Attachment 7

Financial Statement for CHI for the Years Ending June 30, 2012 and 2011

Consolidated Financial Statements and Supplemental Information

Catholic Health Initiatives
Years Ended June 30, 2012 and 2011
With Report of Independent Auditors

Ernst & Young LLP

ERNST & YOUNG

Catholic Health Initiatives
Consolidated Financial Statements
and Supplemental Information

Years Ended June 30, 2012 and 2011

Contents

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Report of Independent Auditors

Board of Stewardship Trustees
Catholic Health Initiatives

We have audited the accompanying consolidated balance sheets of Catholic Health Initiatives (CHI) as of June 30, 2012 and 2011, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of CHI's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of Alegent Health-Bergan Mercy Health System, a wholly sponsored direct affiliate of CHI, which statements reflect total assets of $716 million and $708 million as of June 30, 2012 and 2011, respectively, and total revenues of $452 million and $466 million, respectively, for the years then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Alegent Health-Bergan Mercy Health System, is based solely on the report of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of CHI's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of CHI's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Catholic Health Initiatives at June 30, 2012 and 2011, and the consolidated results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.

Ernst + Young LLP

September 18, 2012

Catholic Health Initiatives
Consolidated Balance Sheets

	June 30 2012	June 30 2011
	(In Thousands)	
Assets		
Current assets:		
Cash and equivalents	**$ 403,972**	$ 449,674
Net patient accounts receivable, less allowances of $687,631 and $636,815 in 2012 and 2011, respectively	**1,353,928**	1,090,882
Other accounts receivable	**116,607**	105,361
Current portion of investments and assets limited as to use	**1,901**	19,554
Inventories	**185,571**	163,387
Assets held for sale	**474,990**	497,545
Prepaid and other	**87,179**	68,214
Total current assets	**2,624,148**	2,394,617
Investments and assets limited as to use:		
Internally designated for capital and other funds	**4,588,519**	4,617,181
Mission and Ministry Fund	**110,918**	117,832
Capital Resource Pool	**320,218**	268,690
Held by trustees	**228**	229
Held for insurance purposes	**745,127**	739,071
Restricted by donors	**171,123**	146,569
Total investments and assets limited as to use	**5,936,133**	5,889,572
Property and equipment, net	**5,347,475**	4,546,748
Deferred financing costs	**28,717**	23,699
Investments in unconsolidated organizations	**307,918**	343,640
Intangible assets and goodwill, net	**162,880**	55,617
Notes receivable and other	**605,113**	639,466
Total assets	**$ 15,012,384**	$ 13,893,359

Continued on following page

Catholic Health Initiatives
Consolidated Balance Sheets (continued)

	June 30 2012	June 30 2011
	(In Thousands)	
Liabilities and net assets		
Current liabilities:		
Compensation and benefits	**$ 418,597**	$ 384,095
Third-party liabilities	**76,660**	62,034
Accounts payable and accrued expenses	**718,897**	585,750
Liabilities held for sale	**103,633**	104,611
Variable-rate debt with self liquidity	**321,455**	163,400
Commercial paper and current portion of debt	**643,083**	836,201
Total current liabilities	**2,282,325**	2,136,091
Pension liability	**892,820**	315,523
Self-insured reserves and claims	**513,584**	448,940
Other liabilities	**236,763**	215,231
Long-term debt	**3,778,709**	3,135,225
Total liabilities	**7,704,201**	6,251,010
Net assets:		
Net assets attributable to CHI	**6,922,466**	7,448,161
Net assets attributable to noncontrolling interests	**180,863**	8,967
Unrestricted	**7,103,329**	7,457,128
Temporarily restricted	**136,821**	122,795
Permanently restricted	**68,033**	62,426
Total net assets	**7,308,183**	7,642,349
Total liabilities and net assets	**$ 15,012,384**	$ 13,893,359

See accompanying notes.

Catholic Health Initiatives
Consolidated Statements of Operations

	Year Ended June 30 2012	2011
	(In Thousands)	
Revenues:		
Net patient services	$ **9,223,859**	$ 8,316,852
Nonpatient:		
Donations	**27,968**	23,425
Changes in equity of unconsolidated organizations	**22,934**	33,835
Investment income used in operations	**37,169**	30,475
Other	**532,341**	431,863
Total nonpatient revenues	**620,412**	519,598
Total operating revenues	**9,844,271**	8,836,450
Expenses:		
Salaries and wages	**3,776,388**	3,339,440
Employee benefits	**749,055**	700,293
Purchased services, medical professional fees, consulting and legal	**925,427**	750,323
Supplies	**1,566,367**	1,431,037
Bad debts	**709,654**	691,218
Utilities	**120,205**	105,777
Rentals, leases, maintenance and insurance	**523,076**	462,786
Depreciation and amortization	**473,773**	434,652
Interest	**129,648**	117,179
Other	**511,125**	464,615
Total operating expenses before restructuring, impairment and other losses	**9,484,718**	8,497,320
Income from operations before restructuring, impairment and other losses	**359,553**	339,130
Restructuring, impairment and other losses	**47,735**	20,363
Income from operations	**311,818**	318,767
Nonoperating gains (losses):		
Investment income, net	**19,829**	803,554
Loss on defeasance of bonds	**(70,555)**	–
Realized and unrealized losses on interest rate swaps	**(153,411)**	(4,870)
Other nonoperating (losses) gains	**(12,215)**	16,462
Total nonoperating (losses) gains	**(216,352)**	815,146
Excess of revenues over expenses	$ **95,466**	$ 1,133,913
Excess of revenues over expenses attributable to noncontrolling interest	$ **537**	$ 3,298
Excess of revenues over expenses attributable to CHI	$ **94,929**	$ 1,130,615

Community benefit provided to the poor and broader community and the unpaid cost of Medicare (unaudited) was $1.1 billion in each of 2012 and 2011 (see Note 2 of the accompanying notes).

Catholic Health Initiatives
Consolidated Statements of Changes in Net Assets
(In Thousands)

	Unrestricted Net Assets					
	Attributable to CHI	Attributable to Noncontrolling Interests	Total	Temporarily Restricted Net Assets	Permanently Restricted Net Assets	Total Net Assets
Balances, June 30, 2010	$ 5,875,377	$ 8,204	$ 5,883,581	$ 112,207	$ 53,408	$ 6,049,196
Excess of revenues over expenses	1,130,615	3,298	1,133,913	–	–	1,133,913
Net loss from discontinued operations	(13,231)	–	(13,231)	–	–	(13,231)
Decrease in pension liability	404,768	–	404,768	–	–	404,768
Temporarily and permanently restricted contributions	–	–	–	44,502	3,803	48,305
Net assets released from restriction for capital	26,270	–	26,270	(26,270)	–	–
Net assets released from restriction for operations	–	–	–	(13,868)	–	(13,868)
Investment income	–	–	–	7,718	1,737	9,455
Other changes in net assets	24,362	(2,535)	21,827	(1,494)	3,478	23,811
Net increase in net assets	1,572,784	763	1,573,547	10,588	9,018	1,593,153
Balances, June 30, 2011	7,448,161	8,967	7,457,128	122,795	62,426	7,642,349
Excess of revenues over expenses	**94,929**	**537**	**95,466**	–	–	**95,466**
Net loss from discontinued operations	**(45,177)**	–	**(45,177)**	–	–	**(45,177)**
Increase in pension liability	**(618,141)**	**(878)**	**(619,019)**	–	–	**(619,019)**
Temporarily and permanently restricted contributions	–	–	–	**39,117**	**(122)**	**38,995**
Net assets released from restriction for capital	**18,119**	–	**18,119**	**(18,119)**	–	–
Net assets released from restriction for operations	–	–	–	**(19,689)**	–	**(19,689)**
Investment income	**232**	–	**232**	**1,007**	**47**	**1,286**
KentuckyOne Health noncontrolling interest	–	**181,551**	**181,551**	–	–	**181,551**
Other changes in net assets	**24,343**	**(9,314)**	**15,029**	**11,710**	**5,682**	**32,421**
Net (decrease) increase in net assets	**(525,695)**	**171,896**	**(353,799)**	**14,026**	**5,607**	**(334,166)**
Balances, June 30, 2012	**$ 6,922,466**	**$ 180,863**	**$ 7,103,329**	**$ 136,821**	**$ 68,033**	**$ 7,308,183**

See accompanying notes.

Catholic Health Initiatives
Consolidated Statements of Cash Flows

	Year Ended June 30 2012	2011
	(In Thousands)	
Operating activities		
(Decrease) increase in net assets	$ (334,166)	$ 1,593,153
Adjustments to reconcile (decrease) increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	473,773	434,652
Provision for bad debts	709,654	691,218
Changes in equity of unconsolidated organizations	(22,934)	(33,835)
Net gains on sales of facilities and investments in unconsolidated organizations	(57,383)	(3,540)
Noncash operating expenses related to restructuring, impairment and other losses	16,024	9,644
Loss on defeasance of bonds	70,555	–
Decrease (increase) in fair value of interest rate swaps	121,949	(26,876)
Increase (decrease) in unfunded pension liability	601,990	(404,768)
Net changes in current assets and liabilities:		
Net patient and other accounts receivable	(883,703)	(710,994)
Other current assets	(10,992)	(20,318)
Current liabilities	2,771	(40,549)
Noncontrolling equity of acquisition of JHSMH	(181,551)	–
Other changes	(75,749)	21,452
Net cash provided by operating activities before net change in investments and assets limited as to use	430,238	1,509,239
Net decrease (increase) in investments and assets limited as to use	286,773	(729,424)
Net cash provided by operating activities	717,011	779,815
Investing activities		
Purchases of property, equipment and other capital assets	(861,034)	(761,713)
Purchase of CHS, net of cash acquired	–	(35,533)
Purchase of NHH, net of cash acquired	(130,982)	–
Purchase of JHSMH, net of cash acquired	(28,685)	–
Net cash proceeds from asset sales	22,159	4,992
Distributions from investments in unconsolidated organizations	40,214	44,748
Cash from net repayments (issuances) of notes receivable	29,740	(4,635)
Other changes	21,373	6,889
Net cash used in investing activities	(907,215)	(745,252)
Financing activities		
Proceeds from bank loan and issuance of long-term debt	1,126,463	276,598
Net costs associated with issuance of long-term debt	(8,855)	–
Repayment of long-term debt	(973,106)	(355,974)
Net cash provided by (used in) financing activities	144,502	(79,376)
Decrease in cash and equivalents	(45,702)	(44,813)
Cash and equivalents at beginning of year	449,674	494,487
Cash and equivalents at end of year	$ 403,972	$ 449,674
Supplemental disclosures of cash flow information		
Cash paid during the year for interest, including amounts capitalized	$ 151,837	$ 149,822

See accompanying notes.

