Consolidated Financial Statements and Supplementary Information

Beacon Health System, Inc. and Affiliated Corporations
Years Ended December 31, 2013 and 2012
With Reports of Independent Auditors

Ernst & Young LLP

Building a better working world

Beacon Health System, Inc. and Affiliated Corporations

Consolidated Financial Statements
and Supplementary Information

Years Ended December 31, 2013 and 2012

Contents

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Report of Independent Auditors

The Board of Directors
Beacon Health System, Inc. and Affiliated Corporations

We have audited the accompanying consolidated financial statements of Beacon Health System, Inc. and Affiliated Corporations (the Corporation), which comprise the consolidated balance sheets as of December 31, 2013 and 2012, and the related consolidated statements of operations and changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audit 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 consolidated financial statements are free of material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Beacon Health System, Inc. and Affiliated Corporations at December 31, 2013 and 2012, and the results of their operations and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

March 6, 2014

Beacon Health System, Inc. and Affiliated Corporations

Consolidated Balance Sheets
(In Thousands)

	December 31 2013	December 31 2012
Assets		
Current assets:		
Cash and cash equivalents	**$ 91,057**	$ 78,316
Short-term investments	**43,072**	7,305
Patient accounts receivable, less allowances for doubtful accounts (2013 – $23,123; 2012 – $19,393)	**138,950**	137,442
Due from third-party payors	**7,230**	18,573
Other receivables	**10,299**	8,844
Inventories	**21,641**	21,316
Prepaid expenses	**11,146**	9,345
Total current assets	**323,395**	281,141
Assets limited as to use:		
Internally designated investments	**558,918**	531,354
Externally designated investments under debt agreements	**28,812**	–
Externally designated investments – insurance trust	**2,582**	2,584
Board-designated endowment	**20,968**	19,332
Endowment and temporarily restricted investments	**6,278**	5,235
	617,558	558,505
Property and equipment:		
Land	**45,955**	38,347
Buildings and improvements	**595,141**	573,562
Furniture and equipment	**375,603**	338,814
Construction in progress	**32,060**	24,751
	1,048,759	975,474
Less allowances for depreciation and amortization	**505,566**	478,597
	543,193	496,877
Unamortized bond issuance costs, net	**2,474**	1,995
Deferred charges and other assets	**26,411**	30,243
	$ 1,513,031	$ 1,368,761

	December 31	
	2013	**2012**
Liabilities and net assets		
Current liabilities:		
Accounts payable	**$ 53,531**	$ 45,915
Accrued salaries and benefits	**43,942**	46,161
Accrued expenses	**4,971**	5,314
Due to third-party payors	**10,753**	6,063
Current maturities of long-term debt	**6,899**	6,920
Total current liabilities	**120,096**	110,373
Noncurrent liabilities:		
Long-term debt, less current maturities	**256,237**	208,140
Pension and other liabilities	**65,484**	122,563
Interest rate and basis swaps	**36,761**	30,017
	358,482	360,720
Total liabilities	**478,578**	471,093
Net assets:		
Unrestricted:		
Undesignated	**1,000,532**	867,771
Board-designated endowment	**20,968**	19,332
Total unrestricted	**1,021,500**	887,103
Temporarily restricted	**12,362**	9,974
Permanently restricted	**591**	591
Total net assets	**1,034,453**	897,668
	$ 1,513,031	$ 1,368,761

See accompanying notes.

Beacon Health System, Inc. and Affiliated Corporations

Consolidated Statements of Operations and Changes in Net Assets

(In Thousands)

	Year Ended December 31	
	2013	**2012**
Unrestricted revenue, gains, and other support		
Net patient service revenue	**$ 840,408**	$ 897,737
Provision for bad debts	**(62,724)**	(51,950)
Net patient service revenue less provision for bad debts	**777,684**	845,787
Other revenue	**42,726**	39,670
Net assets released from restrictions used for operations	**458**	620
	820,868	886,077
Expenses		
Salaries and wages	**329,320**	302,454
Employee benefits	**90,072**	94,783
Supplies and other	**192,834**	208,416
Professional fees and purchased services	**107,094**	107,310
Depreciation and amortization	**44,169**	46,858
Interest	**6,594**	6,228
	770,083	766,049
Income from operations	**50,785**	120,028
Nonoperating		
Investment income, net	**49,466**	50,178
Unrealized (losses) gains on swap transactions, net	**(6,744)**	12,333
Loss on bond refunding	**(3,734)**	–
Realized loss on swap termination	**–**	(290)
Revenue and gains in excess of expenses	**89,773**	182,249

Beacon Health System, Inc. and Affiliated Corporations

Consolidated Statements of Operations and Changes in Net Assets (continued)

(In Thousands)

	Year Ended December 31 2013	2012
Unrestricted net assets		
Revenue and gains in excess of expenses	**$ 89,773**	$ 182,249
Net assets released from restrictions used for capital purposes	**529**	304
Net assets released from board designated endowment	**(690)**	–
Other	**(53)**	122
Capital contributions	**–**	257
Postretirement benefit adjustments other than periodic costs	**44,838**	(10,239)
Increase in unrestricted net assets	**134,397**	172,693
Temporarily restricted net assets		
Contributions temporarily restricted for use	**2,182**	1,502
Investment income	**1,193**	649
Net assets released from restrictions used for operating and capital purposes	**(987)**	(924)
Increase in temporarily restricted net assets	**2,388**	1,227
Permanently restricted net assets		
Contributions permanently restricted for use	**–**	–
Increase in permanently restricted net assets	**–**	–
Increase in net assets	**136,785**	173,920
Net assets at beginning of year	**897,668**	723,748
Net assets at end of year	**$ 1,034,453**	$ 897,668

See accompanying notes.

Beacon Health System, Inc. and Affiliated Corporations

Consolidated Statements of Cash Flows

(In Thousands)

	Year Ended December 31	
	2013	**2012**
Operating activities		
Change in net assets	**$ 136,785**	$ 173,920
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	**44,169**	46,858
Provision for bad debts	**62,724**	51,950
Unrealized gains on swap transactions, net	**6,743**	(12,333)
Realized loss on swap termination	**–**	290
Loss on early extinguishment of debt	**3,735**	–
Loss on disposal of assets	**–**	105
Postretirement benefit adjustments other than periodic costs	**(44,838)**	10,239
Realized gains on investments	**(8,670)**	(1,498)
Restricted contributions and investment income	**(3,375)**	(2,151)
Changes in operating assets and liabilities:		
Patient accounts receivable	**(64,232)**	(71,901)
Other receivables, inventories, and prepaid expenses	**(3,581)**	535
Other assets	**3,452**	(3,694)
Investments – trading	**(86,151)**	(118,226)
Accounts payable, accrued salaries and benefits, and accrued expenses	**5,054**	12,786
Due to/from third-party payors, net	**16,033**	(11,023)
Other long-term liabilities	**(12,071)**	(9,704)
Net cash provided by operating activities	**55,777**	66,153
Investing activities		
Net additions to property and equipment	**(86,423)**	(47,938)
Net cash used in investing activities	**(86,423)**	(47,938)
Financing activities		
Principal payments on long-term debt and other debt obligations	**(149,505)**	(6,806)
Net proceeds from issuance of long-term debt and other debt obligations	**191,337**	55
Payment of bond issue costs	**(1,820)**	–
Restricted contributions and investment income	**3,375**	2,151
Net cash provided by (used in) financing activities	**43,387**	(4,600)
Increase in cash and cash equivalents	**12,741**	13,615
Cash and cash equivalents at beginning of year	**78,316**	64,701
Cash and cash equivalents at end of year	**$ 91,057**	$ 78,316
Supplemental disclosure of cash flow information		
Interest paid	**$ 5,748**	$ 6,312

See accompanying notes.

1. Organization and Basis of Consolidation

The accompanying consolidated financial statements represent the accounts of Beacon Health System, Inc. (the Corporation or BHS) and its various affiliated corporations under the control of the Corporation. The Corporation is an Indiana not-for-profit corporation exempt from federal income tax under Internal Revenue Code (the Code) Section 501(a) as an organization described in Section 501(c)(3) and a public charity as described in Section 509(a)(3). In December 2011, the Corporation became the sole corporate member of the following entities:

Elkhart General Hospital, Inc. (EGH); Memorial Hospital of South Bend, Inc. (MHSB); Memorial Health Foundation, Inc. (MHF); Beacon Medical Group, Inc. (BMG), formerly Memorial Health System, Inc.; and Beacon Health Ventures, Inc. (BHV). EGH, MHSB, BMG, and MHF are also exempt from federal income tax under Section 501(a) as organizations described in Section 501(c)(3) and as public charities described in Sections of 509(a)(1) and 509(a)(2), respectively. BHV is an Indiana for-profit corporation. All significant intercompany accounts and transactions have been eliminated in the consolidation. EGH is a 365 licensed bed (270 available) acute care community hospital located in Elkhart, Indiana. MHSB is a 657 licensed bed (409 available) acute care trauma center located in South Bend, Indiana. EGH and MHSB (collectively, the Hospitals) provide inpatient, outpatient, and 24-hour emergency care services for residents of Elkhart and South Bend, Indiana, and the surrounding communities. MHF is organized primarily to promote and encourage philanthropic activities for the support of the Corporation and its affiliates. BHV manages the taxable operations of the Corporation, including home care and other non-acute health care services. BMG operates the physician enterprise of the Corporation.

The Corporation owns a less than majority ownership or controlling interest in the following:

- 50% interest in Community Health Alliance LLC, an Indiana physician hospital organization
- 40% interest in Skyway Limited Partnership, a professional medical building venture
- 50% interest in Memorial Spine and Neuroscience Center, LLC, an outpatient surgery center specializing in neurologic, spine, and pain control procedures
- 45% interest in LaPorte Medical Group Surgery Center, LLP, an outpatient surgery center
- 35% interest in Physicians Hospital LLC, a long-term acute care facility

1. Organization and Basis of Consolidation (continued)

- 50% interest in Valparaiso Medical Development, LLC, a professional medical building venture
- 25% interest in Magnetic Resonance Imaging, LLC, an imaging and radiology center
- 33% interest in Michiana Information Health Network, Inc, a health information exchange
- 40% interest in Northern Indiana Ambulatory Surgery Center, LLC, an ambulatory surgery center
- 26% interest Community Occupational Medicine, LLC, an occupational health care facility
- 42% interest in Wakarusa Medical Clinic, LLC, a medical clinic
- 50% interest in Wanee Walk in Clinic, LLC, a medical clinic

Aggregate financial information relating to these investments is as follows (in thousands):

	2013	2012
Assets	**$ 42,419**	$ 40,292
Liabilities	**20,746**	24,096
Net income	**8,236**	8,149

2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Although estimates are considered to be fairly stated at the time the estimates are made, actual results could differ from those estimates.

2. Summary of Significant Accounting Policies (continued)

Cash Equivalents

All investments that are not limited as to use with a maturity of three months or less at the time of acquisition are reflected as cash equivalents. Cash equivalents include checking accounts, money market accounts, corporate credit card accounts, and petty cash. The carrying value of cash equivalents approximates fair value.

Short-Term Investments

Short-term investments include cash reinvested on a daily basis, accrued interest on investments, and money expected to be used in less than a year as part of the Corporation's community benefit. Also included in short-term investments are restricted and unrestricted investment donations that are in the process of being liquidated.

