset backed securities	-	4,940	-	4,940
Mutual funds:				
Equity mutual funds	57,107	-	-	57,107
Fixed mutual funds	21,477	-	-	21,477
Commingled funds:				
Equity commingled funds	-	75,406	-	75,406
Fixed income commingled funds	-	806	-	806
Hedge funds	-	26,518	4,265	30,783
Other	<u>702</u>	<u>-</u>	<u>-</u>	<u>702</u>
<b>Total</b>	<b>\$ <u>125,336</u></b>	<b>\$ <u>165,313</u></b>	<b>\$ <u>4,265</u></b>	<b>\$ <u>294,914</u></b>

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

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

**NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)**

<b>At December 31, 2013</b>	<b>Level I</b>	<b>Level II</b>	<b>Level III</b>	<b>Total</b>
Cash and cash equivalents	\$ 10,611	\$ -	\$ -	\$ 10,611
Equity securities	43,821	-	-	43,821
Debt securities:				
Government and government agency obligations	-	18,067	-	18,067
Corporate bonds	-	39,010	-	39,010
Asset backed securities	-	3,392	-	3,392
Mutual funds:				
Equity mutual funds	38,636	-	-	38,636
Fixed mutual funds	18,382	-	-	18,382
Commingled funds:				
Equity commingled funds	-	85,148	-	85,148
Fixed income commingled funds	-	1,160	-	1,160
Hedge funds	-	18,675	-	18,675
<b>Total</b>	<b>\$ 111,450</b>	<b>\$ 165,452</b>	<b>\$ -</b>	<b>\$ 276,902</b>

Pursuant to the CHE and Trinity Health merger, certain investments have been aligned to conform to Trinity Health's fair value policy. Accordingly, certain balances previously reported as Level III and Level II have been reclassified to Level II and Level I, respectively.

A roll forward of those marketable securities that have been classified by the defined benefit plan as Level 3 within the fair value hierarchy (defined above) is as follows:

	<b>2014</b>
Fair value January 1	\$ -
Purchases	4,250
Realized and unrealized gains	15
Fair value December 31	<u>\$ 4,265</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 \$23,507 to the pension plan trust in 2015 to be allocated amongst participating entities.

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

2015	\$ 18,734
2016	\$ 20,618
2017	\$ 22,705
2018	\$ 24,703
2019	\$ 27,146
2020 - 2024	\$ 173,289



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

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

**NOTE 10. EMPLOYEE BENEFIT PLANS (CONTINUED)**

	<u>2014</u>	<u>2013</u>
<b>Weighted average assumptions used to determine end of the year benefit obligations:</b>		
Discount rate	4.20%	5.05%
Rate of compensation increase	3.50%	3.50%
<b>Weighted average assumptions used to determine net periodic pension cost:</b>		
Discount rate	5.05%	3.95%
Expected long-term rate of return on plan assets	7.75%	8.00%
Measurement date	12/31/2014	12/31/2013

**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. Prior to September 1, 2013, the combined primary and buffer limits for healthcare professional and general liability were \$6,000 per occurrence and were insured by Stella Maris Insurance Company, Limited (Stella), a Cayman-domiciled insurer wholly-owned by Catholic Health East (CHE). Subsequent to September 1, 2013, the primary limits were \$20,000 per occurrence for healthcare professional liability and general liability. Professional and general liabilities are insured by Venzke Insurance Company, Ltd. (Venzke), a Cayman-domiciled insurer wholly-owned by Trinity Health. Subsequent to the merger of CHE and Trinity Health, on January 1, 2014, Stella was merged with and into Venzke. 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 financial statement date. The System has independent actuaries estimate the ultimate costs of such unasserted claims, which were discounted at 3% in 2014 and 2013. The System's current portion of liability for unasserted claims at December 31, 2014 and 2013 is \$471 and \$410, respectively, which has been included in accrued expenses. The System's long term portion of liabilities for unpaid and incurred but not reported claims at December 31, 2014 and 2013 is \$63,192 and \$52,186, respectively. The charges to expenses for professional and general liability for 2014 and 2013 approximated \$9,661 and \$7,150, respectively, which has been included in insurance expense. In 2011, the System adopted the principles of insurance claim and recovery accounting for professional and general liabilities. The required claims liability and any anticipated insurance recoveries are to be reported on a gross basis versus the previous practice of netting the recoveries against claims liability. Amounts recognized as insurance receivables related to the claims approximated \$54,241 and \$44,400 at December 31, 2014 and 2013, respectively and is included in other non-current assets. Insurance recoveries are measured on the same basis as the liability subject to the need for a valuation allowance on uncollectible amounts.

## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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#### NOTE 11. INSURANCE ARRANGEMENTS

##### **Workers Compensation Arrangements**

The System's insurance program for workers' compensation has a deductible of \$750 per occurrence in 2014 and \$350 per occurrence in 2013 and prior. 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 2014 and 2013, respectively. The System's current portion of liabilities for unpaid and incurred but not reported claims at December 31, 2014 and 2013 is \$8,472 and \$7,032, 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, 2014 and 2013 is \$60,137 and \$59,111, respectively, and is included in other long-term liabilities.

The charges to expenses for workers' compensation costs approximated \$14,149 and \$11,790 in 2014 and 2013, respectively, which has been included in employee benefits expense. In 2011, the System adopted the principles of insurance claim and recovery accounting for workers' compensation. The required claims liability and any anticipated insurance recoveries are to be reported on a gross basis versus the previous practice of netting the recoveries against claims liability. Amounts recognized as insurance receivables related to the claims approximated \$26,406 and \$30,477 at December 31, 2014 and 2013, 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 \$350 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, 2014 and 2013, was \$8,509 and \$7,991, 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. Management believes it is in compliance with such laws and regulations and no unknown or unasserted claims were known at this time, which could have a material adverse affect on the System's future financial position, results from operations or cash flows.

## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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#### 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>2014</u>	<u>2013</u>
Medicare	36%	34%
Medicaid	16	11
Blue Cross	6	7
Other third-party payors	30	33
Patients/residents	<u>12</u>	<u>15</u>
	<u>100%</u>	<u>100%</u>

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

#### NOTE 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, exchange traded funds, debt securities, mutual funds, and commingled funds. Liabilities measured at fair value on a recurring basis for disclosure only include interest rate swaps and 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 System assesses the inputs used to measure fair value using a three level hierarchy based on the extent to which inputs used in measuring fair value are observable in the market. The fair value hierarchy is as follows:

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

## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

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#### NOTE 14. FAIR VALUE MEASUREMENTS (CONTINUED)

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

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

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

Valuation Methodologies - Exchange-traded securities whose fair value is derived using quoted prices in active markets are classified as Level 1. In instances where quoted market prices are not readily available, fair value is estimated using quoted market prices and/or other market data for the same or comparable instruments and transactions in establishing the prices, discounted cash flow models and other pricing models. These models are primarily industry-standard models that consider various assumptions, including time value and yield curve as well as other relevant economic measures. The inputs to these models 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 2 within the fair value hierarchy.

The System's Level 3 securities are primarily investments in hedge funds. Based on the information available, we believe that the fair values provided by the third-party pricing services and investment fund managers are representative of prices that would be received to sell the assets at December 31, 2014.

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 the System used for instruments recorded at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy:

**Cash and cash equivalents:** The carrying amounts reported in the consolidated balance 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.

**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.

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(in thousands of dollars)

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NOTE 14. FAIR VALUE MEASUREMENTS (CONTINUED)

**Exchange-traded securities:** Exchange traded funds are valued at the NAV of shares held by the System at year end.

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

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

**Commingled Funds:** Commingled funds are developed for investment by institutional investors only and therefore do not require registration with the Securities and Exchange Commission. Commingled funds are recorded at fair value based on either the underlying investments that have a readily determinable market value or based on net asset value, which is calculated using the most recent fund financial statements. Commingled funds are categorized as Level 2 unless they have a redemption restriction greater than 90 days, in which case they are categorized as Level 3.

**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. Hedge funds are categorized as Level 2 unless they have a redemption restriction greater than 90 days, in which case they are categorized as Level 3.

**Equity Method Investments:** The System has a 1% ownership interest in equity method investments which are maintained in a Trinity Health corporate pooled investment program at December 31, 2014.

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

**Long-Term Debt:** The fair value of the based on current rates offered for similar issues with similar security terms and maturities, or estimated using a discount rate that a market participant would demand. The carrying value of the long-term debt approximates fair value as of December 31, 2014 and 2013. Long-term debt would be classified as Level 2 in the fair value hierarchy.

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

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

**NOTE 14. FAIR VALUE MEASUREMENTS (CONTINUED)**

The following tables summarize the fair values, by input hierarchy, of financial instruments measured at fair value on a recurring basis at December 31, 2014:

<b>At December 31, 2014</b>	<b><u>Level I</u></b>	<b><u>Level II</u></b>	<b><u>Level III</u></b>	<b><u>Total</u></b>
<b>Assets limited as to use:</b>				
Cash and cash equivalents	\$ 14,036	\$ 6,338	\$ -	\$ 20,374
Equity securities	11	-	-	11
Government and government agency obligations	5,228	480	-	5,708
Other	<u>-</u>	<u>13</u>	<u>-</u>	<u>13</u>
	<u>\$ 19,275</u>	<u>\$ 6,831</u>	<u>\$ -</u>	<u>\$ 26,106</u>
<b>Investments:</b>				
Cash and cash equivalents	\$ 1,143	\$ 1	\$ -	\$ 1,144
Equity securities	4,550	-	-	4,550
Exchange traded funds	658	-	-	658
Debt securities:				
Government and government agency obligations	1,015	52	-	1,067
Corporate bonds	-	616	-	616
Fixed income	-	-	-	-
Intermediate term bonds	-	309	-	309
Mutual funds	169	-	-	169
Commingled funds	-	116	-	116
Hedge funds	-	106	90	196
Other	<u>-</u>	<u>458</u>	<u>-</u>	<u>458</u>
Equity method investments	<u>-</u>	<u>-</u>	<u>-</u>	<u>236</u>
	<u>\$ 7,535</u>	<u>\$ 1,658</u>	<u>\$ 90</u>	<u>\$ 9,519</u>
Interest rate swap liability	<u>\$ -</u>	<u>\$ 5,853</u>	<u>\$ -</u>	<u>\$ 5,853</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(in thousands of dollars)

NOTE 14. FAIR VALUE MEASUREMENTS (CONTINUED)

At December 31, 2013	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Total</u>
<b>Assets limited as to use:</b>				
Cash and cash equivalents	\$ 10,954	\$ 5,459	\$ -	\$ 16,413
Equity securities	11	-	-	11
Government and government agency obligations	12,711	1,935	-	14,646
Other	<u>-</u>	<u>34</u>	<u>-</u>	<u>34</u>
	<u>\$ 23,676</u>	<u>\$ 7,428</u>	<u>\$ -</u>	<u>\$ 31,104</u>
<b>Investments:</b>				
Cash and cash equivalents	\$ 329	\$ -	\$ -	\$ 329
Equity securities	-	387	-	387
Exchange traded funds	5,671	-	-	5,671
Debt securities:				
Government and government agency obligations	848	-	-	848
Corporate bonds	-	589	-	589
Fixed income	34	49	-	83
Intermediate term bonds	-	380	-	380
Mutual funds	87	-	-	87
Commingled funds	-	-	-	-
Hedge funds	-	-	136	136
Other	<u>-</u>	<u>443</u>	<u>-</u>	<u>443</u>
	<u>\$ 6,969</u>	<u>\$ 1,848</u>	<u>\$ 136</u>	<u>\$ 8,953</u>
Interest rate swap liability	<u>\$ -</u>	<u>\$ 8,956</u>	<u>\$ -</u>	<u>\$ 8,956</u>

Management reports managed and hedge funds as a component of its total investment portfolio; therefore it is included in the accompanying table of investments as of December 31, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Fund of Hedge funds (A)	\$ 90	\$ 113
Real estate (B)	-	10
Private equity (C)	<u>-</u>	<u>13</u>
Total	<u>\$ 90</u>	<u>\$ 136</u>

- (A) The hedge funds have an undetermined life and had varying redemption terms based on quarter ends, semi-annual periods or anniversary dates and required prior written notice ranging from 45 to 95 days. The hedge funds have varying redemption restrictions including 1 to 2 year lock up periods and gate provisions with expiration ranging from 1 to 3.5 years.