1. Summary of Significant Accounting Policies

Organization

Catholic Health Initiatives (CHI), established in 1996, is a tax-exempt Colorado corporation and has been granted an exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code. CHI sponsors market-based organizations (MBOs) and other facilities in 19 states, including 74 acute-care hospitals, of which 21 are designated as critical access hospitals by the Medicare program, two community health service organizations (CHSOs), two accredited nursing colleges, home health agencies, and 40 other sites including long-term care, assisted living and residential facilities. CHI also has an offshore captive insurance company, First Initiatives Insurance, Ltd. (FIIL).

The mission of CHI is to nurture the healing ministry of the Church, bringing it new life, energy and viability in the 21st century. CHI is committed to fidelity to the Gospel, with emphasis on human dignity and social justice in the creation of healthier communities. CHI is sponsored by a lay-religious partnership, calling on other Catholic sponsors and systems to unite to ensure the future of Catholic health care.

Principles of Consolidation

CHI consolidates all direct affiliates in which it has sole corporate membership or ownership (Direct Affiliates) and all entities in which it has greater than 50% equity interest with commensurate control. All significant intercompany accounts and transactions are eliminated in consolidation.

Fair Value of Financial Instruments

Financial instruments consist primarily of cash and equivalents, patient accounts receivable, notes receivable, accounts payable and long-term debt. The carrying amounts reported in the consolidated balance sheets for these items approximate fair value.

Cash and Equivalents

Cash and equivalents include all deposits with banks and investments in interest-bearing securities with maturity dates of 90 days or less from the date of purchase. In addition, cash and equivalents include deposits in short-term funds held by professional managers. The funds generally invest in high-quality, short-term debt securities, including U.S. government securities, securities issued by domestic and foreign banks, such as certificates of deposit and bankers'

1. Summary of Significant Accounting Policies (continued)

acceptances, repurchase agreements, asset-backed securities, high-grade commercial paper and corporate short-term obligations.

Net Patient Accounts Receivable and Net Patient Services Revenues

Net patient accounts receivable has been adjusted to the estimated amounts expected to be collected. These estimated amounts are subject to further adjustments upon review by third-party payors.

The provision for bad debts is based upon management's assessment of historical and expected net collections, taking into consideration historical business and economic conditions, trends in health care coverage and other collection indicators. Management routinely assesses the adequacy of the allowances for uncollectible accounts based upon historical write-off experience by payor category. The results of these reviews are used to modify, as necessary, the provision for bad debts and to establish appropriate allowances for uncollectible net patient accounts receivable. After satisfaction of amounts due from insurance, CHI follows established guidelines for placing certain patient balances with collection agencies, subject to the terms of certain restrictions on collection efforts as determined by each facility.

CHI records net patient services revenues in the period in which services are performed. CHI has agreements with third-party payors that provide for payments at amounts different from its established rates. The basis for payment under these agreements includes prospectively determined rates, cost reimbursement and negotiated discounts from established rates and per diem payments.

Net patient services revenues are reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments due to future audits, reviews and investigations, and excluding estimated amounts considered uncollectible. The differences between the estimated and actual adjustments are recorded as part of net patient services revenues in future periods, as the amounts become known, or as years are no longer subject to such audits, reviews and investigations.

Investments and Assets Limited as to Use

Investments and assets limited as to use include assets set aside by CHI for future long-term purposes, including capital improvements and self-insurance. In addition, assets limited as to use include amounts held by trustees under bond indenture agreements, amounts contributed by donors with stipulated restrictions and amounts held for Mission and Ministry programs.

1. Summary of Significant Accounting Policies (continued)

CHI has designated its investment portfolio as trading. Accordingly, unrealized gains and losses on marketable securities are reported within excess of revenues over expenses. In addition, cash flows from the purchases and sales of marketable securities are reported as a component of operating activities in the accompanying consolidated statements of cash flows.

Direct investments in equity securities with readily determinable fair values and all direct investments in debt securities have been measured at fair value in the accompanying consolidated balance sheets. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in excess of revenues over expenses unless the income or loss is restricted by donor or law.

Investments in limited partnerships and limited liability companies are recorded using the equity method of accounting (which approximates fair value as determined by the net asset values of the related unitized interests) with the related changes in value in earnings reported as investment income in the accompanying consolidated financial statements.

Inventories

Inventories, primarily consisting of pharmacy drugs, and medical and surgical supplies, are stated at lower of cost (first-in, first-out method) or market.

Assets and Liabilities Held for Sale

A long-lived asset or disposal group of assets and liabilities that is expected to be sold within one year is classified as held for sale. For long-lived assets held for sale, an impairment charge is recorded if the carrying amount of the asset exceeds its fair value less costs to sell. Such valuations include estimates of fair values generally based upon discounted cash flows and incremental direct costs to transact a sale.

Property and Equipment

Property and equipment are stated at historical cost or, if donated or impaired, at fair value at the date of receipt or impairment. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. For property and equipment under capital lease, amortization is determined over the shorter period of the lease term or the estimated useful life of the property and equipment. Interest cost incurred during the period of construction of major capital projects is capitalized as a component of the cost of acquiring those assets. Capitalized interest of $14.6 million and $14.7 million was recorded in 2012 and 2011, respectively.

1. Summary of Significant Accounting Policies (continued)

Costs incurred in the development and installation of internal-use software are typically expensed if they are incurred in the preliminary project stage or post-implementation stage, while certain costs are capitalized if incurred during the application development stage. Amounts capitalized are amortized over the useful life of the developed asset following project completion.

Investments in Unconsolidated Organizations

Investments in unconsolidated organizations are accounted for under the cost or equity method of accounting, as appropriate, based on the relative percentage of ownership or degree of influence over that organization. The equity income or loss on these investments is recorded in the consolidated statements of operations as changes in equity of unconsolidated organizations.

Intangible Assets and Goodwill

Intangible assets are amortized over the estimated useful life of each class of amortizable asset using the straight-line method. Amortization expense of $4.9 million and $6.1 million was recorded in 2012 and 2011, respectively. Intangible assets increased $20.8 million in 2012 due to the Nebraska Heart Hospital and Nebraska Heart Institute acquisition discussed in Note 4, *Acquisitions and Divestitures*, and the acquisition of a cardiology practice in Tacoma.

Goodwill is not amortized but is subject to annual impairment tests as well as more frequent reviews whenever circumstances indicate a possible impairment may exist. Impairment testing of goodwill is done at the MBO level by comparing the fair value of the MBO's net assets against the carrying value of the MBO's net assets, including goodwill. The fair value of net assets is calculated based on quantitative analysis of discounted cash flows. The fair value of goodwill is determined by assigning fair values to assets and liabilities and calculating any remaining fair value as the implied fair value of goodwill.

Goodwill increased $91.2 million due to the Nebraska Heart Hospital and Nebraska Heart Institute acquisition discussed in Note 4, *Acquisitions and Divestitures*, and the acquisition of a cardiology practice in Tacoma.

1. Summary of Significant Accounting Policies (continued)

A summary of intangible assets and goodwill is as follows as of June 30 (in thousands):

	2012	2011
Intangible assets	**$ 62,754**	$ 41,930
Less accumulated amortization	**(20,298)**	(15,525)
	42,456	26,405
Goodwill	**120,424**	29,212
Total intangible assets and goodwill, net	**$ 162,880**	$ 55,617

Notes Receivable and Other Assets

Other assets consist primarily of notes receivable, pledges receivable, deferred compensation assets, deposits and other long-term assets. Notes receivable include balances from the following related entities: Alegent Health and Alegent Health Immanuel Medical Center (collectively, Alegent), the Nebraska joint operating company (JOC) and non-CHI joint operating agreement (JOA) partner, respectively; and Bethesda Hospital, Inc. (Bethesda), the non-CHI JOA partner in the Cincinnati, Ohio JOA. All of the notes bear interest at rates commensurate with the CHI blended interest cost and require monthly debt service payments.

A summary of notes receivable and other assets is as follows as of June 30 (in thousands):

	2012	2011
Notes receivable from related entities:		
Total notes receivable from related entities	**$ 465,400**	$ 511,091
Reinsurance recoverable on unpaid losses and loss adjustment expense	**42,703**	39,066
Deferred compensation assets	**18,809**	21,726
Other long-term assets	**78,201**	67,583
Total notes receivable and other	**$ 605,113**	$ 639,466

Alegent and Bethesda are Designated Affiliates in the CHI credit group under the Capital Obligation Document (COD). As conditions of joining the CHI credit group, the Designated Affiliates have agreed to certain covenants related to corporate existence, insurance coverage, exempt use of bond-financed facilities, maintenance of certain financial ratios and compliance with limitations on the incurrence of additional debt. Based upon management's review of the creditworthiness of the Designated Affiliates and their compliance with the covenants and limitations, no allowances for uncollectible notes receivable were recorded at June 30, 2012 and 2011.

1. Summary of Significant Accounting Policies (continued)

Net Assets

Temporarily restricted net assets are those whose use has been limited by donors to a specific time period or purpose. Permanently restricted net assets consist of gifts with corpus values that have been restricted by donors to be maintained in perpetuity, including endowment funds. Temporarily restricted net assets and earnings on permanently restricted net assets, including earnings on endowment funds, are used in accordance with the donor's wishes primarily to purchase equipment, to provide charity care and to provide other health and educational programs and services.

Unconditional promises to receive cash and other assets are reported at fair value at the date the promise is received. Conditional promises and indications of donors' intentions to give are reported at fair value at the date the conditions are met or the gifts are received. All unrestricted contributions are included in the excess of revenue over expenses as donation revenues. Other gifts are reported as either temporarily or permanently restricted if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as donations revenue when restricted for operations or as unrestricted net assets when restricted for property and equipment.

