NorthShore University HealthSystem

Unaudited Interim Statements for the Periods Ended June 30, 2017 and 2016

Issued: August 7, 2017

NorthShore University HealthSystem
Consolidated Balance Sheets
(Dollars in Thousands)

	June 30 2017	September 30 2016
Assets		
Current assets:		
Cash and cash equivalents	$ 89,904	$ 57,499
Other short-term investments	1,121	1,047
Internally designated investments, current portion	47,570	48,223
Patient accounts receivable, less allowances:		
(Jun 2017 - $114,585; Sep 2016 - $109,206)	327,192	323,043
Inventories, prepaid expenses, and other	84,388	79,304
Total current assets	550,175	509,116
Investments available for general use	1,652,935	1,559,893
Investments limited as to use	204,366	193,833
Property and equipment:		
Land and improvements	107,473	106,110
Buildings	1,479,311	1,451,248
Equipment and furniture	433,644	441,200
Construction-in-progress	141,541	146,320
Accumulated depreciation	(1,087,335)	(1,091,631)
Total property and equipment, net	1,074,634	1,053,247
Other noncurrent assets	236,022	229,540
Total assets	$ 3,718,132	$ 3,545,629
Liabilities and net assets		
Current liabilities:		
Accounts payable	$ 73,211	$ 65,893
Accrued expenses	177,201	178,683
Current portion of self-insurance	36,800	37,928
Due to third-party payors	114,621	120,180
Current maturities of long-term debt	10,858	10,383
Total current liabilities	412,691	413,067
Noncurrent liabilities:		
Long-term debt, less current maturities	325,404	334,642
Employee retirement and deferred compensation plans	158,119	154,167
Accrued self-insurance and other	248,268	228,875
Total noncurrent liabilities	731,791	717,684
Net assets:		
Unrestricted	2,373,256	2,225,864
Temporarily restricted	123,302	112,157
Permanently restricted	77,092	76,857
Total net assets	2,573,650	2,414,878
Total liabilities and net assets	$ 3,718,132	$ 3,545,629

See accompanying notes

NorthShore University HealthSystem
Consolidated Statements of Operations and Changes in Net Assets
(Dollars in Thousands)

	For the Three Month Period Ended June 30		For the Nine Month Period Ended June 30		For the Year Ended September 30
	2017	2016	2017	2016	2016
Unrestricted revenues and other support					
Net patient service and premium revenue	$ 497,652	$ 510,203	$ 1,520,712	$ 1,496,026	$ 1,998,590
Provision for uncollectible accounts	(10,931)	(15,471)	(38,316)	(44,710)	(56,712)
Net patient service and premium revenue	486,721	494,732	1,482,396	1,451,316	1,941,878
Investment earnings supporting current activities	11,250	10,500	33,750	31,500	42,000
Net assets released from restrictions used for operations	3,844	4,966	9,340	12,572	15,428
Other revenue	12,675	12,586	37,861	40,012	51,395
Total unrestricted revenues and other support	514,490	522,784	1,563,347	1,535,400	2,050,701
Expenses					
Salaries and benefits	277,544	265,402	825,822	795,039	1,063,228
Supplies, services, and other	169,736	169,258	520,658	497,652	671,603
Depreciation and amortization	27,328	27,750	82,744	82,518	111,031
Insurance	10,255	4,814	28,496	20,141	21,854
Medicaid assessment	10,848	10,079	32,732	30,237	36,838
Interest	1,903	1,850	5,631	5,378	7,263
Total expenses	497,614	479,153	1,496,083	1,430,965	1,911,817
Income from operations	16,876	43,631	67,264	104,435	138,884
Nonoperating income					
Dividend and interest income	8,408	8,389	24,245	24,342	32,158
Net realized gains on investments	20,285	8,888	39,425	5,840	8,090
Net unrealized gains on investments	38,138	15,990	85,845	55,058	107,359
Transfer of investment earnings supporting current activities	(11,250)	(10,500)	(33,750)	(31,500)	(42,000)
Other, net	(16,291)	(8,029)	(34,126)	(101,325)	(110,874)
Total nonoperating income (loss)	39,290	14,738	81,639	(47,585)	(5,267)
Revenue, gains, and other support in excess of expenses	56,166	58,369	148,903	56,850	133,617
Unrestricted net assets					
Revenue, gains, and other support in excess of expenses	56,166	58,369	148,903	56,850	133,617
Pension-related changes other than net periodic costs	-	-	-	77,688	64,283
Net assets released from restrictions used for capital	-	22	100	50	50
Other transfers, net	22	(93)	(1,611)	(44)	68
Increase in unrestricted net assets	56,188	58,298	147,392	134,544	198,018
Temporarily restricted net assets					
Contributions and other	2,560	2,198	6,780	8,761	9,705
Net realized gains (losses) on investments	294	(14)	976	4,749	5,682
Net unrealized gains on investments	5,751	2,892	12,829	6,055	9,025
Net assets released from restrictions	(3,844)	(4,987)	(9,440)	(12,621)	(15,478)
Increase in temporarily restricted net assets	4,761	89	11,145	6,944	8,934
Permanently restricted net assets					
Contributions	30	200	235	(1,099)	(908)
Increase (Decrease) in permanently restricted net assets	30	200	235	(1,099)	(908)
Increase in net assets	60,979	58,587	158,772	140,389	206,044
Net assets at beginning of period	2,512,671	2,290,636	2,414,878	2,208,834	2,208,834
Net assets at end of period	$ 2,573,650	$ 2,349,223	$ 2,573,650	$ 2,349,223	$ 2,414,878