Accounts Receivable

The Corporation evaluates the collectibility of its accounts receivable based on the length of time the receivable is outstanding, payor class, and the anticipated future uncollectible amounts based on historical experience. Accounts receivable are charged to the allowance for doubtful accounts when they are deemed uncollectible.

Assets Limited as to Use

Assets limited as to use include assets set aside by the Board of Directors (the Board) for future capital improvements and community health enhancement initiatives that the Board, at its discretion, may subsequently use for other purposes. In addition, assets limited as to use also include assets held by trustees under self-funded insurance agreements, and investments externally designated under indenture or donor restriction.

Investments

The Corporation classifies substantially all of its investments as trading. Under a trading classification, all unrestricted realized and unrealized gains and losses are included in revenues, and gains in excess of expenses.

2. Summary of Significant Accounting Policies (continued)

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value based on quoted market prices for those or similar investments. Dividend and interest income, realized gains and losses, and changes to fair values of investments are reported as nonoperating investment income in the consolidated statements of operations and changes in net assets.

Investments in alternative investments, primarily hedge fund of funds, that invest in marketable securities and derivative products are reported using the equity method. The estimated fair values are provided by the respective fund managers and are based on historical costs, appraisals, and other estimates that require varying degrees of judgment. Because alternative investments are not readily marketable, their estimated value is subject to uncertainty and may differ from the value that would have been used had a ready market for such investments existed. Resulting differences could be material. The financial statements of the hedge funds are audited annually. Equity earnings related to these alternative investments are included in nonoperating investment income. The Corporation’s holding reflects net contributions to the hedge fund and an allocated share of realized and unrealized investment income and expense.

Inventories

Inventories are stated at the lower of cost (average cost method) or market.

Unamortized Bond Issuance Costs

Costs incurred in connection with the issuance of long-term debt are deferred and amortized over the term of the related financing, which approximates the effective interest method.

Fair Value of Financial Instruments

The Corporation’s carrying amount for its financial instruments, which include cash and cash equivalents, investments and assets limited as to use, and accounts receivable, at December 31, 2013 and 2012, approximates fair value. The estimated fair value amounts have been determined by the Corporation using available market information and appropriate valuation methodologies.

Property and Equipment

Property and equipment are carried at cost, except donated assets, which are recorded at fair value at the date of donation. Allowances for depreciation and amortization are computed primarily utilizing the straight-line method over the estimated useful lives of the assets, which range from 3 to 40 years.

Asset Impairment

The Corporation considers whether indicators of impairment are present and performs the necessary tests to determine if the carrying value of an asset is appropriate. Impairment write-downs are recognized in operating expenses at the time the impairment is identified. There was no impairment of long-lived assets in 2013 or 2012.

The carrying value of goodwill amounted to approximately $7,853,000 and $6,507,000 at December 31, 2013 and 2012, respectively, and is included in deferred charges and other assets in the consolidated balance sheets. Goodwill is assessed for impairment on an annual basis at the reporting unit level. If the fair value of the reporting unit is less than the carrying value, an impairment loss equal to the difference between the implied fair value of the reporting unit goodwill and the carrying value of the reporting unit goodwill is recognized. There was no impairment of goodwill in 2013 or 2012.

Deferred Charges and Other Assets

Included in deferred charges and other assets are intangible assets and investments in unconsolidated affiliates.

The acquisition of a business entity can result in the recording of intangible assets. Acquired definite-lived intangible assets (excluding goodwill) are amortized over the useful life of the assets. Goodwill is carried at acquisition value, less any impairment reductions.

The Corporation accounts for its investments in less than majority owned and controlled affiliates using either the cost basis or the equity method of accounting. Income from these investments is reflected in other revenue in the consolidated statements of operations and changes in net assets.

2. Summary of Significant Accounting Policies (continued)

Endowment Investments

Income is received directly by MHF from MHF board-designated endowment investments and is included in investment income within temporarily restricted net assets. EGH receives a portion of the income from investments in endowments directly as they are released from restriction. These endowment investments have perpetual existence.

Contributions

Unconditional pledges to give cash and other assets are reported at fair value at the date the pledge is received to the extent estimated to be collectible by the Corporation. Pledges received with donor restrictions that limit the use of the donated assets are reported as either temporarily or permanently restricted support. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions.

Temporarily Restricted Net Assets

Temporarily restricted net assets are used to differentiate resources, the use of which is restricted by donors or grantors to a specific time period or purpose, from resources on which no restrictions have been placed or that arise from the general operations of the Corporation. Temporarily restricted gifts and bequests are recorded as an addition to temporarily restricted net assets in the period received. Assets released from restrictions that are used for the purchase of property and equipment or capital purposes are reported in the consolidated statements of operations and changes in net assets as additions to unrestricted net assets. Resources restricted by donors for specific operating purposes are reported in unrestricted revenue, gains, and other support to the extent expended within the period.

Permanently Restricted Net Assets

Permanently restricted net assets have been restricted by donors to be maintained by the Corporation in perpetuity. In accordance with the restriction, a majority of the investment income and investment gains or losses from permanently restricted net assets are restricted by the donor for a specific purpose and are therefore temporarily restricted. A specified portion of income earned by the temporarily restricted net assets is released from restriction and used for operations each year and, therefore, is included in the consolidated statements of operations and changes in net assets as other revenue.

2. Summary of Significant Accounting Policies (continued)

Net Patient Service Revenue

The Corporation has agreements with various third-party payors that provide for payments to the Corporation at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts received or due from patients, third-party payors, and others for services rendered. These amounts include estimated adjustments under certain reimbursement agreements with third-party payors, which are subject to audit by the applicable administering agency. These adjustments are accrued on an estimated basis and are adjusted in future periods as final settlements are determined (see Note 3).

Community Commitment

The Hospitals provide care to all patients regardless of their ability to pay. Charity care provided is excluded from net patient service revenue (see Note 4).

Revenue and Gains in Excess of Expenses

The consolidated statements of operations and changes in net assets includes revenue and gains in excess of expenses. Changes in unrestricted net assets, which are excluded from revenue and gains in excess of expenses, consistent with industry practice, include contributions of long-lived assets, including assets acquired using contributions, which, by donor restrictions, were to be used for the purpose of acquiring such assets, and pension-related changes other than net periodic costs.

Allocation of Costs

The Corporation's ability to exercise control over consolidated entities could result in the entities having a financial position or operating results that are significantly different from those that would have been obtained if the entities were autonomous. The manner of allocating certain shared and centralized costs, such as accounts payable processing, information technology support, and other Corporation-managed administration costs, is determined by the Corporation utilizing Internal Revenue Service transfer pricing guidance. Alternate methods of accounting for these cost allocations may produce significantly different operating results for each of the consolidated entities.

2. Summary of Significant Accounting Policies (continued)

Interest Rate and Basis Swaps

All interest rate and basis swaps are measured at fair value based on quoted market interest rates. None of the swaps are designated as hedging instruments; therefore, the unrealized gains or losses on the fair value of the swaps are included in revenue and gains in excess of expenses in the consolidated statements of operations and changes in net assets.

Asset Retirement Obligations

The Corporation accounts for the fair value of legal obligations associated with long-lived asset retirements by recognizing an expense and accreting a liability over the life of the asset to cover potential legal obligations at the end of the asset's useful life. The asset retirement obligation primarily relates to future asbestos remediation related to buildings on MHSB's campus, as well as ground/soil remediation associated with the removal of underground fuel tanks. The carrying value of the obligation amounted to approximately $4,343,000 and $4,512,000 at December 31, 2013 and 2012, respectively, and is reflected in pension and other liabilities on the consolidated balance sheets.

New Accounting Pronouncement

In December 2011, the FASB issued guidance that enhances disclosures about financial and derivative instruments that are either offset on the consolidated balance sheet or subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset on the consolidated balance sheet. Adoption of this new guidance on January 1, 2013 did not have a material impact on the Corporation's consolidated financial statements.

Reclassifications

Certain reclassifications were made to the 2012 consolidated financial statements to conform with classifications made in 2013. The reclassifications had no effect on the changes in net assets or on net assets previously reported.

3. Contractual Arrangements With Third-Party Payors and Uncollectible Accounts

The Medicare and Medicaid programs reimburse the Corporation for inpatient and outpatient services at predetermined rates based on diagnosis and treatment. Changes in the Medicare and Medicaid programs or reduction in funding of the programs could have an adverse effect on future amounts recognized as net patient service revenue.

The laws and regulations governing the Medicare and Medicaid programs are 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.

Managed care reimbursement agreements provide for payment of patient services at a fixed percentage of covered charges. The Corporation has also entered into contractual arrangements with various health maintenance and preferred provider organizations, the terms of which call for the Corporation to be paid for covered services at predetermined rates, including percent of charges, per diem, and case rate.

Net patient service revenue is recorded in the period in which services are rendered, based upon estimated amounts due from patients and third-party payors. Third parties include Medicare, Medicaid, managed health care plans, and other commercial plans. Estimated amounts due are calculated from contractually obligated terms of payment for each payor, as well as uninsured discounts applied for patients with no insurance coverage. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the year ended December 31 from these major payor sources is as follows (in thousands):

Payor	Net Revenue 2013	Net Revenue 2012
Anthem	**$ 180,080**	$ 174,833
Commercial	**249,960**	239,119
Medicare	**237,436**	230,485
Medicaid	**77,446**	169,295
Self Pay	**95,486**	84,005
Revenues before provision for bad debt	**840,408**	897,737
Provision for bad debts	**(62,724)**	(51,950)
Net patient service revenue	**$ 777,684**	$ 845,787

3. Contractual Arrangements With Third-Party Payors and Uncollectible Accounts (continued)

Net patient service revenue related to the Medicare program are 28% and 26% for the year ended December 31, 2013 and 2012, respectively. Net patient service revenue related to the Medicaid program are 9% and 19% for the years ended December 31, 2013 and 2012, respectively. Amounts reported under the Anthem Payor Contract account for 21% and 19%, of net patient service revenue for the year ended December 31, 2013 and 2012, respectively. Credit is granted without collateral to patients, most of whom are local residents and are insured under third-party arrangements. Major components of net patient accounts receivable include 30% from Medicare and 20% from Blue Cross at December 31, 2013, and 24% from Medicare and 19% from Blue Cross at December 31, 2012.