Performance Indicator

The performance indicator is the excess of revenues over expenses, which includes all changes in unrestricted net assets other than changes in the pension liability funded status, net assets released from restrictions for property acquisitions, the cumulative effect of changes in accounting principles, discontinued operations, contributions of property and equipment, and other changes not required to be included within the performance indicator under generally accepted accounting principles.

Operating and Nonoperating Activities

CHI's primary mission is to meet the health care needs in its market areas through a broad range of general and specialized health care services, including inpatient acute care, outpatient services, physician services, long-term care and other health care services. Activities directly associated with the furtherance of this purpose are considered to be operating activities. Earnings from fixed-income investments held by FIIL are also classified within operating activities as such earnings support FIIL operations. Other activities that result in gains or losses peripheral to CHI's primary mission are considered to be nonoperating. Nonoperating activities include all other investment earnings; losses from bond defeasance; net interest cost and changes in fair value of interest rate swaps; and the nonoperating component of JOA income share adjustments.

1. Summary of Significant Accounting Policies (continued)

Charity Care

As an integral part of its mission, CHI accepts and treats all patients without regard to the ability to pay. Services to patients are classified as charity care in accordance with standards established across all MBOs. Charity care represents services rendered for which partial or no payment is expected, and includes the cost of providing services to persons who cannot afford health care due to inadequate resources and/or who are uninsured or underinsured. The cost of charity care is determined on the basis of an MBO's total cost as a percentage of total charges applied to the charges incurred by patients qualifying for charity care under CHI's policy and is not included in net patient services revenues in the accompanying consolidated statements of operations and changes in net assets. The estimated cost of charity care provided was $248.7 million and $235.8 million in 2012 and 2011, respectively, for continuing operations, and $24.6 million and $9.2 million in 2012 and 2011, respectively, for discontinued operations.

Other Nonpatient Revenues

Other nonpatient revenues include gains and losses on the sales of assets, the operating portion of revenue-sharing income or expense associated with Direct Affiliates that are part of JOAs, cafeteria sales, rental income, retail pharmacy and durable medical equipment sales, auxiliary and gift shop revenues, and revenues from other miscellaneous sources.

Derivative and Hedging Instruments

CHI uses derivative financial instruments (interest rate swaps) in managing its capital costs. These interest rate swaps are recognized at fair value on the consolidated balance sheets. CHI has not designated its interest rate swaps related to CHI's long-term debt as hedges. The net interest cost and change in the fair value of such interest rate swaps is recognized as a component of nonoperating gains (losses) in the accompanying consolidated statements of operations. It is CHI's policy to net the value of collateral on deposit with counterparties against the fair value of its interest rate swaps in other liabilities on the consolidated balance sheets.

Functional Expenses

CHI provides inpatient, outpatient, ambulatory, long-term care and community-based services to individuals within the various geographic areas supported by its facilities. Support services include administration, finance and accounting, information technology, public relations, human resources, legal, mission services and other functions that are supported centrally for all of CHI. Support services expenses as a percent of total operating expenses were approximately 5.0% and 4.7% in 2012 and 2011, respectively.

1. Summary of Significant Accounting Policies (continued)

Restructuring, Impairment and Other Losses

CHI periodically evaluates property, equipment, goodwill and certain other intangible assets to determine whether assets may have been impaired. Management determined there were certain property and equipment impairments in both 2012 and 2011 to the extent that the fair values (estimated based upon discounted cash flows) of those assets were less than the underlying carrying values.

During the years ended June 30, 2012 and 2011, CHI recorded total charges of $58.7 million and $25.7 million, respectively, relating to asset impairments and changes in business operations, including reorganization and severance costs. Of this amount, $47.7 million and $20.4 million were from continuing operations and reported in the consolidated statements of operations for 2012 and 2011, respectively, and $11.0 million and $5.3 million were reported as discontinued operations in the consolidated statements of changes in net assets for 2012 and 2011, respectively.

Income Taxes

CHI is a tax-exempt Colorado corporation and has been granted an exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code. CHI owns certain taxable subsidiaries and engages in certain activities that are unrelated to its exempt purpose and therefore subject to income tax.

Management reviews its tax positions annually and has determined that there are no material uncertain tax positions that require recognition in the accompanying consolidated financial statements.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results could vary from the estimates.

1. Summary of Significant Accounting Policies (continued)

New Accounting Pronouncements and Adoption of New Accounting Standards

In August 2010, the Financial Accounting Standards Board (FASB) released Accounting Standards Update (ASU) No. 2010-23, *Measuring Charity Care for Disclosure.* ASU 2010-23 requires the disclosure of charity care amounts and requires that cost be used as the measurement basis for charity care. The accounting provisions also specifically require that charity care not be reduced by reimbursement for charity care, and that the amount of reimbursements for charity care be disclosed. CHI adopted the disclosure provisions of ASU 2010-23 during 2012.

In August 2010, the FASB released ASU No. 2010-24, *Presentation of Insurance Claims and Related Insurance Recoveries.* ASU 2010-24 applies to malpractice claims and similar contingent liabilities and requires that such liabilities disregard the effect of any anticipated insurance recoveries in determining the liability amounts. The accounting provisions also provide accounting guidance for recording any insurance recovery receivables. ASU 2010-24 was effective for fiscal years beginning after December 15, 2010, and was adopted by CHI in fiscal year 2012, with no material effect on its overall consolidated results of financial position, operations or cash flows.

In July 2011, the FASB released ASU No. 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Entities.* ASU 2011-07 requires health care entities to change the presentation of their statement of operations by reclassifying the provision for bad debts associated with patient services revenues from an operating expense to a deduction from patient services revenues (net of contractual allowances and discounts). Additionally, enhanced disclosures will be required surrounding the entity's policies for recognizing revenue and assessing bad debts. ASU 2011-07 is effective for fiscal years and interim periods within those fiscal years beginning after December 15, 2011. CHI does not believe its adoption of ASU 2011-07 will have a material effect on its overall consolidated results of financial position, operations or cash flows.

Meaningful Use of Certified Electronic Health Record Technology Incentive Payments

The American Recovery and Reinvestment Act of 2009 provides for Medicare and Medicaid incentive payments beginning in 2011 to certain hospitals and professionals that implement and achieve meaningful use of certified electronic health record (EHR) technology in ways that demonstrate improved quality and effectiveness of care. Eligibility for annual Medicare incentive payments is dependent on providers demonstrating meaningful use of EHR technology in each period over a four-year period. An initial Medicaid incentive payment is available to providers that adopt, implement or upgrade certified EHR technology. However, in order to receive additional Medicaid incentive payments in subsequent years, providers must demonstrate continued meaningful use of EHR technology.

1. Summary of Significant Accounting Policies (continued)

CHI accounts for meaningful use incentive payments under the gain contingency model. Medicare EHR incentive payments are recognized as revenues when eligible providers demonstrate meaningful use of certified EHR technology and the cost report information for the full cost report year that will determine the full calculation of the incentive payment is available. Medicaid EHR incentive payments are recognized as revenues when an eligible provider demonstrates meaningful use of certified EHR technology. For fiscal year 2012, CHI recognized $11.3 million of Medicare meaningful use revenues and $20.7 million of Medicaid meaningful use revenues in its consolidated statements of operations.

Reclassifications

Certain reclassifications were made to the 2011 consolidated financial statement presentation to conform to the 2012 presentation.

2. Community Benefit (Unaudited)

In accordance with its mission and philosophy, CHI commits substantial resources to sponsor a broad range of services to both the poor and the broader community. Community benefit provided to the poor includes the cost of providing services to persons who cannot afford health care due to inadequate resources and/or who are uninsured or underinsured. This type of community benefit includes the costs of traditional charity care; unpaid costs of care provided to beneficiaries of Medicaid and other indigent public programs; services such as free clinics and meal programs for which a patient is not billed or for which a nominal fee has been assessed; and cash and in-kind donations of equipment, supplies or staff time volunteered on behalf of the community.

Community benefit provided to the broader community includes the costs of providing services to other populations who may not qualify as poor but may need special services and support. This type of community benefit includes the costs of services such as health promotion and education, health clinics and screenings, all of which are not billed or can be operated only on a deficit basis; unpaid portions of training health professionals such as medical residents, nursing students and students in allied health professions; and the unpaid portions of testing medical equipment and controlled studies of therapeutic protocols.

2. Community Benefit (Unaudited) (continued)

A summary of the cost of community benefit provided to both the poor and the broader community is as follows (in thousands):

	2012	2011
Cost of community benefit:		
Cost of charity care provided	**$ 248,667**	$ 235,756
Unpaid cost of public programs, Medicaid and other indigent care programs	**280,785**	235,326
Nonbilled services	**28,514**	23,327
Cash and in-kind donations	**3,221**	2,950
Education and research	**49,640**	33,165
Other benefit	**52,369**	61,362
Total cost of community benefit from continuing operations	**663,196**	591,886
Total cost of community benefit from discontinued operations	**51,815**	20,260
Total cost of community benefit	**715,011**	612,146
Unpaid cost of Medicare from continuing operations	**368,245**	439,316
Unpaid cost of Medicare from discontinued operations	**26,226**	22,042
Total unpaid cost of Medicare	**394,471**	461,358
Total cost of community benefit and the unpaid cost of Medicare	**$ 1,109,482**	$ 1,073,504

The summary above has been prepared in accordance with the policy document of the Catholic Health Association of the United States (CHA), *Community Benefit Program – A Revised Resource for Social Accountability*. Community benefit is measured on the basis of total cost, net of any offsetting revenues, donations or other funds used to defray cost.

The total cost of community benefit from continuing and discontinued operations was 7.0% and 6.6% of total expenses before operating expenses related to restructuring, impairment and other losses in 2012 and 2011, respectively. The total cost of community benefit and the unpaid cost of Medicare from continuing and discontinued operations was 10.8% and 11.6% of total expenses before operating expenses related to restructuring, impairment and other losses in 2012 and 2011, respectively.

3. Joint Operating Agreements and Investments in Unconsolidated Organizations

Joint Operating Agreements

CHI participates in JOAs with hospital-based organizations in five separate market areas. The agreements generally provide for, among other things, joint management through JOCs of the combined operations of the local facilities included in the JOAs. CHI retains ownership of the assets, liabilities, equity, revenues and expenses of the CHI facilities that participate in the JOAs. The financial statements of the CHI facilities managed under all JOAs are included in the CHI consolidated financial statements. Transfers of assets from facilities owned by the JOA participants generally are restricted under the terms of the agreements.

