

ORIGINAL

E-001-14



ILLINOIS HEALTH FACILITIES AND SERVICES REVIEW BOARD

**CHANGE OF OWNERSHIP EXEMPTION APPLICATION
FOR AN EXISTING HEALTH CARE FACILITY
AUGUST 2013 EDITION**

RECEIVED

JAN 03 2014

ILLINOIS HEALTH FACILITIES AND SERVICES REVIEW BOARD
INSTRUCTIONS FOR THE COMPLETION OF APPLICATION FOR EXEMPTION
CHANGE OF OWNERSHIP FOR AN EXISTING HEALTH CARE FACILITY

The attached form must be used for all transactions proposing a change of ownership of a health care facility. The requirements for issuance of an exemption are contained in 77 IAC 1130.520. Applicants should refer to IAC 1130.140 for definitions of a change of ownership and control of a health care facility. Applicants should also refer to 77 IAC 1130.220(a) for information on who the applicant(s) should be. Note the following requirements and guidelines pertaining to the Application for Exemption:

- 1 IAC 1130.520(a) prohibits any person from acquiring or entering into an agreement to acquire an existing health care facility prior to receiving approval from the State Board.
- 2 Complete the application with all applicable attachments. All pages and documents must be on single-sided paper size 8 1/2" x 11". Applicants should note that the required attachments to the application must be labeled and identified by attachment number. FAILURE TO DO SO WILL RESULT IN THE APPLICATION BEING DEEMED INCOMPLETE.
- 3 It is noted that all applications for exemption for the change of ownership of a health care facility are subject to the opportunity for a public hearing and public hearing requirements (77 IAC 1130.520(c) and (d)).
4. Applicants must submit a complete original application with original signature(s) and required appendices and attachments, as well as the APPLICATION FEE of \$2,500 payable by check or money order to the Illinois Department of Public Health. Submit the material to:

Courtney Avery, Administrator
Illinois Health Facilities and Services Review Planning Board
525 West Jefferson Street, Second Floor
Springfield, Illinois 62761-0001

5. Per IAC 1130.550(b), the State Agency is allowed 30 DAYS (from the date of receipt of the application) to determine the application's completeness. PLEASE REFRAIN FROM TELEPHONING THE STATE AGENCY FOR A STATUS REPORT ON YOUR APPLICATION. STAFF TIME ANSWERING PHONE INQUIRIES TAKES FROM STAFF TIME TO REVIEW APPLICATIONS. The State Agency will contact you if your application is incomplete.

NOTE: "The Illinois Health Facilities and Services Review Board does not discriminate on the basis of handicap in admission or access to, or treatment or employment in its programs and activities in compliance with Section 504 of the Rehabilitation Act of 1973, as amended. The Equal Employment Opportunity Officer is responsible for coordination of compliance efforts; voice (217) 785-2034; TDD (217) 785-2088."

**ILLINOIS HEALTH FACILITIES AND SERVICES REVIEW BOARD
APPLICATION FOR EXEMPTION FOR THE
CHANGE OF OWNERSHIP FOR AN EXISTING HEALTH CARE FACILITY**

1. INFORMATION FOR EXISTING FACILITY

Current Facility Name Passavant Area Hospital
Address 1600 West Walnut Street
City Jacksonville, Illinois Zip Code 62650 County Morgan
Name of current licensed entity for the facility The Passavant Memorial Area Hospital Association
Does the current licensee: own this facility X OR lease this facility _____ (if leased, check if sublease ☐)
Type of ownership of the current licensed entity (check one of the following:) _____ Sole Proprietorship
X Not-for-Profit Corporation _____ For Profit Corporation _____ Partnership _____ Governmental
_____ Limited Liability Company _____ Other, specify _____
Illinois State Senator for the district where the facility is located: Sen. Sam McCann
State Senate District Number 50 Mailing address of the State Senator 221 Dunlap Court, Jacksonville, IL 62650
Illinois State Representative for the district where the facility is located: Rep. C.D. Davidsmeyer
State Representative District Number 100 Mailing address of the State Representative 325 West State Street, Suite 102, P.O. Box 160, Jacksonville, IL 62650