See accompanying notes

NorthShore University HealthSystem
Consolidated Statements of Cash Flows
(Dollars in Thousands)

	For the Three Month Period Ended June 30		For the Nine Month Period Ended June 30		For the Year Ended September 30
	2017	2016	2017	2016	2016
Operating activities					
Increase in net assets	$ 60,979	$ 58,587	$ 158,772	$ 140,389	$ 206,044
Adjustments to reconcile increase in net assets to net cash provided by operating activities:					
Change in net unrealized gains on investments	(43,889)	(18,882)	(98,674)	(61,113)	(116,384)
Change in trading portfolio investments, net	(16,038)	(9,826)	(4,901)	20,589	16,949
Restricted contributions	(2,590)	(2,400)	(7,015)	(7,663)	(8,798)
Depreciation and amortization	27,328	27,750	82,744	82,518	111,031
Bond premium amortization	(22)	(22)	(66)	(66)	(88)
Pension-related changes other than net periodic cost	-	-	-	(77,688)	(64,283)
Provision for uncollectible accounts	10,931	15,471	38,316	44,710	56,712
Changes in operating assets and liabilities:					
Patient accounts receivable	(10,623)	(27,525)	(49,459)	(80,364)	(96,837)
Other current assets	80	7,364	(4,505)	(2,146)	(17,005)
Noncurrent assets and liabilities	980	2,557	16,820	84,434	65,459
Accounts payable and accrued expenses	41,509	36,532	4,709	(13,685)	(5,354)
Due to (from) third-party payors	4,162	(6,530)	1,436	(9,901)	10,546
Net cash provided by operating activities	72,807	83,076	138,177	120,014	157,992
Investing activities					
Investments in property and equipment, net	(32,696)	(43,778)	(103,992)	(109,659)	(161,027)
Sale of other long-term assets, net	-	(12)	-	(12)	(12)
Net cash used in investing activities	(32,696)	(43,790)	(103,992)	(109,671)	(161,039)
Financing activities					
Restricted contributions	2,590	2,400	7,015	7,663	8,798
Payments of long-term debt	(8,795)	(8,400)	(8,795)	(8,400)	(9,910)
Net cash used in financing activities	(6,205)	(6,000)	(1,780)	(737)	(1,112)
Increase in cash and cash equivalents	33,906	33,286	32,405	9,606	(4,159)
Cash and cash equivalents at beginning of period	55,998	37,978	57,499	61,658	61,658
Cash and cash equivalents at end of period	$ 89,904	$ 71,264	$ 89,904	$ 71,264	$ 57,499

See accompanying notes

Notes to Consolidated Financial Statements

(Dollars in Thousands)

1. Organization and Basis of Presentation

NorthShore University HealthSystem (NorthShore) is an integrated health care system dedicated to providing health care services, including inpatient acute and non-acute care, primary and specialty physician services, and various outpatient services. NorthShore operates four acute care facilities, including Evanston Hospital, Highland Park Hospital, Glenbrook Hospital, and Skokie Hospital, that serve the greater Chicago "North Shore" and northern Illinois communities. NorthShore also includes research activities, home health and hospice care, and foundation operations.

NorthShore is the sole corporate member of NorthShore University HealthSystem Faculty Practice Associates (FPA), Radiation Medicine Institute (RMI), and NorthShore University HealthSystem Insurance International (Insurance International). FPA is the sole shareholder of NorthShore Physician Associates (NPA). NPA is the sole shareholder of Community Care Partners (CCP), which was established in August 2014 to facilitate Medicaid managed care services. All significant intercompany accounts and transactions have been eliminated in consolidation. The accompanying consolidated financial statements include the accounts and transactions of NorthShore and its affiliates (collectively, the Corporation).

NorthShore, FPA, and RMI are tax-exempt organizations under Section 501(c)(3) of the Internal Revenue Code (IRC). NPA and CCP are for-profit corporations. Insurance International is a foreign corporation organized in the Cayman Islands, which does not tax the activities of this organization.

The Corporation is the primary teaching affiliate of the University of Chicago Pritzker School of Medicine (Pritzker), under which the Corporation sponsors graduate medical education programs for physicians and other health care-related personnel.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information. These statements do not include all of the information and footnotes required by GAAP for complete financial statements, although in the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal and recurring nature.

Certain reclassifications were made to the 2016 consolidated financial statements to conform with the classifications used in fiscal year 2017. The reclassifications had no effect on the change in net assets or on net assets as previously reported.

2. New Accounting Pronouncements

Adopted

In February 2015, the FASB issued ASU 2015-02, *Amendments to the Consolidation Analysis.* The guidance in this update modifies the analysis that companies must perform to determine whether certain legal entities should be consolidated, including limited partnerships and similar legal entities

2. New Accounting Pronouncements (continued)

that would be considered variable interest entities and investments in certain investment funds. This new guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015, with early adoption permitted. The Corporation adopted the new guidance on October 1, 2016, and there was no significant impact on the consolidated financial statements.