CHI has a 70% interest in a JOC based in Colorado and has interests of 50% in three other JOCs associated with other JOAs. These interests are included in investments in unconsolidated organizations and totaled $99 million and $125 million at June 30, 2012 and 2011, respectively. CHI recognizes its investment in all JOCs under the equity method of accounting. The JOCs provide varying levels of services to the related JOA sponsors, and operating expenses of the JOCs are allocated to each sponsoring organization. The unconsolidated JOCs had total assets of $688 million and $721 million at June 30, 2012 and 2011, respectively, and net assets of $156 million and $209 million, respectively.

Investments in Unconsolidated Organizations

CHI Kentucky – Effective on January 1, 2012, CHI purchased a controlling interest in Jewish Hospital and St. Mary's Healthcare Inc. and affiliates (JHSMH). CHI contributed its controlling interest, including its 25% joint venture investment in JHSMH, into a newly formed consolidated subsidiary, KentuckyOne Health (see Note 4, *Acquisitions and Divestitures*). As a result of the change in control of its investment in JHSMH, CHI recognized a gain on the remeasurement of its joint venture investment of $45.0 million reported in other revenue.

CHI's prior 25% joint venture investment in JHSMH was created on November 1, 2005, with CHI contributing substantially all of the net assets of the former MBO in Louisville, Kentucky, with a value of $7 million, along with $20 million, paid in quarterly installments through August 2008. The investment in the joint venture was accounted for under the equity method of accounting. It had a book value of $30 million at June 30, 2011, and was included in investments in unconsolidated organizations. In fiscal year 2011, the joint venture had annual operating revenues of approximately $1.0 billion, and total assets of $920 million and net assets of $335 million as of June 30, 2011. Prior to the contribution of the 25% joint venture investment in January 2012, the joint venture had executed a note to CHI with monthly payments of principal and interest. The note was included in other assets as of June 30, 2011, and had a balance of $25 million. Subsequent to the contribution of the 25% joint venture investment in JHSMH into KentuckyOne Health, the note is considered an intercompany transaction and eliminated in consolidation.

3. Joint Operating Agreements and Investments in Unconsolidated Organizations (continued)

Preferred Professional Insurance Corporation (PPIC) – PPIC is an unconsolidated affiliate of CHI. PPIC provides professional liability insurance and other related services to preferred physician and other health care providers that are associated with its owners. CHI owns a 27% interest in PPIC and accounts for its investment under the equity method of accounting. The book value of the investment was $50 million and $49 million at June 30, 2012 and 2011, respectively. PPIC had net assets of $184 million and $183 million at December 31, 2011 and 2010, respectively.

Other Entities – The summarized financial positions and results of operations for the other entities accounted for under the equity method as of and for the periods ended June 30, excluding the investments described above, are as follows (in thousands):

	2012					
	Medical Office Buildings	**Outpatient and Diagnostic Services**	**Ambulatory Surgery Centers**	**Physician Practices**	**Other Investees**	**Total**
Total assets	**$ 29,557**	**$ 141,683**	**$ 58,575**	**$ 19,997**	**$ 258,784**	**$ 508,596**
Total debt	**27,793**	**12,866**	**10,627**	**8,637**	**18,062**	**77,985**
Net assets	**1,160**	**102,401**	**42,396**	**8,462**	**169,870**	**324,289**
Net patient services revenues	**–**	**159,001**	**125,121**	**33,254**	**228,446**	**545,822**
Total revenues, net	**5,845**	**159,805**	**125,326**	**35,685**	**439,806**	**766,467**
Excess of revenues over expenses	**477**	**26,251**	**34,367**	**5,854**	**26,072**	**93,021**

	2011					
	Medical Office Buildings	**Outpatient and Diagnostic Services**	**Ambulatory Surgery Centers**	**Physician Practices**	**Other Investees**	**Total**
Total assets	$ 28,439	$ 129,620	$ 63,130	$ 21,028	$ 246,490	$ 488,707
Total debt	26,315	42,133	13,023	10,664	20,013	112,148
Net assets	1,263	86,316	46,024	8,054	164,528	306,185
Net patient services revenues	–	125,066	116,927	33,991	195,163	471,147
Total revenues, net	5,834	139,594	117,020	37,452	481,395	781,295
Excess of revenues over expenses	679	16,236	31,659	6,142	95,751	150,467

4. Acquisitions and Divestitures

Continuing Operations

KentuckyOne Health – Effective on January 1, 2012, CHI acquired an additional 58% interest in JHSMH from Jewish Hospital HealthCare Services, Inc. (JHHS) in exchange for a noncontrolling interest in KentuckyOne Health, a new statewide health care network in the state of Kentucky, through the combination of JHSMH and St. Joseph Health System, a CHI-sponsored MBO. CHI has a controlling interest of approximately 83% in KentuckyOne Health and JHHS has the remaining 17% interest. The fair value of the noncontrolling interest of $181.6 million was determined using valuation techniques including discounted cash flows.

Upon the change in control, the fair value of the assets and liabilities of JHSMH were allocated as follows (in thousands):

Patient receivables	$ 116,733
Other receivables	6,307
Current portion of assets limited as to use	5,567
Inventory	15,772
Prepaid and other current assets	11,672
Cash, investments and assets limited as to use	275,764
Property and equipment	451,662
Deferred financing costs	3,945
Investments in unconsolidated organizations	5,290
Other assets	8,095
Accrued compensation and benefits	(33,683)
Third-party liabilities	(1,691)
Accounts payable and accrued expenses	(107,903)
Current portion of long-term debt	(7,518)
Other liabilities	(87,459)
Long-term debt	(404,050)
Net assets acquired	$ 258,503

CHI began consolidating the results of JHSMH's operations effective January 1, 2012. The acquisition of JHSMH added $477.1 million of operating revenues and $62.2 million of deficit of revenues over expenses to the CHI consolidated results of operations from January 1 to June 30, 2012. On an unaudited pro forma basis, had CHI owned JHSMH at the beginning of each fiscal year, JHSMH would have reported $959.9 million and $991.4 million of operating revenues in 2012 and 2011, respectively, $84.2 million of deficiency of revenues over expenses in 2012, and $32.1 million of excess of revenues over expenses in 2011. However, the unaudited pro forma

4. Acquisitions and Divestitures (continued)

information is not necessarily indicative of the historical results that would have been obtained had the transaction actually occurred on those dates, nor of future results.

Nebraska Heart Hospital and Nebraska Heart Institute – Effective on August 1, 2011, CHI acquired Nebraska Heart Hospital and Nebraska Heart Institute. The acquisition allowed CHI to expand cardiac, thoracic and vascular care across the state of Nebraska. The gross purchase price of $131.1 million cash consideration was allocated as follows (in thousands):

Cash	$ 146
Patient receivables	8,080
Other receivables	1,735
Inventory	1,302
Prepaid and other assets	1,777
Property and equipment	45,150
Intangible assets	10,123
Goodwill	69,786
Accrued compensation and benefits	(3,063)
Accounts payable and accrued expenses	(3,354)
Other liabilities	(555)
Purchase price	$ 131,127

Nebraska Heart Hospital and Nebraska Heart Institute added $81.2 million of operating revenues and $5.7 million of excess of revenues over expenses to the CHI consolidated results of operations from August 1, 2011 to June 30, 2012. On an unaudited pro forma basis, had CHI owned Nebraska Heart Hospital and Nebraska Heart Institute at the beginning of each fiscal year, they would have reported $90.2 million and $95.1 million of operating revenues in 2012 and 2011, respectively, and $6.3 million and $14.7 million of excess of revenues over expenses in 2012 and 2011, respectively. However, the unaudited pro forma information is not necessarily indicative of the historical results that would have been obtained had the transaction actually occurred on those dates, nor of future results.

Consolidated Health Services (CHS) – Effective on October 1, 2010, CHI acquired CHS, headquartered near Cincinnati, Ohio, from Bethesda, Inc., an Ohio nonprofit corporation. CHS is a home health care service provider operating in 30 locations in Indiana, Kentucky and Ohio. The gross purchase price of the acquisition was $43.3 million ($35.5 million, net of cash acquired), which was allocated as follows (in thousands):

4. Acquisitions and Divestitures (continued)

Cash	$ 7,814
Patient receivables	6,534
Current deferred tax asset	2,077
Property and equipment	3,260
Investment in unconsolidated organizations	17,900
Intangibles	12,064
Deferred tax asset	1,503
Goodwill	6,479
Other assets	5,960
Other liabilities	(13,210)
Deferred tax liability	(7,034)
Purchase price	$ 43,347

Consolidated Health Services contributed $60.3 million of operating revenues and $2.9 million of excess of revenues over expenses to the CHI consolidated results of operations for fiscal year 2012, and $47.8 million of operating revenues and $2.5 million of excess of revenues over expenses to the CHI consolidated results of operations for fiscal year 2011.

Discontinued Operations

CHI has committed to a plan to sell the MBOs in Denville, New Jersey; Towson, Maryland; and Pierre, South Dakota. Effective in March 2012, CHI entered into exclusive negotiations with the intent of signing a non-binding Letter of Intent to transfer ownership of the Denville MBO to Ascension Health Care Network, Inc., an affiliate of Ascension Health; the Towson MBO to the University of Maryland Medical Systems; and the Pierre MBO to Avera Health. All the transactions are subject to governmental and Church approvals. It is anticipated that a definitive asset purchase agreement for the sale of the Denville MBO will be finalized and have a closing date prior to January 1, 2013. The asset purchase agreement for the sale of the Towson MBO is being negotiated with an expected closing date of November 1, 2012. No final agreement has been reached for the sale of the Pierre MBO as discussions are ongoing with Avera Health. In accordance with Accounting Standards Codification (ASC) 205-20, *Discontinued Operations,* and ASC 360-10, *Impairment and Disposal of Long-Lived Assets,* the results of operations associated with these MBOs have been reported as discontinued operations and are included in the consolidated statements of changes in net assets. Assets held for sale consist primarily of cash and investments, net patient accounts receivable, net property and other long-term assets. Liabilities held for sale consist of accounts payable and accrued compensation and benefits.

