



Disclosure Statement

June 30, 2017



MIDMICHIGAN HEALTH DISCLOSURE STATEMENT: JUNE 30, 2017

This Disclosure Statement discusses MidMichigan Health's results of operations, financial condition, liquidity, risk management activities, and significant accounting policies. MidMichigan's fiscal year ends on June 30th. The following is an outline of the analysis included herein:

- Business Overview
 - Governance
 - MidMichigan Health Facilities & Campus Descriptions
 - Medical Staff
 - Board of Directors
 - Service Area
- University of Michigan Health System Affiliation
- Summary of Results
- Management's Review of Consolidated Results
- Historical Capitalization
- Historical Debt Service Coverage
- Liquidity
- Insurance and Risk Management
- Issued But Not Yet Adopted Accounting Standards
- Forward-Looking Information

The Appendix includes additional information that the reader may find useful but is not required.

BUSINESS OVERVIEW

MidMichigan Health, headquartered in Midland, Michigan, is a Michigan nonprofit corporation qualified as a tax-exempt organization described in Section 501(c)(3) of the Internal Revenue Code. MidMichigan Health operates a system of health care organizations serving the middle and northern Michigan. MidMichigan Health is affiliated with the University of Michigan Health System ("UMHS") through Michigan Health Corporation. Michigan Health Corporation held a one-tenth of one percent (0.1%) membership interest in MidMichigan Health, during the initial term of the affiliation agreement (through June, 2017). On July 1, 2017 the membership interest increased to twelve percent. In 2016, MidMichigan Health was named one of the nation's 15 Top Health Systems® by Truven Health Analytics™ (Truven). Midland was named one of the nation's 2016 100 Top Hospitals® by Truven and also one of a select few to earn the 2016 100 Top Hospital's Everest® Award. In 2017, Truven named Midland one of the nation's Top 50 Cardiovascular Hospitals.

MidMichigan Health's mission is to provide excellent health services to improve the quality of life for people in our communities. MidMichigan Health's vision is ***to celebrate the power of health throughout life - with you.*** MidMichigan Health promotes health throughout each person's lifetime by providing seamless care through coordinated hospitals, home care, and urgent care, as well as through physician services and advanced medical technology. MidMichigan Health provides quality, comprehensive health care to each and every person we serve. The parent company provides long-range strategic planning for, and coordinates the activities of, its subsidiary organizations. With respect to its subsidiaries, MidMichigan Health has the right to appoint the Board of Directors and must approve any amendments to the articles of incorporation and bylaws. Further, it has the authority to approve major expenditures and long-term borrowings of its subsidiaries. MidMichigan Health is the sole member of each of its subsidiaries. See **GOVERNANCE** herein.

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MidMichigan Health includes: one acute care Level II Trauma teaching hospital, one sole community hospital, two acute care rural hospitals, one critical access hospital, home health services, ambulatory centers and programs, multi-specialty physician practices, a managed care company, and various medical office buildings. It also provides radiation therapy and positron emission tomography (PET) imaging services in connection with other healthcare systems. MidMichigan Health serves a primary service area with a population of approximately 305,000 people including Alpena (U.S. Census Bureau, 2010 data estimated to 2017).

Changes to the organizational structure included the following:

- Effective April 1, 2017, MidMichigan Assurance Group (MAG) was dissolved and liquidated.
- Effective July 1, 2016, MidMichigan Health Foundation was formed to enhance the mission of MidMichigan Health by raising funds and public support and funding MidMichigan Health's services, programs, projects, and initiatives to further its exempt purposes.

Alpena Regional Medical Center

On April 1, 2016, MidMichigan Health acquired Alpena Regional Medical Center (ARMC), a 501(c)(3) exempt acute care hospital located in Alpena, Michigan that primarily serves the municipality of Alpena, and Alpena County. The integration of Alpena has continued during fiscal 2017 and resulted in various, organizational, financial and clinical synergies including, improved recruitment efficiency, centralized labor relations, increased contract savings, access to specialists, and alignment of policies. The new electronic health record (EPIC), which was implemented for the other hospitals on April 1, 2017, went live in Alpena on September 30, 2017, including all revenue cycle functions.

West Branch Regional Medical Center

MidMichigan Health has entered into an affiliation process with West Branch Regional Medical Center (WBRMC). The WBRMC Board of Trustees voted on the selection of MidMichigan Health as the preferred health system to proceed with partnership negotiations and named MidMichigan Health as the exclusive health system with which WBRMC will work to finalize an affiliation agreement. See forward-looking information for discussion of the pending acquisition.

MidMichigan Health, for itself and as Credit Group Representative on behalf of the Members of the Obligated Group ("Obligated Group") entered into a Master Indenture, dated December 1, 2014 with The Bank of New York Mellon Trust Company, N.A., as Master Trustee. Under the Master Indenture, the Members of the Obligated Group are jointly and severally obligated to repay Obligations issued under the Master Indenture. Currently, the Obligated Group only includes MidMichigan Health and MidMichigan Medical Center—Midland ("Midland"). The Master Indenture also requires the Obligated Group Members to cause each Designated Subsidiary to pay or otherwise transfer to the Credit Group Representative (MidMichigan Health) or Obligated Group Member (Midland) such amounts as are necessary to duly and punctually pay the principal of, or premium, if any, interest on and purchase price of Obligations issued under the Master Indenture. All of MidMichigan Health's active controlled subsidiaries, with the exception of MidMichigan Collaborative Care Organization, LLC (MCCO) are Designated Subsidiaries. The MidMichigan Health Credit Group is comprised of the Members of the Obligated Group and each Designated Subsidiary. As of June 30, 2017, MCCO held assets of \$1.0 million while total consolidated assets equaled approximately \$1.3 billion, including MCCO. Unless otherwise noted, MidMichigan Health is used herein to include MidMichigan Health and all of its consolidated subsidiaries.

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BUSINESS OVERVIEW: GOVERNANCE

MidMichigan Health serves as the parent company for all controlled subsidiaries which, together, provide diverse quality healthcare and related services to the residents of the central and northern Michigan area. The principal function of MidMichigan Health is to establish and coordinate long-term plans and objectives for each entity that is a part of the System. MidMichigan Health was incorporated for the benefit and governance oversight of MidMichigan Health and other controlled subsidiaries and is legally designated as the "sole member" of its directly controlled subsidiaries. MidMichigan Health and its controlled subsidiaries are listed and described in the following table as of June 30, 2017.

Legal Entity and How Referred to in this Statement	Description	Reference (a)
MidMichigan Health	The parent company and Credit Group Representative	1
MidMichigan Medical Center-Midland (Midland)	A 324-bed acute care teaching hospital (Level II Trauma Verified)	2
MidMichigan Medical Center-Alpena (Alpena)	A 139-bed acute care rural sole community hospital	3
MidMichigan Medical Center-Gratiot (Gratiot)	A 93-bed acute care rural hospital, including 44 rehabilitation and behavioral mental health beds	4
MidMichigan Medical Center-Clare (Clare)	A 49-bed acute care rural hospital	5
MidMichigan Medical Center-Gladwin (Gladwin)	A 25-bed critical access hospital	6
MidMichigan Physicians Group (MPG)	A physician employment and management subsidiary	7
MidMichigan Visiting Nurse Association (MVNA), d.b.a. MidMichigan Home Care (MHC)	A Medicare-certified subsidiary offering skilled nursing and physical, occupational, respiratory, and speech therapies, hospice, private duty nursing, and durable medical equipment.	8
MidMichigan Health Development Associates (MHDA)	A tax-exempt real estate development and management corporation	9
MidMichigan Collaborative Care Organization, LLC (MCCO)	A limited liability company (LLC) working with providers toward a coordinated system of health care	10
MidMichigan Health Foundation (Foundation)	A foundation to manage philanthropic and public support	11
MidMichigan Assurance Group, Ltd. (MAG)	A primary care captive insurance company which was dissolved and liquidated as of April 1, 2017	12

(a) References MidMichigan Health Facilities and Campus Descriptions

(b) Effective January 1, 2018, private duty patients have been transitioned to other home care providers as this function has been determined to be a non-core service

BUSINESS OVERVIEW: MIDMICHIGAN HEALTH FACILITIES & CAMPUS DESCRIPTIONS

1. MidMichigan Health – Parent company

As an integrated health care delivery network, in addition to the five hospitals, MidMichigan Health includes a number of other subsidiaries which provide support services to its hospitals and the communities they serve. These include an employed physicians group, home health services, and various medical office buildings. All non-acute operations made up approximately 6.5% of MidMichigan Health's consolidated net patient service revenue as of June 30, 2017. Brief descriptions of MidMichigan Health subsidiaries follow:

2. MidMichigan Medical Center-Midland - 250 Operated Beds (234 Acute; 16 Mental Health)

Midland, a 324-licensed bed hospital located in Midland, Michigan, is the only hospital within its county. The campus consists of approximately 180 acres and represents MidMichigan Health's flagship acute care facility. It provides a continuum of primary, secondary and tertiary services and has been designated as a sole community hospital by Medicare. Midland's services include general medicine and surgery, bariatric surgery, cardiology, vascular, orthopedic, acute and ambulatory psychiatric services, ambulatory rehabilitation medicine, oncology, pediatrics, telemedicine, basic and complex diagnostic services (including magnetic resonance imaging), and a full range of ambulatory services at Midland's main campus. Midland began operating a full cardiac program in August 2007 and was designated by Truven Health Analytics™ as one of the nation's Top 50 Cardiovascular Hospitals in 2017. MidMichigan Health started building a heart and vascular regional referral center in the spring of 2017, which is scheduled to be completed by the summer of 2020. It will be a three-story building that will occupy cardiovascular services, imaging services, neurology services and potentially UMHS clinics. Significant resources have also been committed to musculoskeletal and oncology service lines. Each of these service lines is led by a physician service line chief. Midland also maintains a 24-resident, four-year family practice medical education residency program, which is one of the oldest such programs in the country.

In December 2011, MidMichigan Health completed the renovation and expansion of the hospital on time and within budget. The total construction square footage (new and remodeled) added approximately 280,000 square feet. The expansion consisted of three new floors which replaced existing semi-private rooms with 36 private rooms on each floor including critical care rooms. The renovation also included an enlarged surgical services department, including four additional operating rooms and two remodeled and renovated rooms, pre-surgical, recovery areas, and support areas such as cardiac catheterization, post anesthesia care, and interventional radiology departments.

Midland's trauma program was re-verified by the American College of Surgeons Committee on Trauma and re-designated by the State of Michigan as an adult Level II trauma center following an on-site review in January of 2017. The two-day review focused on chart review, performance improvement review, staff interviews and data analysis on over 850 cases. As with their inaugural review in 2014, no deficiencies were found in the program and the Medical Center received a full three year verification. Midland is the highest level trauma center in the MidMichigan Health network and is one of twenty-four Level II trauma centers in the State of Michigan.

Midland is a regional leader in investing in advanced technology, offering state-of-the-art equipment and procedures typically found only in large academic medical centers. For example, Midland offers one of the region's most advanced robotic surgery capabilities using the da Vinci® SI Surgical System. In addition, Midland is the only hospital in Michigan to offer Gamma Knife® Perfexion™ (the most advanced Gamma Knife) which is the most precise intracranial radiosurgery tool on the market today – with an accuracy of

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.05 mm while providing radiation shielding up to 100 times better than other technologies; advantages that are currently unmatched in the region.

Advanced technologies available at Midland include:

Advanced Imaging

- 128-slice Computed Tomography (CT) Scanning
- Magnetic resonance imaging (3.0 T closed and 1.0 T open)
- Positron Emission Tomography (PET)

Neuroscience

- Deep Brain Stimulation (DBS)
- O-ARM intraoperative imaging device

Robotic Surgery

- da Vinci® SI Surgical System

Stereotactic radiosurgery

- BodyArray
- Gamma Knife® Perfexion™

Cardiovascular Technology

- Tacticath Ablation Catheter
- Certrimag Left Ventricular Assist System
- Laser Lead extraction
- Intravascular Ultrasound (IVUS)
- SPY imaging system
- Transmyocardial revascularization (TMR)
- Transcatheter Aortic Valve Replacement (TAVR) (performed 82 procedures)
- WATCHMAN (Left Atrial Occlusion Device) procedures started in September 2017 (9 procedures performed)

3. MidMichigan Medical Center-Alpena - 123 Operated Beds (93 Acute; 15 Rehab; 15 Mental Health)

Alpena, 139-licensed acute care hospital, is located in Alpena, Michigan. Alpena has operated continuously since 1940, serving a six county area in Northeastern Michigan, as the only hospital in this region. Alpena is designated as a “sole” community hospital by Medicare. In addition to inpatient services Alpena offers a wide range of outpatient services including radiology, ultrasound, MRI, PET scan, CT, laboratory services, retail pharmacy, physical, occupational, and speech therapy, as well as, a broad base of surgery, respiratory therapy, medical oncology, and wound care. Alpena has offered radiation oncology services on site since 1999 through the North Eastern Michigan Cancer Center, a joint venture between Alpena and University of Michigan Health System that provides cancer treatments under the care of UMHS and Alpena physicians. In February 2016, the emergency room renovation project was completed, increasing capacity to 20 private rooms and significantly upgrading technology and medical equipment. Alpena patients also have improved access to a wide range of services through Midland.

4. MidMichigan Medical Center-Gratiot - 93 Operated Beds (49 Acute; 18 Rehab; 26 Mental Health)

Gratiot, a 93-licensed bed rural acute care hospital, is located in Alma, Michigan. Gratiot is the only hospital located within its county. In addition to specialty services commonly found in community hospitals, Gratiot also provides a full range of inpatient and outpatient rehabilitation services, urgent care, psychiatry, and specialty centers for sleep disorders, pain management, and magnetic resonance imaging services. In September 2008, Gratiot opened its 140,000-square-foot patient tower. As of July 1, 2014, Gratiot began operating as a 49 bed rural acute care hospital (excluding 12 mental health and 18 rehabilitation beds) allowing it to receive additional reimbursement for its rural health clinics. In collaboration with Michigan State University College of Human Medicine, MidMichigan Medical Center - Gratiot has a new three-year program approved for training allopathic medicine. The MSU/MidMichigan Medical Center - Gratiot Family Medicine Residency Program is focused on rural, community-based hospital and clinical practice. The program received approval by the Accreditation Council for Graduate Medical Education (ACGME) in October 2015 and admitted the inaugural class of four first-year residents in July 2016. On February 1, 2017

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the MidMichigan Health Park – Mt. Pleasant opened, increasing the size of the original Health Park. The renovation added a 24-hour emergency department, five short stay beds, outpatient surgery center and wide range of other services. During fiscal 2017 Gratiot was approved for 14 additional inpatient mental health beds, four of which were transferred from Midland. Additional services are available to Gratiot patients through Midland.