The objective of the hedge funds investments is to achieve equity and fixed income-like returns utilizing a conservative strategy with low risk and volatility. All hedge fund investing is done in a fund of funds approach and the use of diversified funds.

- (B) Real estate investments had an unfunded commitment totaling \$2 at December 31, 2013 with remaining lives ranging from 1.5 to 9 years. These investments were sold in 2014.

## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

#### NOTE 14. FAIR VALUE MEASUREMENTS (CONTINUED)

- (C) Private equity investments had an unfunded commitment totaling \$13 at December 31, 2013 and remaining lives ranging from 2.5 to 14.5 years. These investments were sold in 2014.

The objective of the private equity and real estate portfolios was to enhance return while reducing the overall risk through investments in limited partnerships in funds with expertise in these categories. These illiquid, longer term investments sought higher returns but were held at a very low percentage of the investment portfolio.

A roll forward of those managed funds that have been classified as Level 3 within the fair value hierarchy (defined above) is as follows:

	<u>2014</u>	<u>2013</u>
Fair value January 1	\$ 136	\$ 125
Purchases (Settlements)	(52)	11
Realized and unrealized gains (losses)	<u>6</u>	<u>-</u>
Fair value December 31	\$ <u>90</u>	\$ <u>136</u>

#### NOTE 15. RELATED PARTY TRANSACTIONS

Trinity Health charged the System dues for participation in certain programs and governance matters. Amounts charged to expense related to these dues amounted to approximately \$4,284 in both 2014 and 2013, and are included as a component of other expenses.

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

As discussed in Note 11, the System obtains insurance coverage from Trinity Health.

Caritas Medical Arts Building L.L.C. is a joint venture between Sisters of Charity Hospital and Ciminelli Development Company. In 2009, Caritas Medical Arts Building, L.L.C. refinanced its mortgage. As of December 31, 2014, there was \$1,930 of debt outstanding, of which SCH has guaranteed \$643. Per the guaranty agreement, SCH's obligation shall decrease on a dollar for dollar basis as the principal amount of the obligation is paid down.

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. In 2007, Marian Professional Center Associates, L.P. refinanced its mortgage. As of December 31, 2014, there was \$4,754 of debt outstanding, of which MHB has guaranteed \$2,377. Per the guaranty agreement, MHB's obligation shall decrease on a dollar for dollar basis as the principal amount of the obligation is paid down.



## CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

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

#### NOTE 16. DISCONTINUED OPERATIONS

The following subsidiaries, which have been closed in prior years as referenced, have been accounted for in discontinued operations: St. Francis Geriatric Healthcare Services, Inc. (2009) and Nazareth Home of the Franciscan of the Immaculate Conception (2007).

The residual assets (net of inter-company receivables), liabilities and net assets (deficit) of these discontinued operations were \$2,744, \$960 and \$1,784, respectively, as of December 31, 2014 and \$3,105, \$1,095 and \$2,010, respectively, as of December 31, 2013 and are included within their natural classifications in the accompanying consolidated balance sheets.

The System entered into asset purchase agreements and real estate purchase agreements with a third-party, under which the third party would assume control over St. Francis Home of Williamsville, St. Elizabeth's Home and St. Vincent's Home for the Aged. Certain assets and liabilities of SFHW, SEH and SVH are classified as held for sale. As of December 31, 2014 and 2013, SFHW, SEH, and SVH's operating results are reflected as discontinued operations in the consolidated financial statements.

The aggregated loss from discontinued operations for assets held for sale as well as the closed facilities was approximately \$1,972 and \$1,302 in 2014 and 2013, respectively.

Details of the assets held for sale related to the discontinued operations of SFHW, SEH, and SVH at December 31 are provided below:

<b>Assets Held for Sale</b>	<b>2014</b>	<b>2013</b>
Inventories	\$ 16	\$ 17
Property and equipment, net	<u>2,586</u>	<u>2,675</u>
Total assets	<u>\$ 2,602</u>	<u>\$ 2,692</u>

#### NOTE 17. PENDING AFFILIATION AGREEMENT

On August 21, 2014, the System and Ascension Health entered into an Affiliation Agreement for Mount St. Mary's Hospital (a 175 bed community Hospital sponsored by Ascension Health and located in Niagara County, New York) whereby Catholic Health System will replace Ascension Health as the sole corporate member of Mount St. Mary's Hospital as of the closing date, integrating its operations with that of the System. Legal and regulatory approvals have been filed, due diligence has been completed, and management anticipates closing on the transaction on or about July 1, 2015.

#### NOTE 18. FUNCTIONAL EXPENSES

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

	<b>2014</b>	<b>2013</b>
Healthcare services	\$ 691,942	\$ 668,029
General and administrative	<u>220,839</u>	<u>222,290</u>
	<u>\$ 912,781</u>	<u>\$ 890,319</u>

## INDEPENDENT AUDITOR'S REPORT ON ACCOMPANYING SUPPLEMENTARY INFORMATION

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

We have audited the consolidated financial statements of Catholic Health System, Inc. and its subsidiaries (together the System) as of December 31, 2014 and 2013 and for the years then ended and our report thereon appears on page 1 of this document. These audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The Schedule of Net Cost of Providing Care of Persons Living in Poverty and Community Benefit Programs (Schedule of Social Accountability) is the responsibility of management and is provided for purposes of additional analysis of the consolidated financial statements. Such information is unaudited and therefore, we do not express an opinion on the Schedule of Net Cost of Providing Care of Persons Living in Poverty and Community Benefit Programs (Schedule of Social Accountability).

