CHILDREN'S HEALTH CARE

d.b.a. Children's Hospitals & Clinics of Minnesota

Quarterly Financial Report
For the Quarterly Period Ended June 30, 2010

CERTIFICATE RELATING TO

QUARTERLY CONTINUING DISCLOSURE

The undersigned, Susan R. Slocum, Treasurer of Children's Health Care, a Minnesota nonprofit corporation (d/b/a Children's Hospitals and Clinics of Minnesota) (the "Corporation") hereby certifies, pursuant to Section 5 of each of the Continuing Disclosure Agreement, dated as of August 15, 2004, between the Corporation and U.S. Bank National Association and the Continuing Disclosure Agreement, dated as of November 1, 2007, between the Corporation and U.S. Bank National Association (collectively, the "Continuing Disclosure Agreements"), that:

1. Attached hereto are the unaudited June 30, 2010 Consolidated Financial Statements with accompanying schedules of the Obligated Group.

2. Attached hereto is updated Table 7, "Discharges and Patient Days", in the form presented in Appendix A to the Official Statement, dated November 1, 2007, relating to the Series 2007A Bonds, as of June 30, 2010.

3. Capitalized terms as used herein shall have the meaning given such terms in the Continuing Disclosure Agreements.

CHILDREN'S HEALTH CARE

By Susan Slocum

Susan R. Slocum
Treasurer
952 240-3721

Table 7

Children's Hospitals and Clinics of Minnesota
Admissions and Patient Days

	For Year Ending December 31,					For the Six Months Ending June 30,	
Admissions	2006	2007	2008	2007	2009	2009	2010
Perinatal Services	1,707	1,864	2,064	2,064	1,859	864	903
Intensive Care Services	1,734	1,738	1,879	1,879	1,857	939	807
Medical and Surgical Services	9,665	10,431	10,228	10,228	10,161	5,222	4,873
Total	13,106	14,033	14,171	14,171	13,877	7,025	6,583
Patient Days							
Perinatal Services	37,292	38,454	37,810	37,810	38,429	18,082	17,781
Intensive Care Services	9,478	9,970	9,518	9,518	9,838	5,138	5,258
Medical and Surgical Services	39,039	41,028	39,596	39,596	39,275	20,885	18,874
Total	85,809	89,452	86,924	86,924	87,542	44,105	41,913
Average Daily Census	235.1	245.1	237.5	245.1	239.8	243.6	231.6

Obligated Group Unrestricted Cash and Investments at June 30, 2010:	$363,184,000
Obligated Group Days Cash on Hand:	251.1 days

CHILDREN'S HEALTH CARE

TABLE OF CONTENTS

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis of Children's financial condition and results of operations together with the consolidated financial statements and the related notes. Some of the information contained in this discussion and analysis or set forth elsewhere in this quarterly report, including information with respect to Children's plans and strategy for its organization and expected financial results, includes forward-looking statements that involve risks and uncertainties. These risks and uncertainties could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis. You should read this quarterly report in conjunction with the audited consolidated financial statements for the twelve months ended December 31, 2009.

BUSINESS DESCRIPTION

Children's Health Care, d.b.a. Children's Hospitals and Clinics of Minnesota ("Children's"), is a Minnesota nonprofit corporation that provides a broad range of pediatric health care services for children in the upper midwest. Through its hospitals with 410 licensed inpatient beds and numerous ambulatory services programs, Children's offers a continuum of health care services for children, including a full range of pediatric medical and surgical subspecialty services, Levels II through IIIc (sometimes referred to as Level IV) newborn intensive care, pediatric intensive care, and ambulatory and preventive care services.

Children's owns and operates two tertiary acute care facilities, Children's – Minneapolis and Children's – St. Paul. Children's – Minneapolis currently has 199 staffed beds and 227 licensed beds. It was originally incorporated in 1953 and began inpatient operations in 1973. Children's – St. Paul, first established in 1924, has 133 staffed beds and 183 licensed beds.

Children's Health Care Services, Inc. ("Children's – Minnetonka"), a Children's subsidiary, owns and operates a pediatric facility in the western Minneapolis suburb of Minnetonka, Minnesota, that provides pediatric ambulatory surgical services and other pediatric diagnostic services. The Children's – Minnetonka campus also includes a medical office building.

Obligated Group Members. The members of the Obligated Group under the Master Indenture securing the Bonds are Children's and Children's – Minnetonka.

Non-Obligated Group Members. Children's is the sole member of Children's Health Care Foundation, d.b.a. Children's Foundation ("Children's Foundation"), which performs fund-raising functions and endowment management. Children's is also the sole voting member of Children's Health Insurance Network Ltd. ("CHIN"), a Cayman Island domiciled insurance entity. The financial statements of both Children's Foundation and CHIN are consolidated into the financial statements of Children's, but neither Children's Foundation nor CHIN is a member of the Obligated Group.

Children's is the sole corporate and nonvoting member of Children's Health Care Physician Hospital Organization, d.b.a. Children's Physician Network ("CPN"), a taxable, nonprofit corporation. The primary purpose of the CPN is to provide the community with an integrated network of pediatric health care providers focused on quality care. The financial statements of the CPN are not consolidated into the financial statements of Children's, and the CPN is not a member of the Obligated Group.

RESULTS OF OPERATIONS

Results of Operations for the quarter ended June 30, 2010 compared to the quarter ended June 30, 2009.

Operating results for the quarter were significantly impacted by the decrease in utilization as measured by a 15.5% year-over-year decline in average daily census. Contributing to this decline was the June nursing work stoppage, the planned and averted July nursing work stoppage, and overall economic conditions. The net result was a 2.3% decline in total revenue equal to $3.2 million. The decline in revenue coupled with increased operating expenses and expenses related to the nursing work stoppage resulted in an operating loss of $7.3 million. Operating expenses increased $5.6 million reflecting an increase in depreciation, financing costs, and strategic spending as detailed below.

Total Revenue. Revenue decreased ($3,237), or 2.3%, to $137,652 for the three months ended June 30, 2010 from $140,889 for the three months ended June 30, 2009.