5. MidMichigan Medical Center-Clare - 49 Operated Beds

Clare, a 49-licensed bed rural acute care hospital, is located in Clare, Michigan. Clare is the only hospital located within its county. It offers services that are reflective of rural facilities, such as primary care services including inpatient, 24-hour emergency room coverage, urgent care medicine and radiology services. In addition to these services, Clare also provides service for intensive and progressive care patients and several provider based rural health clinics. Ultrasound including echocardiography, nuclear medicine services, mobile MRI and fixed CT scanning equipment are located in Clare to provide diagnostic imaging. Clare completed its 14,000-square-foot surgical suites addition to the medical center in June 2008 that included operating rooms, communication, and video and telemedicine capabilities which enhance its patient safety and diagnostic capabilities. Additional services are available to Clare patients through Gratiot and Midland.

6. MidMichigan Medical Center-Gladwin - 25 Operated Beds

Gladwin, a 25-licensed bed critical access hospital, is located in Gladwin, Michigan. Gladwin is the only hospital located within its county. It offers services similar to Clare, reflective of its rural location. These services include primary care services including inpatient, 24-hour emergency room coverage, nuclear medicine, infusion, medical oncology and radiology services. Ultrasound including echocardiography, mobile MRI and fixed CT scanning equipment are located in Gladwin, providing diagnostic services to Gladwin patients. MidMichigan Health broke ground on October 5, 2017 for a new medical offices building in Gladwin. The facility will house physician offices, an urgent care, lab drawing station, and diagnostic x-ray services. Additional services are available to Gladwin patients primarily through Midland.

7. MidMichigan Physicians Group is a multi-specialty physician enterprise covering a 22-county region in MidMichigan and northeast Michigan. As of June 30, 2017 there were over 32 specialties and subspecialties including cardiology, hematology/oncology, orthopedics, vascular surgery, family medicine and more. Physician compensation is based on data available through the Medical Group Management Association (MGMA) and American Medical Group Association (AMGA). Physicians participate in an incentive plan based on median compensation and median worked relative value units (RVUs) as determined by MGMA-AMGA data. The Physician Enterprise employs approximately 290 full-time equivalent (FTE) physicians and advanced care providers.

8. MidMichigan Home Care is a multidisciplinary post-acute care provider with a 12 county service area, providing skilled nursing services, physical, occupational, and speech therapy, social work, as well as home health aide assistance for people in their homes. The agency has a licensed home health program that provides approximately 60,000 home health visits to patients per year. It also operates a robust hospice program, including the Woodland Hospice House, bereavement and respite services providing patients and families with over 20,000 hospice visits spanning more than 36,000 days of care. The home infusion services provide over 30,000 days of pharmaceutical therapy to home bound patients each year while the private duty program supplements in home assistance through nearly 60,000 hours of care for families. The agency also provides medical equipment, oxygen and respiratory therapy by filling over 50,000 orders each year. MidMichigan Home Care's home health and hospice programs are certified by the State of Michigan on behalf of the Centers for Medicare and Medicaid Services. The private duty, home infusion and home medical equipment programs are accredited by the Accreditation Commission for Health Care.

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9. MidMichigan Health Development Associates is a real estate development and management company. It is a tax-exempt corporation which supports the other patient care organizations by providing physician office space that is convenient for patients.

10. MidMichigan Collaborative Care Organization, LLC is wholly owned by MidMichigan Health. MCCO collaboratively works with healthcare providers in our community to provide excellent, efficient, coordinated care. The physician leadership works collaboratively with all healthcare services in our area to provide optimal patient care. This organization was created to optimize MidMichigan Health's population health strategy.

11. MidMichigan Health Foundation was formed to enhance the mission of MidMichigan Health by raising funds and public support and funding MidMichigan Health's services, programs, projects, and initiatives to further its exempt purposes.

12. MidMichigan Assurance Group, Ltd was a primary captive insurance company domiciled in the Cayman Islands. MAG was dissolved and liquidated effective April 1, 2017.

BUSINESS OVERVIEW: MEDICAL STAFF

The chart below shows the number of physicians affiliated with MidMichigan Health according to practice status as of June 30, 2015, 2016 and 2017. The Medical Staff is organized into groups according to type of hospital affiliation.

The categories of MidMichigan Health's Medical Staff membership are as follows:

<i>Active</i>	Physicians who qualify as Active members of the Medical Staff and who regularly perform a major part of their hospital medical practice at a MidMichigan Health hospital
<i>Courtesy</i>	Physicians who qualify as Active members of the Medical Staff but use MidMichigan Health hospitals infrequently

Physician Status	2015	2016*	2017*
Active	275	363	396
Courtesy	<u>165</u>	<u>272</u>	<u>244</u>
Total	<u>440</u>	<u>635</u>	<u>640</u>
% of Active Physicians Board Certified	82%	90%	92%
<i>*Data includes Alpena</i>			
<i>Source: MidMichigan Health Medical Staff Records</i>			

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As of June 30, 2017, the specialties of MidMichigan Health's physicians were:

Physicians by Specialty	Number of Physicians
Allergy & Immunology	4
Anesthesiology	26
Cardiology	17
Critical Care Medicine	2
Dental	7
Dermatology	2
Electrophysiology	2
Emergency Medicine	72
Endocrinology	3
Family Practice	84
Gastroenterology	5
Hospice & Palliative	1
Hospitalist	67
Infectious Diseases	3
Internal Medicine	32
Nephrology	10
Neurology, including Neurosurgery	21
Obstetrics and Gynecology	30
Oncology, including Radiation Oncology	25
Ophthalmology/Optometry	20
Orthopedic Surgery	17
Otolaryngology	6
Pain Management	1
Pathology	6
Pediatrics (includes general Pediatrics and subspecialties)	21
Physical Medicine and Rehabilitation	5
Podiatry	16
Psychiatry	17
Pulmonary Diseases	3
Radiology*	96
Rheumatology	1
Sports Medicine	1
Surgery (includes general and subspecialties)	37
Telemedicine	23
Urgent Care & Occupational Medicine	3
Urology	<u>12</u>
Total	<u>698</u>
*Includes approximately 58 Nighthawk Teleradiologists	

MidMichigan Health conducts an annual assessment of physician staffing needs and is continuously involved in recruiting primary care and specialty care physicians to all five MidMichigan Health hospitals.

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BUSINESS OVERVIEW: BOARD OF DIRECTORS

MidMichigan Health is governed by a Board of Directors consisting of not less than 11 and not more than 18 individuals. Terms of the Board of Directors are for three years. MidMichigan Health's Board of Directors must include at least two directors nominated by the University of Michigan Health System through Michigan Health Corporation (or 12% representation if the number of directors increases above 18). No director (other than the Chief Executive Officer (CEO) and the two Michigan Health Corporation directors) may serve more than three consecutive terms.

In June 2013, MidMichigan Health amended its Articles of Incorporation and Bylaws to provide for two member classes. One consists solely of the Michigan Health Corporation which currently holds a 12% membership interest. The other consists of the President/CEO of MidMichigan Health and other directors nominated by members of this second member class. Those individuals, who previously held the role of Corporate Members, were transitioned to members of MidMichigan Health's Advisory Council, which utilizes their involvement and expertise as advocates and ambassadors of MidMichigan Health throughout the 22-county region.

Under the bylaws, articles of organization or articles of association of each of the controlled subsidiaries (as applicable), MidMichigan Health has certain reserved powers. These reserved powers include MidMichigan Health's right to approve the following:

- Changes in the purposes of the subsidiaries;
- Changes in the subsidiary's Articles of Incorporation, Articles of Organization, Articles of Association or Bylaws (as applicable);
- Reorganizations, mergers, consolidations or affiliations;
- Sales, conveyances, assignments, transfers, alienations, pledges, or other encumbrances of any assets of the subsidiary;
- Annual operating and capital budgets and any capital expenditures of the subsidiary in excess of the amount designated from time to time by MidMichigan Health;
- Guarantees by the subsidiary of the debt of others; and
- Incurrence by the subsidiary of any debt or lease obligation in excess of an amount designated from time to time by MidMichigan Health.
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Subject to the powers and authorities reserved for MidMichigan Health, each subsidiary maintains its separate existence with its own Board of Directors. The members of each subsidiary board are elected by MidMichigan Health. Subsidiary boards utilize the mission, vision, values and strategic plan of MidMichigan Health. MidMichigan Health is the sole member of each subsidiary.

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BUSINESS OVERVIEW: SERVICE AREA

Market Environment (including Alpena)

MidMichigan Health's service area consists of the following five primary service areas and cities:

- Alpena: Alpena, Hillman, Lincoln, Hubbard Lake, Lachine, Herron, and Ossineke
- Northwest Area: Clare, Harrison, Farwell, and Lake
- Northeast Area: Beaverton and Gladwin
- Southeast Area: Sanford, Coleman, Midland, Freeland, Hope, and Auburn
- Southwest Area: St. Louis, Alma, Elwell, Breckenridge, Riverdale, Shepherd, Wheeler, Vestaburg, Ithaca, Sumner, Edmore, Rosebush, Blanchard, Mt. Pleasant, and Weidman

MidMichigan Health serves the majority of the population in these cities, with only one other competing hospital in Mt. Pleasant. Since the 2010 census, the MidMichigan Health service area is estimated to have declined slightly (0.9%) with the declines in the adult (18-20) and adult (45-54) age category partly offset by an increase in the senior age category. The 65+ age category has increased from 15.3% of the population in 2010 to 18.0% in 2017. It is estimated that this age category will increase to 20.2% of the population by 2022. (See the following table.)

Map of MidMichigan Health's Service Area (including Alpena)



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The following table shows the current and projected population count, composition, and five-year growth rate for the service area by age group.

	<u>Population</u>		<u>% of Total</u>		<u>Growth Rate</u>	
	2017	Projected 2022	2017	Projected 2022	Projected 2017-2022	Average
Population Breakdown						
Total Population	304,905	304,056	100.0%	100.0%	0.0%	-0.1%
Population by Age						
Children 0-20	77,474	74,016	25.4%	24.3%	-4.5%	-0.9%
Young Adults 21-34	58,924	60,090	19.3%	19.8%	2.0%	0.4%
Adults 35-54	70,957	66,147	23.3%	21.8%	-6.8%	-1.4%
Older Adults 55-64	42,559	42,243	14.0%	13.9%	-0.7%	-0.2%
Seniors 65-plus	54,991	61,560	18.0%	20.2%	11.9%	2.4%
Source: Michigan Health and Hospital Association, MHASC Data Services as of June 2017 (annualized)						

The 2016 median household income of the service area was \$38,829 compared to \$49,576 for the state of Michigan. The 2016 median household income for Midland County was \$54,059.

Source: US Census Bureau, 2016 data (most current data available as of October 2017)

Market Share by Service (including Alpena)

MidMichigan Health's market share by service line as of June 2017 follows:

Service Line	Market Share
General Medicine/Surgery	64.2%
Cardiovascular	63.3%
Women's Health	62.7%
Orthopedics	57.7%
Neurosciences	58.4%
Behavioral Health/Other	79.9%
Cancer	38.5%
Spine	35.8%
Neonatology/Normal Newborn	46.8%
Source: Michigan Health and Hospital Association, MHASC Data Services as of June 2017 (annualized)	

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Competition (including Alpena)

The table below discloses information relating to the discharges of patients residing in the MidMichigan Health service area for MidMichigan Health and its major competitors during fiscal 2015-2017, the most recent data available. MidMichigan Health is the market leader, with a service area market share of 61.5% in fiscal 2017.

	Miles from Nearest MidMichigan Health Location	Market Share (% of Inpatient Discharges)			Change
		FY2015	FY2016*	FY2017*	FY2015- FY2017
MidMichigan Health	--	58.6%	60.0%	61.5%	2.9%
Covenant Medical Center – Saginaw	32	6.3%	6.6%	6.6%	0.3%
University of Michigan Health System	118	4.2%	3.6%	4.3%	0.1%
St. Mary's of Michigan – Saginaw	33	2.0%	2.0%	1.8%	-0.2%
McLaren – Bay Region	25	3.7%	3.5%	3.4%	-0.3%
McLaren – Central Michigan – Mt. Pleasant	18	11.6%	9.3%	9.2%	-2.4%
All Other		<u>17.8%</u>	<u>15.0%</u>	<u>13.2%</u>	-4.6%
Total		<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	

*data includes Alpena
Source: *Michigan Health and Hospital Association, MHASC Data Services as of June 2017(annualized)*

In fiscal 2017, MidMichigan Health saw a 1.5 percentage point increase in inpatient market share primarily in Midland, and partially offset by small declines in the other hospitals. Both the cancer and orthopedics service lines have shown a decline, but all other service lines have increased since fiscal 2016.

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UNIVERSITY OF MICHIGAN HEALTH SYSTEM AFFILIATION

On June 21, 2013, the University of Michigan Regents through its operating division, the University of Michigan Health System (UMHS), and Michigan Health Corporation, together with MidMichigan Health, executed an affiliation agreement (the “Agreement”). The Agreement objectives include improvement of the health of our residents; increased access to high-quality service; achievement of significant efficiencies; enhancement of clinical integration; and the furtherance of both MidMichigan Health’s and UMHS’s missions.

Membership Interests

As a result of this transaction, MidMichigan Health established two member classes:

- The Michigan Health Corporation Member Class consisting of a one-tenth of one percent (0.1%) membership interest in MidMichigan Health during the initial term of the Agreement; and
- The MidMichigan Health Member Class consisting of a 99.9% membership interest in MidMichigan Health during the initial term of the Agreement.

In order to preserve the benefits of the affiliation, the Agreement was amended on June 30, 2016. The Amendment resulted in the following changes to the Agreement, after the initial term expired June 30, 2017:

- The membership change in ownership from 0.1% to 12.0% effective July 1, 2017;
- The automatic renewal for successive 20 year terms;
- The right to purchase up to an additional 8% interest expiring on June 30, 2019;
- The continuation of the reserve powers (such as termination, dissolution, and approval of certain capital expenditures in excess of various thresholds); and
- With respect to the financials provisions:
 - The elimination of all value sharing payments; and
 - The indexing for inflation of the annual distribution amount.

The Agreement includes certain restrictive covenants, including the rights of first refusal related to the provision of clinical care, exclusivity, and noncompetes upon the termination of the Agreement and allows for MidMichigan Health’s use of the MidMichigan/UMHS Brand.

The Agreement may be terminated under certain conditions. The termination payments range from MidMichigan Health making an exit payment to UMHS, from \$20 million to \$75 million.

The Agreement includes provisions relating to reserved powers, financial and termination provisions, related party transactions, and conditions of use criteria related to MidMichigan Health’s use of the MidMichigan/UMHS brand. These provisions are discussed in more detail in footnote 16 of MidMichigan Health’s audited consolidated financial statements as of and for the year ended June 30, 2017.

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REVIEW OF CONSOLIDATED RESULTS

The following table presents selected inpatient, outpatient, and ancillary service utilization and other data for MidMichigan Health for the Fiscal Years 2015-2017.