In January 2015, the FASB issued ASU 2015-01, *Income Statement – Extraordinary and Unusual Items.* This update eliminates from GAAP the concept of extraordinary items. The Corporation adopted the new guidance October 1, 2016 and there was no significant impact on the consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, *Simplifying the Presentation of Debt Issuance Costs.* The amendments in this update require that the carrying amount of the debt liability be presented net of debt issuance costs, consistent with the presentation of debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this update. The Corporation adopted the new guidance in the fourth quarter of fiscal year 2016, and there was no significant impact on the consolidated financial statements.

In May 2015, the FASB issued ASU 2015-07, *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent).* Under the new guidance, investments measured at net asset value per share, which have unobservable inputs, will be excluded from the fair value hierarchy table. Other disclosure requirements for these investments are unchanged and will continue to be included in the investment disclosures. The Corporation adopted the new guidance in the fourth quarter of fiscal year 2016, and there was no significant impact on the consolidated financial statements.

In November 2015, the FASB issued ASU 2015-17, *Balance Sheet Classification of Deferred Taxes.* The update requires companies to classify all deferred tax assets and liabilities as noncurrent on the balance sheet instead of separating into current and noncurrent amounts. The Corporation adopted the new guidance on October 1, 2016, and there was no significant impact on the consolidated financial statements.

Prospective

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers.* The amendments in this update require not-for-profit entities that are conduit bond obligors to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This will result in the Corporation making additional judgments, such as estimates of the collectability of revenue. In March 2016, the FASB issued ASU 2016-08 clarifying the implementation guidance on principal versus agent considerations. During third quarter of 2016, the FASB issued ASU 2016-10

2. New Accounting Pronouncements (continued)

and 2016-12. ASU 2016-20 was issued in the first quarter of 2017. The amendments in these updates further clarify key guidance related to revenue recognition. The Corporation is required to adopt the new guidance in conjunction with ASU 2014-09. This new guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2017, with early adoption not permitted. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2018, and is currently evaluating the impact this guidance will have on its consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, *Simplifying the Measurement of Inventory*. Under the new guidance, entities using the FIFO method for inventory valuation will be required to compare the cost of inventory to only one measure, its net realizable value. The amendment is effective for fiscal periods and interim periods within those years beginning December 15, 2016. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2017, however, the Corporation is not expecting this guidance to have a material impact on its consolidated financial statements as inventory is currently valued using a similar method.

In January 2016, the FASB issued ASU 2016-01, *Financial Instrument: Classification and Measurement.* The amendments in this update will no longer allow equity investments to be valued under the cost method. Investments, except for those accounted for under the equity method of accounting, or those that result in consolidating the investment, will be measured at fair value with changes in fair value recognized in net income. This new guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2018, and is currently evaluating the impact this guidance will have on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases*. Under the new guidance lessees are required to capitalize leases with greater than 12 months term on the balance sheet. Leases will be classified as operating or financing. Both types of leases will be recorded on the balance sheet. Operating leases will reflect lease expense on a straight line basis whereas financing leases will accelerate lease expense in the early period of the lease term and decline with passage of time similar to current accounting for capital leases. The amendments in this update are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2019, and is currently evaluating the impact this guidance will have on its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-07, *Investments: Equity Method and Joint Ventures.* The amendments in this update eliminate the requirement to retroactively adjust an investment when it

2. New Accounting Pronouncements (continued)

becomes qualified for use under the equity method as a result of an increase in the level of ownership interest or degree of influence. In January 2017, the FASB issued ASU 2017-03 which adds comments related to accounting for tax benefits resulting from investments in qualified affordable housing. This portion of the update does not apply to the Corporation. The amendments in this update are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. Early adoption is permitted. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2017, and is currently evaluating the impact this guidance will have on its consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments: Credit Losses*. The FASB proposed a single, principles-based model for all entities to account for credit losses on loans, debt securities, trade, lease, and other receivables. The allowance for expected credit losses at each reporting date would represent the current estimate of contractual cash flows not expected to be collected. The ASU applies to financial assets subjected to credit losses that are not already classified as fair value through net income. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2021, and is currently evaluating the impact this guidance will have on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities.* The amendments in this update replace the three classes of net assets (unrestricted, temporary, and permanent) with two classes (with and without donor restrictions). The ASU also requires additional disclosures relating to net assets and expenses. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2018, and is currently evaluating the impact this guidance will have on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, *Classification of Certain Cash Receipts and Cash Payments.* The amendments in this update clarify the classification of eight types of transactions in the statement of cash flows to reduce diversity in practices. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2018, however, the Corporation is not expecting this guidance to have a material impact on its consolidated financial statements.

In November of 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows: Restricted Cash*. The guidance requires entities to show the changes in the total cash, cash equivalents, restricted cash and restricted cash equivalents in the statement of cash flows. As a result, entities will no longer be required to present transfers between these categories. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2018, and is currently evaluating the impact this guidance will have on its consolidated financial statements.

In January of 2017, the FASB issued ASU 2017-04, *Intangibles – Goodwill and Other*. The amendments in this update are intended to simplify the accounting for goodwill impairments. Goodwill impairment will be determined by using the difference in fair value and carrying value rather than the

2. New Accounting Pronouncements (continued)

original two-step approach. Early adoption is permitted. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2022, however, the Corporation is not expecting this guidance to have a material impact on its consolidated financial statements.