The decrease was primarily due to a decrease in net patient service revenues, a 3.5% decrease, reduced by favorable non-patient service revenues. Favorable non-patient service revenues were primarily due to higher medical education and research revenues. Net patient service revenues were unfavorable to prior year primarily due to a lower adjusted average daily census of 324.6 as compared to prior year of 361.8, a 10.3% decline. The unfavorable census to prior year reflects the June nursing work stoppage, the planned and averted July nursing work stoppage, and overall economic conditions. Partially offsetting the decline in patient volume were planned rate increases and disproportionate share (DSH) payments.

Payer mix for the three months ended June 30, 2010 and 2009, respectively, was as follows.

	Three Months Ended June 30,	
	2010	**2009**
Medicaid and Medicare	43.1%	41.2%
Negotiated Contracts	53.9%	55.0%
Commercial and Others	3.0%	3.8%
	100.0%	100.0%

Operating Expenses and Operating Income (Loss). Operating expenses increased $5,638, or 4.1%, to $143,659 for the three months ended June 30, 2010 from $138,021 for the three months ended June 30, 2009.

The increase in operating expenses was primarily due to higher depreciation, interest expense, and strategic spending to increase market share. Higher depreciation expense was due to the campus expansion project, as discussed below. Higher interest expense reflects the increase in average debt outstanding, $47 million, the conversion of variable rate debt to fixed rate debt, and lower capitalized interest due to the further completion of the campus expansion project. The increase in strategic spending primarily reflects an increase in advertising and public relations.

Operating margin decreased to a loss of 5.3% for the three months ended June 30, 2010 from a gain of 2.0% for the same period last year. The decrease in operating margin was primarily due to the decrease in total revenues, cost increases as discussed above, expenses related to the nursing work stoppage, and the semi-fixed nature of union labor costs.

Nonoperating Gains (Losses). Nonoperating gains (losses) for the quarter was a net loss of ($9,689) as compared to a net gain of $24,816 for the corresponding period of 2009.

The decrease was primarily due to the unrealized impact of interest rate changes on interest rate swap valuations and unfavorable investment returns. The LIBOR based swap contracts experienced an $11,154 unrealized loss for the three months as compared to a $14,351 unrealized gain for the corresponding period of 2009. The decrease in LIBOR rates was the primary driver of the change in swap valuations. Children's does not have collateral posting thresholds or requirements under the current terms of its swap agreements. Unfavorable investment returns reflect the overall difference in investment market returns between the corresponding periods.

Results of Operations for the six months ended June 30, 2010 compared to the six months ended June 30, 2009.

Operating results for the six months were significantly impacted by the second quarter decrease in utilization that offset favorable first quarter utilization. The result was a 4.9% year-over-year decline in average daily census. Contributing to this decline was the June nursing work stoppage, the planned and averted July nursing work stoppage, and overall economic conditions. Rate increases reduced the impact of the utilization decline resulting in a net $1.4M decline in patient service revenues. The decline in patient service revenues was offset by non-patient service revenues resulting in a slight increase in total revenues. Higher operating expenses and expenses related to the nursing work stoppage resulted in an operating loss of $2.4 million. Operating expenses increased $10.9 million reflecting an increase in salaries and benefits, depreciation, financing costs, and strategic spending, reduced by lower bad debt expense as detailed below.

Total Revenue. Revenue increased $557, or 0.2%, to $286,139 for the six months ended June 30, 2010 from $285,582 for the six months ended June 30, 2009.

Total revenue was slightly above prior year levels with favorable non-patient service revenues offsetting a 0.5% decrease in net patient service revenues. Favorable non-patient service revenues were primarily due to higher medical education and research revenues. Net patient service revenues were unfavorable to prior year primarily due to a lower adjusted average daily census of 358.3 as compared to prior year of 368.9, a 2.9% decline. The unfavorable census to prior year reflects the June nursing work stoppage, the planned and averted July nursing work stoppage, and overall economic conditions. Partially offsetting the decline in patient volume were planned rate increases and disproportionate share (DSH) payments.

Payer mix for the six months ended June 30, 2010 and 2009, respectively, was as follows.

	Six Months Ended June 30,	
	2010	**2009**
Medicaid and Medicare	43.8%	39.6%
Negotiated Contracts	53.1%	56.5%
Commercial and Others	3.1%	3.9%
	100.0%	100.0%

Operating Expenses and Operating Income (Loss). Operating expenses increased $10,892, or 3.9%, to $287,236 for the six months ended June 30, 2010 from $276,344 for the six months ended June 30, 2009.

The increase in operating expenses was primarily due to higher salaries and benefits, depreciation, interest expense, costs associated with the 2010 bond issuance and remarketing of the 1995B and 2004A bonds, and strategic spending to increase market share, reduced by lower bad debt expense. The increase in salaries and benefits primarily reflects wage increases and bonus expense adjustments, reduced by favorable medical and dental benefit costs. Higher depreciation expense was due to the campus expansion project, as discussed below. Higher interest expense reflects the increase in average debt outstanding, $24 million, the conversion of variable rate debt to fixed rate debt, and lower capitalized interest due to the further completion of the campus expansion project. The increase in strategic spending primarily reflects an increase in advertising and public relations.

Operating margin decreased to a loss of 0.8% for the six months ended June 30, 2010 from a gain of 3.2% for the same period last year. The decrease in operating margin was primarily due to the decrease in total revenues, cost increases as discussed above, expenses related to the nursing work stoppage, and the semi-fixed nature of union labor costs.

Nonoperating Gains (Losses). Nonoperating gains (losses) for the six months of 2010 was a net gain of $52 as compared to a net gain of $23,188 for the corresponding period of 2009.

The decrease was primarily due to the unrealized impact of interest rate changes on interest rate swap valuations reduced by favorable returns on investments. Net investment gains reflected the overall improvement in the investment markets.