Summary Consolidated Historical Utilization of Services Statistics			
	Fiscal Year Ended June 30,		
	2015	2016	2017
Licensed Beds			
Acute (including rehabilitation and mental health) ⁽¹⁾	481	620	630
Extended Care ⁽²⁾	210	0	0
Operated Beds			
Acute ⁽¹⁾	400	500	540
Extended Care ⁽²⁾	198	0	0
Acute Admissions ⁽¹⁾	18,418	19,696	23,837
Acute Length of Stay (in days)	3.9	3.8	3.9
Medicare Case Mix Index: (all acute)	1.70	1.61	1.73
Medicare Case Mix Index: Midland	1.87	1.84	1.91
Patient Days			
Acute ⁽¹⁾	72,099	75,812	92,052
Extended Care	57,505	42,387	0
% Occupancy (based on operated beds)			
Acute ⁽¹⁾	49.4%	41.5%	46.8%
Extended Care	79.6%	70.4%	0%
Outpatient Visits ⁽¹⁾	446,288	494,601	575,410
Physician Visits ^{(1) (5)}	515,959	545,838	623,544
Emergency Room Visits ⁽¹⁾	69,874	77,609	100,013
Urgent Care Visits ⁽³⁾	95,232	100,583	101,285
Ambulatory Surgery Visits ⁽¹⁾	40,499	45,257	48,481
Home Health Visits ^{(4) (5)}	82,623	82,228	94,889
<i>Source: MidMichigan Health records</i>			
(1) 2016 includes one quarter (April – June) of Alpena; 2017 includes 12 months of Alpena			
(2) The sale of long term care facilities was complete as of May 1, 2016, bringing the extended care beds to 0 at 6/30/16. Extended care patient days include July 2015 – April 2016 for 2016.			
(3) Includes urgent care visits for Clare, Gladwin, Gratiot, Midland, Freeland and West Branch.			
(4) Includes home health, palliative care, and hospice visits.			
(5) 2017 includes Alpena's satellite office statistics			

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Management's Discussion of Recent Utilization Trends

The utilization trend highlights for **2017** include the following:

- Acute care admissions for the system increased from fiscal 2016 to fiscal 2017 approximately 21.0%. The increase results primarily from Alpena being part of the system for 12 months in 2017 compared to 3 months in 2016. Excluding Alpena, acute care admissions for the system increased 5.5%.
- Observation visits increased 30.0% from fiscal 2016 to fiscal 2017. The increase is partially related to Alpena being part of the system for 12 months in 2017 compared to 3 months in 2016. Excluding Alpena, observations increased 8.4%.
- MidMichigan Health's outpatient visits increased 16.3% from fiscal 2016 to fiscal 2017 driven by an increase in all outpatient areas. Excluding Alpena, outpatient visits decreased by (4.0)%.
- Physician visits increased 14.2% from fiscal 2016 to fiscal 2017 driven by an increase in all physician visits (primary care, specialty care, and family practice center visits), partially offset by a decrease in rural health clinics.
- Urgent Care visits increased 0.7% from fiscal 2016 as compared to fiscal 2017 as access increased slightly.

The utilization trend highlights for **2016** include the following:

- Acute care admissions for the system increased from fiscal 2015 to fiscal 2016 approximately 6.9%. The increase results primarily from the acquisition of Alpena on April 1, 2016. Excluding Alpena, acute care admissions for the system decreased 0.7%.
- Observation visits increased 12.8% from fiscal 2015 to fiscal 2016. The increase is partially related to the acquisition of Alpena. Excluding Alpena, observations increased 6.3%.
- MidMichigan Health's outpatient visits increased 10.8% from fiscal 2015 to fiscal 2016 driven primarily by one quarter of Alpena's activity. Excluding Alpena, observations and other outpatient visits increased 1.4%.
- Physician visits increased 5.8% from fiscal 2015 to fiscal 2016 driven by an increase in all physician visits (primary care, specialty care, rural health clinics, and family practice center visits).
- Urgent Care visits increased 5.6% from fiscal 2015 as compared to fiscal 2016. The largest increases were seen in Midland, Freeland and West Branch, and were partially offset by decreases at Gratiot and Clare locations.

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FINANCIAL SUMMARY

The summary of consolidated financial information presented below for MidMichigan Health for each of the three Fiscal Years ended June 30, 2015, 2016 and 2017 has been derived by MidMichigan Health's management from MidMichigan Health's audited consolidated financial statements for the periods presented. The following summary of consolidated financial information should be read in conjunction with the audited consolidated financial statements and related notes to the consolidated financial statements of MidMichigan Health.

SUMMARY CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS (In millions)			
	Fiscal Year Ended June 30,		
	2015	2016*	2017**
REVENUE:			
Patient service revenue (net of contractual allowances and discounts)	\$611.4	\$676.1	\$801.5
Provision for uncollectible accounts	<u>(26.5)</u>	<u>(26.4)</u>	<u>(39.2)</u>
Net patient service revenue less provision for uncollectible accounts	584.9	649.7	762.3
Other revenue	<u>26.4</u>	<u>28.3</u>	<u>34.5</u>
Total revenue	<u>611.3</u>	<u>678.0</u>	<u>796.8</u>
EXPENSES:			
Salaries and wages	264.1	288.9	339.7
Employee benefits	70.1	76.5	88.2
Supplies	100.6	115.8	140.9
Purchased services and other	55.8	68.5	80.8
Fees	45.1	52.3	63.0
Depreciation and amortization	38.0	41.6	45.7
Utilities	10.2	9.9	10.2
Interest	8.9	8.2	7.5
Insurance	<u>5.4</u>	<u>3.4</u>	<u>5.2</u>
Total expenses	<u>598.2</u>	<u>665.1</u>	<u>781.2</u>
OPERATING INCOME BEFORE OTHER ITEMS	13.1	12.9	15.6
OTHER ITEMS			
Impairment of goodwill	-	-	(56.2)
Asset charges for electronic health record legacy cost	-	-	(14.0)
Gain on sale of long-term care	-	3.5	-
Pension settlement loss	<u>-</u>	<u>(6.6)</u>	<u>-</u>
Total other items	<u>-</u>	<u>(3.1)</u>	<u>(70.2)</u>
OPERATING (LOSS) INCOME	<u>13.1</u>	<u>9.8</u>	<u>(54.6)</u>
NONOPERATING INCOME (EXPENSE):			
Investment income	12.3	15.8	15.7
Loss on extinguishment of debt	<u>(27.2)</u>	<u>-</u>	<u>-</u>
Total nonoperating income (expense)	<u>(14.9)</u>	<u>15.8</u>	<u>15.7</u>
(DEFICIENCY) EXCESS OF REVENUE OVER EXPENSES	\$ (1.8)	\$ 25.6	\$ (38.9)
*2016 Includes Alpena for one quarter (April - June)			
**2017 Includes Alpena for 12 months			

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SUMMARY CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS			
(In millions)			
	Fiscal Year Ended June 30,		
	2015	2016	2017
UNRESTRICTED NET ASSETS:			
(Deficiency) excess of revenue over expenses	(\$1.8)	\$25.6	(\$38.9)
Net assets released from restrictions used for purchase of property and equipment	0.3	5.7	2.9
Change in unrealized investment return	(2.8)	(15.0)	45.0
Distributions to noncontrolling interest	(0.1)	-	-
Postretirement-related changes other than net periodic postretirement cost	<u>(23.6)</u>	<u>(44.3)</u>	<u>73.7</u>
Increase (Decrease) in unrestricted net assets	<u>(28.0)</u>	<u>(28.0)</u>	<u>82.7</u>

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SUMMARY OF FINANCIAL RESULTS

The finance highlights for **2017** include the following:

- Total operating revenue for the year was \$796.8 million, an increase of \$118.8 million, or 17.5% over the prior year. The increase is driven primarily by Alpena being part of the system for 12 months of the fiscal year, compared to 3 months last year. Other operating revenue increased \$6.2 million due to the release of restricted funds.
- Reported operating loss for the year was \$54.6 million, a decrease of \$64.4 million from fiscal 2016. Goodwill impairment of \$(56.2) million and asset charges for electronic health record legacy costs of \$(14.0) million, were the primary drivers of the decline in operating income. Operating income before these other items was \$15.6 million in fiscal 2017 compared to \$12.9 million in fiscal 2016.
- Operating EBIDA (Earnings before Interest, Depreciation and Amortization) was \$63.6 million compared to \$59.6 million a year ago. Total EBIDA remains strong at 8.3%.
- MidMichigan Health experienced unrealized investment return of \$45.0 million compared to losses of approximately \$15.0 million a year ago driven by improvements in the equity markets.
- MidMichigan Health recorded a minimum pension and postretirement credit of approximately \$73.7 million. The favorable change primarily results from the increased discount rate from 3.55% to 3.80% in fiscal 2017, as well as favorable assumption changes for rate of return on assets and mortality. In addition MidMichigan Health made combined annual contributions totaling \$42.8 million in fiscal 2017 and \$12.0 million in fiscal 2016 to its two defined benefit pension plans consistent with its funding policy.

The finance highlights for **2016** include the following:

- Total operating revenue for the year was \$678.0 million, an increase of \$66.7 million, or 10.8% over the prior year. The acquisition of Alpena increased net patient revenue by \$33.4 million. Higher outpatient volumes and physician visits in fiscal 2016 also had a favorable impact on total operating revenue.
- Reported operating income for the year was \$9.8 million, a decrease of \$3.3 million from fiscal 2015. A pension settlement loss of \$6.6 million, resulting from total lump sum settlements exceeding the sum of service and interest costs, was the primary driver of the decline in operating income. This was partially offset by the gain on sale of long-term care facilities of \$3.5 million. Operating income before these other items was \$12.9 million in fiscal 2016 compared to \$13.1 million in fiscal 2015.
- Operating EBIDA (Earnings before Interest, Depreciation and Amortization) remained strong at \$59.6 million compared to \$60.0 million in fiscal 2015. Total EBIDA also continued to remain strong at 10.6%.
- Excess of revenue over expense as of June 30, 2016 included \$15.8 million of investment income, an increase of \$3.6 million over the prior year.
- MidMichigan Health experienced unrealized investment losses of approximately \$15.0 million compared to losses of \$2.8 million a year ago primarily due to the decline in equity markets. Both equity and fixed income investment classes showed decreases from fiscal 2015 levels.
- MidMichigan Health recorded a minimum pension and postretirement charge of approximately \$44.3 million. Approximately \$13.1 million results from the Alpena pension plan and the remainder of the increase is driven by a decrease in the discount rate and long-term rate of return on assets, in accordance

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with generally accepted accounting principles compared to a \$23.6 million charge in fiscal 2015. In addition MidMichigan Health made annual contributions totaling \$12.0 million in both fiscal 2016 and 2015 to its defined benefit pension plan (a cash balance plan) consistent with its funding policy.

- The financial impact of acquiring Alpena was \$220.6 million of assets acquired, including \$56.9 million of goodwill, and \$214.4 million of liabilities assumed.

Third-Party Reimbursement and Sources of Payment

Payments on behalf of a majority of the patients are made to MidMichigan Health by the federal government under the Medicare and Medicaid programs, by Blue Cross Blue Shield of Michigan (BCBSM), and other commercial insurance carriers. The communities which MidMichigan Health serves have experienced varying degrees of managed care penetration. Currently, managed care levels primarily represent direct contracts with commercial payors in the markets served by MidMichigan Health. Health Maintenance Organization ("HMO") penetration remains very small and currently no contracts have capitated payment arrangements.

The sources of payment for services provided by MidMichigan Health for fiscal 2015-2017 were as follows:

Sources of Payment	Percent of Net Revenue		
	FY2015	FY2016	FY2017
Medicare	39.0%	40.5%	43.1%
Medicaid	12.7%	13.1%	11.9%
Blue Cross	21.2%	19.7%	19.8%
Commercial, self-pay, and other	<u>27.1%</u>	<u>26.7%</u>	<u>25.2%</u>
Total	100.0%	100.0%	100.0%

Medicare is a major insurer of health care services and is administered by the federal government. The federal government contracts with regional organizations to operate as intermediaries and carriers to enforce Medicare policies and make payments to organizations that contract and bill for services provided to Medicare beneficiaries. Payment for hospitalization is made on the basis of diagnosis related groups (DRG) covering both the operating and capital costs of care. Medicare payments for Mental Health hospitalization are made through a prospective per diem methodology and rehabilitation hospitalization is paid prospectively and set per discharge with the amount based on case mix groups (CMG). MidMichigan Medical Center – Gladwin is designated as a critical access hospital and is paid 101% of reimbursable costs. Medicare payments are subject to a 2% reduction under the sequestration law. Medicare Advantage Plans constitute 21% of all Medicare payments.

Ambulatory services are paid on a fee schedule based on individual services provided to each patient, either from the physician fee schedule, laboratory fee schedule, or ambulatory payment classification (APC) schedule. Services to homebound patients are made based on prospectively set rates using home health resource groups (HHRG) that cover a 60-day episode of care.

Blue Cross Blue Shield of Michigan (BCBSM) has been changed to a non-profit mutual insurance company as of 2014. The name, "Blue Cross" is licensed for use from the Blue Cross Blue Shield Association, a national not-for-profit association. The basis of payment to hospitals from BCBSM is covered under the Participating Hospital Agreement (PHA) signed in 1989. This standard agreement has been amended by subsequent Letters of Understanding, the most recently signed in 2013. The PHA makes payment for

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hospitalization to large hospitals on the basis of DRGs and to small rural hospitals generally on a percentage of charges. Payment for mental health and rehabilitation hospitalization is made based on per diem rates. A new PHA contract revises payment rate setting methods for DRG, incentives, and outpatient. BCBSM will continue to recognize other agreements with Providers until they expire or the Provider signs onto the new PHA. MidMichigan Health entered into a Value Based Contract (VBK) with BCBSM. This was effective July 1, 2013 and continues for three years. This arrangement is part of an effort by BCBSM to move away from traditional fee-for-service reimbursement and toward rewarding for population health management and collaboration among providers. BCBSM has agreed to provide infrastructure funding for population management which includes an all-payor patient registry, health information exchange, and implementation of coordinated processes of care at the population level. The funding will be provided on a quarterly basis over the course of the next three years. In addition to the infrastructure funding, the agreement allows for potential shared savings for both hospital cost efficiency and for total cost of care (population based) efficiencies. There is no downside risk to this shared savings component. The VBK agreement expired as of June 30, 2016, however, BCBSM is currently considering an amendment to extend the agreement for one of the three components previously offered. There will not be any additional infrastructure payments or shared savings opportunity for hospital cost efficiencies. The amendment will essentially add the opportunity to share in population-based efficiencies for one more year. The amendment was executed to extend the agreement until June 30, 2017. The extension only allowed for one of the three components, population-based performance opportunities.