The provision for bad debts is based upon management's assessment of historical and expected net collections taking into consideration the trends in health care coverage, historical economic trends, and other collection indicators. Management assesses the adequacy of the allowances periodically throughout the year based upon historical write-off experience by major payor category. The results of the review are then utilized to make modifications, as necessary, to the provision for bad debts to provide for an appropriate allowance for uncollectible accounts. A significant portion of the Corporation's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Corporation records a significant provision for bad debts related to uninsured patients in the period the services are provided. The allowance for doubtful accounts recognized at December 31 by major payor source is as follows (in thousands):

Payor	Allowance for Doubtful Accounts 2013	Allowance for Doubtful Accounts 2012
Third Party	**$ 13,550**	$ 10,203
Self Pay	**9,573**	9,190
	$ 23,123	$ 19,393

3. Contractual Arrangements With Third-Party Payors and Uncollectible Accounts (continued)

Adjustments arising from reimbursement arrangements with third-party payors are accrued for on an estimated basis in the period in which the services are rendered, with the exception of Indiana Medicaid Disproportionate Share (DSH) reimbursement. DSH payments by the state of Indiana, if eligible, are paid according to the fiscal year of the state, which ends on June 30 of each year, and are based on the cost of uncompensated care provided by the DSH providers during their respective fiscal year ended during the state fiscal year. DSH payments are recorded after eligibility is determined, and payments are probable and reasonably estimable. Estimates for DSH, cost report settlements, and contractual allowances can differ from actual reimbursement based on the results of subsequent reviews, government regulatory changes, and cost report audits. In 2012, MHSB qualified for another two (2) years of State DSH payments for State Fiscal Year (SFY) 2012 and 2013. The amounts related to SFY 2013 and 2012 DSH were not determinable at December 31, 2012. As a result, MHSB recorded net patient service revenue of $23,071,000 in the year ended December 31, 2013 related to SFY 2013 and 2012 DSH payments. As the result of notification of successful appeal of the prior State DSH ruling related to SFY 2011 and 2010, MHSB recorded net patient service revenue of $52,953,000 for the year ended December 31, 2012.

In May 2012, the Indiana Hospital Assessment Fee program (HAF) was approved by the Federal Centers for Medicare and Medicaid Services for the period July 1, 2011 through June 30, 2013. The State of Indiana has approved HAF effective July 2013 through June 2017. The Federal Centers for Medicare and Medicaid Services (CMS) as of the date of this report has not ratified the HAF program. HAF was therefore suspended effective July 1, 2013. Under HAF, Indiana hospitals receive additional federal Medicaid funds for the State's health care system, administered by the Indiana Family and Social Services Administration. HAF includes both a payment to the Hospitals from the State (included in net patient service revenue) and an assessment (included in supplies and other expenses) against the Hospitals, which is paid to the State the same year.

Payments recognized for the six months ended June 30, 2013 totaled $28,954,000 and assessments for the same period were $14,486,000. No payments have been received or assessments paid after June 30, 2013 until approval of the HAF program by CMS. Because the program was approved mid-year 2012, payments recognized for the year ended December 31, 2012 included payments totaling $28,283,000 and assessments of $10,942,000 related to the

3. Contractual Arrangements With Third-Party Payors and Uncollectible Accounts (continued)

period July 1, 2011 through December 31, 2011. Payments recognized for the 12-month period covering January 1, 2012 through December 31, 2012 totaled $57,535,000 and assessments of $21,884,000. HAF payments are included in net patient service revenue and HAF assessments are included in supplies and other expenses in the consolidated statements of operations and changes in net assets.

During 2012, the Corporation recognized $5,400,000 as part of net patient service revenue for the Medicare Rural Floor Budget Neutrality Act settlement. This settlement with the Centers for Medicare & Medicaid Services involved approximately 2,200 hospitals nationwide and was made to resolve a challenge made by the plaintiff for underpayment of Medicare services dating back to 1999.

Estimates for cost report settlements and contractual allowances can differ from actual reimbursement based on the results of subsequent reviews and cost report audits. For the years ended December 31, 2013 and 2012, net patient service revenue has been decreased by approximately $259,000 and $42,000, respectively, for third-party payor settlements related to prior years.

4. Community Commitment

Community commitment represents charity care and/or unreimbursed costs for services rendered at a reduced fee, or no fee, due to the inability of the patient to pay for services. The amount of the community commitment provided was approximately $12,092,000 and $8,862,000 for the years ended December 31, 2013 and 2012, respectively, at estimated cost. The Corporation utilized a cost to charge ratio methodology for the cost analysis. The only reimbursement for financial assistance care received by the Corporation is determined through a settlement process in the Hospitals' annual Medicare cost report filing. Financial assistance care reimbursement was approximately $340,000 and $169,000 for the years ended December 31, 2013 and 2012, respectively.

4. Community Commitment (continued)

In addition, the Corporation reinvests funds into the community to improve the health status of community members, in particular underserved populations. Each year, the Corporation tithes based on the Corporation's income from operations plus certain investment earnings in a separate unrestricted current asset account. The estimated amount of tithing funds expended was approximately $2,556,000 and $2,176,000 for the years ended December 31, 2013 and 2012, respectively.

5. Pension Plans

The Corporation maintained a defined-contribution employee retirement and savings plan for MHSB, BMG, MHF, and BHV for all employees who have attained 21 years of age and have completed 12 months of continuous service. The Corporation's contributions are based on 100% of the employee's contributions, up to 4% of the employee's salary, both employee and the Corporation contributions were subject to certain limitations. Contributions were approximately $5,498,000 for the year ended December 31, 2012.

The Corporation maintained a defined-contribution employee retirement and savings plan for all employees of EGH. The Corporation's contributions are based on 100% of the employee's contributions, up to 4% of the employee's salary. Both employee and the Corporation contributions were subject to certain limitations. Contributions were approximately $2,162,000 for the year ended December 31, 2012.

Effective January 1, 2013, the defined-contribution plans were rolled into one plan under the Corporation. There were no changes to the contribution formula from the previous defined-contribution plans. Contributions were approximately $8,972,000 for the year ended December 31, 2013.

The Corporation also has a noncontributory, defined-benefit pension plan (the MEM Plan), which includes MHSB, BMG, MHF, and BHV with a final average pay plan and a cash balance plan. The cash balance plan was frozen for new participants and accrual of benefits as of December 31, 2007, and the much smaller grandfathered final average pay plan, with fewer participants, remains frozen and has not been altered. The assets in the cash balance plan will continue to earn interest, but service credits are frozen.

5. Pension Plans (continued)

The Corporation also has a noncontributory, defined-benefit pension plan (the EGH Plan) for EGH. As of December 31, 2007, the EGH Plan was frozen for all participants who had not attained the age of 50 and accumulated 15 years of vesting service as of December 31, 2007. No new participants are allowed into the plan as of December 31, 2007. Participants who were at least 50 years old and had accumulated 15 years of service at December 31, 2007, continued to accrue benefits under the terms of the EGH Plan until it was frozen effective January 1, 2013. Additionally, a lump-sum payout option was effective for all participants on July 1, 2012.

The Corporation's defined-benefit plan expense was as follows (in thousands):

	EGH	MEM	Total
December 31, 2013	**$ 2,659**	**$ 2,201**	**$ 4,860**
December 31, 2012	4,034	2,518	6,552

The Corporation's expected plan expense for the year ended December 31, 2014, is as follows (in thousands):

	EGH	MEM	Total
Plan expense	$ 879	$ 1,446	$ 2,325

5. Pension Plans (continued)

The measurement date of December 31 is utilized for both plans. The summary of the changes in the benefit obligation and plan assets and the resulting funded status of the plans are as follows (in thousands):

	December 31, 2013		
	EGH	**MEM**	**Total**
Accumulated benefit obligation	**$ 140,205**	**$ 129,976**	**$ 270,181**
Change in projected benefit obligation:			
Projected benefit obligation at beginning of year	**$ 162,292**	**$ 143,213**	**$ 305,505**
Service cost	**–**	**1,386**	**1,386**
Interest cost	**5,506**	**4,892**	**10,398**
Actuarial gain	**(18,490)**	**(12,847)**	**(31,337)**
Benefits and administrative expenses paid	**(4,985)**	**(6,668)**	**(11,653)**
Lump-sum benefits paid	**(4,118)**	**–**	**(4,118)**
Projected benefit obligation at end of year	**$ 140,205**	**$ 129,976**	**$ 270,181**
Change in plan assets:			
Fair value of plan assets at beginning of year	**$ 106,512**	**$ 96,953**	**$ 203,465**
Actual return on plan assets	**11,245**	**9,181**	**20,426**
Employer contributions	**5,000**	**2,750**	**7,750**
Benefits and administrative fees paid	**(4,985)**	**(6,668)**	**(11,653)**
Lump-sum benefits paid	**(4,118)**	**–**	**(4,118)**
Fair value of plan assets at end of year	**$ 113,654**	**$ 102,216**	**$ 215,870**
Funded status:			
Funded status of the plan and amounts recognized as pension and other liabilities in the consolidated balance sheet	**$ (26,551)**	**$ (27,760)**	**$ (54,311)**

5. Pension Plans (continued)

	December 31, 2012 EGH	MEM	Total
Accumulated benefit obligation	$ 162,292	$ 140,640	$ 302,932
Change in projected benefit obligation:			
Projected benefit obligation at beginning of year	$ 149,018	$ 131,413	$ 280,431
Service cost	806	1,332	2,138
Interest cost	6,237	5,444	11,681
Actuarial loss	14,768	11,764	26,532
Benefits and administrative expenses paid	(4,605)	(6,740)	(11,345)
Lump-sum benefits paid	(849)	–	(849)
Curtailment	(3,083)	–	(3,083)
Projected benefit obligation at end of year	$ 162,292	$ 143,213	$ 305,505
Change in plan assets:			
Fair value of plan assets at beginning of year	$ 88,598	$ 90,581	$ 179,179
Actual gain on plan assets	11,868	8,602	20,470
Employer contributions	11,500	4,510	16,010
Benefits and administrative fees paid	(4,605)	(6,740)	(11,345)
Lump-sum benefits paid	(849)	–	(849)
Fair value of plan assets at end of year	$ 106,512	$ 96,953	$ 203,465
Funded status:			
Funded status of the plan and amounts recognized as other long-term liabilities in the consolidated balance sheet	$ (55,780)	$ (46,260)	$ (102,040)

5. Pension Plans (continued)

Included in unrestricted net assets are the following amounts that have not been recognized in net periodic pension cost (in thousands):

	At December 31, 2013		
	EGH	**MEM**	**Total**
Prior service cost	**$ –**	**$ (5)**	**$ (5)**
Actuarial net gain	**40,766**	**29,463**	**70,229**
	$ 40,776	**$ 29,458**	**$ 70,224**

	At December 31, 2012		
	EGH	**MEM**	**Total**
Prior service cost	$ –	$ (1)	$ (1)
Actuarial net loss	67,654	47,420	115,074
	$ 67,654	$ 47,419	$ 115,073

The estimated prior service cost and actuarial net losses that will be amortized into expense over the next fiscal year (in thousands):

	At December 31, 2013		
	EGH	**MEM**	**Total**
Prior service cost	**$ –**	**$ (4)**	**$ (4)**
Actuarial net loss	**2,674**	**1,553**	**4,227**
Estimated benefit cost amortizations in the next fiscal year	**$ 2,674**	**$ 1,549**	**$ 4,223**

5. Pension Plans (continued)

Changes in the plan's assets and benefit obligations recognized in unrestricted net assets include the following (in thousands):

	Year ended December 31, 2013		
	EGH	**MEM**	**Total**
Current year actuarial gain	**$ (26,888)**	**$ (17,957)**	**$ (44,845)**
Current year amortization prior service cost	**–**	**7**	**7**
	$ (26,888)	**$ (17,950)**	**$ (44,838)**

	Year ended December 31, 2012		
	EGH	**MEM**	**Total**
Current year actuarial loss	$ 2,828	$ 7,414	$ 10,242
Current year amortization prior service cost	(9)	6	(3)
	$ 2,819	$ 7,420	$ 10,239

The components of net periodic benefit cost for the defined-benefit pension plans was as follows (in thousands):