SUMMARY OF UTILIZATION

Inpatient utilization, as measured by the average daily census, was unfavorable to the corresponding prior year period for the quarter, unfavorable 15.5%, and for the six months, unfavorable 4.9%. Average occupancy also declined from 71% to 60% for the quarter and from 73% to 70% for the six months. Outpatient activity, as measured by clinic visits, was unfavorable to the corresponding prior year period for the quarter, unfavorable 3.0%, and for the six months, unfavorable 0.1%. The unfavorable utilization was primarily due to the June nursing work stoppage, the planned and averted July nursing work stoppage, and overall economic conditions.

	For the Three Months Ended June 30,		For the Six Months Ended June 30,		For the Twelve Months Ended December 31,	
	2010	2009	2010	2009	2009	2008
Admissions						
Perinatal Services	466	431	907	862	1,859	2,064
Intensive Care Services	405	454	793	940	1,857	1,879
Medical and Surgical Services	2,087	2,408	4,880	5,217	10,161	10,228
Total	2,958	3,293	6,580	7,019	13,877	14,171
Patient Days						
Perinatal Services	8,332	9,458	17,783	18,080	38,429	37,810
Intensive Care Services	2,375	2,444	5,257	5,138	9,838	9,518
Medical and Surgical Services	7,547	9,682	18,876	20,886	39,275	39,596
Total	18,254	21,584	41,916	44,104	87,542	86,924
Average Daily Census	200.5	237.2	231.6	243.6	239.8	237.5
Staffed Beds	332	332	332	332	332	332
Average Length of Stay	6.2	6.6	6.4	6.3	6.3	6.1
Average Occupancy	60%	71%	70%	73%	72%	72%
Clinic Visits	31,498	32,483	64,846	64,932	137,853	116,834
Emergency Room Visits	19,945	24,054	40,687	46,845	90,963	82,433
Avg. Adjusted Daily Census	324.6	361.8	358.3	368.9	363.7	353.0

BALANCE SHEET, CASH FLOWS, AND LIQUIDITY

Working capital increased $26,248 to $50,862 for the six months ended June 30, 2010 from $24,614 at December 31, 2009. This increase was largely due to the 2010 bond offering and a higher mix of cash and short-term investments to long-term investments. Unrestricted cash, cash equivalents, and investments increased $32,195 to $369,667 at June 30, 2010 from $337,472 at December 31, 2009. This increase primarily reflects the 2010 bond offering and cash provided by operations, reduced by expenditures for the campus expansion. Days cash on hand improved 18 days to 251 days on hand at June 30, 2010 from 233 days on hand at December 31, 2009. The debt to capitalization ratio for the Obligated Group was 39.7% at June 30, 2010 as compared to 34.6% at December 31, 2009, reflecting the Series 2010A debt issuance.

The $50 million in new debt issued in March 2010 (Series 2010A) was accompanied by a conversion of approximately $45 million from variable rate demand obligations to fixed rate bonds (Series 1995B and Series 2004A-1). This conversion has reduced Children's reliance on its Standby Bond Purchase facility (liquidity facility) from approximately $220 million to $170 million and has resulted in an increase in interest expense. The renewal of the U.S. Bank liquidity facility associated with the remaining variable rate bonds (Series 2004A, Series 2004B, and Series 2007A) was completed in June of 2010 with a new expiration date of June 30, 2012.

CAMPUS EXPANSION

Children's is currently in progress on construction projects that will expand, renovate and add equipment to the Children's – Minneapolis and Children's – St. Paul campuses, as described below. Total construction costs are estimated to be $293 million, expended from 2008 through 2012, with approximately $230 million budgeted for improvements to, and expansion of, the Children's – Minneapolis campus (the "Minneapolis Project") and approximately $63 million budgeted for improvements to, and expansion of, the Children's – St. Paul campus (the "St. Paul Project"). The Minneapolis Project and the St. Paul Project will be financed by (i) proceeds of the Series 2007A Bonds issued in November 2007, (ii) revenue generated by the operation of Children's existing facilities, (iii) an estimated $57 million of near term cash receipts of a $100 million capital campaign that commenced in 2007 and (iv) Children's available cash balances. As of June 30, 2010, Children's had received pledges totaling $47.6 million toward this capital campaign. The Minneapolis campus was approximately eighty percent complete and the St. Paul campus was approximately forty-five percent complete as of June 30, 2010.

MARKET RISKS

Children's invests in various securities, including corporate stocks, corporate bonds, U.S. government obligations, foreign investments, mutual funds, and exchange-traded futures and options contracts. Investment securities, in general, are exposed to various market risks, such as interest rate, credit, liquidity, and price volatility. Because of these possible risks associated with the equity and bond markets, it is reasonably possible that changes in the values of various investment positions could occur in the near term and that such changes could materially affect the amounts reported in the consolidated financial statements. To monitor the risk of the investment portfolio, Children's has investment policies in place and monitors the performance of all securities on a regular basis.

Children's is exposed to interest rate risk with its variable rate debt structure. To manage these risks, Children's has entered into certain fixed payer swap agreements for all of its outstanding variable rate debt. These swap agreements hedge its variable interest rate risk, which is primarily exposed to LIBOR changes. Generally, under these swaps, Children's agrees with a counterparty to exchange the difference between fixed-rate and floating-rate interest amounts based on an agreed upon notional principal amount. Swap valuations are dependent on the LIBOR swap curve and fluctuate with directional or yield curve changes in that market.

LITIGATION AND COMPLIANCE WITH LAWS AND REGULATIONS

Litigation — Children's is a defendant in legal proceedings arising in the ordinary course of business. Although the outcome of these proceedings cannot presently be determined, in the opinion of management, disposition of these proceedings will not have a material adverse effect on the consolidated financial statements of Children's.

Compliance With Laws and Regulations — The health care industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations can be subject to government review and interpretations, as well as regulatory actions unknown and unasserted at this time. Government activity has increased with respect to investigations and allegations concerning possible violations of regulations by health care providers, which could result in the imposition of significant fines and penalties, as well as significant repayments of previously billed and collected revenues. Management believes that Children's compliance procedures lead to substantial compliance with current laws and regulations.