The consolidating information 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 2014 and 2013 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 26, 2015

**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, 2014 and 2013**

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*(in thousands of dollars)*

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

	<u>2014</u>	<u>2013</u>
Charity care	\$ 7,208	\$ 7,970
Cost of community benefit programs	27,435	23,001
Unpaid cost of Medicaid programs	<u>47,427</u>	<u>46,638</u>
	<u>\$ 82,070</u>	<u>\$ 77,609</u>

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2014

ASSETS	Parent	Acute Care Subsidiaries	Long-term Care Subsidiaries	Home Care Subsidiaries	Other Subsidiaries	Eliminations	Total
<b>Current assets:</b>							
Cash and cash equivalents	\$ 31,890	\$ 257,337	\$ 4,966	\$ 22,927	\$ 5,331	\$ -	\$ 322,451
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$25,207	-	116,961	5,983	8,046	723	-	131,713
Other receivables	1,462	7,662	327	-	30	-	9,481
Inventories	-	21,898	56	594	-	-	22,548
Prepaid expenses and other current assets	4,144	1,501	117	169	30	-	5,961
Due from affiliates	64,218	654	1,187	-	-	(66,059)	-
<b>Total current assets</b>	101,714	406,013	12,636	31,736	6,114	(66,059)	492,154
Interest in net assets of related Foundation	-	2,852	91	-	226	(317)	2,852
Assets limited as to use	5,354	6,738	13,222	-	792	-	26,106
Investments	-	9,519	-	-	-	-	9,519
Property and equipment, net	77,225	236,025	6,365	1,193	15,871	-	336,679
Other assets	2,977	78,789	2,904	4,172	605	(7)	89,440
Due from affiliates	2,802	12,010	2,165	1,423	24	(18,424)	-
<b>Total assets</b>	\$ 190,072	\$ 751,946	\$ 37,383	\$ 38,524	\$ 23,632	\$ (84,807)	\$ 956,750
<b>LIABILITIES AND NET ASSETS</b>							
<b>Current liabilities:</b>							
Current portion of long-term obligations	\$ 831	\$ 16,487	\$ 453	\$ 477	\$ 1,602	\$ -	\$ 19,850
Line of credit payable	8,380	-	-	-	-	-	8,380
Accounts payable	4,001	38,375	224	738	1,564	(11)	44,891
Accrued expenses	23,592	30,700	2,754	2,166	727	(203)	59,736
Due to third-party payors	-	34,868	1,665	1,314	564	-	38,411
Due to affiliates	554	44,746	13,233	1,129	2,329	(61,991)	-
<b>Total current liabilities</b>	37,358	165,176	18,329	5,824	6,786	(62,205)	171,268
Long-term obligations, net	57,820	108,371	5,575	994	11,226	-	183,986
Due to affiliates, net	13,883	-	220	2,661	5,514	(22,278)	-
Other long-term liabilities	57,497	373,011	12,372	9,356	3,040	-	455,276
<b>Total liabilities</b>	166,558	646,558	36,496	18,835	26,566	(84,483)	810,530
<b>Net assets (deficit):</b>							
Unrestricted	23,514	99,051	796	19,689	(3,570)	-	139,480
Temporarily restricted	-	6,091	91	-	636	(324)	6,494
Permanently restricted	-	246	-	-	-	-	246
<b>Total net assets (deficit)</b>	23,514	105,388	887	19,689	(2,934)	(324)	146,220
<b>Total liabilities and net assets</b>	\$ 190,072	\$ 751,946	\$ 37,383	\$ 38,524	\$ 23,632	\$ (84,807)	\$ 956,750

CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS

(in thousands of dollars)

For the Year Ended December 31, 2014

	Parent	Acute Care Subsidiaries	Long-term Care Subsidiaries	Home Care Subsidiaries	Other Subsidiaries	Eliminations	Total
<b>Unrestricted revenues other support:</b>							
Net patient/resident service revenue	\$ -	\$ 879,576	\$ 16,179	\$ 61,064	\$ 14,048	\$ (8,878)	\$ 961,989
Provision for bad debts	-	(19,897)	(172)	(1,154)	(69)	-	(21,292)
Net patient/resident service revenue, less provision for bad debts	-	859,679	16,007	59,910	13,979	(8,878)	940,697
Other revenue	127,758	14,270	352	-	4,775	(134,566)	12,589
Net assets released from restrictions	-	277	-	-	-	-	277
<b>Total unrestricted revenues and other support</b>	<b>127,758</b>	<b>874,226</b>	<b>16,359</b>	<b>59,910</b>	<b>18,754</b>	<b>(143,444)</b>	<b>953,563</b>
<b>Expenses:</b>							
Salaries and wages	62,448	365,505	10,256	30,939	2,576	(62,870)	408,854
Employee benefits	16,868	115,078	2,335	7,105	614	(17,948)	124,052
Medical and professional fees	5,034	29,273	199	425	9,911	(4,057)	40,785
Purchased services	25,833	74,265	1,175	1,904	1,515	(34,003)	70,689
Supplies	601	170,078	1,220	7,789	73	(1,656)	178,105
Depreciation and amortization	4,659	38,495	604	541	1,501	(4,659)	41,141
Interest	1,451	7,286	346	181	594	(1,479)	8,379
Insurance	313	10,119	218	115	71	(313)	10,523
Other expenses	10,411	33,212	406	2,765	1,168	(17,709)	30,253
<b>Total expenses</b>	<b>127,618</b>	<b>843,311</b>	<b>16,759</b>	<b>51,764</b>	<b>18,023</b>	<b>(144,694)</b>	<b>912,781</b>
<b>Income (loss) from operations</b>	<b>140</b>	<b>30,915</b>	<b>(400)</b>	<b>8,146</b>	<b>731</b>	<b>1,250</b>	<b>40,782</b>
<b>Nonoperating revenues and losses:</b>							
Investment income	36	1,241	100	-	-	(36)	1,341
Other, net	478	1,030	-	66	(53)	(856)	665
<b>Total nonoperating revenues and losses</b>	<b>514</b>	<b>2,271</b>	<b>100</b>	<b>66</b>	<b>(53)</b>	<b>(892)</b>	<b>2,006</b>
<b>Excess (deficiency) of revenues over expenses</b>	<b>\$ 654</b>	<b>\$ 33,186</b>	<b>\$ (300)</b>	<b>\$ 8,212</b>	<b>\$ 678</b>	<b>\$ 358</b>	<b>\$ 42,788</b>

**CATHOLIC HEALTH SYSTEM, INC. AND SUBSIDIARIES**
**CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (CONTINUED)**

(in thousands of dollars)