Medicaid is a jointly funded program of the state and federal governments, administered by the state government. Federal law establishes minimum eligibility requirements and the state may exceed the federal minimums. The funding split is set by federal law and is made on the basis of matching amounts spent by the state government for covered services. Payment for hospitalization is made under a DRG system tailored to Medicaid recipients by the state. Rehabilitation hospitalization services are paid on the basis of per diem rates. Payment for mental health services are made through county administered boards. The state contracts with the county board, and the county board is then authorized to contract for needed services with area providers. Ambulatory services are paid on a fee-for-service rate system. Other payments received include allocations of state-wide pools for Small Rural and Sole Community Provider, State Plan enrollees, Managed Care Organization Plan enrollees, County Mental Health Care Plan enrollees, Disproportionate Share Hospitals and Graduate Medical Education. The state has contracted with managed care organizations ("MCOs") for providing the majority of acute care services for Medicaid enrollees. These MCOs may then contract with providers to obtain services for covered enrollees or pay providers based on rates set by the State. MidMichigan Health has operated under this program since fiscal 2000. To maximize federal matching funds, the State has instituted assessments on hospitals and nursing homes. The assessment funds are then used to increase Medicaid payments matched with federal funds and a portion is retained for other uses.

MidMichigan Health through its Joint Venture, MidMichigan Health Network, has worked to contract directly with local businesses for health care services through its ConnectCare product or by joining select commercial insurance networks covering regional or national businesses. The ConnectCare network is also leased to other commercial payors. These contracts generally pay based on discounts off of charges or on a set fee for a given service and do not have capitated or risk sharing arrangements. Individuals covered by these insurances are only responsible for any co-insurance amounts or non-covered services.

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Summary of Operations

The summary of consolidated financial information presented below for MidMichigan Health summarizes operating income from 2017 versus 2016 and 2016 versus 2015.

FY 2017 versus FY 2016

in millions	Comments	2016	2017	Change \$	Change %
Revenue					
Net patient service revenue		\$649.7	\$762.3	\$112.6	17.3%
Other revenue		28.3	34.5	6.2	21.9%
Total Operating Revenue	1	678.0	796.8	118.8	17.5%
Total Operating Expenses	2	665.1	781.2	116.1	17.5%
Operating Income Before Other Items		12.9	15.6	2.7	20.9%
Impairment of goodwill		-	(56.2)	(56.2)	0.0%
Asset charges for electronic health record legacy costs		-	(14.0)	(14.0)	0.0%
Gain on divestiture of long-term care		3.5	-	(3.5)	0.0%
Pension settlement loss		(6.6)	-	6.6	0.0%
Total Other Items		(3.1)	(70.2)	(67.1)	0.0%
Operating (Loss) Income		9.8	(54.6)	(64.4)	-657.1%
Nonoperating income (expenses)	3	15.8	15.7	(0.1)	-0.6%
(Deficiency) Excess of Revenue over Expenses		25.6	(38.9)	(64.5)	-252.0%
Change in unrealized investment return	4	(15.0)	45.0	60.0	-400.0%
Net change in pension and postretirement related items	5	(44.3)	73.7	118.0	-266.4%
Other		5.7	2.9	(2.8)	-49.1%
Increase (Decrease) in Unrestricted Net Assets		(\$28.0)	\$82.7	\$110.7	-395.4%

Comments

1. Total operating revenue in 2017 was \$796.8 million, an increase of \$118.8 million or 17.5% versus 2016. This includes patient service revenue less adjustments for amounts contractually agreed to primarily for Medicare, Medicaid, and Blue Cross Blue Shield of Michigan, adjustments for bad debt write offs and other operating revenue from non-patient activities. The increase is driven primarily by the addition

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Alpena to the health system for the entire fiscal year, compared to only one quarter in fiscal 2016. Other operating revenue increased \$6.2 million due to the release of restricted funds for their donor-intended purposes.

2. The operating expenses in 2017 increased \$116.1 million, or 17.5% compared to fiscal 2016. The addition of Alpena to the health system for a full year versus one quarter (April – June) increased all expense categories and impacted total operating expenses by \$103.9 million in fiscal 2017. Details related to total operating expenses follow.

Expenses	Comments	2016	2017	Change \$	Change without Alpena
Salaries & Benefits	a	\$ 365.3	\$ 428.0	\$ 62.7	\$ 7.1
Supplies	b	115.7	140.9	25.2	1.5
Purchased Services and other	c	68.6	80.8	12.2	2.4
Fees / Other	d	65.7	78.3	12.6	3.2
Depreciation, amortization and Interest		49.8	53.2	3.4	(2.0)
Total Operating Expenses		\$ 665.1	\$ 781.2	\$ 116.1	\$ 12.2

- a. Salaries and benefits increased approximately \$62.7 million driven primarily by Alpena being part of the system for an entire year compared to three months in fiscal 2016 (\$55.6 million). In addition, the implementation of EPIC resulted in increased productive wages.
 - b. Supplies increased \$25.6 million with increases seen in patient related supplies, specifically pharmaceuticals. A full year of Alpena supplies accounted for \$23.7 million of the increase.
 - c. Purchased services and other increased \$11.7 million of which \$9.8 million was the result of Alpena being part of the system for the entire year. There was also an increased usage of locums and contract labor.
 - d. Fees and other increased \$12.8 million driven by Alpena being part of the system for an entire year compared to three months in fiscal 2016 which accounted for \$9.6 million of the increase. The additional increase was primarily in physician fees.
3. Other items include \$14.0 million of asset charges for electronic health record legacy costs and \$56.2 million of impairment of goodwill.
4. Change in unrealized investment return consists of the unrealized gains on all other investments not accounted for using the fair value option and the equity method. Increases were seen in most investment types driven by improvement in the equity market.
5. During fiscal 2017 MidMichigan Health recorded a minimum pension and postretirement credit of approximately \$73.7 million driven by an increase in the discount rate from 3.55% to 3.80% at June 30, 2017. In addition MidMichigan Health made annual contributions totaling \$42.8 million in fiscal 2017 and \$12.0 million in fiscal 2016 to its two defined benefit pension plans consistent with its funding policy.

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FY 2016 versus FY 2015

in millions	Comments	2015	2016	Dollar Change \$	Percent Change %
Revenue					
Net patient service revenue		\$584.9	\$649.7	\$64.8	11.1%
Other revenue		26.4	28.3	1.9	7.2%
Total Operating Revenue	1	611.3	678.0	66.7	10.9%
Total Operating Expenses	2	598.2	665.1	66.9	11.2%
Operating Income Before Other Items		13.1	12.9	(0.2)	-1.5%
Gain on divestiture of long-term care		-	3.5	3.5	0.0%
Pension settlement loss		-	(6.6)	(6.6)	0.0%
Total Other Items		-	(3.1)	(3.1)	0.0%
Operating Income		13.1	9.8	(3.3)	-25.2%
Nonoperating income (expenses)	3	(14.9)	15.8	30.7	-206.0%
Excess (Deficiency) of Revenue over Expenses		(\$1.8)	\$25.6	\$27.4	-1522.2%
Change in unrealized investment return	4	(2.8)	(15.0)	(12.2)	435.7%
Net change in pension and postretirement related items	5	(23.6)	(44.3)	(20.7)	87.7%
Other		0.2	5.7	5.5	2750.0%
(Decrease) in Unrestricted Net Assets		\$ (28.0)	\$ (28.0)	\$ -	0.0%

Comments

1. Total operating revenue in 2016 was \$678.0 million, an increase of \$66.7 million or 10.9% versus 2015. This includes patient service revenue less adjustments for amounts contractually agreed to primarily for Medicare, Medicaid, and Blue Cross Blue Shield of Michigan, adjustments for bad debt write offs and other operating revenue from non-patient activities. The increase in total operating revenue resulted from the acquisition of Alpena \$33.6 million and the remainder from increased outpatient activity.
2. The operating expenses in 2016 increased \$66.9 million, or 11.2% compared to fiscal 2015. The addition of Alpena to the health system for one quarter (April – June) increased all expense categories and impacted total operating expenses by \$34.2 million in fiscal 2016. Details related to total operating expenses follow.

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Expenses	<u>Comments</u>	<u>2015</u>	<u>2016</u>	<u>Change \$</u>
Salaries & Benefits	a	\$ 334.2	\$ 365.3	\$ 31.1
Supplies	b	100.6	115.7	15.1
Purchased Services and other	c	55.8	68.6	12.8
Fees / Other	d	60.7	65.7	5.0
Depreciation, amortization and Interest		46.9	49.8	2.9
Total Operating Expenses		\$ 598.2	\$ 665.1	\$ 66.9

- e.** Salaries and benefits increased approximately \$31.1 million driven by increased volumes, One Person One Record (EPIC) training, and the addition of Alpena (\$16.8 million).
 - f.** Supplies increased \$15.1 million related to an increase in patient-related supplies, and minor equipment which was offset by an increase in other operating revenue. Supply expense of \$8.4 million relates to Alpena.
 - g.** Purchased services and other increased \$12.8 million driven by locum usage, unbudgeted contract labor, and \$3.0 million of Alpena expenses.
 - h.** Fees and other increased \$5.0 million due to higher Medicaid assessment fees and the addition of Alpena (\$4.3 million). Partially offsetting those increases is a decrease in insurance, due to lower claims activity in workers compensation and professional liability.
- 3.** Nonoperating income (expense) increased \$30.7 million. Investment income of \$15.9 million increased compared to \$12.3 million a year ago. Fiscal 2015 also includes \$27.2 million of loss on extinguishment of debt related to the advance refunding of outstanding Michigan State Hospital Finance Authority Revenue Bonds Series 2009 and 2006.
 - 4.** Change in unrealized investment return consists of the unrealized gains on all other investments not accounted for using the fair value option and the equity method. Decreases were seen in most investment types.
 - 5.** During fiscal 2016 MidMichigan Health recorded a minimum pension and postretirement charge of approximately \$44.3 million driven partially by Alpena (\$13.1 million) and a decrease in the discount rate from 4.40% to 3.55% at June 30, 2016, as well as a decrease in the long-term rate of return on assets. In addition MidMichigan Health made annual contributions totaling \$12.0 million in both fiscal 2016 and 2015 to its defined benefit pension plan (a cash balance plan) consistent with its funding policy.

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HISTORICAL CAPITALIZATION

The following table sets forth the capitalization of MidMichigan Health for the fiscal years ended June 30, 2015, 2016, and 2017.

Debt to Total Capitalization (Dollars in Thousands)			
	As of June 30,		
	2015	2016	2017
Revenue Bonds, Series 2014	\$170,595	\$168,950	\$167,235
Revenue Bonds, Series 2016 ⁽¹⁾	0	0	24,466
Other Debt ⁽²⁾	9,824	7,588	5,413
Unamortized Premium and Debt Issue Costs	<u>18,605</u>	<u>16,161</u>	<u>15,291</u>
Long-term Obligations (A)	199,024	192,699	212,405
Unrestricted Net Assets ⁽³⁾	<u>628,924</u>	<u>600,891</u>	<u>683,568</u>
Total Capitalization (B)	<u>\$827,948</u>	<u>\$793,590</u>	<u>\$895,973</u>
Debt to Total Capitalization (A/B)	<u>24.0%</u>	<u>24.3%</u>	<u>23.7%</u>
(1) Issuance of Series 2016 bonds. (2) Includes Hospital Equipment Loan Program ("HELP") bonds and capital lease obligations. (3) Does not include Temporarily or Permanently Restricted Net Assets.			

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HISTORICAL DEBT SERVICE COVERAGE

The following table presents MidMichigan Health's historical coverage of estimated maximum annual debt service on the indebtedness of MidMichigan Health for the previous three years shown.

Debt Service Coverage (Dollars in Thousands)			
	Fiscal Year Ended June 30,		
	2015	2016	2017
(Deficiency) Excess of revenue over expenses	\$(1,830)	\$25,633	\$(38,963)
Increases			
Depreciation and amortization	38,032	41,624	45,677
Interest	8,932	8,220	7,499
Impairment of goodwill	0	0	56,215
Asset charges for electronic health record legacy cost	0	0	8,896
Pension settlement loss	0	6,646	0
Loss on retirement of assets and extinguishment of debt	27,188	0	0
Decreases			
Change in unrealized values for investments accounted for using the fair value option and the equity method, including impairment losses	(341)	(2,346)	(2,920)
Gain on divestiture of long-term care	<u>0</u>	<u>(3,498)</u>	<u>0</u>
Income available for debt service (A) ⁽¹⁾	<u>\$71,981</u>	<u>\$76,279</u>	<u>\$76,404</u>
Maximum annual debt service (B) ⁽²⁾	\$15,535	\$15,535	\$16,333
Debt service coverage ratio (A/B)	<u>4.6 times</u>	<u>4.9 times</u>	<u>4.7 times</u>
⁽¹⁾ The above schedule has been prepared in compliance with Section 508 of the Master Indenture dated December 1, 2014 ("Master Indenture") between MidMichigan Health and The Bank of New York Mellon Trust Company, N.A.. Income available for debt service was calculated as described in Section 101 of the Master Indenture. Income available for debt services does not include the unrealized gain or loss on investments. This treatment is consistent with prior years' calculation of the historical debt service coverage. The Hospital Equipment Loan Program bonds are variable rate debt and debt service for such bonds is calculated based upon the most current rates provided by the State of Michigan.			
⁽²⁾ Maximum annual debt service has been defined as the greatest amount of annual debt service and includes the aggregate principal and interest due on all Long-Term Indebtedness of the Credit Group, becoming due and payable in any Fiscal Year including the Fiscal Year in which the calculation is made or any subsequent Fiscal Year.			

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MidMichigan Health Disclosure Statement
June 30, 2017

LIQUIDITY

The following table sets forth the consolidated cash position and liquidity of MidMichigan Health as of June 30, 2015, 2016 and 2017. Liquidity includes operating cash, investments, and assets limited as to use by Board for capital acquisitions (funded depreciation). Excluded are temporarily and permanently restricted assets, trustee-held bond funds, and self-insurance assets.

Liquidity (Dollars in Thousands)			
	As of June 30,		
	2015	2016	2017
Cash and cash equivalents ⁽¹⁾	\$ 11,331	\$ 23,747	\$ 20,488
Limited as to use by Board for capital	377,439	410,362	455,033
Investments ⁽²⁾	163,613	183,195	150,989
Current portion of long-term obligation	<u>(3,362)</u>	<u>(3,890)</u>	<u>(5,663)</u>
Total Liquid Assets	<u>\$549,021</u>	<u>\$613,414</u>	<u>\$620,847</u>
Days Cash on Hand Ratio ⁽³⁾	<u>357.7</u>	<u>360.1</u>	<u>308.1</u>
⁽¹⁾ Includes all highly liquid deposits and debt securities with maturities of three-months or less at the date of purchase.			
⁽²⁾ Includes debt securities, fixed income funds, equity securities, and real estate funds.			
⁽³⁾ Total cash and investments, divided by total operating expenses minus depreciation and amortization, divided by 365 in fiscal 2015 and 2017, and 366 in 2016.			