FORWARD-LOOKING STATEMENTS

Any statements that are not based upon historical facts, including the outcome of events that have not yet occurred and our expectations for future performance, are forward-looking statements. The words “potential,” “believe,” “estimate,” “expect,” “intend,” “may,” “could,” “will,” “plan,” “anticipate,” and similar words and expressions are intended to identify forward-looking statements. Such statements are based upon the current beliefs and expectations of Children’s. Such forward-looking information involves important risks and uncertainties that could significantly affect anticipated results in the future and, accordingly, such results may differ from those expressed in any forward-looking statements made by or on behalf of Children’s.

* * * * * *

CHILDREN'S HEALTH CARE

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
AS OF JUNE 30, 2010 AND DECEMBER 31, 2009
(In thousands)

	June 30, 2010 (unaudited)	December 31, 2009 (audited)
ASSETS		
CURRENT ASSETS		
Cash & cash equivalents	$ 18,928	$ 14,051
Short-term investments (Note 2)	26,731	16,186
Funds held by trustee (Note 3)	14,842	1,641
Patient accounts receivable - less allowance for uncollectible accounts of $6,832 and $7,405 at 2010 and 2009, respectively	54,272	58,317
Prepaid expenses and other current assets	33,951	29,922
Total current assets	148,724	120,117
INVESTMENTS (Note 2)		
Donor-restricted cash and investments	39,383	41,781
Unrestricted investments	324,008	307,235
Total investments	363,391	349,016
OTHER ASSETS	62,116	64,305
LAND, BUILDINGS, AND EQUIPMENT - Net	333,520	310,397
TOTAL	$ 907,751	$ 843,835
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Current maturities of long-term debt	$ 5,910	$ 5,910
Accounts payable and accrued expenses	26,638	37,288
Accrued salaries, wages, and benefits	59,101	46,032
Other current liabilities	6,213	6,273
Total current liabilities	97,862	95,503
FAIR VALUE OF INTEREST RATE SWAPS (Note 2)	28,642	16,391
OTHER LONG-TERM LIABILITIES	44,758	47,770
LONG-TERM DEBT - excluding current maturities (Note 3)	263,696	211,269
Total liabilities	434,958	370,933
NET ASSETS		
Unrestricted	403,104	401,392
Temporarily restricted	43,320	45,046
Permanently restricted	26,369	26,464
Total net assets	472,793	472,902
TOTAL	$ 907,751	$ 843,835

See notes to consolidated financial statements

CHILDREN'S HEALTH CARE

CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2010 AND 2009
(In thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
REVENUE:				
Net patient service revenue	$ 129,401	$ 134,129	$ 270,996	$ 272,444
Foundation transfers for operations	1,993	1,768	3,589	3,209
Other	6,258	4,992	11,554	9,929
Total revenue	137,652	140,889	286,139	285,582
EXPENSES:				
Salaries, wages, and employee benefits	86,804	86,687	173,397	169,575
Professional fees and purchased services	14,802	14,604	30,654	30,321
Supplies	13,149	12,824	28,696	28,254
Facilities	3,320	2,829	6,388	5,551
Depreciation and amortization	8,772	7,710	17,350	14,993
Financing costs	2,757	1,289	4,387	2,911
Provision for uncollectibles	2,759	2,945	4,857	6,085
Health services taxes	4,269	4,020	8,646	8,213
Other	7,027	5,113	12,861	10,441
Total expenses	143,659	138,021	287,236	276,344
OPERATING (LOSS) INCOME BEFORE NON-RECURRING ITEM	(6,007)	2,868	(1,097)	9,238
Expenses related to nursing work stoppage - net	1,277	-	1,277	-
OPERATING (LOSS) INCOME	(7,284)	2,868	(2,374)	9,238
NONOPERATING GAINS (LOSSES):				
Investment gain (loss)	4,163	660	8,666	(17,359)
Income on investments accounted for under the equity method	1,236	836	2,373	1,145
Net change in unrealized gains on investments	(3,719)	9,184	1,694	17,939
Change in unrealized interest rate swap valuation (Note 2)	(11,154)	14,351	(12,251)	21,910
Other	(215)	(215)	(430)	(447)
Total nonoperating gains (losses)	(9,689)	24,816	52	23,188
EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES	(16,973)	27,684	(2,322)	32,426
OTHER CHANGES:				
Net assets released from restrictions - capital acquisitions	2,025	2,541	4,034	5,266
CHANGE IN UNRESTRICTED NET ASSETS	$ (14,948)	$ 30,225	$ 1,712	$ 37,692

See notes to consolidated financial statements

CHILDREN'S HEALTH CARE

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2010 AND 2009
(In thousands)

	Three Months Ended June 30, 2010 (unaudited)	Three Months Ended June 30, 2009 (unaudited)	Six Months Ended June 30, 2010 (unaudited)	Six Months Ended June 30, 2009 (unaudited)
UNRESTRICTED NET ASSETS:				
Excess (deficiency) of revenue over expenses	$ (16,973)	$ 27,684	$ (2,322)	$ 32,426
Net assets released from restrictions - capital acquisitions	2,025	2,541	4,034	5,266
Increase (decrease) in unrestricted net assets	(14,948)	30,225	1,712	37,692
TEMPORARILY RESTRICTED NET ASSETS:				
Contributions	3,917	2,901	6,757	5,663
Investment income	151	797	440	(549)
Net change in unrealized gains (losses) on investments	(1,918)	2,036	(1,299)	1,401
Net assets released from restrictions - operations	(1,993)	(1,769)	(3,590)	(3,210)
Net assets released from restrictions - capital acquisitions	(2,025)	(2,541)	(4,034)	(5,266)
Increase (decrease) in temporarily restricted net assets	(1,868)	1,424	(1,726)	(1,961)
PERMANENTLY RESTRICTED NET ASSETS:				
Contributions	1	-	101	93
Change in value of perpetual trusts held by others	(122)	520	(196)	34
Increase (decrease) in permanently restricted net assets	(121)	520	(95)	127
CHANGE IN NET ASSETS	(16,937)	32,169	(109)	35,858
NET ASSETS - BEGINNING OF PERIOD	489,730	374,080	472,902	370,391
NET ASSETS - END OF PERIOD	$ 472,793	$ 406,249	$ 472,793	$ 406,249