- 2. OUTSTANDING PERMITS.** Does the facility have any projects for which the State Board issued a permit that will not be completed (refer to 1130.140 "Completion or Project Completion" for a definition of project completion) by the time of the proposed ownership change? Yes ☐ No X. If yes, refer to Section 1130.520(f), and indicate the projects by Project # NA

3. NAME OF APPLICANT (complete this information for each co-applicant and insert after this page).

Exact Legal Name of Applicant Memorial Health System
Address 701 N. First Street
City, State & Zip Code Springfield, IL 67781
Type of ownership of the current licensed entity (check one of the following:) _____ Sole Proprietorship
X Not-for-Profit Corporation _____ For Profit Corporation _____ Partnership _____ Governmental
_____ Limited Liability Company _____ Other, specify _____

4. NAME OF LEGAL ENTITY THAT WILL BE THE LICENSEE/OPERATING ENTITY OF THE FACILITY NAMED IN THE APPLICATION AS A RESULT OF THIS TRANSACTION.

Exact Legal Name of Entity to be Licensed The Passavant Memorial Area Hospital Association
Address 1600 West Walnut Street City, State & Zip Code Jacksonville, IL 62650
Type of ownership of the current licensed entity (check one of the following:) _____ Sole Proprietorship
X Not-for-Profit Corporation _____ For Profit Corporation _____ Partnership _____
Governmental _____ Limited Liability Company _____ Other, specify _____

5. BUILDING/SITE OWNERSHIP. NAME OF LEGAL ENTITY THAT WILL OWN THE "BRICKS AND MORTAR" (BUILDING) OF THE FACILITY NAMED IN THIS APPLICATION IF DIFFERENT FROM THE OPERATING/LICENSED ENTITY

Exact Legal Name of Entity That Will Own the Site The Passavant Memorial Area Hospital Association
Address 1600 West Walnut Street
City, State & Zip Code Jacksonville, Illinois, 62650
Type of ownership of the current licensed entity (check one of the following:) _____ Sole Proprietorship
X Not-for-Profit Corporation _____ For Profit Corporation _____ Partnership _____ Governmental
_____ Limited Liability Company _____ Other, specify _____

**ILLINOIS HEALTH FACILITIES AND SERVICES REVIEW BOARD
APPLICATION FOR EXEMPTION FOR THE
CHANGE OF OWNERSHIP FOR AN EXISTING HEALTH CARE FACILITY**

4. NAME OF APPLICANT (complete this information for each co-applicant and insert after this page).

Exact Legal Name of Applicant The Passavant Memorial Area Hospital Association

Address 1600 West Walnut Street City, State & Zip Code Jacksonville, IL 62650

Type of ownership of the current licensed entity (check one of the following:) ☐ Sole Proprietorship

☒ Not-for-Profit Corporation ☐ For Profit Corporation ☐ Partnership ☐ Governmental