In March of 2017, the FASB issued ASU 2017-07, *Compensation – Retirement Benefits.* The amendments in this update require an employer to separate the service cost component from the other components of net benefit cost. The service cost component will be reported as part of compensation while the remaining components will be reflected in non-operating income. The update does not change any of the calculations or reporting provisions of current retirement benefit accounting. The amendments in this update should be applied retrospectively for the presentation of the service cost component and other components of net period pension costs and net periodic postretirement benefit costs in the income statement. Since the Corporation's pension plan is currently frozen, it does not have service costs. All other components will be presented as a part of non-operating income. The Corporation is required to adopt the new guidance for the fiscal year beginning on October 1, 2019, however, the Corporation is not expecting this guidance to have a material impact on its consolidated financial statements.

3. Provision for Uncollectible Accounts

The Corporation's estimation of the allowance for doubtful accounts is based primarily upon the type and age of patient accounts receivable and the effectiveness of the Corporation's collection efforts. The Corporation's policy is to establish reserves for a portion of all self-pay receivables, including amounts due from the uninsured and amounts related to co-payments and deductibles, as these charges are recorded. The allowance for uncollectible accounts as a percentage of all accounts receivable was 26% and 25% as of June 30, 2017 and September 30, 2016, respectively. The Corporation's total reserve for self-pay accounts receivable, including the allowance for uncollectible accounts and charity care, was 83% of self-pay accounts receivable at June 30, 2017 and 85% of self-pay accounts receivable at September 30, 2016.

On a monthly basis, the Corporation reviews its accounts receivable balances and employs various analytics to support the determination of its estimates. These efforts primarily consist of reviewing the following: historical write-off and collection experience, revenue and volume trends by payor (particularly self-pay components), changes in the aging and payor mix of accounts receivable (including accounts due from the uninsured and accounts that represent co-payments and deductibles due from patients), trending of days revenue in accounts receivable, and various allowance coverage statistics.

For the three months ended June 30, 2017, total patient service revenue, net of contractual allowances and discounts, was $479,137 which included third-party payor revenue of $458,510 and self-pay revenue of $20,627. For the three months ended June 30, 2016, total patient service revenue, net of

(Dollars in Thousands)

3. Provision for Uncollectible Accounts (continued)

contractual allowances and discounts, was $494,232 which included third-party payor revenue of $473,607 and self-pay revenue of $20,625.

For the nine months ended June 30, 2017, total patient service revenue, net of contractual allowances and discounts, was $1,469,561 which included third-party payor revenue of $1,405,179 and self-pay revenue of $64,382. For the nine months ended June 30, 2016, total patient service revenue, net of contractual allowances and discounts, was $1,447,373 which included third-party payor revenue of $1,393,856 and self-pay revenue of $53,517.

4. Investments

Investments in equity securities and mutual funds are carried at fair values based on quoted market prices. Commingled funds are carried at fair value based on other observable inputs. Debt securities are valued using institutional bids or pricing services. Alternative investments, primarily limited partnership and hedge funds, are accounted for using the cost or equity method, depending on the extent of the Corporation's ownership of the fund. Investments held at cost are evaluated for impairment quarterly. No related investments were impaired for the three months ended June 30, 2017 and 2016. For the nine months ended June 30, 2017, no related investments were impaired. For the nine months ended June 30, 2016, a previously impaired investment was written down further, resulting in the Corporation recording a loss reserve of $1,576 and an overseas fund investment measured at cost was closed resulting in the Corporation recording a loss of $6,215.

Investments limited as to use include investments internally designated by the Board of Directors (Board) for property and equipment replacement and expansion which the Board, at its discretion, may subsequently use for other purposes, and investments externally designated under indenture or donor restriction.

The presentation of investments is as follows:

	As of June 30 2017	As of September 30 2016
Other short-term investments	**$ 1,121**	$ 1,047
Investments available for general use	**1,652,935**	1,559,893
Investments limited as to use:		
Current portion	**47,570**	48,223
All other (noncurrent)	**204,366**	193,833
Other noncurrent assets	**79,411**	70,414
Total investments	**$ 1,985,403**	$ 1,873,410

(Dollars in Thousands)

4. Investments (continued)

Total investment returns for the periods indicated are as follows:

	For the Three Months Ended June 30		For the Nine Months Ended June 30		For the Year Ended September 30
	2017	2016	**2017**	2016	2016
Nonoperating :					
Dividend and interest income	**$ 8,408**	$ 8,389	**$ 24,245**	$ 24,342	$ 32,158
Net realized gains on investments	**20,285**	8,888	**39,425**	5,840	8,090
Net unrealized gains on investements	**38,138**	15,990	**85,845**	55,058	107,359
Total nonoperating investment return	**66,831**	33,267	**149,515**	85,240	147,607
Temporarily restricted:					
Net realized gains (losses)	**294**	(14)	**976**	4,749	5,682
Net unrealized gains	**5,751**	2,892	**12,829**	6,055	9,025
Total temporarily restricted investment return	**6,045**	2,878	**13,805**	10,804	14,707
Total investment return	**$ 72,876**	$ 36,145	**$ 163,320**	$ 96,044	$ 162,314

The state of Illinois passed the Uniform Prudent Management of Institutional Funds Act (UPMIFA) effective June 30, 2009. The Corporation has interpreted UPMIFA as sustaining the preservation of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulation to the contrary. In compliance with this interpretation of UPMIFA, the Corporation classifies permanently restricted net assets as (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated in a manner consistent with the standard of prudence prescribed by UPMIFA.