4. Acquisitions and Divestitures (continued)

Related to the MBOs held for sale, CHI recorded a deficiency of revenues over expenses of $45.2 million and $13.2 million for the years ended June 30, 2012 and 2011, respectively, which is reported as discontinued operations in the accompanying consolidated statements of changes in net assets. Total operating revenues and deficiency of revenues over expenses included in the results of discontinued operations for the years ended June 30 are summarized below (in thousands):

	2012	2011
Total operating revenues	**$ 714,405**	$ 727,886
Total operating expenses	**(748,388)**	(753,466)
Restructuring and other losses	**(10,987)**	(5,293)
Nonoperating (losses) gains	**(207)**	17,642
Deficiency of revenues over expenses	**$ (45,177)**	$ (13,231)

The consolidated statements of cash flows include the use of $45.4 million and $12.8 million of operating, investing and financing activities related to discontinued operations for the years ended June 30, 2012 and 2011, respectively.

Dayton Heart and Vascular Hospital – Effective on July 28, 2011, the Dayton Heart and Vascular Hospital was sold for $16.0 million. No gain or loss was recorded as a result of the sale. The property was classified as an asset held for sale on the consolidated balance sheet as of June 30, 2011.

5. Net Patient Services Revenues

Net patient services revenues are derived from services provided to patients who are either directly responsible for payment or are covered by various insurance or managed care programs. CHI receives payments from the federal government on behalf of patients covered by the Medicare program, from state governments for Medicaid and other state-sponsored programs, from certain private insurance companies and managed care programs and from patients themselves. A summary of payment arrangements with major third-party payors follows:

Medicare – Inpatient acute care and certain outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge or procedure. These rates vary according to patient classification systems based on clinical, diagnostic and other factors. Certain CHI facilities have been designated as critical access hospitals and, accordingly, are reimbursed their cost of providing services to Medicare beneficiaries. Professional services rendered by physicians are paid based on the Medicare allowable fee schedule.

5. Net Patient Services Revenues (continued)

Medicaid – Inpatient services rendered to Medicaid program beneficiaries are primarily paid under the traditional Medicaid plan at prospectively determined rates per discharge. Certain outpatient services are reimbursed based on a cost reimbursement methodology, fee schedules or discounts from established charges.

Other – CHI has also entered into payment agreements with certain managed care and commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to CHI under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

CHI's Medicare, Medicaid and other payor utilization percentages, based upon net patient services revenues, are summarized as follows:

	2012	**2011**
Medicare	**31%**	30%
Medicaid	**7**	8
Managed care	**39**	39
Self-pay	**8**	8
Commercial and other	**15**	15
	100%	100%

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 will change by a material amount in the near term. Estimated settlements related to Medicare and Medicaid of $57 million and $44 million at June 30, 2012 and 2011, respectively, are included in third-party liabilities. Net patient services revenues from continuing operations increased by $20.5 million in 2012 and $32.1 million in 2011 due to favorable changes in estimates related to prior-year settlements. Also during 2012, CHI prevailed on the appeal of two cost report settlements from the Centers for Medicare and Medicaid Services (CMS) related to the calculation used by CMS for the rural floor wage index and for the disallowance of insurance premiums paid to FIIL. The settlement amounts are included in the 2012 net patient services revenues from continuing operations, and totaled $76.7 million for the rural floor wage index and $19.8 million for the insurance premiums. The appeals spanned years from 1997 through 2011.

6. Investments and Assets Limited as to Use

CHI's investments and assets limited as to use as of June 30 are reported in the accompanying consolidated balance sheets as presented in the following table (in thousands):

	2012	2011
Cash and equivalents	**$ 155,418**	$ 141,283
CHI Investment Program	**4,827,922**	4,891,140
Marketable equity securities	**315,064**	308,846
Marketable fixed-income securities	**477,440**	416,484
Hedge funds and other investments	**162,190**	151,373
	5,938,034	5,909,126
Less current portion	**(1,901)**	(19,554)
	$ 5,936,133	$ 5,889,572

Net unrealized gains at June 30, 2012 and 2011, were $144.0 million and $298.0 million, respectively.

CHI attempts to reduce its market risk by diversifying its investment portfolio using cash equivalents, fixed-income securities, marketable equity securities and alternative investments. Most of the U.S. Treasury, money market funds and corporate debt obligations as well as exchange-traded marketable securities held by CHI and the CHI Investment Program (the Program) have an actively traded market. However, CHI also invests in commercial paper, mortgage-backed or other asset-backed securities, alternative investments (such as hedge funds, private equity investments, real estate funds, funds of funds, etc.), collateralized debt obligations, municipal securities and other investments that have potential complexities in valuation based upon the current conditions in the credit markets. For some of these instruments, evidence supporting the determination of fair value may not come from trading in active primary or secondary markets. Because these investments may not be readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had an active market for such investments existed. Such differences could be material. However, management reviews the CHI investment portfolio on a regular basis and seeks guidance from its professional portfolio managers related to U.S. and global market conditions to determine the fair value of its investments. CHI believes the carrying amount of these financial instruments in the consolidated financial statements is a reasonable estimate of fair value. Additionally, CHI assesses the risk of impairment related to securities held in its investment portfolio on a regular basis and noted no impairment during the years ended June 30, 2012 and 2011.

6. Investments and Assets Limited as to Use (continued)

Substantially all CHI long-term investments are held in the Program. The Program is structured under a Limited Partnership Agreement with CHI as managing general partner and numerous limited partners, most sponsored by CHI. The partnership provides a vehicle whereby virtually all entities associated with CHI, as well as certain other unrelated entities, can seek to optimize investment returns while managing investment risk. Entities participating in the Program that are not consolidated in the accompanying financial statements have the ability to direct their invested amounts and liquidate and/or withdraw their interest without penalty as soon as practicable based on market conditions but within 180 days of notification. The Limited Partnership Agreement permits a majority vote of the noncontrolled limited partners to terminate the partnership. Accordingly, CHI recognizes only the portion of Program assets attributable to CHI and its sponsored affiliates. Program assets attributable to CHI and its direct affiliates represented 86% of total Program assets at June 30, 2012 and 2011.

The Program asset allocation at June 30 is as follows:

	2012	2011
Marketable equity securities	**44%**	45%
Marketable fixed-income securities	**35**	34
Alternative investments	**19**	19
Cash and equivalents	**2**	2
	100%	100%

The CHI Investment Committee (the Investment Committee) of the Board of Stewardship Trustees is responsible for determining asset allocations among fixed-income, equity and alternative investments. At least annually, the Investment Committee reviews targeted allocations and, if necessary, makes adjustments to targeted asset allocations. Given the diversity of the underlying securities in which the Program invests, management does not believe there is a significant concentration of credit risk.

6. Investments and Assets Limited as to Use (continued)

Investment income is comprised of the following for the years ended June 30 (in thousands):

	2012	2011
Dividend and interest income	$ 123,432	$ 116,710
Net realized gains	86,566	268,526
Net unrealized (losses) gains	(153,000)	448,793
Total investment income from continuing operations	$ 56,998	$ 834,029
Included in other nonpatient revenue	$ 37,169	$ 30,475
Included in nonoperating gains	19,829	803,554
Total investment income from continuing operations	56,998	834,029
Total investment (loss) income from discontinued operations	(207)	17,642
Total investment income	$ 56,791	$ 851,671

Direct expenses of the Program are less than 0.4% of total assets. Fees paid to the alternative investment managers are not included in the total expense calculation as they are not a direct expense of the Program.

7. Fair Value of Assets and Liabilities

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. FASB ASC 820, *Fair Value Measurements and Disclosures*, establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement).

The three levels of the fair value hierarchy and a description of the valuation methodologies used for instruments measured at fair value are as follows:

> Level 1 – Valuation is based upon quoted prices (unadjusted) for identical assets or liabilities in active markets.
>
> Level 2 – Valuation is based upon quoted prices for similar assets and liabilities in active markets or other inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial asset or liability.

7. Fair Value of Assets and Liabilities (continued)

Level 3 – Valuation is based upon other unobservable inputs that are significant to the fair value measurement.

Certain of CHI's alternative investments are made through limited liability companies (LLCs) and limited liability partnerships (LLPs). These LLCs and LLPs provide CHI with a proportionate share of the investment gains (losses). CHI accounts for its ownership in the LLCs and LLPs under the equity method. CHI also accounts for its ownership in the Partnership under the equity method. As such, these investments are excluded from the scope of ASC 820.

Financial assets and liabilities measured at fair value on a recurring basis were determined using the following inputs at June 30 (in thousands):

	2012 Fair Value Measurements at Reporting Date Using			
		(Level 1)	(Level 2)	(Level 3)
	Fair Value as of June 30	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Assets				
Assets limited as to use:				
Cash and short-term investments	$ 155,418	$ 108,448	$ 46,970	$ –
Marketable equity securities	315,064	315,064	–	–
Marketable fixed-income securities	477,440	900	476,540	–
Other investments	1,953	–	–	1,953
Deferred compensation assets:				
Cash and short-term investments	10,852	10,852	–	–
	$ 960,727	$ 435,264	$ 523,510	$ 1,953
Liabilities				
Interest rate swaps	$ 238,549	$ –	$ 238,549	$ –
Deferred compensation liability	10,852	10,852	–	–
	$ 249,401	$ 10,852	$ 238,549	$ –

7. Fair Value of Assets and Liabilities (continued)

	2011 Fair Value Measurements at Reporting Date Using			
		(Level 1)	(Level 2)	(Level 3)
	Fair Value as of June 30	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Assets				
Assets limited as to use:				
Cash and short-term investments	$ 141,283	$ 133,011	$ 8,272	$ –
Marketable equity securities	308,846	308,846	–	–
Marketable fixed-income securities	416,484	79,903	336,581	–
Other investments	2,255	–	–	2,255
Deferred compensation assets:				
Cash and short-term investments	12,761	12,761	–	–
	$ 881,629	$ 534,521	$ 344,853	$ 2,255
Liabilities				
Interest rate swaps	$ 116,601	$ –	$ 116,601	$ –
Deferred compensation liability	12,761	12,761	–	–
	$ 129,362	$ 12,761	$ 116,601	$ –

The fair values of the instruments included in Level 1 were determined through quoted market prices. Level 1 instruments include money market funds, mutual funds and marketable debt and equity securities. The fair values of Level 2 instruments were determined through evaluated bid prices based on recent trading activity and other relevant information, including market interest rate curves and referenced credit spreads; estimated prepayment rates, where applicable, are used for valuation purposes and are provided by third-party services where quoted market values are not available. Level 2 instruments include corporate fixed-income securities, government bonds, mortgage and asset-backed securities, and interest rate swaps. The fair values of Level 3 securities are determined primarily through information obtained from the relevant counterparties for such investments. Information on which these securities' fair values are based is generally not readily available in the market.