	Year ended December 31, 2013		
	EGH	**MEM**	**Total**
Service cost	**$ –**	**$ 1,386**	**$ 1,386**
Interest cost	**5,506**	**4,892**	**10,398**
Expected return on plan assets	**(7,990)**	**(7,144)**	**(15,134)**
Prior service credit recognized	**–**	**(6)**	**(6)**
Amortization of recognized losses	**5,143**	**3,073**	**8,216**
Benefit cost	**$ 2,659**	**$ 2,201**	**$ 4,860**

5. Pension Plans (continued)

	Year ended December 31, 2012		
	EGH	MEM	Total
Service cost	$ 806	$ 1,332	$ 2,138
Interest cost	6,237	5,444	11,681
Expected return on plan assets	(8,003)	(6,699)	(14,702)
Prior service credit recognized	–	(6)	(6)
Amortization of recognized losses	4,994	2,447	7,441
Benefit cost	$ 4,034	$ 2,518	$ 6,552

Assumptions used to determine benefit obligations at the measurement date are as follows:

	December 31, 2013	
	EGH	**MEM**
Discount rates	**4.40%**	**4.40%**
Expected return on plan assets	**7.00**	**7.00**
Rate of compensation increase	**N/A**	**3.00**

	December 31, 2012	
	EGH	MEM
Discount rates	3.50%	3.50%
Expected return on plan assets	7.50	7.50
Rate of compensation increase	N/A	3.00

5. Pension Plans (continued)

Assumptions used to determine net pension expense for the fiscal year are as follows:

	December 31, 2013	
	EGH	**MEM**
Discount rates	**3.50%**	**3.50%**
Expected return on plan assets	**7.50**	**7.50**
Rate of compensation increase	**N/A**	**3.00**

	December 31, 2012	
	EGH	**MEM**
Discount rates	4.25%	4.25%
Expected return on plan assets	8.50	7.50
Rate of compensation increase	N/A	3.00

The following is a summary of the pension plan asset actual allocations at December 31, 2013 and December 31, 2012:

	EGH/MEM	**December 31, 2013**		**December 31, 2012**	
Asset Category	**Target**	**EGH**	**MEM**	**EGH**	**MEM**
Equity securities	58%	51%	31%	63%	38%
Debt securities	32	27	11	36	9
Other	10	22	58	1	53
Total	100%	100%	100%	100%	100%

5. Pension Plans (continued)

The following table sets forth by level, within the fair value hierarchy (see Note 11), the combined MEM and EGH plan assets carried at fair value as of December 31, 2013 (in thousands):

	Level 1	Level 2	Level 3	Fair Value
Short-term investment funds[a]	$ 34,082	$ –	$ –	$ 34,082
Mutual funds:[a]				
Large cap equity	31,010	–	–	31,010
International equity	50,378	–	–	50,378
Small cap equity	4,481	–	–	4,481
Blended fund	41,850	–	–	41,850
Total mutual funds	127,719	–	–	127,719
Common stocks[a]	4,061	–	–	4,061
Common/collective trust funds[b]	–	334	–	334
Long/short funds:[b,c]				
Long/short	–	18,326	–	18,326
Leveraged capital	–	6,386	–	6,386
Hedge funds:[c]				
Multi-strategy	–	16,425	–	16,425
Long/short hedge	–	880	–	880
Fixed and convertible arbitrage	–	1,979	–	1,979
Long commodities	–	4,761	–	4,761
Other	–	917	–	917
	$ 165,862	$ 50,008	$ –	$ 215,870

5. Pension Plans (continued)

The following table sets forth by level, within the fair value hierarchy (see Note 11), the combined MEM and EGH plan assets carried at fair value as of December 31, 2012 (in thousands):

	Level 1	Level 2	Level 3	Fair Value
Short-term investment funds[a]	$ 7,172	$ –	$ –	$ 7,172
Mutual funds:[a]				
Large cap equity	61,790	–	–	61,790
International equity	22,952	–	–	22,952
Small cap equity	3,361	–	–	3,361
Total return fund	9,639	–	–	9,639
Blended fund	49,959	–	–	49,959
Total mutual funds	147,701	–	–	147,701
Common stocks[a]	2,993	–	–	2,993
Common/collective trust funds[b]	–	314	–	314
Long/short funds:[b,c]				
Long/short	–	15,985	–	15,985
Leveraged capital	–	6,067	–	6,067
Hedge funds:[c]				
Multi-strategy	–	10,608	–	10,608
Long/short hedge	–	813	–	813
Fixed and convertible arbitrage	–	1,830	–	1,830
Long commodities	–	5,317	–	5,317
Other	–	849	–	849
Fund of funds[c]	–	–	3,816	3,816
	$ 157,866	$ 41,783	$ 3,816	$ 203,465

5. Pension Plans (continued)

(a) Pricing for common stocks, mutual funds, and short-term investments is based on the open market and is valued on a daily basis.

(b) Pricing is based on the market value of the securities and is valued on a monthly basis. In the event that a security is not actively traded in the open market, the characteristics are matched to a comparable issue to appropriately value the holding.

(c) Investments in other funds, long/short funds, and hedge funds are valued using the net asset value (NAV) provided by the administrator of the fund. These investments are not otherwise traded on a securities exchange. The NAV is based on the underlying assets owned by the fund, minus its liabilities, and then divided by the number of shares outstanding.

The table below sets forth a summary of changes in the fair value of Level 3 assets for the years ended December 31, 2013 and 2012 (in thousands):

Balance as of January 1, 2012	$ 3,027
Sales	(863)
Realized gains	483
Unrealized gains	1,169
Balance as of December 31, 2012	3,816
Sales	**(4,075)**
Realized gains	**590**
Unrealized gains	**(331)**
Balance as of December 31, 2013	**$ –**

5. Pension Plans (continued)

In addition to understanding fair value methodologies, the long/short, hedge, and other funds may be subject to redemption and/or liquidity restrictions. Restrictions of such funds by category are as follows (dollars in thousands):

Type of Fund	Fair Value at December 31, 2013	Fair Value at December 31, 2012	Redemption Restrictions	Liquidity Time Frame
Long/short funds				
Long/short	**$ 9,589**	$ 8,189	None	Under 95 days
Long/short	**8,737**	7,797	None	Annual
Long/short leveraged capital	**6,386**	6,067	None	Under 95 days
Hedge funds				
Multi-strategy hedge funds	**16,425**	10,608	None	Under 95 days
Long/short hedge funds	**880**	813	None	Under 95 days
Fixed and convertible arbitrage hedge funds	**1,979**	1,830	None	Under 95 days
Long commodities	**4,761**	5,317	None	Under 95 days
Other hedge funds	**917**	849	None	Under 95 days
Fund of funds	**–**	3,816	None	Under 95 days

The Corporation employs a total return investment approach, whereby a mix of equities and fixed-income investments are used to maximize the long-term return of plan assets for a prudent level of risk. Risk tolerance is established through careful consideration of plan liabilities, plan funded status, and corporate financial condition. The investment portfolio contains a diversified blend of equity, fixed-income, and alternative investments. Equity investments are diversified across U.S. and non-U.S. corporate stocks, as well as growth, value, and small and large capitalizations.

5. Pension Plans (continued)

Other assets, such as hedge funds, are used to enhance long-term returns while improving portfolio diversification. The Corporation's external investment managers may use derivatives to gain market exposure in an efficient and timely manner. Investment risk is measured and monitored on an ongoing basis through quarterly investment portfolio reviews, annual liability measurements, and periodic asset/liability studies.

The following pension benefit payments, which reflect expected future service, as appropriate, are expected to be paid in the years ended December 31 (in thousands):

	EGH	MEM	Total
2014	$ 10,085	$ 7,285	$ 17,370
2015	9,311	7,704	17,015
2016	9,811	7,981	17,792
2017	9,955	8,516	18,471
2018	10,177	8,536	18,713
2019 – 2022	47,343	46,471	93,814

The Corporation contributed the following to plan assets for the years ended December 31, 2013 and 2012 from employer assets (in thousands):

	EGH	MEM	Total
2013 contributions	**$ 5,000**	**$ 2,750**	**$ 7,750**
2012 contributions	$ 11,500	$ 4,510	$ 16,010

The Corporation anticipates contributing the following to the plan assets from employer assets in 2014 (in thousands):

	EGH	MEM	Total
Anticipated 2014 total contributions	$ 4,000	$ 4,200	$ 8,200

6. Lease Obligations

The Corporation leases certain office space and equipment under noncancelable operating leases. At December 31, 2013, the minimum future rental payments under these leases are as follows:

2014	$ 4,262,000
2015	3,413,000
2016	1,804,000
2017	1,398,000
2018	1,273,000
Thereafter	6,721,000
	$ 18,871,000

Rental expense for the years ended December 31, 2013 and 2012, was approximately $5,671,000 and $5,084,000, respectively, which is included in supplies and other expense.

7. Long-Term Debt

Long-term debt consists of the following at December 31 (in thousands):

	2013	2012
Tax-exempt bonds issued on behalf of BHS by the Indiana Finance Authority:		
BHS Revenue Bonds, Series 2013A, bearing interest at fixed rates between 2.00% and 5.00%, due in varying annual installments on August 15 of each year through 2034	**$ 110,265**	$ –
BHS Revenue Note, Series 2013B, bearing interest at a fixed rate of 1.17%, at December 31, 2013, due in monthly installments through 2020	**6,805**	–
Tax-exempt bonds issued on behalf of BHS by the Hospital Authority of St. Joseph County:		
BHS Revenue Bonds, Series 2013C, bearing interest at fixed rates between 3.75% and 5.00% , due in varying annual installments on August 15 of each year through 2044	**46,130**	–
Tax-exempt bonds issued on behalf of MHSB by the Hospital Authority of St. Joseph County:		
MHSB Revenue Bonds, Series 2008A, bearing interest at variable rates retaining the hedge from Series 2006 with a floating fixed interest rate swap of 3.52% at December 31, 2013 and 2012, due in varying annual installments on August 15 of each year through 2033	**38,065**	38,230
MHSB Revenue Bonds, Series 2008B, bore interest at a variable rate of 0.14% at December 31, 2012	–	36,370
MHSB Revenue Bonds, Series 2007, bore interest at a variable rate of 1.08% at December 31, 2012	–	1,000
MHSB Revenue Bonds, Series 1998A, bore interest of 4.75%, at December 31 2012	–	58,000

7. Long-Term Debt (continued)

	2013	2012
Tax-exempt bonds issued on behalf of EGH by the Hospital Authority of Elkhart County:		
EGH Revenue Bonds, Series 2008, bearing interest at a variable rates of 0.05% and 0.14% at December 31, 2013 and 2012, due annually on May 1 of each year through 2033	**43,790**	44,685
EGH Revenue Bonds, Series 1998, bore interest at a fixed rate of 5.25%	**–**	37,590
Mortgage – bearing interest at a variable rates of 2.42% and 2.46% at December 31, 2013 and 2012, LIBOR plus 2.25%, due in varying annual installments on the last day of every month through 2015	**1,217**	1,419
Capital leases	**11**	275
	246,283	217,569
Unamortized premium (discount)	**16,853**	(2,509)
	263,136	215,060
Less current portion	**6,899**	6,920
	$ 256,237	$ 208,140

In May 2013, the Indiana Finance Authority, on behalf of BHS, issued revenue refunding bonds Series 2013A (2013A) in the principal amount of $116,705,000. The interest rate for 2013A is a fixed rate varying between 2.00% and 5.00%. The proceeds from 2013A were utilized to refund the MHSB Revenue Bonds, Series 2008B, MHSB Revenue Bonds, Series 1998A, and the EGH Revenue Bonds, Series 1998.