For the Year Ended December 31, 2014

	Parent	Acute Care Subsidiaries	Long-term Care Subsidiaries	Home Care Subsidiaries	Other Subsidiaries	Eliminations	Total
<b>Unrestricted net assets:</b>							
Excess (deficiency) of revenues over expenses	\$ 654	\$ 33,186	\$ (300)	\$ 8,212	\$ 678	\$ 358	\$ 42,788
Change in unrealized loss on interest rate swap	-	(2,221)	-	-	(586)	-	(2,807)
Change in pension obligation, other than net periodic cost	(14,031)	(72,337)	(1,834)	(2,081)	(90)	-	(90,373)
Net assets released from restrictions	-	1,147	-	-	50	-	1,197
Grant revenue for capital expenditures	-	168	-	-	-	-	168
Contributions	4,468	-	-	-	-	-	4,468
Other	12,382	(10,401)	(29)	-	503	-	2,455
(Decrease) increase in unrestricted net assets before effects of discontinued operations	3,473	(50,458)	(2,163)	6,131	555	358	(42,104)
Loss from discontinued operations	-	-	(1,614)	-	-	(358)	(1,972)
Increase (decrease) in unrestricted net assets	3,473	(50,458)	(3,777)	6,131	555	-	(44,076)
<b>Temporarily restricted net assets:</b>							
Contributions and other	-	1,058	-	-	66	-	1,124
Investment income	-	3	-	-	-	-	3
Special events revenue, net	-	33	-	-	-	-	33
Change in temporarily restricted interest in related Foundation	-	(1,764)	(2)	-	-	2	(1,764)
Temporarily restricted net assets released from restrictions	-	(1,424)	-	-	(50)	-	(1,474)
Other	(24)	1	-	-	-	-	(23)
(Decrease) increase in temporarily restricted net assets	(24)	(2,093)	(2)	-	16	2	(2,101)
Increase (decrease) in net assets	3,449	(52,551)	(3,779)	6,131	571	2	(46,177)
Net assets, beginning of year	20,065	157,939	4,666	13,558	(3,505)	(326)	192,397
Net assets, end of year	<u>\$ 23,514</u>	<u>\$ 105,388</u>	<u>\$ 887</u>	<u>\$ 19,689</u>	<u>\$ (2,934)</u>	<u>\$ (324)</u>	<u>\$ 146,220</u>

CATHOLIC HEALTH SYSTEM - ACUTE CARE SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2014

ASSETS	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Total
<b>Current assets:</b>				
Cash and cash equivalents	\$ 85,470	\$ 129,670	\$ 42,197	\$ 257,337
Patient/resident accounts receivable, net of allowance for doubtful accounts of \$21,874	53,406	42,154	21,401	116,961
Other receivables	3,017	2,318	2,327	7,662
Inventories	12,956	6,427	2,515	21,898
Prepaid expenses and other current assets	674	529	298	1,501
Due from affiliates	-	654	-	654
<b>Total current assets</b>	<u>155,523</u>	<u>181,752</u>	<u>68,738</u>	<u>406,013</u>
Interest in net assets of related Foundation	-	-	2,852	2,852
Assets limited as to use	339	-	6,399	6,738
Investments	1,547	7,972	-	9,519
Property and equipment, net	98,198	76,272	61,555	236,025
Other assets	34,119	28,581	16,089	78,789
Due from affiliates	228	10,303	1,479	12,010
<b>Total assets</b>	<u>\$ 289,954</u>	<u>\$ 304,880</u>	<u>\$ 157,112</u>	<u>\$ 751,946</u>
<b>LIABILITIES AND NET ASSETS</b>				
<b>Current liabilities:</b>				
Current portion of long-term obligations	\$ 5,611	\$ 4,373	\$ 6,503	\$ 16,487
Accounts payable	16,100	13,444	8,831	38,375
Accrued expenses	12,778	11,831	6,091	30,700
Due to third-party payors	17,482	11,344	6,042	34,868
Due to affiliates	13,805	19,838	11,103	44,746
<b>Total current liabilities</b>	<u>65,776</u>	<u>60,830</u>	<u>38,570</u>	<u>165,176</u>
Long-term obligations, net	45,421	33,833	29,117	108,371
Other long-term liabilities	195,234	123,740	54,037	373,011
<b>Total liabilities</b>	<u>306,431</u>	<u>218,403</u>	<u>121,724</u>	<u>646,558</u>
<b>Net assets (deficit):</b>				
Unrestricted	(17,380)	83,902	32,529	99,051
Temporarily restricted	780	2,452	2,859	6,091
Permanently restricted	123	123	-	246
<b>Total net assets (deficit)</b>	<u>(16,477)</u>	<u>86,477</u>	<u>35,388</u>	<u>105,388</u>
<b>Total liabilities and net assets</b>	<u>\$ 289,954</u>	<u>\$ 304,880</u>	<u>\$ 157,112</u>	<u>\$ 751,946</u>

CATHOLIC HEALTH SYSTEM - ACUTE CARE SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS

(in thousands of dollars)

For the Year Ended December 31, 2014

	Mercy Hospital	Sisters Hospital	Kenmore Mercy Hospital	Total
<b>Unrestricted revenues other support:</b>				
Net patient/resident service revenue	\$ 393,515	\$ 325,127	\$ 160,934	\$ 879,576
Provision for bad debts	(10,081)	(7,320)	(2,496)	(19,897)
Net patient/resident service revenue, less provision for bad debts	383,434	317,807	158,438	859,679
Other revenue	6,292	6,325	1,653	14,270
Net assets released from restrictions	101	176	-	277
<b>Total unrestricted revenues and other support</b>	<b>389,827</b>	<b>324,308</b>	<b>160,091</b>	<b>874,226</b>
<b>Expenses:</b>				
Salaries and wages	155,069	143,199	67,237	365,505
Employee benefits	50,501	44,922	19,655	115,078
Medical and professional fees	12,178	12,706	4,389	29,273
Purchased services	32,128	28,320	13,817	74,265
Supplies	80,512	55,999	33,567	170,078
Depreciation and amortization	16,191	14,860	7,444	38,495
Interest	3,024	2,345	1,917	7,286
Insurance	3,680	5,264	1,175	10,119
Other expenses	16,441	11,600	5,171	33,212
<b>Total expenses</b>	<b>369,724</b>	<b>319,215</b>	<b>154,372</b>	<b>843,311</b>
<b>Income from operations</b>	<b>20,103</b>	<b>5,093</b>	<b>5,719</b>	<b>30,915</b>
<b>Nonoperating revenues and losses:</b>				
Investment income	466	622	153	1,241
Other, net	48	936	46	1,030
<b>Total nonoperating revenues and losses</b>	<b>514</b>	<b>1,558</b>	<b>199</b>	<b>2,271</b>
<b>Excess of revenues over expenses</b>	<b>\$ 20,617</b>	<b>\$ 6,651</b>	<b>\$ 5,918</b>	<b>\$ 33,186</b>