8. Property and Equipment

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

	2012	2011
Land and improvements	$ 393,367	$ 327,766
Buildings and improvements	5,098,617	4,630,792
Equipment	3,814,458	3,491,942
	9,306,442	8,450,500
Less accumulated depreciation	(4,594,277)	(4,267,741)
	4,712,165	4,182,759
Construction in progress	635,310	363,989
	$ 5,347,475	$ 4,546,748

CHI evaluates whether events and circumstances have occurred that indicate the remaining useful life of property, equipment and certain other intangible assets may not be recoverable. Management determined there were impairment issues in both 2012 and 2011, to the extent that the undiscounted cash flows estimated to be generated by certain assets were less than the underlying carrying value. CHI recorded $16.0 million and $7.8 million in impairment losses in continuing operations for 2012 and 2011, respectively, resulting from charges related to estimated fair value deficiencies (based upon projected discounted cash flows) at various MBOs. Impairment charges of $1.1 million related to assets held for sale were included in discontinued operations in the consolidated statement of changes in net assets for 2011.

9. Debt Obligations

The following is a summary of debt obligations as of June 30 (in thousands):

	Interest Rates at June 30, 2012	2012	2011
Variable-rate Bonds:			
Series 1997B, maturing through 2022	0.28%	$ **18,900**	$ 24,400
Series 2000B, maturing through 2028	0.18%	**27,300**	81,800
Series 2002B, maturing 2032	0.17–0.18%	**103,300**	106,100
Series 2004B, maturing through 2044	0.17–0.23%	**180,700**	290,900
Series 2004C, maturing through 2044	0.15–0.17%	**163,300**	163,400
Series 2008A, maturing through 2036	0.17%	**120,260**	120,260
Series 2008C, maturing through 2041	0.16%	**50,000**	–
Series 2011B, maturing through 2046	0.18%	**158,155**	–
Series 2011C, maturing through 2046	0.16%	**125,000**	–
Fixed-rate Bonds:			
Series 1989A		**–**	3,390
Series 1995C		**–**	10,145
Series 1997A		**–**	12,950
Series 2000A		**–**	39,600
Series 2002A, maturing 2017	5.50%	**4,140**	4,845
Series 2004A, maturing through 2034	4.75–5.00%	**146,605**	146,605
Series 2006A, maturing through 2041	4.00–5.00%	**384,135**	384,135
Series 2006C, maturing through 2041	3.85–5.10%	**250,000**	250,000
Series 2008C, maturing through 2041	4.00–5.00%	**105,000**	215,000
Series 2008D, maturing through 2038	5.00–6.38%	**473,950**	473,950
Series 2009A, maturing through 2039	3.00–5.50%	**772,110**	794,345
Series 2009B, maturing through 2039	5.00%	**260,995**	260,995
Series 2011A, maturing through 2041	2.00–5.25%	**526,090**	–
Series 2012A, maturing through 2035	3.00–5.00%	**271,260**	–
Commercial Paper		**475,625**	617,400
Unamortized debt issuance premium		**58,832**	21,427
Unamortized debt issuance discount		**(9,801)**	(9,203)
Total CHI debt issued under the COD		**4,665,856**	4,012,444
Capital leases and other debt		**77,391**	122,382
		4,743,247	4,134,826
Less: Amounts classified as current			
Variable-rate debt with self-liquidity		**(321,455)**	(163,400)
Commercial paper and current portion of debt		**(643,083)**	(836,201)
Long-term debt		**$ 3,778,709**	$ 3,135,225

9. Debt Obligations (continued)

The fair value of debt obligations was approximately $5.0 billion at June 30, 2012. Management has determined the carrying values of the variable-rate bonds are representative of fair values as of June 30, 2012, as the interest rates are set by the market participants. The fair value of the fixed-rate tax-exempt bond obligations as of June 30, 2012, is determined by applying credit spreads for similar tax-exempt obligations in the marketplace, which are then used to calculate a price/yield for the outstanding obligations.

A summary of scheduled principal payments, based upon stated maturities, on long-term debt for the next five years is as follows (in thousands):

	Amounts Due
Year Ending June 30:	
2013	$ 639,763
2014	174,229
2015	168,793
2016	183,205
2017	72,071

CHI issues the majority of its debt under the COD and is the sole obligor. Bondholder security resides both in the unsecured promise by CHI to pay its obligations and in its control of its Direct and Designated Affiliates. Covenants include a minimum CHI debt service coverage ratio and certain limitations on secured debt. The Direct Affiliates of CHI, defined as Participants under the COD, have agreed to certain covenants related to corporate existence, maintenance of insurance and exempt use of bond-financed facilities.

In November 2011, CHI issued $809.2 million of fixed-rate, variable-rate and Windows variable-rate bonds (Windows) in the states of Colorado, Kentucky and Washington. Proceeds were used to refund $223.5 million of existing debt and to redeem $116.8 million of commercial paper outstanding. Concurrent with the issuance of these bonds, CHI converted $50.0 million of Ohio Series 2008C-2 bonds to bear interest at weekly rates. Also, during November 2011, CHI redeemed $55.8 million of existing debt. These redemptions resulted in a loss on extinguishment of $0.7 million.

In connection with the acquisition of JHSMH in January 2012, CHI acquired $342.0 million of JHSMH 2008 series bonds and $43.0 million of JHSMH 1996 series bonds. In January 2012, the 1996 bonds were legally defeased, which resulted in a loss on defeasance of $0.5 million. In April 2012, CHI issued $271.3 million of par value bonds in the state of Kentucky. Debt proceeds of $299.7 million and cash of $114.3 million were used to refund $322.9 million and

9. Debt Obligations (continued)

legally defease $88.4 million of the 2008 bonds. The transaction resulted in a loss on extinguishment of $69.4 million.

CHI has two types of external liquidity facilities: those that are dedicated to specific series of variable-rate demand bonds (VRDBs) and those that are not dedicated to a particular series of VRDBs but may be used to support CHI's obligations to fund tenders of VRDBs and pay the maturing principal of commercial paper. Liquidity facilities that are dedicated to specific series of bonds were $625.5 million and $623.5 million at June 30, 2012 and 2011, respectively, of which $9.4 million and $18.8 million, respectively are classified as current debt. The remaining $616.1 million and $604.7 million at June 30, 2012 and 2011, respectively, are reported as long term debt due to the repayment terms on any associated drawings extending beyond the subsequent fiscal year under the terms of the specific agreements.

Liquidity facilities not dedicated for specific series of VRDBs but used to support CHI's obligations to fund tenders and to pay maturing principal of commercial paper were $435.0 million and $565.0 million at June 30, 2012 and 2011, respectively. At June 30, 2012 and 2011, respectively, $475.6 million and $617.4 million of commercial paper were classified as current due to maturities of less than one year, and $321.5 million of VRDBs and Windows, and $163.4 million of VRDBs, respectively, were classified as current due to the holder's ability to put such VRDBs and Windows back to CHI without liquidity facilities dedicated to these bonds.

At June 30, 2012, CHI had a $60.0 million credit facility with Wells Fargo Bank. Letters of credit totaling $58.6 million have been issued for the benefit of third parties, principally in support of the self-insurance programs administered by FIIL. At June 30, 2012 and 2011, no amounts were outstanding under this credit facility.

CHI is a party to seven floating-to-fixed interest rate swap agreements with notional amounts totaling $931.8 million and $942.8 million at June 30, 2012 and 2011, respectively. Generally, it is CHI policy that all counterparties have an AA rating or better. The swap agreements require CHI to provide collateral if CHI's liability, determined on a mark-to-market basis, exceeds a specified threshold that varies based upon the rating on the corporation's long-term indebtedness. These fixed-payor swap agreements convert CHI's variable-rate debt to fixed-rate. The seven swaps have varying maturity dates ranging from May 2025 to December 2036. The fair value of the swaps is estimated based on the present value sum of anticipated future net cash settlements until the swaps' maturities. At June 30, 2012 and 2011, the fair value was $238.5 million and $116.6 million, respectively. Cash collateral balances of $140.7 million and $47.0 million at June 30, 2012 and 2011, respectively, are netted against the fair value of the swaps, and the net amount is reflected in other liabilities. The change in the fair value of these agreements was a net loss of $121.9 million in 2012 and a net gain of $26.9 million in 2011.

10. Retirement Plans

CHI and its direct affiliates maintain noncontributory, defined benefit retirement plans (Plans) covering substantially all employees. Benefits in the Plans are based on compensation, retirement age and years of service. Vesting occurs over a five-year period. Substantially all of the Plans are qualified as church plans and are exempt from certain provisions of both the Employee Retirement Income Security Act and Pension Benefit Guaranty Corporation premiums and coverage. Funding requirements are determined through consultation with independent actuaries.

CHI recognizes the funded status (that is, the difference between the fair value of plan assets and the projected benefit obligations) of its Plans in the consolidated balance sheets, with a corresponding adjustment to net assets. Actuarial gains and losses that arise and are not recognized as net periodic pension cost in the same periods are recognized as a component of net assets.

In connection with the acquisition of JHSMH in January 2012, CHI acquired the pension liabilities of JHSMH, herein referred to as the JHSMH plan.