In May 2013, the Indiana Finance Authority, on behalf of BHS, issued a revenue note Series 2013B (2013B) in the principal amount of $7,492,188. The interest rate for 2013B is a fixed rate of 1.17%. Proceeds from the bond were utilized for the purchase of a Helicopter.

In May 2013, the Hospital Authority of St. Joseph County, on behalf of BHS, issued revenue bonds Series 2013C (2013C) in the principal amount of $46,130,000. The interest rate for 2013C is afixed rate varying between 3.75% and 5.00%. The proceeds from 2013C were utilized to refund the MHSB Revenue Bonds, Series 2007. The remaining proceeds are set aside in externally designated investments for future projects.

7. Long-Term Debt (continued)

In August 2008, the Hospital Authority of St. Joseph County, on behalf of MHSB, issued revenue refunding bonds in the principal amount of $78,495,000. The interest rate for the Series 2008A is a weekly interest rate determined by the remarketing agent. The 2008 bond issue is secured by an irrevocable direct-pay letter of credit issued by JPMorgan Chase Bank (JPMorgan). The JPMorgan letters of credit expire on October 12, 2015. As long as no default has occurred, draws on the direct-pay letter of credit made for failed remarketing will be required to be repaid in 12 equal quarterly installments commencing 12 months after the date of draw.

The Series 2008A Bonds are subject to mandatory redemption through the operation of a sinking fund on each August 15 commencing with the year 2011 to, and including the year, 2033 in amounts sufficient to redeem the principal amounts.

In May 2007, the Hospital Authority of St. Joseph County, on behalf of MHSB, issued revenue bonds in the principal amount of $80,000,000 (the Series 2007 Bonds). MHSB purchased $27,000,000 par value of the Series 2007 Bonds for $13,230,000 in March 2009. In October 2008, MHSB purchased $52,000,000 par value of the Series 2007 Bonds for $29,640,000. The par value of the Series 2007 Bonds remains outstanding, with MHSB as owner of record. The consolidated balance sheets reflect these purchases as a reduction of long-term debt for the Series 2007 Bonds of $79,000,000 at par value. These bonds were refunded and reissued in May 2013 under the Series 2013C bonds.

The Hospital Authority of Elkhart County issued $47,800,000 of Series 2008 Hospital Revenue Bonds (the Series 2008 Bonds). EGH borrowed the proceeds of the sale of the Series 2008 Bonds and evidenced this loan with a loan agreement, issued under a Trust Indenture dated December 1, 2008.

The proceeds of the Series 2008 Bonds were issued to retire interest and principal payments of previously outstanding bonds. The Series 2008 Bonds require EGH to hold a letter of credit with JPMorgan. The letter of credit expires on January 15, 2015, and decreases by the principal payments made by EGH on the Series 2008 Bonds. The Series 2008 Bonds mature in May 2033.

As long as no default has occurred, draws on the direct-pay letter of credit made for failed remarketing will be required to be repaid in eight equal quarterly installments commencing on the last business day of the fourth calendar quarter after the stated expiration date of the letter of credit (January 15, 2015).

7. Long-Term Debt (continued)

As of the date of the issuance of the Series 2007 Bonds, under the terms of a Master Trust Indenture, BMG and MHSB formed the Obligated Group (the Obligated Group). MHF and BHV constitute designated affiliates under the terms of the Master Trust Indenture.

The MHSB Series 2008A 2008B, 2007, and 1998A Bonds were issued pursuant to the Master Trust Indenture, and the bonds are secured by pledged revenues of the Obligated Group and contain various covenants, including achievement of specified financial ratios and limitations on additional debt.

In December 2012, the Corporation was admitted into the Obligated Group and became the Obligated Group Agent. On December 31, 2012, EGH was admitted into the Obligated Group. The Series 2008 and 1998 EGH Bonds were substituted into the existing MHSB Master Trust Indentures and the EGH Trust Indentures were cancelled and released.

The loan agreements require maintenance of certain debt service coverage ratios, limit additional borrowings, and require compliance with various other restrictive covenants. The Corporation was in compliance with all covenants during 2013 and 2012.

Interest capitalized for the years ended December 31, 2013 and 2012, was approximately $645,000 and $199,000.

Maturities of long-term debt and capital lease obligations for each of the next five years are as follows (in thousands):

2014	$ 6,899
2015	7,953
2016	7,196
2017	7,563
2018	7,926

8. Lines of Credit

MHSB has a $2,000,000 revolving line of credit with 1st Source Bank. The line of credit was renewed and extended through May 31, 2014. Of the $2,000,000 revolving line of credit, $50,000 and $300,000 for the years ended December 31, 2013 and 2012 respectively, was segregated for the beneficiary of a self-insurance trust. Conversely, $1,950,000 and $1,700,000 was available to be drawn upon at December 31, 2013 and 2012, respectively. No draws were taken by MHSB in either 2013 or 2012. The interest rate on the line of credit is prime rate minus one-half percent. No amounts were outstanding on the line of credit as of December 31, 2013 or 2012.

MHSB has a $7,000,000 revolving line of credit with Merrill Lynch. The line of credit is due on demand and can be terminated by either party with notice. Advances on the line can be made with a variable rate of LIBOR plus 1.25%, at a fixed rate as agreed upon by the parties for a 12-month period or at an agreed-upon term rate for periods greater than 12 months. At any time MHSB may request that variable rate advances be converted into fixed or term rates. No draws were taken by MHSB in either 2013 or 2012. No amounts were outstanding on the line of credit as of December 31, 2013 or 2013.

9. Interest Rate and Basis Swaps

MHSB has various derivative instruments to manage the exposure on interest rates and MHSB's interest expense. Through the use of derivative financial instruments, MHSB is exposed to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contracts. When the fair value of the derivative contract is positive, the counterparty owes MHSB, which creates credit risk to MHSB. When the fair value of the derivative contract is negative, MHSB owes the counterparty, and there is no credit risk to MHSB at that point in time. MHSB minimizes the credit risk in derivative instruments by entering into transactions that require the counterparty to post collateral for the benefit of the fair value of the derivative contract. Market risk is the adverse effect on the value of the financial instrument that results from a change in interest rates. The management of market risk associated with interest rate changes is defined in MHSB's Swap Management Policy (the Policy). The Policy includes continuous monitoring of market conditions, emergent opportunities, and risks. Swap management is meant to be long term in nature, and any modifications to the program are reviewed for the long-term costs and benefits. Management also mitigates risk through periodic reviews of its derivative position in the context of its total blended cost of capital.

9. Interest Rate and Basis Swaps (continued)

In November 2012, MHSB terminated four PNC bank swaps with notional amounts of $30,000,000, $30,000,000, $77,150,000, and $56,000,000. MHSB realized a net loss of $290,000, which is included in nonoperating income on the consolidated statements of operations and changes in net assets.

The derivative instruments require adherence to collateral posting thresholds. For the years ended December 31, 2013 and 2012, the mark to market valuation on the swap portfolio was below the required collateral posting threshold of $30,000,000 with PNC Bank, $25,000,000 with Morgan Stanley, $25,000,000 with Wells Fargo, and $25,000,000 with Deutsche Bank.

The following is a summary of the outstanding fixed payer rate swaps as of December 31, 2013:

Origination Date	Notional Amounts	Corporation Receives	Corporation Pays	Maturity Date
March 2006	$ 38,065,000	61.9% of 30-day LIBOR plus 0.31%	3.5150%	August 2033
March 2003	$ 8,600,000	65% of 30-day LIBOR plus 0.45%	3.8100%	August 2034

The following is a summary of the outstanding fixed payer rate swaps as of December 31, 2012:

Origination Date	Notional Amounts	Corporation Receives	Corporation Pays	Maturity Date
March 2006	$ 38,230,000	61.9% of 30-day LIBOR plus 0.31%	3.5150%	August 2033
March 2003	$ 8,800,000	65% of 30-day LIBOR plus 0.45%	3.8100%	August 2034

9. Interest Rate and Basis Swaps (continued)

The following is a summary of the outstanding basis rate swaps as of December 31, 2013 and 2012:

Origination Date	Notional Amounts	Corporation Receives	Corporation Pays	Maturity Date
January 2007	$ 42,000,000	74.6% of 1M LIBOR	SIFMA tax-exempt index +.0715%	January 2041
August 2007	$ 54,000,000	61.7% of 1M LIBOR + 0.76%	SIFMA tax-exempt index +.0715%	August 2041
March 2001	$ 140,000,000	75.125% of 3M LIBOR	SIFMA tax-exempt index	March 2031
July 2009	$ 63,000,000	74.6% of 1M LIBOR	SIFMA tax-exempt index + 0.17%	January 2041
August 2009	$ 81,000,000	61.7% of 1M LIBOR + 0.76%	SIFMA tax-exempt index + 0.17%	August 2041

Net interest paid or received under the above swap agreements is included in interest expense. The net differential for the Corporation as a result of the swap agreements amounted to payments of approximately $589 and $368 for the years ended December 31, 2013 and 2012, respectively, and is reflected as an increase to interest expense. The swap agreements do not qualify for hedge accounting; therefore, the change in the fair value of the swap agreements is recorded as an unrealized nonoperating loss of approximately $6,743,000 and gain of approximately $12,333,000 for the years ended December 31, 2013 and 2012, respectively, and a realized nonoperating loss of $290,000 for the year ended December 31, 2012.

The fair value of derivative instruments at December 31 is as follows (in thousands):

	Balance Sheet Location	2013	2012
Derivatives not designated as hedging instruments:			
Interest rate contracts	Interest rate and basis swaps	**$ 36,761**	$ 30,017

10. Investments

Total investment return for the years ended December 31, 2013 and 2012, is summarized as follows (in thousands):

	2013	2012
Investment return:		
Net unrealized gains on investments	**$ 17,455**	$ 26,981
Net realized gains on investments	**20,493**	16,859
Net equity earnings on alternative investments	**12,711**	6,987
	50,659	50,827
Reported as:		
Investment income, net (nonoperating)	**49,466**	50,178
Investment income (temporarily restricted net assets)	**1,193**	649
	$ 50,659	$ 50,827

The Corporation's investments are exposed to various kinds and levels of risk. Equity mutual funds expose the Corporation to market risk, performance risk, and liquidity risk. Market risk is the risk associated with major movements of the equity markets. Performance risk is the risk associated with a company's operating performance. Fixed-income securities expose the Corporation to interest rate risk, credit risk, and liquidity risk. As interest rates change, the value of many fixed-income securities is affected, including those with fixed interest rates. Credit risk is the risk that the obligor of the security will not fulfill its obligations. Liquidity risk is affected by the willingness of market participants to buy and sell given securities. Liquidity risk tends to be higher for equities related to small capitalization companies. Due to the volatility of the capital markets, there is a reasonable possibility of changes in fair value, resulting in additional gains and losses in the near term.