Investment Policy

The Investment Committee meets (at a minimum) quarterly and has responsibility for the development, review, and monitoring of the investment policy. This responsibility includes: (1) determining acceptable levels of market risk; (2) determining the allocation of assets among common stock, fixed-income instruments, and such other types of investments as the Committee determines are appropriate; and (3) selection and review of external investment managers. MidMichigan Health has engaged Aon Hewitt Inc. ("Aon") as its investment advisor. Aon measures and reports on investment performance; performs asset/liability modeling studies; recommends changes to objectives, guidelines, manager, or asset class structure; and keeps MidMichigan Health informed of current investment trends and issues.

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MidMichigan Health Disclosure Statement
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The following table summarizes the financial statement presentation of cash and investments as of June 30, 2017:

Cash and Investments As of June 30, 2017 (Dollars in Thousands)	
Cash and cash equivalents (see 1 above: Liquidity table)	\$ 20,488
Pooled income investments:	
Board designated for capital acquisition	\$ 455,033
Investments (see 2 above: Liquidity table)	150,989
Other assets limited or restricted as to use	<u>66,173</u>
	672,195
Pledges receivable, DOW stock, deferred compensation and educational loans	<u>40,541</u>
Total investments	<u>712,736</u>
Total cash and investments	<u>\$733,224</u>

Investments are maintained in pooled investment funds. The following table shows the allocation of cash and investments as of June 30, 2017:

Pooled Investment Funds As of June 30, 2017	
Mutual funds, equity securities	48%
Mutual funds, fixed income	33%
Real estate funds	10%
Hedge funds	4%
Cash and cash equivalents	4%
Equity securities	1%

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Investment management is delegated to professional investment management firms that must adhere to policy guidelines and objectives established by MidMichigan Health. Generally, redemptions must be made within a one month written notice. The following table shows the assets under management in the pooled income funds as of June 30, 2017.

MidMichigan Health Pooled Income Investments As of June 30, 2017 (Dollars in millions)				
Investment Manager	Market Index	Total Assets	Percent of Total	
			Assets	Target Policy
BlackRock	Russell 1000	\$ 132.3	19.7%	18.0%
T. Rowe Price	Russell 2000	<u>13.7</u>	<u>2.0%</u>	<u>2.0%</u>
Domestic Equity		146.0	21.7%	20.0%
BlackRock	MSCI All-Country World ex U.S.	<u>144.4</u>	<u>21.5%</u>	<u>20.0%</u>
International Equity		144.4	21.5%	20.0%
GMO	Global Balanced	<u>67.0</u>	<u>10.0%</u>	<u>10.0%</u>
Balance Fund		67.0	10.0%	10.0%
BlackRock	Intermediate Aggregate	108.7	16.2%	20.0%
PIMCO	Intermediate Aggregate	<u>104.6</u>	<u>15.5%</u>	<u>20.0%</u>
Fixed Income⁽¹⁾		213.3	31.7%	40.0%
ING Clarion	NCREIF ODCE	32.9	4.9%	2.5%
Cornerstone	NCREIF ODCE	<u>37.5</u>	<u>5.6%</u>	<u>2.5%</u>
Real Estate⁽¹⁾		70.4	10.5%	5.0%
Blackstone	HFR Fund of Funds	<u>31.1</u>	<u>4.6%</u>	<u>5.0%</u>
Real Estate		31.1	4.6%	5.0%
Total		<u>\$672.2</u>	<u>100.0%</u>	<u>100.0%</u>
(1) The investment committee made the decision to increase the real estate allocation and reduce the portfolio's exposure to fixed income due to the current market conditions. The committee kept the targets the same during fiscal 2017.				

Debt Management and Derivatives Policy

MidMichigan Health is not currently a party to any derivative transactions. However, as part of the overall debt management policy, MidMichigan Health has established a formal policy with regard to the appropriate use of debt and derivative products. Such derivatives policy is reviewed periodically and is changed or modified as appropriate. Derivative products can be used, within the established parameters, as a debt management tool to manage interest rate risk and increase financial flexibility. MidMichigan Health evaluates the benefits and risks related to each derivative transaction on an independent basis and in light of the overall derivative structure.

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MidMichigan Health may use derivative products in furtherance of the debt management policy to manage targeted fixed/variable rate debt mix (e.g., through the use of interest rate swaps), hedge the prospective issuance of incremental debt (e.g., through the use of a forward-starting contract), and/or hedge and actively manage general interest rate risk (e.g., through the use of a cap or collar). MidMichigan Health also may use derivative products to manage the overall asset/liability structure, to manage the impact of investment returns, and/or to manage tax and basis risks separately from interest rate risk.

MidMichigan Health's debt management and derivatives policy requires that MidMichigan Health enter into derivative transactions with counterparties maintaining at least "A" category credit ratings and uses standard swap documentation on all points between and among existing and potential counterparties (International Swap and Derivatives Association standard master agreement; uniform collateralization requirements, if any; uniform covenants, if any; uniform security, if any). In addition, MidMichigan Health will (if applicable):

- Provide annual reports to the Finance Committee of the MidMichigan Health Board, including: a counterparty status update regarding current credit ratings and recent rating reports; counterparty announcements regarding credit events, rating changes or other announcements during the relevant period; any press releases of counterparty related to credit quality, significant divestitures or acquisitions, collateral posting, if any; and other relevant disclosures.
- Monitor its swap position on a regular basis, if applicable, and report annually to the Finance Committee regarding the mark-to-market valuation and any receipts/payments related to existing derivative products and monitor on a regular basis the termination and rollover risk related to existing derivative products.

As part of MidMichigan Health's governance, management conducts an annual review of the existing debt and derivatives policy to determine any necessary changes in light of MidMichigan Health's debt, the targeted fixed/variable rate debt mix, asset/liability management considerations, or credit changes.

Pension Plans and Other Employee Benefit Plans

Defined Contribution Pension Plans

Effective January 1, 2008, all of the defined contribution plans from the various subsidiaries, excluding Alpena, were merged into one plan. Benefits are based on matching 50% of an employee's contribution up to 4% of eligible pay. Contribution expense for the plan totaled approximately \$4.3 million in fiscal 2017, \$3.8 million in fiscal 2016, and \$3.4 million for the year ended June 30, 2015. Employee elective deferrals are 100% vested from the date of contribution.

Noncontributory Defined Benefit Pension Plan (Pension Plan)

Effective January 1, 2008, MidMichigan Health amended the defined benefit plan to a cash balance plan. Benefits are based on pay credits and interest credits; at the end of each calendar year, participant accounts are credited with a percentage of the participants' annual salary. With the exception of Alpena, all MidMichigan Health subsidiary organizations are included in the amended Pension Plan.

The Pension Plans can be terminated by MidMichigan Health's Board of Directors subject to certain notification requirements. MidMichigan Health, at this time, does not intend to terminate the Pension Plans. The Pension Plans assets are invested primarily in a fixed income fund, government securities, equity securities, and limited liability corporations. The asset allocation for MidMichigan Health's pension plans as of June 30, 2017 is: U.S. equity (25%); non-U.S. equity (21%); global equity (15%); emerging markets equity (2%); and fixed income (37%).

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Alpena Retirement Benefits

Effective April 1, 2016, MidMichigan Health established a new defined benefit pension plan for Alpena employees. This plan is a spinoff of the Municipal Employees Retirement System (MERS) plan that was in place for Alpena employees prior to the acquisition. On the effective date, \$260.7 million of benefit obligations and \$108.7 million of assets were transferred from the MERS plan into the new Alpena Pension Plan.

A new Alpena defined contribution plan was created April 1, 2016 to replace Alpena's previous governmental defined contribution plan. Contribution expense for the plan totaled approximately \$2.1 million in fiscal 2017 and \$0.5 million from April – June in fiscal 2016.

Assumptions used to determine benefit obligations and net periodic benefit cost for fiscal 2015, 2016 and 2017 were as follows:

Pension Plan			
	Fiscal Year Ended June 30,		
	2015	2016	2017
Benefit obligations			
Discount rate	4.40%	3.55%	3.80%
Rate of compensation increase			
2015	3.50		
2016-2017	3.50	3.50-4.00	3.50-4.00
2018 and after	4.00	4.00	4.00
Net periodic benefit cost			
Discount rate	4.25%	3.90-4.40%	3.55%
Expected long-term return on plan assets	6.25	5.50-7.00	6.25
Rate of compensation increase			
2015	3.50		
2016-2017	3.50	3.50-4.00	3.50-4.00
2018 and after	4.00	4.00	4.00

Net periodic pension expense was \$9.5 million, \$20.1 million, and \$16.5 million for fiscal 2015, fiscal 2016, and fiscal 2017, respectively. The increase in net periodic pension expense in fiscal 2016 resulted primarily from settlement costs of \$6.6 million and \$1.6 million related to the acquisition of Alpena.

MidMichigan Health recorded an increase of \$73.7 million in June 2017, a decrease of \$44.3 million in June 2016 and a decrease of \$23.6 million in June 2015 in the unrestricted net assets to the consolidated statement of operations and changes in net assets related to the pension and postretirement funded status of its defined benefit pension and retiree health plans primarily as a result of changes in plan assumptions. In fiscal 2015, the discount rate increased from 4.25% to 4.40%. In fiscal 2016, the discount rate decreased from 4.40% to 3.55%. In fiscal 2017, the discount rate increased from 3.55% to 3.80%.

In fiscal 2013, MidMichigan Health adopted a de-risking plan for its pension. As the Plan's funded ratio improves, the allocation to equities will decline and the allocation to fixed income will increase. Additionally, as the funded ratio and interest rates increase, the target duration of the fixed income assets will be increased. The Pension Plan also allows for potential re-risking in the event that the funded ratio significantly deteriorates.

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As of June 30, 2017, the original amended Pension Plan was funded on a projected benefit obligation basis at 88.9%. The new Alpena plan was funded on a projected benefit obligation basis at 55.4%. MidMichigan Health plans to continue to make contributions to the Alpena plan in excess of the minimum required contribution in fiscal 2018 to continue to improve the funded status of that plan.

Postretirement Health Care Benefits

Postretirement health care benefits for MidMichigan Health were eliminated for most of the active employees on January 1, 2002. Retirees who have post-retirement health care benefits are required to make contributions toward the cost of their benefits based on their years of service at retirement. Effective April 1, 2016, MidMichigan Health assumed a \$1.5 million postretirement obligation for Alpena employees Medicare Part B Reimbursement Program. This plan is unfunded. The plan provides a closed group of retirees' quarterly Medicare Part B premium reimbursement. The reimbursement amounts are fixed at retirement and do not increase. MidMichigan Health reserves the right to amend, modify, or terminate these benefits at any time. Net periodic benefit income for these plans was \$0.7 million in both fiscals 2016 and 2015, and \$0.8 million for fiscal 2017.

Capital Expenditures

The following table sets forth MidMichigan Health's capital expenditures for fiscal 2015, 2016, and 2017.

Fiscal year ended June 30, Capital Expenditures (in millions)	
2015	\$32.4
2016	39.5
2017	96.2

Fiscal 2017 includes a new clinical electronic health record (One Person One Record) (\$40.5 million) and the Mt. Pleasant expansion (\$28.9 million). Projects in progress include a new Cardiovascular Regional Referral Center in Midland including related relocations and the implementation of a new clinical electronic health record (One Person One Record) in Alpena.

Capital Planning and Allocation

MidMichigan Health has a formal capital allocation process with regard to its capital budget for routine capital replacement and strategic growth initiatives. Each year the amount of capital available for allocation is established from the annual depreciation expense and the expected operating income (based on the latest three year forecast). In addition, MidMichigan Health conducts a review of the average age of plant to establish the facility routine replacement capital expenditure commitment. Once the amount of committed capital has been determined, MidMichigan Health conducts a review of both routine capital replacement and strategic growth initiatives to determine the allocation for each.

Routine Capital Replacement The leadership of each subsidiary of MidMichigan Health, in conjunction with their physician leaders, prioritizes routine replacement requests. These requests are evaluated based upon MidMichigan Health's four strategic initiatives (quality, growth, relationships and sustainability), regulatory and facility enhancement criteria.

Strategic Growth Initiatives MidMichigan Health's annual strategic capital expenditures are evaluated based upon earnings growth and operational effectiveness criteria. Investments are evaluated based upon a selective criteria related to positive projected net present value of cash flows related to a specific investment or projects as well as achievement of a minimum modified internal rate of return in excess of the

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organization's weighted average cost of capital (hurdle rate) of 5%. The evaluation team includes representatives from each subsidiary including medical staff representatives.

MidMichigan Health retains approximately 8% for planned annual capital expenditures budget in reserve for small capital (under \$50,000) and unanticipated needs or opportunities.

Management currently anticipates long-term capital budget expenditures to approximate \$94.0 million in fiscal 2018, \$60.0 million in fiscal 2019, and \$56.0 million in fiscal 2020. The fiscal 2018 capital plan includes the completion of the One Person One Record (EPIC) project which replaces the current electronic health record and revenue cycle systems for Alpena. Fiscal 2018 includes the continuation of the cardiovascular regional referral center which will house all Midland outpatient cardiovascular services in one location. Imaging and neurology services will be relocated to the new building as well. Also included in fiscal 2018 are new buildings for expansion into the Bay City market and a physician office building in Gladwin. Fiscal 2019 capital includes the continuation of the heart and vascular regional referral center and emergency department renovations at two of our medical centers. The future years reflect management's focus on maintaining capital levels at expected depreciation amounts and investing in on-going capital projects in preparation for our future within the constantly changing health care environment. While realizing the impact of these projects on its operational costs, MidMichigan Health will continue to focus on reducing overall operating costs. As always, if there are dramatic changes to its financial projections, MidMichigan Health's capital expenditure plans will be adjusted accordingly.

INSURANCE AND RISK MANAGEMENT

The following summarizes current insurance programs for MidMichigan Health. In the opinion of management, these arrangements with respect to coverage of professional and general liability and other insurances are consistent with market practice for such coverage.

Professional and General Liability

MidMichigan Health self-insures primary medical, professional, and general liability claims. Until March 31, 2017, MidMichigan Health operated a primary captive insurance company, MAG, domiciled offshore where it operated and provided professional and general liability insurance coverage to MidMichigan Health and its subsidiaries. MAG was dissolved effective April 1, 2017, and the remaining assets and liabilities were transferred back to MidMichigan Health. MidMichigan Health has limited its liability by membership in Caymich Insurance Company, Ltd. ("Caymich"), which provides excess insurance above the self-insurance and MAG limits.