See notes to consolidated financial statements

CHILDREN'S HEALTH CARE

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JUNE 30, 2010 AND 2009
(In thousands)

	Six Months Ended June 30, 2010 (unaudited)	Six Months Ended June 30, 2009 (unaudited)
CASH FLOWS FROM OPERATING ACTIVITIES:		
(Decrease) increase in net assets	$ (109)	$ 35,858
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:		
Depreciation and amortization	17,350	14,993
Net change in unrealized gains on investments	(395)	(19,331)
Net realized (gains) losses on investments	(3,817)	22,736
Change in fair value of interest rate swaps	12,251	(21,910)
Contributions restricted for long-lived purposes	(1,341)	(3,370)
Income on investments accounted for under equity method	(1,943)	(1,145)
Other	157	342
Changes in assets and liabilities:		
Patient accounts receivable	4,045	7,572
Prepaid expenses and other current assets	(4,029)	7,826
Other assets	3,561	(3,102)
Accounts payable and accrued expenses	837	(3,050)
Accrued salaries, wages, and benefits	13,069	4,448
Other liabilities	(3,260)	1,621
Net cash provided by operating activities	36,376	43,488
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of land, buildings, and equipment	(49,046)	(50,224)
Purchase of investments, funds held by trustee, and other assets	(393,361)	(509,731)
Proceeds from sale and maturities of investments and funds held by trustee	357,315	513,801
Net cash used in investing activities	(85,092)	(46,154)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of long-term debt	94,625	-
Retirement of long-term debt	(44,625)	-
Deferred debt acquisition costs	2,426	-
Proceeds from contributions restricted for long-lived purposes	1,167	2,839
Net cash provided by financing activities	53,593	2,839
NET INCREASE IN CASH AND CASH EQUIVALENTS	4,877	173
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	14,051	21,515
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 18,928	$ 21,688

See notes to consolidated financial statements

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization — Children's Health Care, d/b/a Children's Hospitals and Clinics of Minnesota ("Children's"), is a not-for-profit corporation organized under the laws of the State of Minnesota for the treatment and care of infants, children, and adolescents and the promotion and administration of charitable care, research, and educational activities.

Children's owns and operates two tertiary facilities, Children's — Minneapolis and Children's — St. Paul: two separate and controlled not-for-profit corporations, Children's Health Care Services, Inc., d/b/a Children's - Minnetonka and Children's Health Care Foundation, d/b/a Children's Foundation (the "Foundation"); and a wholly owned subsidiary, Children's Health Insurance Network, Ltd., which handles professional liability claims. The consolidated financial statements include the accounts of Children's and all subsidiaries. The departments of Children's — Minneapolis; Children's — St. Paul; and Corporate, plus the subsidiary Children's – Minnetonka, collectively, are the "Obligated Group".

Basis of Presentation — The accompanying unaudited consolidated financial statements for the three and six months ended June 30, 2010 have been prepared in accordance with accounting principles generally accepted in the United States of America. Financial information as of December 31, 2009 has been derived from Children's audited consolidated financial statements. Children's has omitted footnote disclosures that would substantially duplicate the disclosures contained in the audited financial statements. The unaudited consolidated financial statements should be read together with the audited financial statements and footnote disclosures for the year ended December 31, 2009.

In the opinion of management, the interim consolidated financial statements include all adjustments (consisting of normal recurring accruals) necessary for the fair presentation of the results for interim periods presented. These financial statements include some amounts that are based on management's best estimates and judgments. These estimates may be adjusted as more information becomes available, and any adjustment could be significant. The impact of any change in estimates is included in the determination of financial results in the period in which the change in estimate is identified. Significant estimated amounts in the consolidated financial statements include contractual allowances, allowance for uncollectible accounts and pledges, depreciable lives, benefit obligations, accrued salary, bonuses, and benefit costs, and interest rate swap valuation. Operating results for the six months ended June 30, 2010 are not necessarily indicative of the operating results that may be expected for the year ending December 31, 2010.

Consolidation — The consolidated financial statements include all subsidiaries and entities controlled by Children's. All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements. Investments in entities that Children's does not control, but in which Children's has a substantial ownership interest and can exercise significant influence, are accounted for using the equity method. Investments in entities that Children's does not control, does not have a substantial ownership interest and cannot exercise significant influence are accounted for using the cost method.

Subsequent Events — Children's has evaluated all events or transactions that occurred after June 30, 2010, through August 13, 2010, the date the consolidated financial statements were issued. Children's is not aware of any material subsequent events that would require recognition or disclosure in the consolidated financial statements.

New Accounting Pronouncements Issued — In January 2010, the Financial Accounting Standards Board ("FASB") issued new guidance and additional clarification related to fair value measurements and disclosures. Specifically, this new guidance requires the disclosure of transfers in and out of Level 1 and

Level 2 fair value measurements, the reasons for the transfers, and a roll forward of activity for Level 3 fair value measurements. The new guidance also clarifies that an organization should provide fair value measurements for each class of assets and liabilities and the valuation techniques and inputs used to measure fair values for Level 2 and Level 3. The required roll forward of activity for Level 3 fair value measurements is effective for fiscal years beginning after December 15, 2010. Children's has adopted the other provisions of the new guidance as reflected in the disclosures for the current period.

New Accounting Pronouncements Adopted — In June 2009, the FASB issued new guidance on the consolidation of variable interest entities ("VIE") in response to concerns about the application of certain key provisions of preexisting guidance, including those regarding the transparency of the involvement with a VIE. Specifically, this new guidance requires a qualitative approach to identifying a controlling financial interest in a VIE and requires ongoing assessment of whether an entity is a VIE and whether an interest in a VIE makes the holder the primary beneficiary of the VIE. In addition, this new guidance requires additional disclosures about the involvement with a VIE and any significant changes in risk exposure due to that involvement. Children's adopted this guidance beginning with fiscal year 2010. The adoption of this new guidance did not have a material impact on the consolidated financial statements.