The Corporation has adopted a policy of requiring a minimum donation of $1,500 to establish an endowed chair and $1,000 to establish an endowed research project or endowed clinical program.

The Corporation has adopted endowment investment and spending policies that attempt to provide a predictable stream of funding to programs supported by its endowment, while seeking to maintain the purchasing power of endowment assets. Currently, the Corporation expects its endowment funds over time to provide an average rate of return of approximately 5% annually. To achieve this long-term

4. Investments (continued)

rate of return objective, the Corporation relies on a total return strategy in which investment returns are achieved through capital appreciation (realized and unrealized) and current yield (interest and dividends). Actual returns in any given year may vary from expected.

An endowment fund is considered to be underwater when the market value of the endowment is less than the original (and any subsequent) donations received by the Corporation. The Corporation has adopted a policy that such shortfall amounts will be funded by the Corporation from the Corporation's unrestricted net assets. There were no underwater endowments as of June 30, 2017. Underwater endowments were $1 as of September 30, 2016.

5. Fair Value Measurements

The Corporation holds certain debt securities, equity securities, and investments in funds that are measured using a prescribed fair value hierarchy and related valuation methodologies. The concept of the "highest and best use" of an asset is used for valuation. Highest and best use is determined by the "use of the asset by market participants, even if the intended use of the asset by the reporting entity is different."

ASC 820 specifies a hierarchy of valuation techniques based on whether the inputs to each measurement are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Corporation's assumptions about current market conditions.

The prescribed fair value hierarchy and related valuation methodologies are as follows:

Level 1 **–** Quoted market prices for identical instruments in active markets. Active markets are defined by daily trading and investor ability to exit holdings at the daily pricing. Redemption frequency is daily.

Level 2 **–** Quoted market prices for similar or identical instruments and model-derived valuations in which all significant inputs are observable in the market. The separately managed accounts are based on institutional bid evaluations. Institutional bid evaluations are estimated prices computed by pricing vendors. These prices are determined using observable inputs for similar securities as of the measurement date. Redemption frequency is daily or monthly.

Level 3 **–** Valuation derived from valuation techniques in which one or more significant inputs are unobservable. These prices are based on the net asset value reported from the investee and reviewed by an independent third party as its best estimate of fair market value as of the reporting date for its investments in limited partnerships and hedge funds. Because there are no observable market transactions for interests in investments in limited partnerships and

(Dollars in Thousands)

5. Fair Value Measurements (continued)

hedge funds, any investments of this nature would be classified in Level 3 of the fair value hierarchy. Redemption frequency varies from monthly to longer than one year for hedge funds. Limited partnerships are expected to be held for the life of the fund.

The Corporation's financial assets carried at fair value at June 30, 2017, were as follows:

Nature of investment	Level 1	Level 2	Level 3	Total
Common Stock	$ 160,224	$ -	$ -	$ 160,224
Mutual Funds	219,792	-	-	219,792
Bond Funds	158,397	-	-	158,397
Real Asset Funds	14,500	-	-	14,500
Fixed Income Accounts	-	128,647	-	128,647
Total Assets at Fair Value	$ 552,913	$ 128,647	$ -	$ 681,560

Total investments at June 30, 2017 are $1,985,403. This amount includes $681,560 in investments recorded at fair value and $783,472 in investments measured at net asset value. In addition, this amount includes $508,741 in limited partnerships and funds recorded at cost, $10,026 in limited partnerships recorded using the equity method, and other assets of $1,604 recorded at cost.

The Corporation's financial assets carried at fair value at September 30, 2016, were as follows:

Nature of investment	Level 1	Level 2	Level 3	Total
Common Stock	$ 165,555	$ -	$ -	$ 165,555
Mutual Funds	200,109	-	-	200,109
Bond Funds	209,744	-	-	209,744
Real Asset Funds	15,895	-	-	15,895
Fixed Income Accounts	-	143,518	-	143,518
Total Assets at Fair Value	$ 591,303	$ 143,518	$ -	$ 734,821

Total investments at September 30, 2016 are $1,873,410. This amount includes $734,184 in investments recorded at fair value and $641,734 in investments measured at net asset value. In addition, this amount includes $476,852 in limited partnerships and funds recorded at cost, $18,103 in limited partnerships recorded using the equity method, and other assets of $2,537 recorded at cost.

ASC 825, *Financial Instruments*, permits entities to elect to measure many financial instruments and certain other items at fair value. The fair value option may be applied instrument by instrument and is irrevocable. The Corporation has made no such elections to date.

5. Fair Value Measurements (continued)

There were no transfers between Level 1, Level 2, and Level 3 assets during the three months ended June 30, 2017 or 2016.

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

The estimated fair value of total debt was at $346,243 at June 30, 2017 and $359,187 at September 30, 2016. Under the guidance set forth in ASU 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*, the Corporation's debt is classified as a Level 2 liability. The estimated fair value of the fixed rate debt is determined by recalculating the dollar prices of each of the Corporation's outstanding fixed rate bonds using current market yields. The variable rate debt is remarketed daily or weekly, and par value is considered as fair value. The fair value included a consideration of third-party credit enhancements, which had no impact on the estimated fair value of the debt.