10. Retirement Plans (continued)

A summary of the changes in the benefit obligation, fair value of plan assets and funded status of the Plans at the June 30 measurement dates is as follows (in thousands):

	2012	2011
Change in benefit obligation:		
Benefit obligation, beginning of year	**$ 2,767,988**	$ 2,648,696
Service cost	**169,477**	167,444
Interest cost	**153,204**	143,536
Actuarial loss (gain)	**446,352**	(80,030)
JHSMH plan	**183,733**	–
Settlements	**(8,495)**	–
Benefits paid	**(110,851)**	(111,340)
Expenses paid	**(177)**	(318)
Benefit obligation, end of year	**3,601,231**	2,767,988
Change in the Plans' assets:		
Fair value of the Plans' assets, beginning of year	**2,452,465**	1,917,500
Actual return on the Plans' assets, net of expenses	**45,002**	454,343
Employer contributions	**194,279**	192,280
JHSMH plan	**136,188**	–
Settlements	**(8,495)**	–
Benefits paid	**(110,851)**	(111,340)
Expenses paid	**(177)**	(318)
Fair value of the Plans' assets, end of year	**2,708,411**	2,452,465
Funded status of the Plans	**$ (892,820)**	$ (315,523)
End-of-year values:		
Projected benefit obligation	**$ 3,601,231**	$ 2,767,988
Accumulated benefit obligation	**3,428,819**	2,598,491

Included in net assets at June 30, 2012, are the following amounts that have not yet been recognized in net periodic pension cost: unrecognized prior service cost of $0.9 million and unrecognized actuarial losses of $1.2 billion. The prior service cost and actuarial loss included in net assets and expected to be recognized in net periodic pension cost during the fiscal year ending June 30, 2013, are $0.2 million and $92.5 million, respectively.

10. Retirement Plans (continued)

The components of net periodic pension expense are as follows (in thousands):

	2012	2011
Components of net periodic pension expense:		
Service cost	**$ 169,477**	$ 167,444
Interest cost	**153,204**	143,536
Expected return on the Plans' assets	**(198,093)**	(183,365)
Amortization of prior service benefit	**187**	893
Actuarial losses	**39,029**	47,550
	$ 163,804	$ 176,058
Weighted-average assumptions:		
Discount rate, beginning of year	**5.39%**	5.24%
Discount rate, end of year	**4.06**	5.39
Expected return on the Plans' assets	**7.75**	8.00
Rate of compensation increase	**3.75**	4.25

The assumption for the expected return on the Plans' assets is based on historical returns and adherence to the asset allocations set forth in the Plans' investment policies. The expected return on the Plans' assets for determining pension cost was 7.75% in 2012 and 8.00% in 2011. The decrease in the discount rate to 4.06% at June 30, 2012 increased the pension benefit obligation by approximately $420.3 million.

A summary of the Plans' asset allocation targets, ranges by asset class and allocations by asset class at the measurement dates of June 30 is as follows:

	2012	2011	Target	Range
Fixed-income securities	**29.8%**	26.1%	27.5%	17.5–37.5%
Equity securities	**51.2**	53.7	52.5	42.5–62.5
Alternative investments	**19.0**	20.2	20.0	10.0–30.0

The Plans' assets are invested in a portfolio designed to preserve principal and obtain competitive investment returns and long-term investment growth, consistent with actuarial assumptions, while minimizing unnecessary investment risk. Diversification is achieved by allocating assets to various asset classes and investment styles and by retaining multiple investment managers with complementary philosophies, styles and approaches. Although the objective of the Plans is to maintain asset allocations close to target, temporary periods may exist where allocations are outside of the expected range due to market conditions. The use of leverage is prohibited except as specifically directed in the alternative investment allocation. The portfolio is managed on a basis consistent with the CHI social responsibility guidelines.

10. Retirement Plans (continued)

The Plans' assets measured at fair value on a recurring basis were determined using the following inputs at June 30 (in thousands):

	2012			
	Fair Value Measurements at Reporting Date Using			
		(Level 1)	(Level 2)	(Level 3)
	Fair Value as of June 30	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Cash and short-term investments	$ 128,098	$ 117,585	$ 10,513	$ –
Marketable equity securities	1,318,456	1,318,456	–	–
Marketable fixed-income securities	756,137	230,647	525,490	–
Alternative investments	505,720	–	–	505,720
	$ 2,708,411	$ 1,666,688	$ 536,003	$ 505,720

	2011			
	Fair Value Measurements at Reporting Date Using			
		(Level 1)	(Level 2)	(Level 3)
	Fair Value as of June 30	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Cash and short-term investments	$ 133,920	$ 80,363	$ 53,557	$ –
Marketable equity securities	1,276,810	1,276,810	–	–
Marketable fixed-income securities	547,052	122,806	424,246	–
Alternative investments	494,683	–	–	494,683
	$ 2,452,465	$ 1,479,979	$ 477,803	$ 494,683

10. Retirement Plans (continued)

A summary of the changes in the fair value of the Plans' investments for which Level 3 inputs were used at the June 30 measurement dates is as follows (in thousands):

	2012	2011
Beginning investments at fair value	**$ 494,683**	$ 415,079
Purchases of investments	**24,306**	41,499
Proceeds from sale of investments	**(32,860)**	(23,322)
Net change in unrealized appreciation on investments and effect of foreign currency translation	**2,426**	43,066
Net realized gains on investments	**17,346**	18,369
Net transfers out of Level 3	**(181)**	(8)
Ending investments at fair value	**$ 505,720**	$ 494,683

CHI expects to contribute $195.1 million to the Plans in fiscal year 2013. A summary of expected benefits to be paid to the Plans' participants and beneficiaries is as follows (in thousands):

	Estimated Payments
Year Ending June 30:	
2013	$ 187,219
2014	171,532
2015	183,811
2016	211,306
2017	243,581
2018–2022	1,522,626

11. Concentrations of Credit Risk

CHI grants credit without collateral to its patients, most of whom are insured under third-party payor agreements. CHI's exposure to credit risk on patient accounts receivable is limited by the geographical diversity of its MBOs. The mix of receivables from patients and third-party payors at June 30 approximated the following:

	2012	2011
Medicare	**26%**	23%
Medicaid	**11**	7
Managed care	**32**	36
Self-pay	**6**	10
Commercial and other	**25**	24
	100%	100%

CHI maintains long-term investments with various financial institutions and investment management firms through its investment program, and its policy is designed to limit exposure to any one institution or investment. Management does not believe there are significant concentrations of credit risk at June 30, 2012 and 2011.

12. Commitments and Contingencies

Litigation

During the normal course of business, CHI may become involved in litigation. Management assesses the probable outcome of unresolved litigation and records estimated settlements. After consultation with legal counsel, management believes that any such matters will be resolved without material adverse impact to the consolidated financial position or results of operations of CHI.

Health Care Regulatory Environment

The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Management believes CHI is in compliance with all applicable laws and regulations of the Medicare and Medicaid programs. Compliance with such laws and regulations is complex and can be subject to future governmental interpretation as well as significant regulatory action, including fines, penalties and exclusion from the Medicare and Medicaid programs. Certain CHI entities have

12. Commitments and Contingencies (continued)

been contacted by governmental agencies regarding alleged violations of Medicare practices for certain services. In the opinion of management after consultation with legal counsel, the ultimate outcome of these matters will not have a material adverse effect on CHI's consolidated financial position.

Operating Leases

CHI leases certain real estate and equipment under operating leases, which may include renewal options and escalation clauses. Future minimum lease payments required for the next five years and thereafter for all operating leases that have initial or remaining noncancelable lease terms in excess of one year at June 30, 2012, are as follows (in thousands):

	Amounts Due
Year Ending June 30:	
2013	$ 104,407
2014	91,753
2015	75,761
2016	68,627
2017	61,038
Thereafter	210,019
	$ 611,605

Lease expense under operating leases for continuing operations for the years ended June 30, 2012 and 2011, totaled approximately $175 million and $145 million, respectively.

13. Insurance Programs

FIIL, a wholly owned captive insurance company of CHI, provides hospital professional liability, employment practices liability and commercial general liability coverage, primarily to MBOs related to CHI either on a directly written basis or through reinsurance fronting relationships with commercial carriers such as PPIC. Policies written provide coverage with primary limits in the amount of $8 million for each and every claim. For the policy year July 1, 2011 to July 1, 2012, there is an annual policy aggregate of $75 million eroded by hospital professional liability and commercial general liability claims, subject to a $175,000 continuing underlying per claim limit. Effective July 1, 2011, FIIL provided excess umbrella liability coverage for claims in excess of the underlying limits discussed above. The limits provided under such excess coverage are $200 million per claim and in the aggregate. Prior to July 1, 2011, CHI had obtained excess coverage directly from commercial insurance companies. FIIL reinsured 100% of the excess coverage layer with various commercial insurance companies. At June 30, 2012 and 2011, investments and assets limited as to use held for insurance purposes included $59 million and $58 million, respectively, held as collateral for the reinsurance fronting arrangement with PPIC.

13. Insurance Programs (continued)

FIIL provides workers' compensation coverage, either on a directly written basis or through reinsurance fronting relationships with commercial carriers for amounts above $1 million per claim. Coverage of $500,000 in excess of $500,000 per claim is reinsured with an unrelated commercial carrier. FIIL also underwrites the property and casualty risks of CHI for up to $1 million per claim. Unrelated commercial insurance carriers reinsure losses in excess of the per-claim limits.

The liability for self-insured reserves and claims represents the estimated ultimate net cost of all reported and unreported losses incurred through June 30. The reserves for unpaid losses and loss adjustment expenses are estimated using individual case-based valuations, statistical analyses and the expertise of an independent actuary.

The estimates for loss reserves are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for unpaid losses and loss adjustment expenses are adequate. The estimates are reviewed periodically, with consultation from independent actuaries, and any adjustments to the loss reserves are reflected in current operations. As a result of these reviews of claims experience, estimated reserves were reduced by $47.8 million and $19.3 million in 2012 and 2011, respectively. The reserves for unpaid losses and loss adjustment expenses relating to the workers' compensation program were discounted, assuming a 4% annual return at June 30, 2012 and 2011, to a present value of $147.1 million and $148.8 million at June 30, 2012 and 2011, respectively, and represented a discount of $46.3 million and $32.2 million in 2012 and 2011, respectively. Reserves related to professional liability, employment practices and general liability are not discounted.

FIIL holds $722.1 million and $715.7 million of investments held for insurance purposes as of June 30, 2012 and 2011, respectively. Distribution of amounts from FIIL to CHI are subject to the approval of the Cayman Island Monetary Authority. CHI established a captive management operation (Captive Management Initiatives, Ltd.) based in the Cayman Islands, which currently manages FIIL as well as operations of other unrelated parties.