In April 2009, the FASB issued new guidance regarding the information that a not-for-profit entity provides in its financial reports about a combination with one or more other not-for-profit entities, businesses, or nonprofit activities. Children's adopted this guidance beginning with fiscal year 2010. The adoption of this new guidance did not impact the consolidated financial disclosures for the current period.

2. FINANCIAL INSTRUMENTS, RISK MANAGEMENT ACTIVITIES, AND FAIR VALUE

Financial Instruments — The carrying values of cash and cash equivalents, patient accounts receivable, accounts payable, and other accrued expenses approximate fair value due to their short-term nature. Marketable securities are carried at fair value. All other assets and liabilities that qualify as financial instruments under generally accepted accounting principles are carried at contractual amounts, which approximate fair value. The market value of Children's marketable debt and equity securities, at June 30, 2010 and December 31, 2009, are shown below:

	June 30, 2010	December 31, 2009
Corporate equities	$ 36,646	$ 35,829
Fixed income securities	281,963	253,745
U.S. government obligations	5,226	2,936
Money market funds	33,774	23,578
Foreign investments	43,681	45,283
Perpetual trusts held by others	4,006	4,202
Pending trades	(1,790)	(297)
Interest and dividends receivable	1,458	1,567
Total	$ 404,964	$ 366,843
Investments are reported as:		
Short-term investments	$ 26,731	$ 16,186
Funds held by trustee - current	14,842	1,641
Donor-restricted cash and investments	39,383	41,781
Unrestricted investments	324,008	307,235
Total	$ 404,964	$ 366,843

Classification of marketable securities as current or noncurrent is dependent upon management's intended holding period, the securities maturity date, or both.

Children's has elected the fair value option for all marketable debt and equity securities to improve financial reporting. The election of the fair value option results in these securities being recorded at fair value, with unrealized gains and losses being recorded as nonoperating gains (losses).

As of June 30, 2010 and 2009, the following schedule summarizes the investment return (loss) and its classification in the consolidated statements of operations and changes in net assets:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2010	**2009**	**2010**	**2009**
Investment earnings (losses) in unrestricted net assets:				
Interest and dividend income	$ 2,761	$ 2,339	$ 5,411	$ 4,824
Net realized gains (losses) on investments	1,492	(1,543)	3,437	(21,876)
Net unrealized gains (losses) on investments	(3,719)	9,184	1,694	17,939
Total	534	9,980	10,542	887
Investment earnings (losses) in restricted net assets:				
Interest and dividend income	201	305	400	588
Net realized gains (losses) on investments	(50)	492	40	(1,137)
Net unrealized gains (losses) on investments	(1,918)	2,036	(1,299)	1,401
Total	(1,767)	2,833	(859)	852
Total investment returns (losses)	$ (1,233)	$ 12,813	$ 9,683	$ 1,739
Reported within:				
Other operating revenue	$ 90	$ 136	$ 182	$ 307
Nonoperating gains (losses)	444	9,844	10,360	580
Changes in restricted net assets	(1,767)	2,833	(859)	852
Total investment returns (losses)	$ (1,233)	$ 12,813	$ 9,683	$ 1,739

Children's periodically invests in equity index futures and option contracts to manage its equity exposure within its investment policies. These derivative positions are not designated as hedges for accounting purposes. The changes in fair market value of these instruments are recorded as investments gains (losses) in the consolidated statements of operations. There were no equity index futures or option contracts outstanding in 2010 or at December 31, 2009.

Interest Rate Swaps — Children's has four fixed payer interest rate swap agreements outstanding, which hedge the variable interest rate exposure associated with certain of its variable rate long-term debt.

Children's records the fair values of the interest rate swaps as a component of nonoperating gains (losses) in the consolidated statements of operations. The fair values of the interest rate swaps were a liability of $28,642 as of June 30, 2010, and $16,391 as of December 31, 2009. This liability would have to be paid if the swap agreements were terminated. There are no current collateral posting thresholds or requirements under the swap agreements. The change in fair value of the interest rate swaps of ($11,154) and $14,351 for the quarter and ($12,251) and $21,910 for the six months ended June 30, 2010 and 2009, respectively, is recorded in nonoperating gains (losses) in the consolidated statements of operations as Children's is not applying hedge accounting. Children's recognized interest expense related to these swap agreements in the amounts of $1,514 and $1,405 during the quarter and $2,970 and $2,993 for the six months ended June 30, 2010 and 2009, respectively.

The following table summarizes the notional amounts and interest rates of the interest rate swaps at June 30, 2010.

Swap Agreement	Fair Value	Notional Amount	Rate Paid	Rate Received
2004A	$ (4,737)	$ 23,600	4.127%	70% LIBOR
2004B	(7,166)	42,575	4.266%	70% LIBOR
2007A1	(8,369)	51,500	3.518%	67% LIBOR
2007A2	(8,370)	51,500	3.518%	67% LIBOR
	$ (28,642)	$ 169,175		

Children's is exposed to the risk of loss through credit risk in the event of nonperformance by the counterparty to the interest rate swap agreements.

Fair Value of Financial Instruments — Children's values its financial assets and liabilities in accordance with the accounting guidance that establishes a three-tier fair value hierarchy. Level 1 provides the most reliable measure of fair value, while Level 3 generally requires significant management judgment. Considerable judgment may be required in interpreting market data used to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts that could be realized in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value. Three levels are defined as follows:

Level 1 — Inputs represent unadjusted quoted prices for identical assets or liabilities exchanged in active markets.

Level 2 — Inputs include directly or indirectly observable inputs other than Level 1 inputs, such as quoted prices for similar assets or liabilities exchanged in active or inactive markets; quoted prices for identical assets or liabilities exchanged in inactive markets; or other inputs that are considered in fair value determinations of assets or liabilities.