6. Long-Term Debt and Debt with Self-Liquidity

All bonds issued by the Corporation were used to pay or reimburse the Corporation for certain capital projects, to provide for a portion of the interest on the bonds, and to pay certain expenses incurred in connection with the issuance of the bonds. The variable rate bonds are subject to periodic remarketing and can be converted to a fixed rate subject to certain terms of the loan agreements. The Series 2001B, 2001C, 1995, and 1996 bonds have standby bond purchase agreements (SBPAs), and the 2008 commercial paper has a letter of credit (LOC) to provide liquidity support in the event of a failed remarketing.

The Series 1995 bonds are backed by an SBPA issued by a financial institution that expires on January 15, 2018. The Series 1996 bonds are backed by an SBPA issued by a financial institution that expires on January 6, 2018. In the event these bonds cannot be remarketed, the bond trustee will call the bonds and the bonds will become bank bonds held by the liquidity facility provider. The liquidity facility provider will hold the bonds for 367 days or until a replacement liquidity facility is secured. After the 367-day period, the bonds will begin to amortize over a three-year period. In the event an SBPA cannot be renewed or replaced, the liquidity facility provider will make a loan in the amount necessary to complete the mandatory tender of the bonds. The principal and interest on the loan will be amortized over three years.

The Corporation has two SBPAs in conjunction with the Series 2001B and 2001C bonds with financial institutions. The Series 2001B bonds are backed by an SBPA issued by a financial institution that expires on November 15, 2017. The Series 2001C bonds are backed by an SBPA issued by a financial institution that expires on January 15, 2018. In the event these bonds cannot be remarketed, the bond trustee will call the bonds and the bonds will become bank bonds held by the liquidity facility provider.

(Dollars in Thousands)

6. Long-Term Debt and Debt with Self-Liquidity (continued)

The liquidity facility provider will hold the bonds for 367 days or until a replacement facility is secured.

After the 367-day period, the bonds will begin to amortize over a three-year period. In the event an SBPA cannot be renewed or replaced, the liquidity provider will make a loan in the amount necessary to complete the mandatory tender of the bonds. The principal and interest on the loan will be amortized over three years.

The Corporation has an LOC backup facility with a financial institution in conjunction with the 2008 Pooled Program that expires on November 30, 2019. The LOC may be drawn upon by the trustee to make payments of principal and interest on maturing commercial paper in the event that an issuance of commercial paper does not roll over. Repayments on any liquidity advance received prior to the LOC expiration date will be made in equal quarterly installments beginning on the first subsequent quarter-end date.

The Corporation's 1990A, 1992, and 1998 debt issues with self-liquidity were retired on December 22, 2016. As of September 30, 2016, there were no bonds with self-liquidity outstanding with third parties.

The self-liquidity bonds held by the Corporation are as follows:

Series	**Final Maturity**	**As of June 30 2017**	As of September 30 2016
1990A	2025	**$ -**	$ 50,000
1992	2026	**-**	50,000
1998	2032	**-**	50,000
		$ -	$ 150,000

Under the terms of the long-term debt arrangements, various amounts are on deposit with trustees, and certain specified payments are required for bond redemption, interest payments, and asset replacement. The terms of certain long-term debt agreements require, among other things, the maintenance of various financial ratios and place limitations on additional indebtedness and pledging of assets. The Corporation remained in compliance with these agreements during the reporting periods.

The Corporation has various outstanding LOCs in connection with construction projects and property lease obligations, which amount to $560 as of June 30, 2017 and September 30, 2016, respectively. No amounts have been drawn against these LOCs.

(Dollars in Thousands)

6. Long-Term Debt and Debt with Self-Liquidity (continued)

As of June 30, 2017, the maturities of long-term debt, including an $88 bond premium, are as follows for the fiscal years ended September 30:

Fiscal Year	Maturities Long-Term Debt
2017	$ 1,588
2018	$ 10,793
2019	$ 11,193
2020	$ 11,638
2021	$ 12,133

Interest paid for the three months ended June 30, 2017 and 2016, was $3,307 and $3,282 respectively. Interest of $324 and $177 was capitalized in the same periods, respectively. In addition, bond premium amortization was $22 for both the three months ended June 30, 2017 and 2016.

Interest paid for the nine months ended June 30, 2017 and 2016, was $7,218 and $6,322 respectively. Interest of $916 and $408 was capitalized in the same periods, respectively. In addition, bond premium amortization was $66 for both the nine months ended June 30, 2017 and 2016.

Total long-term debt is summarized as follows:

		Amortization			Outstanding Principal		Interest Rate	
Type/Issuer	**Series**	**Amount Range**	**Years From**	**Years To**	**June 30 2017**	September 30 2016	**June 30 2017**	September 30 2016
Illinois Development Finance Authority Variable Rate Demand Revenue Bonds								
	2001B	$1,800 - $ 5,000	2018	2031	**$ 34,300**	$ 36,000	**0.92%**	0.80%
	2001C	1,800 - 5,000	2018	2031	**34,300**	36,000	**0.91%**	0.78%
Illinois Health Facilities Authority Variable Rate Adjustable Demand Revenue Bonds								
	1995	$1,445 - $ 8,605	2018	2035	**$ 40,020**	$ 41,530	**0.90%**	0.83%
	1996	1,435 - 8,560	2017	2035	**41,570**	41,570	**0.91%**	0.86%
Illinois Educational Facilities Authority Commercial Paper Revenue Note								
	2008	$ 995 - $13,305	2032	2038	**$ 75,000**	$ 75,000	**0.71%**	0.22%
Illinois Finance Authority Revenue Refunding Bonds								
	2010	$ 825 - $ 9,685	2018	2037	**$ 111,765**	$ 115,650	**4.00% - 5.25%**	4.00% - 5.25%
Total long-term debt					**$ 336,955**	$ 345,750		
Less: Current maturities of debt					**10,858**	10,383		
Less: Debt Issuance Costs					**2,441**	2,539		
Plus: 2010 bond premium (current and long-term)					**1,748**	1,814		
Total long-term debt, less current maturities					**$ 325,404**	$ 334,642		