Effective April 1, 2017, coverage limits per claim are \$3 million and \$8 million annual aggregate. Caymich self-insures the next layer, with shared risk among its seven members, and purchases reinsurance above that layer. The first \$20 million reinsured limit is also shared among its seven members, and the remaining \$30 million reinsured limit is MidMichigan Health's unshared limit. The total Caymich limit is \$59 million (\$9 million in the retained layer and \$50 million in the reinsured layers). As of June 30, 2016, the coverage limit per claim through MAG was \$3 million while the annual aggregate was \$8 million. The total amount available for the subsequent layer was \$65 million (shared with the Caymich members). The same structure and limits were in effect from April 1, 2016, through March 31, 2017, as described above. MidMichigan Health also self-insures \$100 per claim in property damage, with commercial insurance providing coverage up to \$650 million per occurrence. Segregated funds, included in assets limited as to use have been established to settle claims, subject to self-insurance.

MidMichigan Health has engaged an independent actuary to assist in its estimate of a range of loss for known claims and unreported incidents and has recorded a liability of \$16.7 million, \$16.9 million, and \$15.2 million as of June 30, 2017, 2016, and 2015 respectively. The discount rate used in calculating the present

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value of the liability was 3.5% for fiscal years ended June 30, 2017, 2016, and 2015. Loss reserves are determined based on assumptions that are reviewed and adjusted as necessary.

MidMichigan Health is subject to various other regulatory investigations, legal proceedings, and claims that are incidental to its normal business activities. Management believes the ultimate disposition of such litigation will not have a material effect on the consolidated financial position of MidMichigan Health. Management also believes that MidMichigan Health is in substantial compliance with current laws and regulations.

Workers' Compensation

MidMichigan Health is a qualified self-insurer within the State of Michigan. MidMichigan Health maintains a trust fund for the payment of claims, which includes provisions for known claims and unreported incidents discounted to their present value at 2.75% as of June 30, 2017, 2016, and 2015. Excess commercial insurance was purchased, on a statutory basis, from an unrelated commercial insurer. As of June 30, 2017, 2016, and 2015, the amount recorded for MidMichigan Health's self-insured workers' compensation liability was \$2.7 million, \$2.9 million, and \$2.8 million, respectively. Loss reserves are determined based on assumptions that are reviewed and adjusted as necessary.

Other Insurance

MidMichigan Health's subsidiaries, either individually or in combination, maintain insurance for property damage, directors' and officers' liability, fiduciary, crime, and other general business risks. The amounts of such policies, the deductibles, and the amounts of self-insurance for such risks are reviewed at least annually.

Pending Litigation

Several civil actions and claims are pending or threatened based on claims of alleged professional or general liability and MidMichigan Health's management is aware of additional potential claims. While it is impossible to accurately predict the outcome of such claims, the management of MidMichigan Health and its counsel believe the ultimate disposition of such litigation will not have a material adverse effect on the financial position of MidMichigan Health. Management is not aware of any material, threatened, or pending suits other than those involving claims based on alleged professional or general liability.

ISSUED BUT NOT YET ADOPTED ACCOUNTING STANDARDS

Following is a discussion of recently issued accounting standards that MidMichigan will be required to adopt in a future period.

In March 2017, the FASB issued ASU No. 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. This guidance requires the service cost component of net periodic benefit cost related to defined benefit pension and postretirement benefit plans to be reported in the same financial statement line as other compensation costs arising from services rendered during the period. The other components of net periodic benefit cost are required to be presented separately from service costs and outside of operating income in the statements of operations. Only the service cost component of net periodic benefit cost will be eligible for capitalization in assets. This guidance is effective for MidMichigan Health beginning July 1, 2019. MidMichigan Health is currently evaluating the impact on its consolidated financial statements.

In November 2016, the FASB issued ASU No. 2016-18, Statement of Cash Flows. This guidance requires the statement of cash flow to explain the change in total cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. This guidance is effective for MidMichigan

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Health beginning July 1, 2019. MidMichigan is currently evaluating the impact on its consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, Classification of Certain Cash Receipts and Cash Payments. This guidance adds or clarifies guidance on the classification of certain cash receipts and payments in the statement of cash flows. This guidance is effective for MidMichigan Health beginning July 1, 2019. MidMichigan Health is currently evaluating the impact on its consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-14, Presentation of Financial Statements of Not-For-Profit Entities. This guidance simplifies and improves how not-for-profit entities classify net assets, as well as the information presented in financial statements and notes about liquidity, financial performance, and cash flows. This guidance is effective for MidMichigan Health beginning July 1, 2018. MidMichigan Health is currently evaluating the impact on its consolidated financial statements.

In May 2016, the FASB issued ASU No. 2016-12, Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients. This guidance amends certain aspects of the FASB's revenue standard, ASU No. 2014-09, Revenue from Contracts with Customers. In March 2016, the FASB issued ASU No. 2016-08, Revenue from Contracts with Customers: Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net). This guidance amends the principal-versus-agent implementation guidance and illustrations in the FASB's revenue standard ASU No. 2014-09, Revenue from Contracts with Customers. In July 2015, the FASB issued ASU No. 2015-14, Revenue From Contracts With Customers (Topic 606): Deferral of the Effective Date, which defers the effective date of the FASB's revenue standard, ASU No. 2014-09, Revenue From Contracts With Customers, by one year for all entities and permits early adoption on a limited basis. In May 2014, the FASB issued ASU No. 2014-09. This guidance outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. After the deferral, this guidance is now effective for MidMichigan Health beginning July 1, 2018. MidMichigan Health is currently evaluating the impact on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases. This guidance increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. This guidance is effective for MidMichigan Health beginning July 1, 2019. MidMichigan Health is currently evaluating the impact on its consolidated financial statements.

In September 2015, the FASB issued ASU No. 2015-16, Simplifying the Accounting for Measurement-Period Adjustments. This guidance requires an acquirer in a business combination to recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The effect on earnings of changes in depreciation or amortization, or other income effects (if any) as a result of change to the provisional amounts, calculated as if the accounting had been completed as of the acquisition date, must be recorded in the reporting period in which the adjustment amounts are determined rather than retrospectively. Also, the acquirer must present separately on the face of the income statement, or disclose in the notes, the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. This guidance is effective for MidMichigan Health beginning July 1, 2017. MidMichigan Health does not expect this guidance to have a material impact on its consolidated financial statements.

In July 2015, the FASB issued ASU No. 2015-11, Simplifying the Measurement of Inventory. This guidance requires entities to measure most inventories at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. This guidance is effective for MidMichigan Health beginning July

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1, 2017. MidMichigan Health does not expect this guidance to have a material impact on its consolidated financial statements.

FORWARD LOOKING INFORMATION

Strategic Initiatives

MidMichigan Health went live with a single electronic medical record system in April 2017. Alpena implemented the system in October 2017. The “One Person, One Record” (EPIC) system will result in faster, more accurate communication, streamlined processes and cost-saving efficiencies. The University of Michigan Health System also uses Epic, and is a valuable resource for sharing best practices.

MidMichigan Health has entered into an affiliation process with West Branch Regional Medical Center (WBRMC). The WBRMC Board of Trustees voted on the selection of MidMichigan Health as the preferred health system to proceed with partnership negotiations and named MidMichigan Health as the exclusive health system with which WBRMC will work to finalize an affiliation agreement. West Branch Regional Medical Center is part of the John Tolfree Health System, which includes Hospice of Helping Hands, the Tolfree Foundation, and Medical Arts Centers in Prudenville and West Branch. The Medical Center is an 88-bed acute care facility with four operating suites, as well as a 24-hour emergency department with 11 patient treatment areas. Located in Ogemaw County, the Medical Center serves a broad region, with 30 zip codes in Ogemaw, Oscoda, Roscommon, Arenac, Iosco, and Gladwin Counties. West Branch Medical Center has approximately 350 employees, 58 volunteers, 25 active staff physicians, as well as 12 associate staff physicians, 53 consulting staff physicians, 23 allied health professionals and 17 telemedicine physicians. **No agreements have been signed but the transaction is expected to close by June 30, 2018.**

MidMichigan Health started building a heart and vascular regional referral center in the spring of 2017. The 160,000 square foot building will replace one of the oldest portions of the medical center in Midland. It will be a three-story building that will occupy cardiovascular services, imaging services, neurology services and potentially UMHS clinics. The \$57 million project should be completed by summer 2020.

MidMichigan Health broke ground on October 5, 2017 for their new medical offices building in Gladwin. The vision for this new building is to provide high quality health care in a convenient location, allowing our patients to remain close to home for their medical care. The 17,000 square foot facility will house physician offices, an urgent care, lab drawing station, and diagnostic x-ray services. The design of this new facility will strengthen our ability to meet the needs of our patients, while enhancing the overall patient experience. The project is scheduled to be completed by summer 2018.

MidMichigan Health broke ground in Bay City, which is a new market for MidMichigan. This project is scheduled to be complete in Fall 2018 and will provide the Bay City community with an additional health care choice.

Operations

Year-to-date MidMichigan Health is \$10.3 million below its target. Management has begun to put in place plans to recover from the shortfall. Plans will be initiated by January 2018. The shortfall primarily results from decreased payments and increased costs for One Person One Record as process changes must occur to meet the technological changes.

APPENDIX

A1 – Historical Perspective

A2 – MidMichigan Health’s Board of Directors

A3 – Key Operating Officers

A4 – Missions, Vision, Values

A5 – Corporate Strategic Plan and Fiscal 2017

A6 – Centralized Management Services

A7 – Accreditations, Affiliations and Awards

A8 – Employees

A9 – Joint Ventures

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Appendix

A1 : Historical Perspective

Year	Description
1944	Midland started providing health care services to MidMichigan residents.
1982	The current operating structure was established with the organization of MidMichigan Health as the parent holding company of MidMichigan Medical Center – Midland and MidMichigan Medical Center – Clare.
1982	Formation of MidMichigan Health Development Associates (MHDA), a real estate holding company.
1984	Created MidMichigan Urgent Care-Midland and an affiliation with MidMichigan Visiting Nurses Association (MVNA).
1985	An affiliation began with MidMichigan Medical Center – Gladwin.
1986	MidMichigan Stratford Village was added and MidMichigan Home Health Services (MHHS) (now merged with MHC) was incorporated.
1987	MidMichigan Gladwin Pines was formed.
1993	Formation of MidMichigan Health Network, LLC (MHN) and the incorporation of Regional Dialysis Services Inc. (RDS).
1996	MidMichigan Physician Group (MPG) was incorporated to provide physician and specialty services.
1999	MidMichigan Health and Gratiot Community Hospital signed an affiliation agreement that resulted in MidMichigan Health acquiring a 33% interest in Gratiot.
2000	MidMichigan Health Park – Mt Pleasant and MidMichigan Gratiot Cancer Center opened.
2002	MidMichigan Regional Imaging (MRI) was formed.
2005	Full affiliation with Gratiot completed.
2008	MVNA, MidMichigan Nurse Support Services, and Gratiot Home Care and Hospice merged into one subsidiary, MHC (the legal entity remained MVNA). MAG began providing professional liability insurance to MidMichigan Health's independent and employed physicians.
2010	MidMichigan Health signed an agreement with NPS Associates, LLC, d.b.a. Great Lakes Bay Surgery & Endoscopy Center, to acquire a 45% membership interest.
2011	MidMichigan Health signed an agreement with ISOMM, LLC, d.b.a. Open MRI Mt. Pleasant, to acquire a 51% membership interest.
2012	MidMichigan Health sold substantially all of the assets of RDS and Great Lakes Renal Network (GLRN).
2013	MidMichigan Health and the University of Michigan Health System executed an Affiliation Agreement; MidMichigan Collaborative Care Organization was formed; and the corporate members of MidMichigan Health became advisory with fiduciary responsibility now held by the MidMichigan Health Board of Directors.
2014	MidMichigan Urgent Care and MRI operations were merged into MPG and Midland, respectively.
2015	Dissolution of the Saginaw Radiation Oncology Center (SROC) joint venture completed.
2016	MidMichigan Health divested both long-term care facilities. MidMichigan acquired Alpena Regional Medical Center, now MidMichigan Medical Center – Alpena. MidMichigan Health signed an agreement with Affirmant Health Partners, LLC to partner with 6 health care systems to create a clinically integrated statewide network.
2017	MidMichigan Health Foundation (Foundation) was formed to enhance the mission of MidMichigan Health by raising funds and public support. Dissolution of MAG was completed.

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A2 : MidMichigan Health's Board of Directors

The MidMichigan Health Board of Directors appoints or approves the boards of all subsidiaries. Selected members of the corporate board also serve on various committees. Key committees of the Board of Directors of MidMichigan Health include Audit, Compensation, Executive, Finance, Governance and Nominating, Investment, and Quality. Descriptions of the major corporate committees for fiscal 2017 follow:

<u>Audit Committee</u>	Meets quarterly and is responsible for selection and appointment of external auditors, oversight of the annual audit results, and review and approval of the annual Corporate Compliance plan, the annual Internal Audit plan, and reports issued by the Corporate Compliance Task Force and Internal Audit.
<u>Compensation Committee</u>	Meets at least three times per year and is responsible for executive compensation and benefit policy, approval of all compensation for operating officers, and approval of the senior management salary structure and incentive compensation. Also reviews and approves all compensation and benefit payments related to employed physicians and for any other person designated as a "disqualified person" by MidMichigan Health and whose compensation arrangement currently exceeds \$500,000.
<u>Executive Committee</u>	Meets as needed to provide guidance on key strategic matters and initiatives. The executive committee may take action on behalf of MidMichigan Health and exercise the power of the MidMichigan Health Board as required, with certain exceptions when it is not practical to call a meeting of the full MidMichigan Health Board. The executive committee will inform the MidMichigan Health Board of any actions it has taken at the next MidMichigan Health board meeting. The executive committee consists of the chair, vice chair, and chief executive officer. The MidMichigan Health Board may appoint additional members to the executive committee as needed. At least one UMHS director must serve on the executive committee at all times.
<u>Finance Committee</u>	Meets quarterly and is responsible for the oversight of financial results, approval of operating and capital budgets, approval of major capital commitments, approval of all financings and significant real estate matters, approval of financial strategies and policies (including acquisitions and divestitures), and review of the three year forecast and related implications.
<u>Governance and Nominating Committee</u>	Meets at least four times a year or when necessary and assists the MidMichigan Health Board of Directors in carrying out its responsibility for effective and efficient practices of governance.
<u>Investment Committee</u>	Meets quarterly to exercise investment oversight with respect to the MidMichigan Health Employees' Pension Plan, the MidMichigan Health Pension Plan for ARMC employees, the 401(a) Plan for Alpena and the 403(b) Savings Plan (collectively the "Plans"); to formulate investment policy; and to select and monitor investments for all the Plans as well as MidMichigan Health's investments and operating funds.
<u>Quality Committee</u>	Meets four times per year to serve as a liaison between the Board of Directors and the medical staff of each medical center and provides a forum

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for discussion of medical and administrative matters pertaining to the efficient operation and quality of patient care provided by MidMichigan Health.

Restructuring

Effective May 1, 2016, the Board of Directors assumed responsibility for the planning and fund development committee.

Fund
Development
Committee

Effective July 1, 2016, the Board of Directors dissolved this committee and created the MidMichigan Health Foundation. It now has a separate Board of Directors like all MidMichigan Health subsidiaries and this board directly reports to the MidMichigan Health Board of Directors.