Level 3 — Inputs include unobservable inputs used in the measurement of assets and liabilities. Management is required to use its own assumptions regarding unobservable inputs because there is little, if any, market activity in the assets or liabilities or related observable inputs that can be corroborated at the measurement date.

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.

Financial assets and liabilities measured at fair value on a recurring basis at June 30, 2010 and December 31, 2009, are summarized in the following table by type of inputs applicable to the fair value measurements (in thousands):

	Fair Value		
	Level 1	**Level 2**	**Total**
As of June 30, 2010:			
Cash equivalents	$ 19,436	$ -	$ 19,436
Corporate equities:			
Large cap	$ 26,669	$ -	$ 26,669
Mid cap	9,706	-	9,706
Small cap	271	-	271
Total corporate equities	36,646	-	36,646
Fixed income securities	281,963	-	281,963
U.S. government obligations	5,226	-	5,226
Money market funds	33,774	-	33,774
Foreign investments:			
Foreign bonds	5,824	25,619	31,443
Foreign equities	6,282	5,956	12,238
Total foreign investments	12,106	31,575	43,681
Perpetual trusts held by others	4,006	-	4,006
Pending trades	(1,790)	-	(1,790)
Interest and dividends receivable	1,458	-	1,458
Total investments	$ 373,389	$ 31,575	$ 404,964
Other assets - deferred compensation	$ 8,033		$ 8,033
Fair value of interest rate swaps liability		$ 28,642	$ 28,642

	Fair Value		
	Level 1	**Level 2**	**Total**
As of December 31, 2009:			
Cash equivalents	$ 13,420	$ -	$ 13,420
Short-term investments	$ 16,186	$ -	$ 16,186
Funds held by trustee	1,641	-	1,641
Donor-restricted cash and investments	37,573	4,208	41,781
Unrestricted investments	277,961	29,274	307,235
Total investments	$ 333,361	$ 33,482	$ 366,843
Other assets - deferred compensation	$ 7,725		$ 7,725
Fair value of interest rate swaps liability		$ 16,391	$ 16,391

Level 2 investments represent commingled funds. The fair value of commingled funds are based on net asset values per fund share (the unit of account), derived from the quoted prices in active market of the underlying securities. The fair value of interest rate swaps are based on observable inputs as of the valuation date, including prices of instruments with similar maturities and characteristics, interest rate yield curves, and measures of interest rate volatility.

Long-Term Debt — Children's variable rate debt is marketed daily by two remarketing agents and consistently trades at par. By observing our own pricing experience and by comparing it to the pricing of similar issues, Children's estimates the fair value of its variable rate debt approximates par. Children's estimates the fair value of its fixed rate debt based on trading activity on or around June 30, 2010. The fair value of Children's long-term debt was $271,033 and $217,705 at June 30, 2010 and December 31, 2009, respectively.

3. LONG-TERM DEBT

Long-term debt at June 30, 2010 and December 31, 2009, consisted of the following:

	June 30, 2010	December 31, 2009
Health Care Revenue Bonds, Series 1995B, interest rate at a variable rate, due through August 15, 2025 (average of 0.30% for 2009)	$ -	$ 21,500
Health Care Revenue Bonds, Series 1995B (remarketed), interest rate at 4.909%, due in installments through August 15, 2025	21,500	-
Health Care Revenue Bonds, Series 1998A, interest rate at 4.45%, due in installments through August 15, 2011	3,905	3,905
Health Care Revenue Bonds, Series 2004A, interest rate at a variable rate, due through August 15, 2034 (average of 0.221% for 2010; 0.30% for 2009)	23,600	46,725
Health Care Revenue Bonds, Series 2004A-1 (remarketed), interest rate at 4.619%, due in installments through August 15, 2034	23,125	-
Health Care Revenue Bonds, Series 2004B, interest rate at a variable rate, due through August 15, 2025 (average of 0.208% for 2010; 0.30% for 2009)	42,575	42,575
Health Care Revenue Bonds, Series 2007A1, interest rate at a variable rate, due through August 15, 2037 (average of 0.185% for 2010; 0.30% for 2009)	51,500	51,500
Health Care Revenue Bonds, Series 2007A2, interest rate at a variable rate, due through August 15, 2037 (average of 0.221% for 2010; 0.30% for 2009)	51,500	51,500
Health Care Revenue Bonds, Series 2010A, interest rate at 5.089%, due in installments through August 15, 2035	50,000	-
	267,705	217,705
In addition (less):		
Unamortized bond premium (discount)	1,901	(526)
Current maturities	(5,910)	(5,910)
Long-term portion	$ 263,696	$ 211,269

Except for the 1998A bonds, all these bonds were issued through the conduit organizations of the City of Minneapolis, Minnesota (the "City") and the Housing and Redevelopment Authority of the City of Saint Paul, Minnesota (the "Authority") on behalf of the Obligated Group, pursuant to the Master Trust Indenture. The 1998A bonds were issued through the City on behalf of the Obligated Group, pursuant to the Master Trust Indenture. All bonds, except for the 2010A bonds, are insured by Assured Guaranty Municipal Corp., a division of Assured Guaranty Ltd., formerly known as Financial Security Assurance Inc., which is currently rated AAA with a negative outlook by S&P and Aa3 with a negative outlook by Moody's.

The Obligated Group must meet certain financial covenants required by the bond insurer and is limited in the amount of additional debt that can be incurred. The Obligated Group was in compliance with the financial covenants at June 30, 2010. The Series 1995B bonds, Series 2004A bonds, Series 2004A-1, Series 2004B bonds, Series 2007A bonds, and the Series 2010A bonds are subject to optional redemption by Children's, in whole or in part, at redemption price equal to 100% of the principal, plus accrued interest during various times as described in the Master Trust Indenture.

The only remaining balance of defeased debt that is outstanding is from a prior financing and totals $2,340 at June 30, 2010.