**CATHOLIC HEALTH SYSTEM - ACUTE CARE SUBSIDIARIES**

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

(in thousands of dollars)

For the Year Ended December 31, 2014

	<b>Mercy Hospital</b>	<b>Sisters Hospital</b>	<b>Kenmore Mercy Hospital</b>	<b>Total</b>
<b>Unrestricted net assets:</b>				
Excess of revenues over expenses	\$ 20,617	\$ 6,651	\$ 5,918	\$ 33,186
Change in unrealized gain on interest rate swap	(1,961)	(312)	52	(2,221)
Change in pension obligation, other than net periodic cost	(36,483)	(28,096)	(7,758)	(72,337)
Net assets released from restrictions	591	556	-	1,147
Grant revenue for capital expenditures	168	-	-	168
Other	(8,198)	(5,334)	3,131	(10,401)
Decrease in unrestricted net assets	(25,266)	(26,535)	1,343	(50,458)
<b>Temporarily restricted net assets:</b>				
Contributions and other	436	622	-	1,058
Investment income	3	-	-	3
Special events revenue, net	-	33	-	33
Change in temporarily restricted interest in related Foundation	-	-	(1,764)	(1,764)
Temporarily restricted net assets released from restrictions	(692)	(732)	-	(1,424)
Other	-	-	1	1
Decrease in temporarily restricted net assets	(253)	(77)	(1,763)	(2,093)
Decrease in net assets	(25,519)	(26,612)	(420)	(52,551)
Net assets, beginning of year	9,042	113,089	35,808	157,939
Net (deficit) assets, end of year	<u>\$ (16,477)</u>	<u>\$ 86,477</u>	<u>\$ 35,388</u>	<u>\$ 105,388</u>

CATHOLIC HEALTH SYSTEM - LONG-TERM CARE SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2014

	Discontinued Operations						
ASSETS	Father Baker Manor	St. Francis Geriatric	St. Francis Home	St. Elizabeth's Home	St. Vincent's Home	Nazareth Home	Total
<b>Current assets:</b>							
Cash and cash equivalents	\$ 1,226	\$ 1,299	\$ 1,495	\$ 49	\$ 15	\$ 882	\$ 4,966
Resident accounts receivable, net of allowance for doubtful accounts of \$1,799	2,579	121	2,778	400	105	-	5,983
Other receivables	154	-	173	-	-	-	327
Inventories	40	-	16	-	-	-	56
Prepaid expenses and other current assets	88	-	14	11	4	-	117
Due from affiliates	49	-	16	-	-	1,122	1,187
<b>Total current assets</b>	<u>4,136</u>	<u>1,420</u>	<u>4,492</u>	<u>460</u>	<u>124</u>	<u>2,004</u>	<u>12,636</u>
Interest in net assets of related Foundations	23	-	68	-	-	-	91
Assets limited as to use	12,099	-	1,123	-	-	-	13,222
Property and equipment, net	3,344	-	1,926	529	131	435	6,365
Other assets	2,411	7	361	75	50	-	2,904
Due from affiliates	-	-	-	2,165	-	-	2,165
<b>Total assets</b>	<u>\$ 22,013</u>	<u>\$ 1,427</u>	<u>\$ 7,970</u>	<u>\$ 3,229</u>	<u>\$ 305</u>	<u>\$ 2,439</u>	<u>\$ 37,383</u>
<b>LIABILITIES AND NET ASSETS</b>							
<b>Current liabilities:</b>							
Current portion of long-term obligations	\$ 453	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 453
Accounts payable	74	-	59	78	12	1	224
Accrued expenses	1,179	7	1,250	205	88	25	2,754
Due to third-party payors	1,002	-	663	-	-	-	1,665
Due to affiliates	1,804	-	7,517	2,843	1,069	-	13,233
<b>Total current liabilities</b>	<u>4,512</u>	<u>7</u>	<u>9,489</u>	<u>3,126</u>	<u>1,169</u>	<u>26</u>	<u>18,329</u>
Long-term obligations, net	5,575	-	-	-	-	-	5,575
Due to affiliates, net	-	-	-	-	-	220	220
Other long-term liabilities	4,987	-	4,870	1,240	568	707	12,372
<b>Total liabilities</b>	<u>15,074</u>	<u>7</u>	<u>14,359</u>	<u>4,366</u>	<u>1,737</u>	<u>953</u>	<u>36,496</u>
<b>Net assets (deficit):</b>							
Unrestricted	6,916	1,420	(6,457)	(1,137)	(1,432)	1,486	796
Temporarily restricted	23	-	68	-	-	-	91
<b>Total net assets (deficit)</b>	<u>6,939</u>	<u>1,420</u>	<u>(6,389)</u>	<u>(1,137)</u>	<u>(1,432)</u>	<u>1,486</u>	<u>887</u>
<b>Total liabilities and net assets</b>	<u>\$ 22,013</u>	<u>\$ 1,427</u>	<u>\$ 7,970</u>	<u>\$ 3,229</u>	<u>\$ 305</u>	<u>\$ 2,439</u>	<u>\$ 37,383</u>

CATHOLIC HEALTH SYSTEM - LONG-TERM CARE SUBSIDIARIES

CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS

(in thousands of dollars)