(Dollars in Thousands)

7. Employee Benefit Programs

The Corporation sponsored a funded, noncontributory, defined benefit pension plan (the NorthShore Plan), which was frozen to all participants on December 31, 2013. Assets held by the NorthShore Plan consist primarily of fixed income securities, domestic/international stocks, limited partnerships, and hedge funds. A plan measurement date of September 30 is used for the NorthShore Plan.

In the spring of 2015, the Corporation surveyed active employees regarding the opportunity to voluntarily receive their frozen NorthShore Plan benefit as a lump-sum distribution while actively employed. The individuals who elected to participate were transferred to a separate pension plan sponsored by the Corporation (the Spin-Off Plan) effective as of June 1, 2015. The Spin-Off Plan was terminated effective as of August 1, 2015. During the first quarter of fiscal year 2016, the Corporation contributed $15,038 to the Spin-Off Plan and $4,000 assets were transferred from the NorthShore Plan to the Spin-Off Plan. Total Spin-Off Plan's employee benefit payments of $221,923 were distributed in the first quarter of fiscal year 2016.

The components of net periodic benefit costs included in the consolidated statements of operations and changes in net assets are as follows:

	For the Three Months Ended	
	June 30, 2017	June 30, 2016
	NorthShore Plan	NorthShore Plan
Interest cost	**$ 2,593**	$ 2,944
Expected return on plan assets	**(3,554)**	(3,623)
Actuarial loss	**519**	408
Net periodic pension benefit cost	**$ (442)**	$ (271)

	For the Nine Months Ended			For the Year ended	
	June 30, 2017	June 30, 2016		September 30, 2016	
	NorthShore Plan	Spin-Off Plan	NorthShore Plan	Spin-Off Plan	NorthShore Plan
Interest cost	**$ 7,779**	$ 790	$ 8,833	$ 790	$ 11,778
Expected return on plan assets	**(10,662)**	-	(10,870)	-	(14,494)
Actuarial loss	**1,556**	121	1,225	121	1,634
Settlement charge	**-**	77,688	-	77,688	-
Net periodic pension benefit cost	**$ (1,327)**	$ 78,599	$ (812)	$ 78,599	$ (1,082)

The Corporation sponsors a defined contribution retirement plan (the RCP Plan), in which it enrolled new employees hired after January 1, 2013 and all employees as of January 1, 2014. The Corporation also sponsors a 403(b) plan that matches employee contributions at an annual discretionary percentage.

8. Professional Liability Insurance

The Corporation has claims-made basis policies in excess of the amounts retained by the Corporation for professional and general liability claims. As of September 30, 2015 (beginning with policy year March 26, 2009), claims are subject to deductibles of $10,000 with a $15,000/$15,000 buffer layer. The estimated professional liability losses are calculated with the assistance of consulting actuaries and an accrual has been made for potential claims to be paid. The discounted reserve balance was $257,135 as of June 30, 2017 and $245,010 as of September 30, 2016 using a 2.5% discount rate. Included in these amounts is a receivable for anticipated insurance recoveries of $13,010 as of June 30, 2017 and September 30, 2016, respectively. The undiscounted reserve balance would have been higher by approximately $24,855 as of June 30, 2017 and $23,683 as of September 30, 2016. The Corporation is not aware of any factors that would cause insurance expense to vary materially from the amounts provided. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during its term but reported subsequently may not be insured.

9. Litigation and Contingencies

In February 2004, the Federal Trade Commission (FTC) issued a complaint against the Corporation challenging its January 2000 merger with Highland Park Hospital (HPH). On April 28, 2008, the FTC issued a Final Order that requires the Corporation to conduct separate negotiations with private third-party payors for health care services of HPH unless a payor specifically elects to opt out and negotiate jointly for all of the Corporation’s hospitals. The Final Order also requires the Corporation to give prior notification to the FTC for any future acquisitions of hospitals within the Chicago Metropolitan Statistical Area through April 2018. The Final Order terminates in April 2028.

In August 2007, three individual private plaintiffs filed a purported antitrust class action lawsuit against the Corporation in Federal District Court in Chicago, Illinois, alleging anticompetitive price increases as a result of the Corporation’s January 2000 merger with HPH. In May 2008, an entity titled the Painters District Council No. 30 Health and Welfare Fund filed a nearly identical antitrust class action against the Corporation. All four of the separate suits have been consolidated into one action. On March 30, 2010, the District Court denied the plaintiffs’ motion for class certification. The plaintiffs appealed the District Court’s denial of class certification to the Seventh Circuit Court of Appeals, and on January 13, 2012, the Seventh Circuit issued an opinion that vacated the District Court’s decision and remanded the case back to the District Court for further proceedings. On April 4, 2012, the plaintiffs filed a renewed motion for class certification that the Corporation opposed on July 12, 2012. On December 10, 2013, the District Court granted plaintiffs’ renewed motion for class certification. On September 4, 2015, the District Court granted in part the Corporation’s motions to compel arbitration against the largest managed care organizations that are alleged to be part of the class. In particular, the District Court found that Aetna, Blue Cross (PPO product), Cigna, United, and Unicare must resolve their dispute with the Corporation (if any) through arbitration, and cannot participate in the class.