☐ Limited Liability Company ☐ Other, specify _____

6. **TRANSACTION TYPE. CHECK THE FOLLOWING THAT APPLY TO THE TRANSACTION:**
- ☐ Purchase resulting in the issuance of a license to an entity different from current licensee;
 - ☐ Lease resulting in the issuance of a license to an entity different from current licensee;
 - ☐ Stock transfer resulting in the issuance of a license to a different entity from current licensee;
 - ☐ Stock transfer resulting in no change from current licensee;
 - ☐ Assignment or transfer of assets resulting in the issuance of a license to an entity different from the current licensee;
 - ☐ Assignment or transfer of assets not resulting in the issuance of a license to an entity different from the current licensee;
 - ☒ Change in membership or sponsorship of a not-for-profit corporation that is the licensed entity;
 - ☐ Change of 50% or more of the voting members of a not-for-profit corporation's board of directors that controls a health care facility's operations, license, certification or physical plant and assets;
 - ☐ Change in the sponsorship or control of the person who is licensed, certified or owns the physical plant and assets of a governmental health care facility;
 - ☐ Sale or transfer of the physical plant and related assets of a health care facility not resulting in a change of current licensee;
 - ☐ Any other transaction that results in a person obtaining control of a health care facility's operation or physical plant and assets, and explain in "Attachment 3 Narrative Description"
7. **APPLICATION FEE.** Submit the application fee in the form of a check or money order for \$2,500 payable to the Illinois Department of Public Health and append as **ATTACHMENT #1**.
8. **FUNDING.** Indicate the type and source of funds which will be used to acquire the facility (e.g., mortgage through Health Facilities Authority; cash gift from parent company, etc.) and append as **ATTACHMENT #2**.
9. **ANTICIPATED ACQUISITION PRICE: \$0** The transaction will not involve funding of an acquisition.
10. **FAIR MARKET VALUE OF THE FACILITY:** \$83,500,000 (See Officer's Affidavit)
(to determine fair market value, refer to 77 IAC 1130.140)
11. **DATE OF PROPOSED TRANSACTION:** _____ April 1, 2014 _____
12. **NARRATIVE DESCRIPTION.** Provide a narrative description explaining the transaction, and append it to the application as **ATTACHMENT #3**.
13. **BACKGROUND OF APPLICANT** (co-applicants must also provide this information). Corporations and Limited Liability Companies must provide a current Certificate of Good Standing from the Illinois Secretary of State. Limited Liability Companies and Partnerships must provide the name and address of each partner/ member and specify the percentage of ownership of each. Append this information to the application as **ATTACHMENT #4**.
14. **TRANSACTION DOCUMENTS.** Provide a copy of the complete transaction document(s) including schedules and exhibits which detail the terms and conditions of the proposed transaction (purchase, lease, stock transfer, etc). Applicants should note that the document(s) submitted should reflect the applicant's (and co-applicant's, if applicable) involvement in the transaction. The document must be signed by both parties and contain language stating that the transaction is contingent upon approval of the Illinois Health Facilities and Services Review Board. Append this document(s) to the application as **ATTACHMENT #5**.
15. **FINANCIAL STATEMENTS.** (Co-applicants must also provide this information) Provide a copy of the applicants latest audited financial statements, and append it to this application as **ATTACHMENT #6**. If the applicant is a newly formed entity and financial statements are not available, please indicate by checking YES _____, and indicate the date the entity was formed _____

16. **PRIMARY CONTACT PERSON.** Individual representing the applicant to whom all correspondence and inquiries pertaining to this application are to be directed. (Note: other persons representing the applicant not named below will need written authorization from the applicant stating that such persons are also authorized to represent the applicant in relationship to this application).

Name: Mitchell L. Johnson, Senior Vice President and Chief Strategy Officer, Memorial Health System
Address: 701 N. First Street City, State & Zip Code: Springfield, IL 62781
Telephone (217-788-3529) Ext. _____

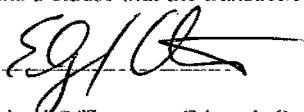
17. **ADDITIONAL CONTACT PERSON.** Consultant, attorney, other individual who is also authorized to discuss this application and act on behalf of the applicant.

Name: Michael I. Copelin, Copelin Healthcare Consulting
Address: 42 Birch Lake Drive
City, State & Zip Code: Sherman, IL, 62684
Telephone (217-496-3712) Ext. _____

18. **CERTIFICATION**

I certify that the above information and all attached information are true and correct to the best of my knowledge and belief. I certify that the number of beds within the facility will not change as part of this transaction. I certify that no adverse action has been taken against the applicant(s) by the federal government, licensing or certifying bodies, or any other agency of the State of Illinois. I certify that I am fully aware that a change in ownership will void any permits for projects that have not been completed unless such projects will be completed or altered pursuant to the requirements in 77 IAC 1130.520(f) prior to the effective date of the proposed ownership change. I also certify that the applicant has not already acquired the facility named in this application or entered into an agreement to acquire the facility named in the application unless the contract contains a clause that the transaction is contingent upon approval by the State Board.

Signature of Authorized Officer



Typed or Printed Name of Authorized Officer Edgar J. Curtis

Title of Authorized Officer: President and Chief Executive Officer, Memorial Health System

Address: 701 N. First Street,

City, State & Zip Code: Springfield, IL 62781

Telephone (217) 788-5450 _____ Date: December 19, 2013

NOTE: complete a separate signature page for each co-applicant and insert following this page.