CHI, through its Welfare Benefit Administration and Development Trust, provides comprehensive health and dental coverage to certain employees and dependents through a self-insured medical plan. Accounts payable and accrued expenses include $54 million and $45 million for unpaid claims and claims adjustment expenses for CHI's self-insured medical plan at June 30, 2012 and 2011, respectively. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for unpaid losses and loss adjustment expenses are adequate. The estimates are reviewed periodically and, as adjustments to the liability become necessary, such adjustments are reflected in current operations. CHI has stop-loss insurance to cover unusually high costs of care beyond a predetermined annual amount per enrolled participant.

14. Subsequent Events

CHI's management has evaluated events subsequent to June 30, 2012 through September 18, 2012, which is the date these consolidated financial statements were available to be issued. There have been no material events noted during this period that would either impact the results reflected herein or CHI's results going forward, except as disclosed below.

Alegent Health

Since 1996, CHI and Immanuel have been party to a Joint Operating Agreement in Omaha, operating under the name Alegent Health (Alegent). Effective in June 2012, CHI and Immanuel signed a letter of intent under which Immanuel will resign its membership and governance role in Alegent, leaving CHI as the sole member and sponsor of Alegent. The transaction is expected to close in late 2012.

In April 2012, Alegent also entered into an agreement with Creighton University to form a long-term strategic affiliation and to acquire Creighton University Medical Center (CUMC). Effective in September 2012, Alegent assumed the operations of CUMC's physician group, Creighton Medical Associates. Although CHI is not currently a party to this transaction, it would become one as a result of the June 2012 letter of intent with Immanuel discussed above.

PeaceHealth

In August 2012, CHI signed a nonbinding letter of intent with PeaceHealth, a Catholic health care system, to create a new integrated regional health care system in the states of Washington, Oregon and Alaska. CHI and PeaceHealth would be equal partners in the new health system and would include CHI's operations in the states of Washington and Oregon. The transaction is subject to various approvals and is expected to be completed before June 30, 2013.

Conifer Health Solutions

Effective in fiscal year 2013, CHI entered into an agreement with Tenet Healthcare to become a minority owner of Conifer Health Solutions (Conifer), a provider of revenue cycle and business management services to hospitals, whereby, in exchange for CHI's ownership interest, Conifer will manage the revenue cycle services for most of CHI's hospitals. CHI will be transitioning its revenue cycle and health information management employees to Conifer over the 2013 fiscal year.

Supplemental Information

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ERNST & YOUNG

Report of Independent Auditors on Supplemental Information

Board of Stewardship Trustees
Catholic Health Initiatives

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements of Catholic Health Initiatives as a whole. The following consolidating financial information is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Ernst + Young LLP

September 18, 2012

1111-1309439

Catholic Health Initiatives
Consolidating Balance Sheet

June 30, 2012
(In Thousands)

	MBOs	Corporate	FHL	CHI Welfare Benefits Trust	Other	Eliminations and Adjustments	Consolidated
Assets							
Current assets:							
Cash and equivalents	$ 329,818	$ 42,280	$ 119	$ 29,705	$ 2,050	$ –	$ 403,972
Net patient accounts receivable, less allowance of $687,631	1,353,928	–	–	–	–	–	1,353,928
Other accounts receivable	127,010	74,618	5,182	313	34,400	(124,916)	116,607
Current portion of investments and assets limited as to use	1,901	–	–	–	–	–	1,901
Inventories	185,571	–	–	–	–	–	185,571
Assets held for sale	474,990	–	–	–	–	–	474,990
Prepaid and other	52,678	34,265	13	157	66	–	87,179
Total current assets	2,525,896	151,163	5,314	30,175	36,516	(124,916)	2,624,148
Investments and assets limited as to use:							
Internally designated for capital and other funds	3,415,100	1,083,825	–	89,594	–	–	4,588,519
Mission and Ministry Fund	–	110,918	–	–	–	–	110,918
Capital Resource Pool	–	320,218	–	–	–	–	320,218
Held by trustees	228	–	–	–	–	–	228
Held for insurance purposes	23,058	–	722,069	–	–	–	745,127
Restricted by donors	170,638	485	–	–	–	–	171,123
Total investments and assets limited as to use	3,609,024	1,515,446	722,069	89,594	–	–	5,936,133
Property and equipment, net	4,870,828	475,473	–	–	1,174	–	5,347,475
Deferred financing costs	188	28,529	–	–	–	–	28,717
Investments in unconsolidated organizations	209,279	1,161,507	–	–	8,922	(1,071,790)	307,918
Intangible assets	162,880	–	–	–	–	–	162,880
Notes receivable and other	76,590	2,995,622	20,518	–	–	(2,487,617)	605,113
Total assets	$ 11,454,685	$ 6,327,740	$ 747,901	$ 119,769	$ 46,612	$ (3,684,323)	$ 15,012,384

Continued on following page

Catholic Health Initiatives
Consolidating Balance Sheet (continued)

June 30, 2012
(In Thousands)

	MBOs	Corporate	FHL	CHI Welfare Benefits Trust	Other	Eliminations and Adjustments	Consolidated
Liabilities and net assets							
Current liabilities:							
Compensation and benefits	$ 363,171	$ 52,224	$ –	$ 1,374	$ 1,828	$ –	$ 418,597
Third-party liabilities	76,660	–	–	–	–	–	76,660
Accounts payable and accrued expenses	551,084	228,885	3,961	53,478	3,326	(121,837)	718,897
Liabilities held for sale	103,633	–	–	–	–	–	103,633
Variable-rate debt with self liquidity	–	321,455	–	–	–	–	321,455
Current portion of long-term debt	124,416	629,115	–	–	–	(110,448)	643,083
Total current liabilities	1,218,964	1,231,679	3,961	54,852	5,154	(232,285)	2,282,325
Pension liability	83,364	809,456	–	–	–	–	892,820
Self-insured reserves and claims	16,338	37,185	460,061	–	–	–	513,584
Other liabilities	118,120	121,722	–	–	–	(3,079)	236,763
Long-term debt	2,440,592	3,715,286	–	–	–	(2,377,169)	3,778,709
Total liabilities	3,877,378	5,915,328	464,022	54,852	5,154	(2,612,533)	7,704,201
Net assets:							
Net assets attributable to CHI	7,367,623	236,379	283,879	64,917	41,458	(1,071,790)	6,922,466
Net assets attributable to noncontrolling interests	5,317	175,546	–	–	–	–	180,863
Unrestricted	7,372,940	411,925	283,879	64,917	41,458	(1,071,790)	7,103,329
Temporarily restricted	136,334	487	–	–	–	–	136,821
Permanently restricted	68,033	–	–	–	–	–	68,033
Total net assets	7,577,307	412,412	283,879	64,917	41,458	(1,071,790)	7,308,183
Total liabilities and net assets	$ 11,454,685	$ 6,327,740	$ 747,901	$ 119,769	$ 46,612	$ (3,684,323)	$ 15,012,384

Catholic Health Initiatives
Consolidating Statement of Operations

Year Ended June 30, 2012
(In Thousands)

	MBOs	Corporate	FIIL	CHI Welfare Benefits Trust	Other	Eliminations and Adjustments	Consolidated
Revenues:							
Net patient services	$ 9,336,797	$ –	$ –	$ –	$ –	$ (112,938)	$ 9,223,859
Nonpatient:	–						
Donations	25,960	2,008	–	–	–	–	27,968
Changes in equity of unconsolidated organizations	16,504	8,642	–	–	(2,206)	(6)	22,934
Investment income from self-insured trust funds	3,024	–	34,145	–	–	–	37,169
Other	379,163	855,699	133,740	372,557	6,516	(1,215,334)	532,341
Total nonpatient revenues	424,651	866,349	167,885	372,557	4,310	(1,215,340)	620,412
Total operating revenues	9,761,448	866,349	167,885	372,557	4,310	(1,328,278)	9,844,271
Expenses:							
Salaries and wages	3,523,165	241,526	–	–	11,743	(46)	3,776,388
Employee benefits	822,465	25,993	–	376,459	1,725	(477,587)	749,055
Purchased services, medical professional fees, consulting and legal	1,129,211	147,068	653	2,094	3,086	(356,685)	925,427
Supplies	1,558,339	7,694	–	–	334	–	1,566,367
Bad debts	709,654	–	–	–	–	–	709,654
Utilities	107,781	12,399	–	–	25	–	120,205
Rentals, leases, maintenance and insurance	310,596	310,725	135,412	–	1,112	(234,769)	523,076
Depreciation and amortization	453,484	19,935	–	–	354	–	473,773
Interest	96,926	134,101	–	–	–	(101,379)	129,648
Other	655,555	11,122	991	598	666	(157,807)	511,125
Total operating expenses before restructuring, impairment and other losses	9,367,176	910,563	137,056	379,151	19,045	(1,328,273)	9,484,718
Income (loss) from operations before restructuring, impairment and other losses	394,272	(44,214)	30,829	(6,594)	(14,735)	(5)	359,553
Restructuring, impairment and other losses	24,226	22,813	–	–	696	–	47,735
Income (loss) from operations	370,046	(67,027)	30,829	(6,594)	(15,431)	(5)	311,818
Nonoperating gains (losses):							
Investment income (loss), net	33,881	(6,377)	(10,159)	2,488	(4)	–	19,829
Loss on defeasance of bonds	(69,878)	(677)	–	–	–	–	(70,555)
Realized and unrealized losses on interest rate swaps	–	(153,411)	–	–	–	–	(153,411)
Other nonoperating (losses) gains	(12,215)	(35,323)	–	–	–	35,323	(12,215)
Total nonoperating (losses) gains	(48,212)	(195,788)	(10,159)	2,488	(4)	35,323	(216,352)
Excess (deficiency) of revenues over expenses	$ 321,834	$ (262,815)	$ 20,670	$ (4,106)	$ (15,435)	$ 35,318	$ 95,466
Excess (deficiency) of revenues over expenses attributable to noncontrolling interest	$ 6,542	$ (6,005)	$ –	$ –	$ –	$ –	$ 537
Excess (deficiency) of revenues over expenses attributable to CHI	$ 315,292	$ (256,810)	$ 20,670	$ (4,106)	$ (15,435)	$ 35,318	$ 94,929

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