For the Year Ended December 31, 2014

	Discontinued Operations						
	Father Baker Manor	St. Francis Geriatric	St. Francis Home	St. Elizabeth's Home	St. Vincent's Home	Nazareth Home	Total
<b>Unrestricted revenues other support:</b>							
Net resident service revenue	\$ 16,179	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 16,179
Provision for bad debts	(172)	-	-	-	-	-	(172)
Net resident service revenue, less provision for bad debts	16,007	-	-	-	-	-	16,007
Other revenue	69	-	-	-	-	283	352
<b>Total unrestricted revenues and other support</b>	16,076	-	-	-	-	283	16,359
<b>Expenses:</b>							
Salaries and wages	10,189	-	-	-	-	67	10,256
Employee benefits	2,312	-	-	-	-	23	2,335
Medical and professional fees	199	-	-	-	-	-	199
Purchased services	1,075	-	-	-	-	100	1,175
Supplies	1,218	-	-	-	-	2	1,220
Depreciation and amortization	540	-	-	-	-	64	604
Interest	346	-	-	-	-	-	346
Insurance	217	-	-	-	-	1	218
Other expenses	380	-	-	-	-	26	406
<b>Total expenses</b>	16,476	-	-	-	-	283	16,759
<b>Loss from operations</b>	(400)	-	-	-	-	-	(400)
<b>Nonoperating revenues and losses:</b>							
Investment income	100	-	-	-	-	-	100
<b>Total nonoperating revenues and losses</b>	100	-	-	-	-	-	100
<b>Deficiency of revenues over expenses</b>	<u>\$ (300)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (300)</u>
<b>Unrestricted net assets:</b>							
Deficiency of revenues over expenses	\$ (300)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (300)
Change in pension obligation, other than net periodic cost	(659)	-	(878)	(212)	(85)	-	(1,834)
Other	(30)	73	-	-	-	(72)	(29)
(Decrease) increase in unrestricted net assets before effects of discontinued operations	(989)	73	(878)	(212)	(85)	(72)	(2,163)
Gain (loss) from discontinued operations	-	229	(722)	(766)	(355)	-	(1,614)
Increase (decrease) unrestricted net assets	(989)	302	(1,600)	(978)	(440)	(72)	(3,777)
<b>Temporarily restricted net assets:</b>							
Change in temporarily restricted interest in related foundations	4	-	(6)	-	-	-	(2)
Increase decrease in temporarily restricted net assets	4	-	(6)	-	-	-	(2)
(Decrease) increase in net assets (deficit)	(985)	302	(1,606)	(978)	(440)	(72)	(3,779)
Net assets (deficit), beginning of year	7,924	1,118	(4,783)	(159)	(992)	1,558	4,666
Net assets (deficit), end of year	<u>\$ 6,939</u>	<u>\$ 1,420</u>	<u>\$ (6,389)</u>	<u>\$ (1,137)</u>	<u>\$ (1,432)</u>	<u>\$ 1,486</u>	<u>\$ 887</u>

**CATHOLIC HEALTH SYSTEM - HOME CARE SUBSIDIARIES**

**CONSOLIDATING BALANCE SHEET**

(in thousands of dollars)

December 31, 2014

	Mercy Home Care	McAuley Seton Home Care	Infusion Pharmacy	Total
<b>ASSETS</b>				
<b>Current assets:</b>				
Cash and cash equivalents	\$ 1,593	\$ 19,459	\$ 1,875	\$ 22,927
Patient accounts receivable, net of allowance for doubtful accounts of \$1,417	290	6,652	1,104	8,046
Inventories	-	36	558	594
Prepaid expenses and other current assets	30	116	23	169
<b>Total current assets</b>	<u>1,913</u>	<u>26,263</u>	<u>3,560</u>	<u>31,736</u>
Property and equipment, net	-	1,082	111	1,193
Other assets	615	3,148	409	4,172
Due from affiliates	386	857	180	1,423
<b>Total assets</b>	<u>\$ 2,914</u>	<u>\$ 31,350</u>	<u>\$ 4,260</u>	<u>\$ 38,524</u>
<b>LIABILITIES AND NET ASSETS</b>				
<b>Current liabilities:</b>				
Current portion of long-term obligations	\$ -	477	-	\$ 477
Accounts payable	643	76	19	738
Accrued expenses	-	1,895	271	2,166
Due to third-party payors	45	1,198	71	1,314
Due to affiliates	1	265	863	1,129
<b>Total current liabilities</b>	<u>689</u>	<u>3,911</u>	<u>1,224</u>	<u>5,824</u>
Long-term obligations, net	-	994	-	994
Due to affiliates, net	-	2,661	-	2,661
Other long-term liabilities	2,512	6,580	264	9,356
<b>Total liabilities</b>	<u>3,201</u>	<u>14,146</u>	<u>1,488</u>	<u>18,835</u>
<b>Net assets (deficit):</b>				
Unrestricted	(287)	17,204	2,772	19,689
<b>Total liabilities and net assets</b>	<u>\$ 2,914</u>	<u>\$ 31,350</u>	<u>\$ 4,260</u>	<u>\$ 38,524</u>

**CATHOLIC HEALTH SYSTEM - HOME CARE SUBSIDIARIES**

**CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS**

(in thousands of dollars)

For the Year Ended December 31, 2014

	<b>Mercy Home Care</b>	<b>McAuley Seton Home Care</b>	<b>Infusion Pharmacy</b>	<b>Total</b>
<b>Unrestricted revenues other support:</b>				
Net resident service revenue	\$ 7,229	\$ 43,403	\$ 10,432	\$ 61,064
Provision for bad debts	(21)	(907)	(226)	(1,154)
<b>Total unrestricted revenues and other support</b>	<b>7,208</b>	<b>42,496</b>	<b>10,206</b>	<b>59,910</b>
<b>Expenses:</b>				
Salaries and wages	4,668	24,247	2,024	30,939
Employee benefits	1,476	5,221	408	7,105
Medical and professional fees	-	380	45	425
Purchased services	407	1,215	282	1,904
Supplies	29	1,308	6,452	7,789
Depreciation and amortization	26	461	54	541
Interest	18	150	13	181
Insurance	46	63	6	115
Other expenses	415	1,925	425	2,765
<b>Total expenses</b>	<b>7,085</b>	<b>34,970</b>	<b>9,709</b>	<b>51,764</b>
<b>Income from operations</b>	<b>123</b>	<b>7,526</b>	<b>497</b>	<b>8,146</b>
<b>Nonoperating revenue and losses:</b>				
Other	32	28	6	66
<b>Total nonoperating revenue and losses</b>	<b>32</b>	<b>28</b>	<b>6</b>	<b>66</b>
<b>Excess revenue over expenses</b>	<b>\$ 155</b>	<b>\$ 7,554</b>	<b>\$ 503</b>	<b>\$ 8,212</b>
<b>Unrestricted net assets:</b>				
Excess revenue over expenses	\$ 155	\$ 7,554	\$ 503	\$ 8,212
Change in pension obligation, other than net periodic cost	(271)	(1,758)	(52)	(2,081)
(Decrease) increase in net assets	(116)	5,796	451	6,131
Net (deficit) asset, beginning of year	(171)	11,408	2,321	13,558
Net (deficit) assets, end of year	<b>\$ (287)</b>	<b>\$ 17,204</b>	<b>\$ 2,772</b>	<b>\$ 19,689</b>