11. Fair Value of Financial Instruments

The carrying values of cash and cash equivalents, accounts receivable, and accounts payable and accrued expenses are reasonable estimates of their fair values due to the short-term nature of these financial instruments.

11. Fair Value of Financial Instruments (continued)

The fair value of the Corporation's long-term debt, excluding capital leases and the mortgage, is approximately $246,103,000 and $216,824,000 at December 31, 2013 and 2012, respectively. The valuation for the estimated fair value of long-term debt is completed by a third-party service and takes into account a number of factors, including, but not limited to, any one or more of the following: (i) general interest rate and market conditions; (ii) macroeconomic and/or deal-specific credit fundamentals; (iii) valuations of other financial instruments that may be comparable in terms of rating, structure, maturity, and/or covenant protection; (iv) investor opinions about the respective deal parties; (v) size of the transaction; (vi) cash flow projections, which, in turn, are based on assumptions about certain parameters that include, but are not limited to, default, recovery, prepayment, and reinvestment rates; (vii) administrator reports, asset manager estimates, broker quotations, and/or trustee reports; and (viii) comparable trades, where observable. Based on the inputs in determining the estimated fair value of debt, this fair value measurement would be considered Level 2.

Accounting Standards Codification (ASC) Topic 820-10-50-2 establishes a three-level valuation hierarchy. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 – Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

- Level 2 – Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active market and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instruments.

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

11. Fair Value of Financial Instruments (continued)

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The following tables present the financial instruments carried as of December 31, 2013 and 2012, by caption, on the consolidated balance sheets by the valuation hierarchy defined above for those instruments carried at fair value, as well as the alternative investments that are reported on the equity method of accounting. Deferred compensation investments are included in other assets on the consolidated balance sheets.

	December 31, 2013					
	Level 1	Level 2	Level 3	Fair Value	Equity Method	Carrying Value
	(In Thousands)					
Assets						
Short-term investments[a]	$ 43,072	$ –	$ –	$ 43,072	$ –	$ 43,072
Internally designated investments:						
Mutual funds:[a]						
Large cap equity	59,188	–	–	59,188	–	59,188
International equity	115,387	–	–	115,387	–	115,387
Small cap equity	49,054	–	–	49,054	–	49,054
Total return fund	5,562	–	–	5,562	–	5,562
Blended fund	194,495	–	–	194,495	–	194,495
Total mutual funds	423,686	–	–	423,686	–	423,686
Common stock[a]	11,807	–	–	11,807	–	11,807
Bonds[b]	–	1,876	–	1,876	–	1,876
Alternatives:						
Fixed income	–	–	–	–	14,867	14,867
Fund of hedge funds	–	–	–	–	59,512	59,512
Long/short credit	–	–	–	–	6,386	6,386
Long/short equity	–	–	–	–	21,891	21,891
Private equity	–	–	–	–	12,468	12,468
Real estate	–	–	–	–	6,425	6,425
Total alternatives	–	–	–	–	121,549	121,549
Total internally designated investments	$435,493	$ 1,876	$ –	$437,369	$121,549	$558,918

11. Fair Value of Financial Instruments (continued)

	December 31, 2013					
	Level 1	Level 2	Level 3	Fair Value	Equity Method	Carrying Value
			(In Thousands)			
Assets						
Ext. designated investment – debt agreements:						
Fixed income[a]	$ 28,812	$ –	$ –	$ 28,812	$ –	$ 28,812
Ext. designated investment – insurance trust:						
Fixed income[a]	2,582	–	–	2,582	–	2,582
Board-designated endowment:						
Mutual funds:[a]						
Equities	10,431	–	–	10,431	–	10,431
Blended fund	5,866	–	–	5,866	–	5,866
Fixed income[a,b]	194	322	–	516	–	516
Equities[a]	983	–	–	983	–	983
Alternatives	–	–	–	–	3,172	3,172
Total board-designated endowment	17,474	322	–	17,796	3,172	20,968
Endowment:						
Mutual funds:[a]						
Fixed income	518	–	–	518	–	518
Equities	847	–	–	847	–	847
Money market[a]	406	–	–	406	–	406
Common collective trust funds[d]	–	4,507	–	4,507	–	4,507
Total endowment	1,771	4,507	–	6,278	–	6,278
Total	$ 529,204	$ 6,705	$ –	$ 535,909	$124,721	$ 660,630
Liabilities						
Swaps[c]	$ –	$ –	$ (36,761)	$ (36,761)	$ –	$ (36,761)
Total	$ –	$ –	$ (36,761)	$ (36,761)	$ –	$ (36,761)

11. Fair Value of Financial Instruments (continued)

	December 31, 2012					
	Level 1	Level 2	Level 3	Fair Value	Equity Method	Carrying Value
	(In Thousands)					
Assets						
Short-term investments[a]	$ 7,305	$ –	$ –	$ 7,305	$ –	$ 7,305
Internally designated investments:						
Mutual funds:[a]						
Large cap equity	47,297	–	–	47,297	–	47,297
International equity	104,668	–	–	104,668	–	104,668
Small cap equity	5,631	–	–	5,631	–	5,631
Long/short equity	4,359	–	–	4,359	–	4,359
Total return fund	81,112	–	–	81,112	–	81,112
Blended fund	167,143	–	–	167,143	–	167,143
Total mutual funds	410,210	–	–	410,210	–	410,210
Common stock[a]	9,490	–	–	9,490	–	9,490
Bonds[b]	–	1,590	–	1,590	–	1,590
Alternatives:						
Fixed income	–	–	–	–	14,372	14,372
Fund of hedge funds	–	–	–	–	33,101	33,101
Long/short credit	–	–	–	–	6,068	6,068
Long/short equity	–	–	–	–	38,432	38,432
Private equity	–	–	–	–	12,027	12,027
Real estate	–	–	–	–	6,064	6,064
Total alternatives	–	–	–	–	110,064	110,064
Total internally designated investments	$ 419,700	$ 1,590	$ –	$ 421,290	$ 110,064	$ 531,354

11. Fair Value of Financial Instruments (continued)

	December 31, 2012					
	Level 1	Level 2	Level 3	Fair Value	Equity Method	Carrying Value
	(In Thousands)					
Assets						
Ext. designated investment – insurance trust:						
Fixed income[a]	$ 2,584	$ –	$ –	$ 2,584	$ –	$ 2,584
Board-designated endowment:						
Mutual funds:[a]						
Equities	8,422	–	–	8,422	–	8,422
Fixed income[a,b]	6,262	259	–	6,521	–	6,521
Long/short equity	1,323	–	–	1,323	–	1,323
Equities[a]	882	–	–	882	–	882
Alternatives	–	–	–	–	2,184	2,184
Total board-designated endowment	16,889	259	–	17,148	2,184	19,332
Endowment:						
Mutual funds:[a]						
Fixed income	397	–	–	397	–	397
Equities	879	–	–	879	–	879
Money market[a]	181	–	–	181	–	181
Common collective trust funds[d]	–	3,778	–	3,778	–	3,778
Total endowment	1,457	3,778	–	5,235	–	5,235
Other long-term assets[a]						
Cash[a]	4,415	–	–	4,415	–	4,415
Fixed-income mutual fund[a]	2,965	–	–	2,965	–	2,965
Total	$ 455,315	$ 5,627	$ –	$ 460,942	$112,248	$ 573,190
Liabilities						
Swaps[c]	$ –	$ –	$ (30,017)	$ (30,017)	$ –	$ (30,017)
Total	$ –	$ –	$ (30,017)	$ (30,017)	$ –	$ (30,017)

(a) Pricing for mutual funds, short-term investments, equities, and government obligations is based on the open market and is valued on a daily basis.

(b) Pricing is based on the fair value of the securities and is valued on a monthly basis. Information used to value this account is provided by International Data Corp. (IDC). In the event that a security is not actively traded in the open market, the characteristics are matched to a comparable issue from the IDC data to appropriately value the holding.

11. Fair Value of Financial Instruments (continued)

(c) Pricing is based on discounted cash flows to reflect a credit spread adjustment to the LIBOR discount curve in order to reflect "nonperformance" risk. The credit spread adjustment is derived from how other comparable entities' bonds price and trade in the market. As the credit spread adjustment is a significant component of the swap valuation and is an unobservable input, the swaps have been classified as Level 3.

(d) Pricing is based on the market value of the securities and is valued on a monthly basis.

In addition to understanding fair value methodologies, the alternative investments may have redemption and/or liquidity restrictions. Restrictions of such funds by category are as follows as of December 31, 2013:

Type of Fund	Carrying Value *(In Thousands)*	Redemption Restrictions	Liquidity Time Frame
Fixed income	$ 14,867	None	Illiquid
Fund of hedge funds	664	None	Illiquid
Fund of hedge funds	1,067	Redemptions upon realization	Illiquid
Fund of hedge funds	60,953	None	Under 95 days
Long/short credit	6,386	None	Under 95 days
Long/short equity	21,891	None	Annual
Private equity	12,468	None	Illiquid
Real estate	6,425	None	Under 95 days

The table below sets forth a summary of changes in the fair value of the Corporation's Level 3 swaps for the years ended December 31, 2013 and 2012 (in thousands):

	2013	2012
Balance, beginning of the year	**$ (30,017)**	$ (42,060)
Unrealized gains, net	**(6,744)**	12,333
Realized loss, net	–	(290)
Balance, end of the year	**$ (36,761)**	$ (30,017)

11. Fair Value of Financial Instruments (continued)

For the year ended December 31, 2013, the Corporation recorded approximately $6,744,000 in nonoperating losses, which relates to losses of $5,444,000 due to the change in the swaps value and loss of $1,299,000 to reflect the fair value of the uncollateralized portion fo the swap balance. For the year ended December 31, 2012, the Corporation recorded approximately $12,043,000 in nonoperating gains, which relates to gains of $13,620,000 due to the change in the swaps' value, $290,000 in realized gain on the termination of swaps, and loss of $1,287,000 to reflect the fair value of the uncollateralized portion of the swap balance.

12. Functional Expenses

The Corporation provides general health care services to residents within its geographic location. Expenses related to this and general and administrative functions for the years ended December 31, 2013 and 2012, are as follows (in thousands):

	2013	2012
Health care services	**$ 544,610**	$ 514,283
Affiliated health services	**103,417**	97,702
General and administrative	**122,056**	154,064
	$ 770,083	$ 766,049

13. Commitments

BMG is a guarantor for a portion of a loan of an unconsolidated joint venture, Valparaiso Medical Development, LLC, in which BMG records an equity interest. The portion of debt guaranteed by BMG is a maximum of $5,760,000 and $6,000,000 at December 31, 2013 and 2012. No amounts have been paid or accrued pursuant to this guarantee as of December 31, 2013 and 2012. The loan is collateralized by the assets, including the facility and land, held by Valparaiso Medical Development, LLC.

The Corporation has committed to investing $40,000,000 in certain hedge funds and alternative investments. During the years ended December 31, 2013 and 2012, the Corporation invested approximately $4,497,000 and $16,107,000, respectively. The Corporation had a remaining unfunded commitment of approximately $12,748,000 at December 31, 2013.

13. Commitments (continued)

The Corporation has entered into various construction projects including related commitments to construction managers, architects and other vendors. The commitments under these agreements was approximately $66,916,000 of which approximately $5,069,000 was paid at December 31, 2013. The Corporation has made additional commitments related to these projects subsequent to December 31, 2013 and through the date of this report of approximately $2,900,000.