Cindy Appenzeller
12/19/2013

19. CERTIFICATION

I certify that the above information and all attached information are true and correct to the best of my knowledge and belief. I certify that the number of beds within the facility will not change as part of this transaction. I certify that no adverse action has been taken against the applicant(s) by the federal government, licensing or certifying bodies, or any other agency of the State of Illinois. I certify that I am fully aware that a change in ownership will void any permits for projects that have not been completed unless such projects will be completed or altered pursuant to the requirements in 77 IAC 1130.520(f) prior to the effective date of the proposed ownership change. I also certify that the applicant has not already acquired the facility named in this application or entered into an agreement to acquire the facility named in the application unless the contract contains a clause that the transaction is contingent upon approval by the State Board.

Signature of Authorized Officer Chester A. Wynn

Typed or Printed Name of Authorized Officer Chester A. Wynn

Title of Authorized Officer: President and Chief Executive Officer, The Passavant Memorial Area Hospital Association

Address: 1600 West Walnut Street _____

City, State & Zip Code: Jacksonville, IL 62650

Telephone (217) 25-9541 (ext. 3112) _____ Date: December 31, 2013 _____

STATE OF ILLINOIS

COUNTY OF MORGAN

I certify that Chester A. Wynn, President and Chief Executive Officer of Passavant Area Hospital, appeared before me and placed his signature on the document above.

Teresa L. Jackson-Degroot

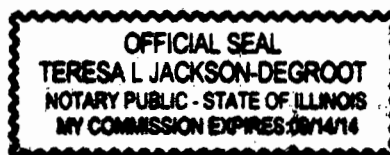
12/31/2013

TERESA L. JACKSON-DEGROOT

DATE

NOTARY PUBLIC

My commission expires 09-14-2014





701 North First Street • Springfield, Illinois 62781-0001
www.memorialmedical.com • Phone (217) 788-3000

December 31, 2013

Courtney R. Avery
Administrator
Illinois Health Facilities and Services Review Board
525 W. Jefferson - Second Floor
Springfield, Illinois 62761

Dear Ms. Avery:

Memorial Health System is a co-applicant with The Passavant Memorial Area Hospital Association for a Change of Ownership of a Health Care Facility project. Memorial Health System would become the sole corporate member and sponsor of The Passavant Memorial Area Hospital Association.

Pursuant to our application for a Certificate of Exemption for this Change of Ownership, Memorial Health System hereby affirms the following.

- That the categories of service and number of beds as reflected in the Inventory of Health Care Facilities will not substantially change for at least 12 months following the project's completion date.
- Memorial Health System certifies that no material adverse action has been taken against Memorial Health System by the federal government, licensing or certifying bodies, or any other agency of the State of Illinois against any health care facility owned or operated by Memorial Health System, directly or indirectly, within three years preceding the filing of this application.
- Memorial Health System intends to be the sole member of the The Passavant Memorial Area Hospital Association for a minimum of three years from the date it first becomes the sole member.
- Projects for which permits have been issued have been completed or will be completed or altered in accordance with the provisions of Section 1130.560.
- The Passavant Memorial Area Hospital Association will not adopt a more restrictive charity care policy than the policy that was in effect one year prior to the transaction and the compliant charity care policy will remain in effect for a two-year period, following the change of ownership transaction.
- Failure to complete the project in accordance with the applicable provisions of section 1130.500(d) no later than 24 months from the date of exemption approval (or by a later date established by the IHFSRB upon a finding that the project has proceeded with due diligence) and failure to comply with the material change requirements of this Section will invalidate the exemption.

Thank you for your consideration.

Sincerely,

A handwritten signature in black ink, appearing to read "EJC", written over a horizontal line.

Edgar J. Curtis
President and CEO
Memorial Health System



Cindy Appenzeller

12/31/2013

OFFICER'S AFFIDAVIT

REGARDING FAIR MARKET VALUE

I, Robert W. Kay, the duly authorized Chief Financial Officer of Memorial Health System, an Illinois not-for-profit corporation (the "**Corporation**"), hereby certify that to the best of my knowledge and belief, the fair market value of The Passavant Memorial Area Hospital Association is approximately \$83,500,000 based on its Earnings Before Interest, Depreciation and Amortization (EBIDA) and Unrestricted Net Assets as of September 30, 2013 which is current financial information available to me in my capacity as an officer of the Corporation, but not as a professional valuation expert.

Dated this 14th day of December, 2013.

Memorial Health System

By: Robert W. Kay

Name: Robert W. Kay

Its: Senior Vice President and Chief Financial
Officer



Cindy Appenzeller
12/19/2013

Attachment #1

Application Fee

A check for the \$2,500 Application Fee is attached and a copy appears on the next page of this attachment.