Under the Master Trust Indenture and related agreements for each bond series, the Obligated Group maintains with a trustee a project fund, a bond interest fund, and a sinking fund, the aggregated balances of which were as follows as of June 30, 2010 and December 31, 2009, respectively:

	June 30, 2010	December 31, 2009
Project fund	$ 8,930	$ -
Bond interest fund	1,476	163
Sinking fund	4,436	1,478

The funds are available to meet debt service and project specific expenditures and are classified as a current asset in the consolidated statements of financial position.

4. EMPLOYEE BENEFIT PLANS

Children's has noncontract and various union-sponsored pension or retirement plans covering substantially all employees.

Pension Plan — The Children's Health Care RSVP Retirement Plan provides benefits to eligible noncontract employees based on final average salary and accumulated pension credits, which are based on years of service.

Contributions to the plan are made in accordance with funding principles as recommended by Children's actuaries and in accordance with Employee Retirement Income Security Act of 1974 requirements as amended by the Pension Protection Act of 2006. Assets of the plan are invested primarily in common stocks, U.S. government debt securities, corporate debt instruments, international equities, and an enhanced S&P 500 index product. Children's uses a December 31 measurement date for its benefit plans.

Components of net periodic benefit cost for the plan for the first quarter of 2010 and 2009 were as follows:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2010	2009	2010	2009
Service cost	$ 1,375	$ 1,325	$ 2,750	$ 2,650
Interest cost	1,075	1,000	2,150	2,000
Expected return on plan assets	(800)	(875)	(1,600)	(1,750)
Amortization of prior service cost	75	50	150	100
Amortization of loss	325	250	650	500
Net periodic pension cost	$ 2,050	$ 1,750	$ 4,100	$ 3,500

Children's expects to contribute $7,400 to the defined benefit pension plan during 2010.

CHILDREN'S HEALTH CARE

COMBINED STATEMENTS OF FINANCIAL POSITION – OBLIGATED GROUP
AS OF JUNE 30, 2010 AND DECEMBER 31, 2009
(In thousands)

	June 30, 2010 (unaudited)	December 31, 2009 (audited)
ASSETS		
CURRENT ASSETS		
Cash & cash equivalents	$ 15,253	$ 9,652
Short-term investments (Note 2)	23,923	13,964
Funds held by trustee (Note 3)	14,842	1,641
Patient accounts receivable - less allowance for uncollectible accounts of $6,832 and $7,405 at 2010 and 2009, respectively	54,272	58,317
Prepaid expenses and other current assets	19,016	15,728
Total current assets	127,306	99,302
INTERCOMPANY ACCOUNTS	1,000	101
UNRESTRICTED INVESTMENTS (Note 2)	324,008	307,235
BENEFICIAL INTEREST IN NET ASSETS OF THE FOUNDATION	72,013	74,691
OTHER ASSETS	46,529	49,332
LAND, BUILDINGS, AND EQUIPMENT - Net	333,317	310,316
TOTAL	$ 904,173	$ 840,977
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Current maturities of long-term debt	$ 5,910	$ 5,910
Accounts payable and accrued expenses	26,452	37,268
Accrued salaries, wages, and benefits	59,101	46,032
Other current liabilities	4,787	5,058
Total current liabilities	96,250	94,268
FAIR VALUE OF INTEREST RATE SWAPS (Note 2)	28,642	16,391
OTHER LONG-TERM LIABILITIES	44,758	47,770
LONG-TERM DEBT - excluding current maturities (Note 3)	263,696	211,269
Total liabilities	433,346	369,698
NET ASSETS		
Unrestricted	401,138	399,769
Temporarily restricted	43,320	45,046
Permanently restricted	26,369	26,464
Total net assets	470,827	471,279
TOTAL	$ 904,173	$ 840,977

CHILDREN'S HEALTH CARE

COMBINED STATEMENTS OF OPERATIONS – OBLIGATED GROUP
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2010 AND 2009
(In thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
REVENUE:				
Net patient service revenue	$ 129,401	$ 134,129	$ 270,996	$ 272,444
Foundation transfers for operations	2,767	1,648	4,996	3,205
Other	5,692	4,772	10,707	9,285
Total revenue	137,860	140,549	286,699	284,934
EXPENSES:				
Salaries, wages, and employee benefits	86,005	85,941	171,900	168,156
Professional fees and purchased services	15,761	15,311	32,471	31,585
Supplies	13,108	12,770	28,601	28,156
Facilities	3,320	2,829	6,388	5,551
Depreciation and amortization	8,757	7,701	17,329	14,982
Financing costs	2,757	1,289	4,387	2,911
Provision for uncollectibles	2,759	2,945	4,857	6,085
Health services taxes	4,269	4,020	8,646	8,213
Other	6,702	4,880	12,459	9,918
Total expenses	143,438	137,686	287,038	275,557
OPERATING (LOSS) INCOME BEFORE NON-RECURRING ITEM	(5,578)	2,863	(339)	9,377
Expenses related to nursing work stoppage - net	1,277	-	1,277	-
OPERATING (LOSS) INCOME	(6,855)	2,863	(1,616)	9,377
NONOPERATING GAINS (LOSSES):				
Investment gain (loss)	4,163	659	8,666	(17,360)
Income on investments accounted for under the equity method	1,236	836	2,373	1,145
Net change in unrealized gains on investments	(3,826)	9,144	1,450	17,921
Change in unrealized interest rate swap valuation (Note 2)	(11,154)	14,351	(12,251)	21,910
Other	(215)	(215)	(430)	(447)
Total nonoperating gains (losses)	(9,796)	24,775	(192)	23,169
EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES	(16,651)	27,638	(1,808)	32,546
OTHER CHANGES:				
Net assets released from restrictions capital acquisitions	2,025	2,541	4,034	5,266
Change in beneficial interest in net assets of the Foundation	(463)	(44)	(857)	(210)
CHANGE IN UNRESTRICTED NET ASSETS	$ (15,089)	$ 30,135	$ 1,369	$ 37,602