14. Professional Liability Insurance

The Corporation is a defendant in certain litigation arising in the ordinary course of business. MHSB and EGH have obtained separate professional liability insurance coverage under claims-made policies. MHSB terminated self-funding of its professional and general liability coverage on November 30, 2009. EGH terminated self-funding of its professional and general liability coverage on April 1, 2012. The Indiana Medical Malpractice Act has provided recovery up to $1,250,000 per occurrence, with the first $250,000 covered by the respective entity. MHSB maintains a trust fund for its self-insurance program, which it will continue to maintain until all claims have been settled. The fair value of the trust fund at December 31, 2013 and 2012, was approximately $2,582,000 and $2,584,000, respectively. The amount of malpractice and general liability claims, including a component for incurred but not reported claims, was approximately $6,043,000 and $6,395,000, gross of an insurance recoverable at December 31, 2013 and 2012, respectively, which is included in pension and other liabilities. The interest rate used to discount these claims was 3.0% at December 31, 2013 and 2012. In addition, at December 31, 2013 and 2012, the Corporation recognized a recoverable insurance asset of approximately $3,908,000 and $3,250,000, respectively, which is included in deferred charges and other assets.

15. Income Taxes

The Corporation and its related affiliates, except for BHV, have been determined to qualify as exempt from federal income tax under Section 501(a) as organizations described in Section 501(c)(3) of the Code.

Most of the income received by the Corporation and its related affiliates, except for BHV, is exempt from taxation, as the income related to the mission of the organization. Accordingly, there is no material provision for income tax for these entities. However, some of the income received by exempt entities is subject to taxation as unrelated business income. The Corporation and its subsidiaries file federal and various state income tax returns in the United States.

16. Restricted Net Assets

Temporarily restricted net assets are available for the following purposes or periods at December 31, 2013 and 2012 (in thousands):

	2013	2012
Net assets currently available for:		
General – health care	**$ 7,907**	$ 6,561
Capital	**2,821**	1,906
Programs	**259**	301
Education	**217**	196
Other	**1,158**	1,010
	$ 12,362	$ 9,974

Permanently restricted net assets generate investment income, which is used to benefit the following purposes at December 31, 2013 and 2012 (in thousands):

	2013	2012
Endowment investments providing income for health care educational purposes	**$ 191**	$ 191
Endowment for charity care at EGH	**400**	400
	$ 591	$ 591

17. Board-Designated Endowment and Endowment Investments

In August 2008, the FASB issued ASC 958, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds*, which, among other things, provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Act of 2006 (UPMIFA) and additional disclosures about an organization's endowment funds. In 2007, the state of Indiana adopted UPMIFA. The adoption of UPMIFA had no effect on accounting for the Corporation's endowment. The following disclosures are made as required by ASC 958.

17. Board-Designated Endowment and Endowment Investments (continued)

The Corporation's endowment consists of a donor-restricted endowment fund and a board-designated endowment fund. As required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The Board of Directors of the Corporation has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary.

MHF has a Board-designated endowment. The Board provides direction to use the income, profits for support, betterment, improvement, upkeep, expansion, and replacement of BMG and its corporate affiliates.

MHF follows its Statement of Investment Objectives and Policy, which established formal yet flexible investment guidelines incorporating prudent risk parameters, appropriate asset guidelines, and realistic return goals. Per the policy, the primary objective is to meet commitments to employees at a reasonable cost to the company. Therefore, MHF will actively invest to achieve real growth of capital over inflation through appreciation of securities held and through the accumulation and reinvestment of dividends and interest income. MHF utilizes an investment consulting firm to assist in development of asset allocation targets, review investment performance to benchmarks, review investment strategies, and communicate this information to the MHF Investment Committee and management.

EGH has a donor-restricted endowment established for patient care purposes. EGH has established an investment and spending policy related to the preservation and appreciation of this endowment. Should the underlying assets fall below this targeted amount, EGH pursues actions consistent with established policies to return the endowment to the targeted amount. Based upon these policies, the investment earnings on the endowment are temporarily restricted until the Board authorizes release of funds for patient care purposes. A portion of the endowment is held as permanently restricted based on the original restriction at the time of donation.

17. Board-Designated Endowment and Endowment Investments (continued)

	December 31, 2013		
	Unrestricted	**Permanently Restricted**	**Total**
	(In Thousands)		
Cash and cash equivalents	**$ –**	**$ 191**	**$ 191**
Board-designated endowment funds	**20,968**	**–**	**20,968**
Endowment and temporarily restricted investments	**–**	**400**	**400**
Total investment funds	**20,968**	**400**	**21,368**
Total funds	**$ 20,968**	**$ 591**	**$ 21,559**

	December 31, 2012		
	Unrestricted	**Permanently Restricted**	**Total**
	(In Thousands)		
Cash and cash equivalents	$ –	$ 191	$ 191
Board-designated endowment funds	19,332	–	19,332
Endowment and temporarily restricted investments	–	400	400
Total investment funds	19,332	400	19,732
Total funds	$ 19,332	$ 591	$ 19,923

17. Board-Designated Endowment and Endowment Investments (continued)

	Unrestricted	Permanently Restricted	Total
		(In Thousands)	
Endowment and board-designated endowment funds and endowment investments, beginning of year (January 1, 2012)	$ 17,525	$ 400	$ 17,925
Investment return:			
Investment income	381	–	381
Net unrealized gains on investments	1,375	–	1,375
Net equity gains on investments	51	–	51
Total investment return	1,807	–	1,807
Endowment and board-designated endowment funds and endowment investments, end of year (December 31, 2012)	19,332	400	19,732
Investment return:			
Investment income	**231**	**–**	**231**
Net unrealized gains on investments	**2,066**	**–**	**2,066**
Net equity gains on investments	**29**	**–**	**29**
Released for use in operations	**(690)**	**–**	**(690)**
Total investment return	**1,636**	**–**	**1,636**
Endowment and board-designated endowment funds and endowment investments, end of year (December 31, 2013)	**$ 20,968**	**$ 400**	**$ 21,368**

18. Subsequent Events

The Corporation evaluated events and transactions occurring subsequent to December 31, 2013 through March 6, 2014, the date of issuance of the consolidated financial statements. During this period, there were no subsequent events requiring recognition or disclosure in the consolidated financial statements, other than those previously disclosed.

Supplementary Information

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Building a better working world

Report of Independent Auditors on Supplementary Information

The Board of Directors
Beacon Health System, Inc. and Affiliated Corporations

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The following financial information is presented for purposes of additional analysis and is not a required part of the 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 financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the 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 financial statements as a whole.

Ernst & Young LLP

March 6, 2014

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Balance Sheet

(In Thousands)

December 31, 2013

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Memorial Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.
Assets								
Current assets:								
Cash and cash equivalents	$ 91,057	$ –	$ 40,007	$ 6,446	$ 5,677	$ 1,990	$ 28,898	$ 8,039
Short-term investments	43,072	–	36,615	–	1,057	–	5,400	–
Patient accounts receivable, net	138,950	–	81,897	8,172	–	7,082	41,535	264
Due from third-party payors	7,230	–	6,612	–	–	–	618	–
Other receivables	10,299	–	3,900	1,119	129	364	4,368	419
Inventories	21,641	–	13,332	–	–	1,760	6,549	–
Prepaid expenses	11,146	–	1,793	382	–	125	1,964	6,882
Due from affiliates	–	(8,303)	2,205	–	–	–	237	5,861
Total current assets	323,395	(8,303)	186,361	16,119	6,863	11,321	89,569	21,465
Assets limited as to use:								
Internally designated investments	558,918	–	326,980	–	–	–	231,938	–
Externally designated investments under debt agreements	28,812	–	28,812	–	–	–	–	–
Externally designated investments – insurance trust	2,582	–	2,551	20	–	11	–	–
Board-designated endowment	20,968	–	–	–	20,968	–	–	–
Endowment and temporarily restricted investments	6,278	–	–	–	–	–	6,278	–
	617,558	–	358,343	20	20,968	11	238,216	–
Property and equipment:								
Land	45,955	–	21,923	2,390	–	–	3,507	18,135
Buildings and improvements	595,141	–	385,328	26,983	–	8,206	172,280	2,344
Furniture and equipment	375,603	–	255,103	11,677	417	7,113	75,759	25,534
Construction in progress	32,060	–	15,575	6,158	–	1,376	7,332	1,619
	1,048,759	–	677,929	47,208	417	16,695	258,878	47,632
Less allowances for depreciation and amortization	505,566	–	339,887	17,426	385	10,739	119,492	17,637
	543,193	–	338,042	29,782	32	5,956	139,386	29,995
Unamortized bond issuance costs, net	2,474	–	1,665	–	–	–	809	–
Deferred charges and other assets	26,411	(12,367)	4,576	16,826	279	7,912	2,384	6,801
Interest in net assets of recipient organization	–	(6,484)	6,484	–	–	–	–	–
	$ 1,513,031	$ (27,154)	$ 895,471	$ 62,747	$ 28,142	$ 25,200	$ 470,364	$ 58,261

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Balance Sheet (continued)

(In Thousands)

December 31, 2013

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Memorial Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.
Liabilities and net assets								
Current liabilities:								
Accounts payable	$ 53,531	$ –	$ 20,836	$ 4,038	$ 16	$ 1,261	$ 24,845	$ 2,535
Accrued salaries and benefits	43,942	–	19,600	3,882	36	2,448	12,952	5,024
Accrued expenses	4,971	–	2,538	837	31	341	831	393
Due to third-party payors	10,753	–	4,978	–	–	–	5,775	–
Due to affiliates	–	(8,303)	–	199	–	8,104	–	–
Current maturities of long-term debt	6,899	–	4,557	–	–	–	2,342	–
Total current liabilities	120,096	(8,303)	52,509	8,956	83	12,154	46,745	7,952
Noncurrent liabilities:								
Long-term debt, less current maturities	256,237	–	172,903	–	–	–	83,334	–
Pension and other liabilities	65,484	–	8,162	27,790	–	20	28,730	782
Interest rate and basis swaps	36,761	–	36,761	–	–	–	–	–
	358,482	–	217,826	27,790	–	20	112,064	782
Total liabilities	478,578	(8,303)	270,335	36,746	83	12,174	158,809	8,734
Net assets:								
Unrestricted:								
Undesignated	1,000,532	(12,367)	618,652	26,001	416	13,026	305,277	49,527
Board-designated endowment	20,968	–	–	–	20,968	–	–	–
Total unrestricted	1,021,500	(12,367)	618,652	26,001	21,384	13,026	305,277	49,527
Temporarily restricted	12,362	(6,484)	6,484	–	6,484	–	5,878	–
Permanently restricted	591	–	–	–	191	–	400	–
Total net assets	1,034,453	(18,851)	625,136	26,001	28,059	13,026	311,555	49,527
	$ 1,513,031	$ (27,154)	$ 895,471	$ 62,747	$ 28,142	$ 25,200	$ 470,364	$ 58,261

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Statement of Operations and Changes in Net Assets

(In Thousands)