Attachment #2

Funding

There is no anticipated acquisition price involved in this transaction. The Passavant Memorial Area Hospital Association (PAH) and Memorial Health System signed an Affiliation Agreement on December 31, 2013 which entitled PAH to become an affiliated corporation of Memorial Health System. The transaction is expected to close by April 14, 2014, subject to regulatory approvals. The parties contemplate that Memorial Health System would become the Sole Corporate Member of PAH through a membership substitution; however Memorial Health System does not presently intend to add PAH to the Obligated Group and there will be no cash consideration paid or transferred to PAH to become a Memorial Health System affiliate, but there are post-closing operational and capital commitments to PAH by Memorial Health System.

Attachment #3

Narrative Description

The proposed project is limited to a change in membership of The Passavant Memorial Area Hospital Association and its licensed health care facility, The Passavant Memorial Area Hospital ("PAH"). PAH is a community hospital with 93 staffed acute beds located in Jacksonville, Illinois. Following the change in membership PAH will become a member of Memorial Health System ("MHS"), and MHS will become the sole corporate member of PAH.

PAH and MHS share a mission, overlapping service areas, and many physicians that practice at PAH and MHS affiliate Memorial Medical Center. The Applicants desire to enter into the Transaction in order to achieve and further the following objectives: 1) continue and strengthen the high-quality health care services each deliver; 2) meet the clinical, financial, and technological demands of delivering health care in Central Illinois; and 3) explore initiatives that enhance the missions and clinical, operational, management, and financial strengths of the Applicants. The Applicants believe Central Illinois residents will benefit from the Transaction through the comprehensive and integrated delivery system that will better serve their health care needs.

PAH and MHS expect that, for a minimum of one (1) year following the change in membership, all programs and services currently provided by PAH will continue to be provided. Consistent with Illinois Health Facilities and Services Review Board requirements, it is also expected that PAH's services will not be diminished.

The proposed project is classified as "non-substantive" as a result of the scope of the project being limited to a change of membership. The Transaction is expected to close on April 1, 2014.

Please refer to the Transaction Documents for a summary of the transaction.

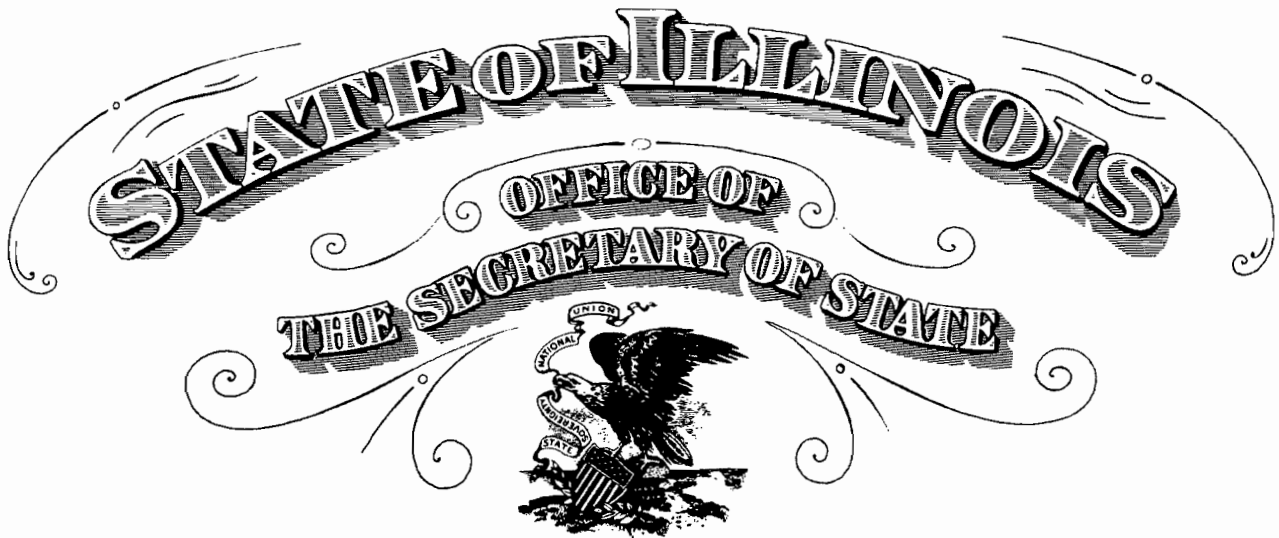
Attachment #4

Attachment #4

Certificate of Good Standing

The following are included in Attachment #4 on the four pages immediately following this page.