Planning
Committee

Effective May 1, 2016, the Board of Directors assumed responsibility for the planning and the progress on MidMichigan Health's strategic plan. The Board also reviews and approves all major strategies, assesses the environmental and competitive pressures facing MidMichigan Health and determines appropriate responses to such pressures. Effective May 1, 2016, the Board of Directors assumed the work of this committee and the committee was dissolved.

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A3 - Key Operating Officers

Diane Postler- Slattery, Ph.D., FACHE, 58 - President and Chief Executive Officer, MidMichigan Health

Postler-Slattery became MidMichigan Health's president in January 2013. She came to MidMichigan from Aspirus Inc. in Wausau, Wisconsin where she had been the president and chief operating officer of the 325-bed regional referral hospital, Aspirus Hospital, since 2005. She also held a system-level position as senior vice president of quality and extended services at Aspirus Inc. Prior to this position, she was the chief operating officer and chief nurse executive of Aspirus Wausau Hospital where she established the vision for nursing practice leading to the magnet achievement award, among other accomplishments. She served Aspirus for twenty-four years. She earned her Ph.D. in education administration in 1995 from the University of Wisconsin – Madison. She received both her Master of Science degree in nursing/nursing administration and Bachelor of Science degree in nursing from the University of Wisconsin – Eau Claire. All of her degrees were earned with honors. She is a fellow in the American College of Healthcare Executives.

Gregory Rogers, HFMA Fellow, CPA (registered status), 62 - Executive Vice President, MidMichigan Health; President, Midland

Rogers became MidMichigan Medical Center-Midland's President and MidMichigan Health's Executive Vice President in July 2008. He is responsible for Midland as well all of the acute care facilities (Alpena, Clare, Gladwin and Gratiot). In addition, he provides the executive sponsorship for MidMichigan Health's service lines. Prior to his current position, Rogers served as senior vice president & treasurer of MidMichigan Health and MidMichigan Medical Center-Midland. During this period, his responsibilities included information technology and supply chain. Prior to that, he served as vice president and controller for Midland. Rogers joined MidMichigan in 1981. Rogers is a certified public accountant and a fellow in the Healthcare Financial Management Association with certifications in healthcare finance, managed care and patient accounting. He received his Bachelor of Arts degree from Albion College in 1978 and completed additional master's level courses at Central Michigan University. He has held local, state and national positions in many professional organizations and has been active in community service and sports organizations.

Francine Padgett, HFMA Fellow, MBA, CPA (registered status), 63 - Senior Vice President and Chief Financial Officer, MidMichigan Health

Padgett is senior vice president, chief financial officer, and treasurer of MidMichigan Health and MidMichigan Medical Center–Midland. In her current role, she provides oversight of all of the financial and investment operations of MidMichigan Health including capital management. Prior to her current position, Padgett served as Corporate Controller of MidMichigan Health. She has worked at MidMichigan Health since 1990. Previously she was a senior manager at Deloitte & Touche. Padgett earned a Bachelor of Science degree from the University of Missouri in 1975 and an MBA from the University of Cincinnati in 1978. All of her degrees were earned with honors. She is a Certified Public Accountant and a Fellow in the Healthcare Financial Management Association. She has held local and national positions with various not-for-profit organizations.

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Donna Rapp, MBA, 67 - Senior Vice President and Secretary, MidMichigan Health

Rapp is senior vice president and secretary of MidMichigan Health and MidMichigan Medical Center-Midland. She oversees strategic planning, marketing, public relations, fund development, volunteer services and physician relations throughout MidMichigan Health. Rapp received her Bachelor of Arts degree from the University of Michigan in Ann Arbor and master's degree from Central Michigan University in Mt. Pleasant. All of her degrees were earned with honors. Rapp joined MidMichigan Health in 1977. She remains active in many community service organizations and is a professor at Northwood University in Midland, MI.

Additional key positions within MidMichigan Health:

- Chief Human Resources Officer;
- Chief Information Officer;
- Chief Medical Officer;
- General Counsel;
- President of Each Subsidiary; and
- Vice President of Business Development.

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A4 : Mission, Vision, Values

In August, 2009 the MidMichigan Health Board approved the first system-wide mission, vision, and values at MidMichigan Health, with the patient as the focus of everything we do. In fiscal 2014, the Board of Directors changed the vision to reflect and encompass contemporary healthcare thinking including wellness and population health. At this time, the Board has reaffirmed both the mission and values.

Mission: ***Our Mission is to provide excellent health services to improve the quality of life for people in our communities.***

Vision: ***Our Vision is to celebrate the power of health throughout life – with you.***

Values: At MidMichigan Health, we demonstrate these values:

Excellence – We offer nothing less than the best. We adhere to the highest standards possible in clinical care and customer service. We continuously measure ourselves and constantly strive to improve.

Integrity – We do the right thing, each time, every time. We treat each individual with compassion and respect, demonstrating the pinnacle of professionalism and dignity. We communicate openly and honestly. We recognize the unique individuality of each person. In all that we do, we exemplify the highest ethical standards.

Teamwork – We provide individual commitment to a group effort. Collaboration benefits everyone – most importantly, our patients. It promotes efficiency, fosters professional and organizational growth, encourages learning, and stimulates innovation.

Accountability – We accept responsibility for all we do. We are accountable for the outcomes of our efforts. We are responsible to the communities we serve, to our patients, and to one another. We recognize that as health care providers we occupy a position of trust.

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A5 : Corporate Strategic Plan

In fiscal 2009, MidMichigan Health began its first comprehensive corporate strategic plan which was completed in fiscal 2010. Prior to this initiative, MidMichigan Health had a decentralized approach to planning and utilized the plans and objectives of each subsidiary. In addition to developing the first corporate strategic plan at the system level, management completed a best practices review of its governance practices and developed the Governance and Nominating, Planning, and Quality committees. The recommendations and implementation plan of the governance review task force were approved by the MidMichigan Health Board of Directors in fiscal 2011 and have been implemented. Given the current economic environment, increased competition and the consolidation within the healthcare industry, MidMichigan Health has updated its strategic plan. A discussion of the four goals for MidMichigan Health and the underlying strategies follows:

Quality – MidMichigan Health’s goal is to build value through accessible, trusted, efficient and effective care that creates and sustains loyalty.

- Support market needs with access to care across all care settings.
- Assist consumers wherever they are in their health journey.

Innovation – As a system MidMichigan Health will create new dimensions of performance through deliberate transformation.

- Create new business models that defy tradition and lead to enhanced consumer satisfaction and excellent clinical outcomes.
- Create by charter and activate an in-house innovation center designed to address new tools, technologies, ideas and workflows.
- Examine convenience opportunities for care delivery (virtual care, locations, hours, partners, settings, etc.).
- Achieve value through a clinically integrated narrow provider network.

Collaboration –MidMichigan Health will connect and engage with others to achieve shared goals.

- Leverage our UMHS partnership and internal resources to become the leading consumer choice for care in middle and northern Michigan.
- Using patient-centered approaches, partner with patients and their families incorporating them as the architects and designers of their health care experience in order to achieve their optimal health.
- Maximize opportunities for research, education, skills training and other advancements through strong academic partnerships.
- Achieve value through a clinically integrated provider network.
- Engage the voices of our communities in solutions-focused forums to improve community health.

Sustainability – MidMichigan Health will ensure our long-term viability through the responsible management of human, financial, environmental and other resources.

- Achieve the size and scale needed in order to optimize our resources, remain viable and responsible to our communities.
- Build our portfolio of programs and service to be “Next Practice”.

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A summary of each of the key priorities and the results of these priorities have been included for your review for fiscal 2017:

Quality – Complete the requirements specified by MHA for participation in Hospital Engagement Network (HEN) 2.0. Meet or exceed national benchmarks for five of five patient overall satisfaction scores and for 100% of metrics as reported on the appropriate Quality & Safety Dashboards as of July 1, 2016.

- We have completed all of the requirements for participation in HEN. We are submitting all quality/safety metrics, have begun pts/family activated response option at all five hospitals and have added pts/family to committees at all five hospitals. We have met 5/5 overall satisfaction scores at top quartile performance.

Growth – Expand to a total of at least twelve telemedicine programs or sites resulting in at least 2,000 virtual care visits. Develop at least two new programs stemming from more than one service line with at least one new program providing services and all new programs seeing a combined total of at least 50 inpatient or 300 outpatient encounters.

- We finished the fiscal year with 18 programs/locations and generated a total of 2,789 virtual visits.
- We exceeded both the inpatient and outpatient targets with 61 inpatient and 374 outpatient encounters in new programs developed in our Oncology and Cardiovascular service lines.

Relationships – 100% of new leaders and no fewer than 50% of invested leaders and engaged learners complete MyLead leadership courses driving 28% of employees to rank MidMichigan as an excellent place to work, with a goal of being top quartile in 2018. Implement two ideas/programs directly related to the Dyad Leadership Model driving 75% of employed providers to answer “would definitely recommend” MidMichigan as a place to practice medicine. Programs include establishing a formal mentorship program with 75% of the mentees rating the program as “valuable”, and having at least two practices prepared to implement online scheduling.

- 100% of new leaders through June 30 have completed the MyLead courses. 93% of invested leaders and six engaged learners have also completed requisite MyLead courses. In regard to the PRC employee engagement survey, 34% of employees ranked MidMichigan Health as “an excellent place to work”.
- The final number were 82.6% of providers “would definitely recommend” MidMichigan as a place to practice medicine. We have made substantive changes to the hospitalist model with help from our physician dyad leaders and an engagement with the UM hospitalist team. We have avoided providers leaving and signed several new ones. We have had extensive input by the dyad leaders on how to move from Cerner and Allscripts into EPIC. Dyad leaders are involved in recruiting in their areas of responsibility. Every new APP hire and physician is being assigned a mentor. We have more than 2 practices that will be implementing online scheduling. Over 90% of the respondents to the survey on mentorship found it valuable.

Sustainability – Implementation of a sustainability plan that enables MidMichigan to attain or exceed a 3.6% operating margin from recurring operations.

- Although we achieved significant improvement over the prior year from recurring operations, we did not meet our 3.6% margin. The results from recurring operations indicate a 3.0% operating margin compared to 1.9% last year. We expect operating results from recurring operation to increase to \$21 million compared to \$13 million in the prior year.

A6 : Centralized Management Services

MidMichigan Health has a strong focus on "systemness" – establishing and following the same strategies and operational goals throughout each operating entity, while meeting the unique needs of each individual community. The senior management group, comprised of corporate executives and the presidents of each facility, directs the strategic and operational activities of MidMichigan Health. In order to meet these expectations and needs, MidMichigan Health operates with decentralized governance, administration, and medical staff models. Where it improves customer service and contributes to economic efficiencies, operations and services are standardized. MidMichigan Health has centralized for cost efficiency purposes the following management services, allowing it to perform well in an increasingly cost-competitive environment. Integration of the newly acquired Alpena is ongoing and will include centralizing these same service areas in the next year or so.

General Management — The centralized senior management group, which includes the executive offices, strategic planning, governance, marketing and business development functions. They also oversee and assist with the operation of the healthcare facilities.

Biomedical Services — A centralized staff services all electronic systems, including patient care equipment.

Business Development Services — Identifies, explores and implements short and long-term plans, goals and objectives, that seek to identify growth opportunities for MidMichigan Health and to minimize the effects of competitive activity to ensure continued growth and viability and create long-term value.

Corporate Compliance — The Corporate Compliance function is managed at the corporate level. The Corporate Compliance Task Force is comprised of employees from all subsidiaries. The work is completed by each subsidiary and monitored centrally by the Corporate Compliance Officer and The Audit Committee.

Financial Management — Overall financial management, debt placement, accounting, internal audit, cash and investment management, revenue cycle, accounts payable, and payroll services are provided centrally. All managed care contracting is also done centrally through ConnectCare, allowing MidMichigan Health to contract with single signature authority through a messenger module.

Human Resources — Employee compensation and benefit programs, recruiting, workforce planning, and other employee programs are administered centrally with strategic partners on-site at most subsidiaries.

Information Technology — Information systems is a crucial centralized service that supports all MidMichigan Health facilities. This department not only supports the hardware throughout the system, it is also actively developing or integrating applicable clinical, financial, and operating information systems, including electronic medical records. In fiscal 2017, MidMichigan Health implemented a new electronic health record for all subsidiaries except Alpena and Home Care. Alpena's implementation occurred on September 30, 2017 which allowed for integration to occur. Home Care will go live with Epic in fiscal 2019. This strategy will deliver increased quality and patient safety, patient satisfaction, and employee and provider satisfaction, and should lower costs and reduce redundancies due to the elimination of multiple clinical and revenue cycle systems.

Insurance/Risk Management — Centralized to ensure all appropriate standards and policies are followed and to allow for the issuance of coverage at an aggregate level.

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Marketing — The corporate marketing function delivers brand and image consistency for all services provided by MidMichigan Health.

Planning and Quality — These corporate functions monitor strategic integration and quality measures throughout the system to strengthen MidMichigan Health as it continues to operate in an increasingly complex and competitive environment.

Supply Chain — Standardization of products is emphasized to the greatest extent practical and is an integral part of the efficiency and cost competitiveness for MidMichigan Health. This group maintains accountability for cost containment and inventory reduction.

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A7 : Accreditations, Affiliations and Awards

Educational Affiliations

MidMichigan Health actively supports a number of educational programs in conjunction with various educational institutions. The Family Medicine Residency Program in Midland is affiliated with Michigan State University-College of Human Medicine. This is a 4 year residency program, training 6 residents in each year. A medical education affiliation agreement was signed on May 12, 2010, with Michigan State University's-College of Human Medicine to develop a "Midland Regional Campus" which now trains 24 medical students per year. In December 2010, MidMichigan Health signed an affiliation agreement with Central Michigan University to affiliate with their College of Medicine and College of Health Professions to offer educational experiences to medical students and other clinical and administrative professionals. In July 2018, MidMichigan Health will also become a campus for CMU College of Medicine, resulting in an additional 24 medical students per year. Gratiot's Family Medicine residency program is sponsored by Michigan State University's College of Human Medicine. This program which began in July 2016 is a 3 year residency program training 4 residents in each year.

Nursing education is conducted through affiliations with Alma College, Davenport University, Delta College, Kirtland Community College, Michigan State University, Mid Michigan Community College, Montcalm Community College, Northern Michigan University, and Saginaw Valley State University. Training is provided for pharmacy programs through Ferris State University, University of Michigan, and Wayne State University. Physical, speech, and occupational therapy programs are provided through affiliations with Central Michigan University, Grand Valley State University, Oakland University, Michigan State University, Saginaw Valley State University, University of Indianapolis, University of Michigan - Flint, Wayne State University, Oakland University and Western Michigan University. Mid-Level Provider training for Nurse Practitioners (NP) and Physician Assistants (PA) include affiliations with Grand Valley State University, Michigan State University, Saginaw Valley State University, University of Michigan - Flint, Central Michigan University and Wayne State University. Other programs supported by MidMichigan Health include medical technology, radiology, physical therapy assistants, phlebotomy and medical social work.