Year Ended December 31, 2013

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Memorial Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.
Unrestricted revenue, gains, and other support								
Net patient service revenue	$ 840,408	$ (1,136)	$ 462,446	$ 58,424	$ –	$ 36,746	$ 283,921	$ 7
Provision for bad debts	(62,724)	–	(35,209)	(2,876)	–	(885)	(23,754)	–
Net patient service revenue less provision for bad debts	777,684	(1,136)	427,237	55,548	–	35,861	260,167	7
Other revenue	42,726	(6,007)	23,419	6,297	728	2,171	14,676	1,442
Net assets released from restrictions used for operations	458		322	17	4	1	–	114
	820,868	(7,143)	450,978	61,862	732	38,033	274,843	1,563
Expenses								
Salaries and wages	329,320	(104)	132,987	58,450	–	23,387	95,210	19,390
Employee benefits	90,072	(3)	36,994	10,806	1	5,052	29,998	7,224
Supplies and other	192,834	(6,579)	105,925	10,880	253	7,363	67,586	7,406
Management fees	–	–	24,332	3,036	181	1,535	17,964	(47,048)
Professional fees and purchased services	107,094	(457)	43,606	2,762	580	1,304	44,303	14,996
Depreciation and amortization	44,169	–	25,408	2,333	37	1,207	13,072	2,112
Interest	6,594	–	4,787	–	–	17	1,790	–
	770,083	(7,143)	374,039	88,267	1,052	39,865	269,923	4,080
Income (loss) from operations	50,785	–	76,939	(26,405)	(320)	(1,832)	4,920	(2,517)
Nonoperating								
Investment income, net	49,466	–	25,527	6	2,403	2	21,156	372
Unrealized gains on swap transactions	(6,743)	–	(6,743)	–	–	–	–	–
Loss on bond refunding	(3,735)	–	(3,040)	–	–	–	(695)	–
Revenue and gains in excess of (less than) expenses	89,773	–	92,683	(26,399)	2,083	(1,830)	25,381	(2,145)

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Statement of Operations and Changes in Net Assets (continued)
(In Thousands)

Year Ended December 31, 2013

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Memorial Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.
Unrestricted net assets								
Revenue and gains in excess of (less than) expenses	$ 89,773	$ –	$ 92,683	$ (26,399)	$ 2,083	$ (1,830)	$ 25,381	$ (2,145)
Net assets released from board designated endowment	529		499	30	–	–	–	–
Net assets released from board designated endowment	(690)	–	–	–	(690)	–	–	–
Other	–		(48,711)	(7,016)	845	1,720	1,490	51,672
Capital contributions	(53)		–	–	–	–	(53)	–
Postretirement benefit adjustments other than periodic costs	44,838		–	17,951	–	–	26,887	–
Increase in unrestricted net assets	134,397	–	44,471	(15,434)	2,238	(110)	53,705	49,527
Temporarily restricted net assets								
Contributions temporarily restricted for use	2,182		–	–	2,182	–	–	–
Investment income	1,193		–	–	152	–	1,041	–
Net assets released from restrictions used for operating and capital purposes	(987)		–	–	(987)	–	–	–
Change in interest in recipient organization	–	(1,345)	1,345	–	–	–	–	–
Increase in temporarily restricted net assets	2,388	(1,345)	1,345	–	1,347	–	1,041	–
Permanently restricted net assets								
Contributions permanently restricted for use	–	–	–	–	–	–	–	–
Increase in permanently restricted net assets	–	–	–	–	–	–	–	–
Increase (decrease) in net assets	136,785	(1,345)	45,816	(15,434)	3,585	(110)	54,746	49,527
Net assets at beginning of year	897,668	(17,506)	579,320	41,435	24,474	13,136	256,809	–
Net assets at end of year	$ 1,034,453	$ (18,851)	$ 625,136	$ 26,001	$ 28,059	$ 13,026	$ 311,555	$ 49,527

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Balance Sheet
(In Thousands)

December 31, 2012

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Memorial Health System, Inc.	Memorial Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.
Assets							
Current assets:							
Cash and cash equivalents	$ 78,316	$ –	$ 36,774	$ 5,430	$ 4,165	$ 1,856	$ 30,091
Short-term investments	7,305	–	5,942	–	914	–	449
Patient accounts receivable, net	137,442	–	75,718	7,342	–	7,211	47,171
Due from third-party payors	18,573	–	15,419	–	–	–	3,154
Other receivables	8,844	–	1,269	1,236	25	695	5,619
Inventories	21,316	–	13,320	–	–	788	7,208
Prepaid expenses	9,345	(1,676)	1,214	4,584	–	74	5,149
Due from affiliates	–	(3,605)	2,643	902	–	–	60
Total current assets	281,141	(5,281)	152,299	19,494	5,104	10,624	98,901
Assets limited as to use:							
Internally designated investments	531,354	–	328,328	–	–	–	203,026
Externally designated investments – insurance trust	2,584	–	2,553	20	–	11	–
Board-designated endowment	19,332	–	–	–	19,332	–	–
Endowment and temporarily restricted investments	5,235	–	–	–	–	–	5,235
	558,505	–	330,881	20	19,332	11	208,261
Property and equipment:							
Land	38,347	–	20,935	15,798	–	–	1,614
Buildings and improvements	573,562	–	343,480	55,042	–	7,824	167,216
Furniture and equipment	338,814	–	228,354	43,797	417	6,228	60,018
Construction in progress	24,751	–	14,896	3,246	–	627	5,982
	975,474	–	607,665	117,883	417	14,679	234,830
Less allowances for depreciation and amortization	478,597	–	305,963	55,809	348	10,012	106,465
	496,877	–	301,702	62,074	69	4,667	128,365
Unamortized bond issuance costs, net	1,995	–	1,317	–	–	–	678
Deferred charges and other assets	30,243	(12,367)	4,044	26,141	115	7,191	5,119
Interest in net assets of recipient organization	–	(5,139)	5,139	–	–	–	–
	$ 1,368,761	$ (22,787)	$ 795,382	$ 107,729	$ 24,620	$ 22,493	$ 441,324

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Balance Sheet (continued)

(In Thousands)

December 31, 2012

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Memorial Health System, Inc.	Memorial Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.
Liabilities and net assets							
Current liabilities:							
Accounts payable	$ 45,915	$ (1,676)	$ 18,600	$ 5,280	$ 1	$ 2,638	$ 21,072
Accrued salaries and benefits	46,161	–	21,420	9,736	91	2,560	12,354
Accrued expenses	5,314	–	2,575	1,195	54	521	969
Due to third-party payors	6,063	–	1,667	–	–	–	4,396
Due to affiliates	–	(3,605)	–	–	–	3,605	–
Current maturities of long-term debt	6,920	–	4,470	–	–	–	2,450
Total current liabilities	110,373	(5,281)	48,732	16,211	146	9,324	41,241
Noncurrent liabilities:							
Long-term debt, less current maturities	208,140	–	128,774	–	–	–	79,366
Pension and other liabilities	122,563	–	8,539	50,083	–	33	63,908
Interest rate and basis swaps	30,017	–	30,017	–	–	–	–
	360,720	–	167,330	50,083	–	33	143,274
Total liabilities	471,093	(5,281)	216,062	66,294	146	9,357	184,515
Net assets:							
Unrestricted:							
Undesignated	867,771	(12,367)	574,181	41,435	(188)	13,136	251,574
Board-designated endowment	19,332	–	–	–	19,332	–	–
Total unrestricted	887,103	(12,367)	574,181	41,435	19,144	13,136	251,574
Temporarily restricted	9,974	(5,139)	5,139	–	5,139	–	4,835
Permanently restricted	591	–	–	–	191	–	400
Total net assets	897,668	(17,506)	579,320	41,435	24,474	13,136	256,809
	$ 1,368,761	$ (22,787)	$ 795,382	$ 107,729	$ 24,620	$ 22,493	$ 441,324

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Statement of Operations and Changes in Net Assets

(In Thousands)

Year Ended December 31, 2012

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Memorial Health System, Inc.	Memorial Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.
Unrestricted revenue, gains, and other support							
Net patient service revenue	$ 897,737	$ (1,451)	$ 515,807	$ 57,226	$ –	$ 31,508	$ 294,647
Provision for bad debts	(51,950)	–	(26,651)	(2,807)	–	(942)	(21,550)
Net patient service revenue less provision for bad debts	845,787	(1,451)	489,156	54,419	–	30,566	273,097
Other revenue	39,670	(2,137)	19,801	10,292	73	1,437	10,204
Net assets released from restrictions used for operations	620	–	392	214	14	–	–
	886,077	(3,588)	509,349	64,925	87	32,003	283,301
Expenses							
Salaries and wages	302,454	(153)	124,829	68,132	–	18,812	90,834
Employee benefits	94,783	(320)	40,708	18,395	53	4,770	31,177
Supplies and other	208,416	(3,115)	113,053	16,514	212	6,149	75,603
Management fees	–	–	21,136	(22,935)	286	1,513	–
Professional fees and purchased services	107,310	–	46,261	11,256	510	1,361	47,922
Depreciation and amortization	46,858	–	23,946	4,782	51	890	17,189
Interest	6,228	–	4,145	–	29	31	2,023
	766,049	(3,588)	374,078	96,144	1,141	33,526	264,748
Income (loss) from operations	120,028	–	135,271	(31,219)	(1,054)	(1,523)	18,553
Nonoperating							
Investment income, net	50,178	–	25,357	465	1,975	2	22,379
Unrealized gains on swap transactions	12,333	–	12,333	–	–	–	–
Realized loss on swap termination	(290)	–	(290)	–	–	–	–
Revenue and gains in excess of (less than) expenses	182,249	–	172,671	(30,754)	921	(1,521)	40,932

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Statement of Operations and Changes in Net Assets (continued)

(In Thousands)

Year Ended December 31, 2012

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Memorial Health System, Inc.	Memorial Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.
Unrestricted net assets							
Revenue and gains in excess of (less than) expenses	$ 182,249	$ –	$ 172,671	$ (30,754)	$ 921	$ (1,521)	$ 40,932
Net assets released from restrictions used for capital purposes	304	–	302	2	–	–	–
Other	122	–	(41,660)	34,780	810	4,034	2,158
Capital contributions	257	–	–	–	–	–	257
Postretirement benefit adjustments other than periodic costs	(10,239)	–	–	(7,420)	–	–	(2,819)
Increase in unrestricted net assets	172,693	–	131,313	(3,392)	1,731	2,513	40,528
Temporarily restricted net assets							
Contributions temporarily restricted for use	1,502	–	–	–	1,502	–	–
Investment income	649	–	–	–	78	–	571
Net assets released from restrictions used for operating and capital purposes	(924)	–	–	–	(924)	–	–
Change in interest in recipient organization	–	(656)	656	–	–	–	–
Increase in temporarily restricted net assets	1,227	(656)	656	–	656	–	571
Permanently restricted net assets							
Contributions permanently restricted for use	–	–	–	–	–	–	–
Increase in permanently restricted net assets	–	–	–	–	–	–	–
Increase (decrease) in net assets	173,920	(656)	131,969	(3,392)	2,387	2,513	41,099
Net assets at beginning of year	723,748	(16,850)	447,351	44,827	22,087	10,623	215,710
Net assets at end of year	$ 897,668	$ (17,506)	$ 579,320	$ 41,435	$ 24,474	$ 13,136	$ 256,809

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