CATHOLIC HEALTH SYSTEM - OTHER SUBSIDIARIES

CONSOLIDATING BALANCE SHEET

(in thousands of dollars)

December 31, 2014

ASSETS	OLV Renaissance Corp.	Continuing Care Foundation	LIFE	Trinity	Total
<b>Current assets:</b>					
Cash and cash equivalents	\$ 854	\$ 442	\$ 3,932	\$ 103	\$ 5,331
Patient accounts receivable, net of allowance for doubtful accounts of \$117	-	-	711	12	723
Other receivables	-	30	-	-	30
Prepaid expenses and other current assets	29	-	1	-	30
<b>Total current assets</b>	<u>883</u>	<u>472</u>	<u>4,644</u>	<u>115</u>	<u>6,114</u>
Interest in net assets of related Foundations	226	-	-	-	226
Assets limited as to use	259	-	533	-	792
Property and equipment, net	15,739	1	131	-	15,871
Other assets	596	-	9	-	605
Due from affiliates	24	-	-	-	24
<b>Total assets</b>	<u>\$ 17,727</u>	<u>\$ 473</u>	<u>\$ 5,317</u>	<u>\$ 115</u>	<u>\$ 23,632</u>
<b>LIABILITIES AND NET ASSETS</b>					
<b>Current liabilities:</b>					
Current portion of long-term obligations	1,602	\$ -	\$ -	\$ -	\$ 1,602
Accounts payable	-	-	1,553	11	1,564
Accrued expenses	496	203	-	28	727
Due to third-party payors	-	-	564	-	564
Due to affiliates	-	-	614	1,715	2,329
<b>Total current liabilities</b>	<u>2,098</u>	<u>203</u>	<u>2,731</u>	<u>1,754</u>	<u>6,786</u>
Long-term obligations, net	11,226	-	-	-	11,226
Due to affiliates, net	5,514	-	-	-	5,514
Other long-term liabilities	2,738	-	302	-	3,040
<b>Total liabilities</b>	<u>21,576</u>	<u>203</u>	<u>3,033</u>	<u>1,754</u>	<u>26,566</u>
<b>Net assets (deficit):</b>					
Unrestricted	(4,075)	(140)	2,284	(1,639)	(3,570)
Temporarily restricted	226	410	-	-	636
<b>Total net (deficit) assets</b>	<u>(3,849)</u>	<u>270</u>	<u>2,284</u>	<u>(1,639)</u>	<u>(2,934)</u>
<b>Total liabilities and net assets</b>	<u>\$ 17,727</u>	<u>\$ 473</u>	<u>\$ 5,317</u>	<u>\$ 115</u>	<u>\$ 23,632</u>

**CATHOLIC HEALTH SYSTEM - OTHER SUBSIDIARIES**

**CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS**

(in thousands of dollars)

For the Year Ended December 31, 2014

	OLV Renaissance Corp.	Continuing Care Foundation	LIFE	Trinity	Total
<b>Unrestricted revenues other support:</b>					
Net patient/resident service revenue	\$ -	\$ -	\$ 13,302	\$ 746	\$ 14,048
Provision for bad debts	-	-	(44)	(25)	(69)
Net patient/resident service revenue, less provision for bad debt	-	-	13,258	721	13,979
Other revenue	4,445	53	-	277	4,775
<b>Total unrestricted revenues and other support</b>	<u>4,445</u>	<u>53</u>	<u>13,258</u>	<u>998</u>	<u>18,754</u>
<b>Expenses:</b>					
Salaries and wages	275	-	1,578	723	2,576
Employee benefits	92	-	313	209	614
Medical and professional fees	48	-	9,773	90	9,911
Purchased services	1,446	-	-	69	1,515
Supplies	44	-	-	29	73
Depreciation and amortization	1,443	-	37	21	1,501
Interest	566	-	-	28	594
Insurance	56	-	-	15	71
Other expenses	26	109	941	92	1,168
<b>Total expenses</b>	<u>3,996</u>	<u>109</u>	<u>12,642</u>	<u>1,276</u>	<u>18,023</u>
<b>Income (loss) from operations</b>	449	(56)	616	(278)	731
<b>Nonoperating revenue and losses:</b>					
Other, net	(5)	-	(4)	(44)	(53)
<b>Total nonoperating revenue and losses</b>	<u>(5)</u>	<u>-</u>	<u>(4)</u>	<u>(44)</u>	<u>(53)</u>
<b>Excess (deficiency) of revenues over expenses</b>	<u>\$ 444</u>	<u>\$ (56)</u>	<u>\$ 612</u>	<u>\$ (322)</u>	<u>\$ 678</u>

**CATHOLIC HEALTH SYSTEM - OTHER SUBSIDIARIES**

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

(in thousands of dollars)

For the Year Ended December 31, 2014

	OLV Renaissance Corp.	Continuing Care Foundation	LIFE	Trinity	Total
<b>Unrestricted net assets:</b>					
Excess (deficiency) of revenues over expenses	\$ 444	\$ (56)	\$ 612	\$ (322)	\$ 678
Change in unrealized gain on interest rate swap	(586)	-	-	-	(586)
Change in pension obligation, other than net periodic cost	-	-	(90)	-	(90)
Net assets released from restrictions	-	50	-	-	50
Other	551	(48)	-	-	503
Increase (decrease) unrestricted net assets	409	(54)	522	(322)	555
<b>Temporarily restricted net assets:</b>					
Contributions and other	-	66	-	-	66
Temporarily restricted net assets released from restrictions	-	(50)	-	-	(50)
Increase in temporarily restricted net assets	-	16	-	-	16
Increase (decrease) in net assets	409	(38)	522	(322)	571
Net (deficit) assets, beginning of year	(4,258)	308	1,762	(1,317)	(3,505)
Net (deficit) assets, end of year	<u>\$ (3,849)</u>	<u>\$ 270</u>	<u>\$ 2,284</u>	<u>\$ (1,639)</u>	<u>\$ (2,934)</u>