Accreditations, Affiliations and Certifications

Each of the acute care hospitals is licensed by the Michigan Department of Community Health and uses The Joint Commission (TJC) accreditation process for deemed status with Centers for Medicare and Medicaid Services (CMS). The Joint Commission accreditation is valid for three years. Each of the acute care hospitals were accredited as follows: Alpena, August 2015; Gladwin, December 2014; Midland, November 2016; Clare, June 2016; and Gratiot, August 2016. Gladwin and Gratiot were surveyed in 2017 and expect to receive a final accreditation decision in early 2018.

Midland's, Alpena's and Gratiot's Mental Health Units are licensed by the State of Michigan Department of Licensing and Regulatory Affairs. Midland's Family Practice Residency program is accredited by the Accreditation Council of Graduate Medical Education. The Council on the Accreditation of Rehabilitation Facilities accredits Gratiot's rehabilitation services.

The hospital laboratories are accredited by the College of American Pathologists (CAP). The laboratories meet all requirements of State and Federal laws, including the Clinical Laboratory Improvement Act of 1988.

The American College of Radiology (ACR) has accredited mammography in Midland, Alpena, Gratiot, Clare, Gladwin, Houghton Lake, and Mount Pleasant. Midland, Gratiot, Clare, and Gladwin are also accredited by the ACR in nuclear medicine. Gratiot, Clare, and Gladwin have attained ACR accreditation for diagnostic ultrasound. Midland and Alpena are ACR accredited for general diagnostic, breast, and ultrasound guided breast biopsy. Midland, Gratiot, Clare and Gladwin are ACR accredited in CT. The MRI

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services in Midland, Gratiot, Clare, Gladwin, and Mount Pleasant also are ACR accredited. Midland is also ACR accredited for breast MRI.

The American College of Surgeons re-verified Midland's Trauma program and the State of Michigan re-designated as a Level II Trauma Center. The hospital received a three year accreditation in January 2017.

The American College of Surgeons Commission on Cancer certified Midland's cancer program and it is an approved "Comprehensive Community Cancer Program." They received three year accreditation in September 2015. The Breast Health Program at MidMichigan Center for Women's Health has also been accredited by the National Accreditation Program for Breast Centers (NAPBC), a program administered by the American College of Surgeons, in September 2012. This designation is given only to centers that have undergone a rigorous evaluation and performance review, demonstrating compliance with NAPBC's standards.

MidMichigan Health is a member of both the American Hospital Association and the Michigan Health & Hospital Association.

Awards and Recognition

The awards and recognitions received are listed for MidMichigan Health and its acute care facilities by subsidiary.

MidMichigan Health

Organizational

- Award of Distinction by Professional Research Consultants, Inc. (PRC), as a place to work – 2017
- 5-Star Performer by Professional Research Consultants, Inc. (PRC), for patient care, degree of people treated fairly, and total compensation package – 2017
- [Truven Health Analytics™](#) names MidMichigan Health one of the nation's 15 Top Health Systems® – 2016
- City of Midland Beautification Award for the Gerstacker Building – 2016
- Business of the Year by the Midland Area Chamber of Commerce – 2016
- Governor's Fitness Award gold award for the state of Michigan – 2015

Programmatic

- Michigan Resuscitation (MiResCu) Community Award to MidMichigan Medical Center – Gladwin EMS – 2015

Marketing

- Marcom Awards include:
 - Gold award – Top 50 Cardiovascular Hospital Campaign – 2017
 - Platinum award - MORE Equals Social Media Video Series – 2017
 - Honorable Mention – Spring 2017 MORE Equals Radio Campaign – 2017
 - Honorable Mention – Opening the Door to MORE MidMichigan Medical Center - Mt. Pleasant Insert – 2017
 - Winter/Spring 2016 MORE Equals Campaign – 2016
 - Gold award for MidMichigan Health Who We Are Brochure – 2016
 - Honorable mention for the Cardiovascular Procedure Guide – 2016
 - Honorable mention for the Laurie Neville Patient Testimonial Video – 2016
 - Platinum award for the Winter/Spring 2015 Health Risk Assessment Campaign
- Aster Awards include:
 - Gold award for More Equation radio campaign – 2017
 - Gold award for More Equation Location Photography – 2017
 - Silver award for Flavorful Cooking video series – 2017
 - Silver award for More Equation video series – 2017

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- Gold award for the nursing home virtual tour series; gold award for the “More Life More Health” assessment radio campaign; and silver award for the health assessment integrated campaign – 2016
- Healthcare Marketing Report awards include:
 - Gold award for the More Equation Video Series – 2017
 - Silver award for the Who We Are Brochure – 2017
 - Merit award for the Flavorful Cooking Video Series – 2017
 - Merit award for the More Equation Radio Campaign – 2017
 - Silver award for the More Life, More Health Campaign - 2016
 - Merit award for the Gorman’s Testimonial Video - 2016
 - Merit award for the Dr. Internet TV Spot - 2016
 - Merit award for the More Life, More Health Radio Spots - 2016
 - Gold award for 3 Good Things employee communication – 2015
 - Silver award for Health Risk Assessment campaign – 2015
 - Merit award for Hunting Safety video – 2015
 - Merit award for MyMidMichigan campaign – 2015
- ADDY Awards include:
 - Silver award for the 2016 More Equation Video Series (Social Media) – 2017
 - Silver award for the 2016 More Campaign Location Photography – 2017
 - Silver award for the 2016-17 More Equation Radio Campaign – 2017
 - Silver award for the STEMI Educational Video – 2017
 - Silver award for the Laurie Neville Cardiovascular Testimonial Video – 2017
 - Silver award for the Gorman’s bariatric testimonial video – 2016
 - Silver award for the nursing home virtual tour campaign – 2016
 - Gold award for the Dr. Internet TV spot – 2016
 - Silver award for the More Life More Health radio campaign – 2016
 - Silver award for the More Equation TV campaign – 2016
 - Silver award for the More Life More Health online campaign – 2016
 - Silver award for the More Equation integrated campaign – 2016
 - Gold award for breast cancer survivor testimonial video – 2015
 - Silver award for heart failure video – 2015
 - Silver award for hunting safety video – 2015
 - Silver award for MyMidMichigan campaign – 2015
 - Silver award for Verified Trauma Center campaign – 2015
 - Silver award for Three Good Things poster – 2015
- Michigan Works! Impact Award – 2017
- WorldatWork 2017 Seal of Distinction – 2017
- eHealthcaregold Leadership award for the Winter/Spring 2015 Health Risk Assessment Campaign - 2015
- CardioVascular Advertising Awards include:
 - (CVAA) gold award for Heart Failure Clinic Videos - 2015
 - (CVAA) gold award for Heart Clinic Patient Education Materials - 2015

MidMichigan Medical Center-Midland

Organizational

- 2017 – Top 50 Cardiovascular Hospital by Truven Health Analytics™, a leading provider of data-driven analytics and solutions to improve the cost and quality of healthcare.
- Leapfrog awards include:
 - Grade A in Patient Safety Fall and Spring 2017 Hospital Safety Score – 2017 (Five As in a row)
 - Grade A in Patient Safety Fall and Spring 2016 Hospital Safety Score – 2017

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- Michigan's Quality Improvement Organization (MPRO) 2017 Governor's Award of Excellence for Outstanding Achievement in Effective Reporting and Measurement: Hospital Value-based Purchasing (HVBP) Acute Care Hospitals – 2017
- MidMichigan Medical Center – Midland received full accreditation as a comprehensive bariatric facility by the Metabolic and Bariatric Surgery Accreditation and Quality Improvement Program - 2017
- 2016 - 100 Top Hospitals® by Truven Health Analytics™, a leading provider of data-driven analytics and solutions to improve the cost and quality of healthcare. The Medical Center was also one of a select few to earn the 2016 100 Top Hospital's Everest® Award - 2016
- Economic Alliance for Michigan Hospital Patient Safety Award – 2016
- Best Value Hospital for 2014 by Verras Healthcare International - 2015

Programmatic

- 2016-17 Best Hospitals Rankings and U.S. News Colloquium on Quality Measures
 - Heart Failure - High performing
 - Hip Replacement - High performing
 - Knee Replacement - High performing
 - Chronic Obstructive Pulmonary Disease (COPD) - High performing
- Emergency Medical Services received the American Heart Association's Mission: Lifeline® EMS Gold Award – 2016
- MidMichigan Medical Center – Midland received full accreditation as a comprehensive bariatric facility by the Metabolic and Bariatric Surgery Accreditation and Quality Improvement Program - 2016

MidMichigan Medical Center-Alpena

Organizational

- Becker's Hospital Review List: 100 Great Community Hospitals – 2017
- National Rural Health Association Top 20 Rural Community Hospital – 2017
- Michigan's Quality Improvement Organization (MPRO) 2017 Governor's Award of Excellence for Outstanding Achievement in Effective Reporting and Measurement: Hospital Value-based Purchasing (HVBP) Acute Care Hospitals – 2017
- Grade B in Patient Safety from Leapfrog's Spring 2016 Hospital Safety Score - 2016

MidMichigan Medical Center-Gratiot

Organizational

- Michigan's Quality Improvement Organization (MPRO) 2017 Governor's Award of Excellence for Outstanding Achievement in Effective Reporting and Measurement: Hospital Value-based Purchasing (HVBP) Acute Care Hospitals – 2017
- Economic Alliance of Michigan Hospital Patient Safety Award – 2017
- Leapfrog awards include:
 - Grade B in Patient Safety from Leapfrog's Spring 2017 Hospital Safety Score – 2017
 - Grade A in Patient Safety from Leapfrog's Spring 2016 Hospital Safety Score - 2016

Programmatic

- Wound Treatment Center at MidMichigan Medical Center – Gratiot received the 2016 Center of Distinction Award from Healogics, Inc. - 2017
- RehabCentre three-year accreditation for inpatient rehabilitation for adults and stroke specialty program by The Commission on Accreditation of Rehabilitation Facilities (CARF) International – 2014

MidMichigan Medical Center-Clare

Organizational

- 4-Star Performer by Professional Research Consultants, Inc. (PRC), for patient care and total compensation package – 2017

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- Michigan's Quality Improvement Organization (MPRO) 2017 Governor's Award of Excellence for Outstanding Achievement in Effective Reporting and Measurement: Hospital Value-based Purchasing (HVBP) Acute Care Hospitals – 2017
- Leapfrog awards include:
 - Grade A in Patient Safety Spring 2017 Hospital Safety Score – 2017
 - Grade A in Patient Safety Spring 2016 Hospital Safety Score - 2016

MidMichigan Medical Center-Gladwin

Organizational

- Top Rural Hospital Award by The Leapfrog Group – December 2017
- 4-Star Performer by Professional Research Consultants, Inc. (PRC), for patient care and total compensation package – 2017
- Michigan's Quality Improvement Organization (MPRO) 2017 Governor's Award of Excellence for Outstanding Achievement in Effective Reporting and Measurement: Ambulatory Surgery Centers, Critical Access Hospitals and Inpatient Psychiatric Facilities – 2017

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A8 : Employees

As of June 30, 2017, MidMichigan Health employed approximately 5,800 people; this represented approximately 5,200 full-time employees. Of the total employees, approximately 1,300 are registered nurses and approximately 10% of MidMichigan Health's employees are part-time, which enables MidMichigan Health to manage staffing levels with volume.

Management considers its relationships with its employees to be positive, despite the national uncertainty in healthcare. MidMichigan Health continues to experience positive labor relations at all of its subsidiaries. The table below shows the various contractual relationships:

Subsidiary	Bargaining Unit	# of Employees	% of total employees	Expiration of Agreement	Type of Employees Represented
Midland	United Steelworkers	303	5.2%	October 6, 2018	Lab & Nursing Services
Midland	United Steelworkers	15	0.2%	January 5, 2019	Radiographers
Alpena	United Steelworkers	220	3.8%	September 30, 2018	Support Services
Alpena	Michigan Nurses Association (MNA)	190	3.3%	March 3, 2018	RN's
Alpena	United Steelworkers	130	2.2%	February 28, 2019	LPN & Support Services
Alpena	MNA	13	0.2%	February 28, 2019	RN's
Clare	United Auto Workers	29	0.5%	July 17, 2020	Imaging
Gladwin	United Steelworkers	87	1.5%	September 30, 2018	Support Services
Gratiot	MNA & Gratiot Medical Center Registered Nurses Associated	153	2.6%	November 9, 2019	RN's
Home Care	United Steelworkers	8	0.1%	September 16, 2019	Support Services
Total		1,148	19.79%		

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There has been a slight decrease in contract activity, from 20.75% to 19.79% in fiscal 2017.

MidMichigan Health provides a competitive compensation and benefits program, which includes a pension plan, life insurance, medical, dental, and disability insurance plans as well as paid vacation and holiday programs. MidMichigan Health is not immune to national labor shortages and has taken steps that have eased potential staffing shortfalls; including implementing an on-line web-enabled clinical scheduling system for open shifts that includes incentive points. The program has resulted in reduced premium labor costs, optimized staffing, and improved consistency of staffing across MidMichigan Health. In addition, MidMichigan Health has a full-time dedicated nurse recruiter to assist in building relationships with the various nursing and clinical programs and potential nursing/clinical student candidates.

Employee engagement remains a critical priority for MidMichigan Health. In its latest employee survey, approximately 34% of employees ranked MidMichigan Health as “an excellent place to work”. As part of its strategy to engage and align employees, an employee incentive program has been designed to focus on quality, patient satisfaction and financial sustainability.

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MidMichigan Health Disclosure Statement
June 30, 2017
Appendix

A9 : Joint Ventures

MidMichigan Health participates in several joint ventures enhancing its ability to provide services to the community, participate in projects with other healthcare organizations, and share financing costs of new facilities and technology. In each of these joint ventures, MidMichigan Health has ownership interest ranging from 14% to 51% and has concluded that it does not control these joint ventures; therefore, the results of these joint ventures are recorded under the equity method of accounting in the consolidated financial statements.

Joint venture interests include:

- ♦ 50% interest in Advanced PET Imaging Network;
- ♦ 50% interest in Jeppesen Radiation Oncology Center (through September 30, 2017);
- ♦ 50% interest in MidMichigan Health Network;
- ♦ 50% interest in North Eastern Michigan Cancer Center with the University of Michigan Health System;
- ♦ 44% membership interest in NPS Associates, LLC, d.b.a. Great Lakes Bay Surgery & Endoscopy Center;
- ♦ 49% interest in Mt. Pleasant Surgery Center;
- ♦ 33% interest in Great Lakes Mobile PET; and
- ♦ 14% interest in Affirmant Health Partners, LLC (formerly known as Federation Care Network).

[Concluded]