9. Litigation and Contingencies (continued)

Several other managed care organizations (MCOs), including Blue Cross (HMO product) and Humana, remain within the class, as do the MCOs' self-insured customers. Fact discovery closed in November 2015. The parties completed expert discovery in April 2017. The parties filed competing motions for summary judgment, motions to decertify the class, and motions to exclude experts during the spring and summer of 2017. The motions are currently pending before the court and a ruling is anticipated during late 2017. No trial date has been set. A final resolution in this matter is not expected until late 2017 or early 2018. The Corporation has denied all allegations within the plaintiffs' complaints and intends to pursue its rights in defense of the claims. The Corporation is unable to predict the ultimate outcomes, including liability, if any, in this litigation; however, such liabilities could be material.

On June 14, 2012, the state of Illinois enacted Illinois Public Act 97-0688, which includes provisions governing property and sales tax exemptions for Illinois nonprofit hospitals. Based on initial interpretations and estimates, the Corporation believes that community benefits provided by each of its hospitals will exceed their respective tax assessments and, therefore, no property tax will be due for the tax years 2012 through 2016. On June 2, 2016, the Illinois Department of Revenue (IDOR) notified the Corporation that the Corporation's sales tax exemption was renewed under Illinois Public Act 97-0688 through July 1, 2021.

Prior to the new legislation, the Corporation filed required applications seeking real estate tax-exempt status for certain of the Corporation's Skokie Hospital and related facilities, which were certified as tax-exempt as part of Rush North Shore Medical Center prior to the merger with the Corporation on January 1, 2009. These applications are now subject to the provisions of Illinois Public Act 97-0688. The IDOR issued real estate tax exemption certificates, which approved the Corporation's tax exemption filing for either full or partial exemption of the Skokie Hospital and related facilities for tax years 2009, 2010, 2011, and 2012. A local school district subsequently intervened in the IDOR's certification and has requested a formal hearing before the IDOR asserting that Public Act 97-0688 is unconstitutional. The next status update hearing with the IDOR is on July 25, 2017.

Separately, on May 5, 2016, Thornmeadow Partners LP, filed a putative class action lawsuit against the Corporation and other unrelated defendants challenging the constitutionality of the Corporation's property tax exemptions. After the favorable ruling by the Illinois Supreme Court in the case involving Carle Clinic for a similar matter, the Plaintiff agreed to withdraw its original complaint and filed an amended complaint. On June 14, 2017, the Corporation filed a motion to dismiss the amended complaint in its entirety. The Corporation expects a ruling from the Judge in late 2017. The Corporation has denied all allegations within the Plaintiff's amended complaint and intends to pursue its rights in defense of the claims.

The Corporation is a defendant in various lawsuits arising in the ordinary course of business. Although the outcome of these lawsuits cannot be predicted with certainty, management believes the ultimate disposition of such matters will not have a material effect on the Corporation's consolidated financial condition or operations.

10. Income Taxes

The Corporation and its related affiliates, except for NPA and CCP, known as NorthShore Exempt Group, have been determined to qualify as a tax-exempt organization under Section 501(c)(3) of the IRC. Most of the income received by NorthShore Exempt Group is exempt from taxation under Section 501(a) of the IRC, as income related to the mission of the organization. Accordingly, there is no material provision for income tax for these entities. Some of the income received by exempt entities is subject to taxation as unrelated business income. NorthShore and its subsidiaries file federal income tax returns and returns for various states in the U.S.

ASC 740-10 *Income Taxes*, requires that realization of an uncertain income tax position is more likely than not (i.e., greater than 50% likelihood of receiving a benefit) before it can be recognized in the financial statements. Furthermore, this interpretation prescribes the benefit to be recorded in the financial statements as the amount most likely to be realized assuming a review by tax authorities having all relevant information and applying current conventions. This interpretation also clarifies the financial statement classification of tax-related penalties and interest and sets forth new disclosures regarding unrecognized tax benefits. No amount was recorded for the periods ended June 30, 2017 or September 30, 2016.

The Corporation currently has a net operating loss carryforward of $6,167, which generated assets of $2,412. NPA currently has a net operating loss carryforward of $642, which generated assets of $251. These assets are 46% offset by valuation allowances. These amounts are consistent for both the period ended June 30, 2017 as well as the period ended September 30, 2016.

11. Other Events

In September 2014, NorthShore entered into a merger and affiliation agreement with Advocate Health Care Network (Advocate) to form Advocate NorthShore Health Partners (ANHP), a 16 hospital system across 7 Illinois counties together with a broad network of clinically integrated employed and affiliated physicians.

After reviews with the FTC and the Federal Courts, the decision was made to terminate the merger and affiliation agreement in light of the Federal Court rulings effective March 10, 2017.