- 1) Certificate of Good Standing for the Co-Applicant Memorial Health System issued by the Illinois Secretary of State.
- 2) Certificate of Good Standing for Co-Applicant The Passavant Memorial Area Hospital Association issued by the Illinois Secretary of State.
- 3) Organizational chart for The Passavant Memorial Area Hospital Association prior to the transaction.
- 4) Organizational chart for The Passavant Memorial Area Hospital Association following the transaction.



To all to whom these Presents Shall Come, Greeting:

I, Jesse White, Secretary of State of the State of Illinois, do hereby certify that

MEMORIAL HEALTH SYSTEM, A DOMESTIC CORPORATION, INCORPORATED UNDER THE LAWS OF THIS STATE ON AUGUST 21, 1981, APPEARS TO HAVE COMPLIED WITH ALL THE PROVISIONS OF THE GENERAL NOT FOR PROFIT CORPORATION ACT OF THIS STATE, AND AS OF THIS DATE, IS IN GOOD STANDING AS A DOMESTIC CORPORATION IN THE STATE OF ILLINOIS.



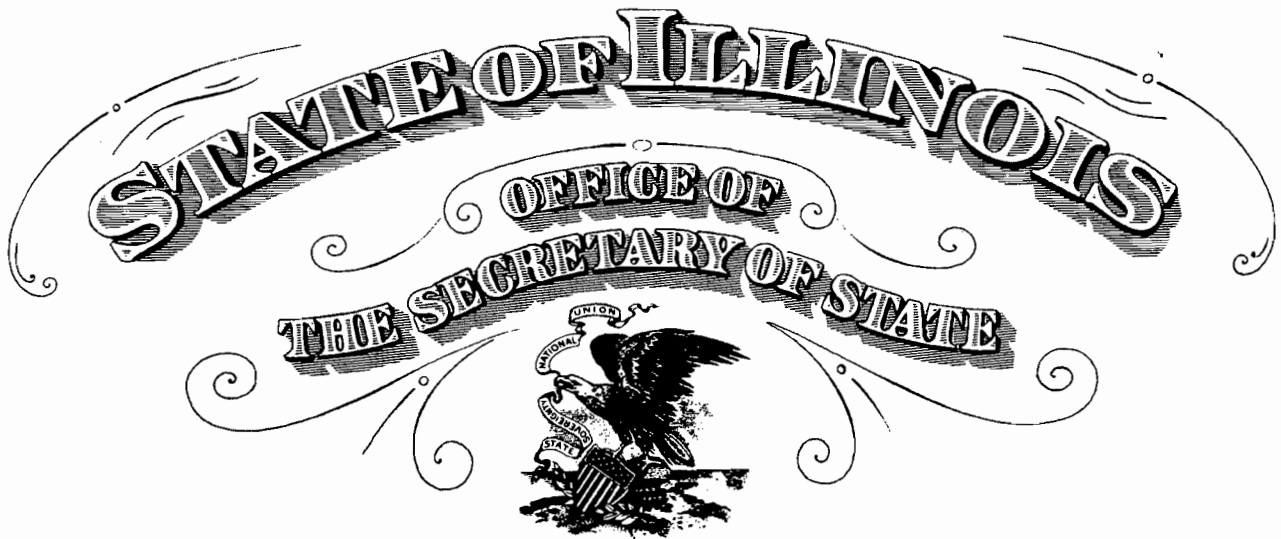
Authentication #: 1332501060

Authenticate at: <http://www.cyberdriveillinois.com>

In Testimony Whereof, I hereto set my hand and cause to be affixed the Great Seal of the State of Illinois, this 21ST day of NOVEMBER A.D. 2013 .

Jesse White

SECRETARY OF STATE



To all to whom these Presents Shall Come, Greeting:

I, Jesse White, Secretary of State of the State of Illinois, do hereby certify that

THE PASSAVANT MEMORIAL AREA HOSPITAL ASSOCIATION, A DOMESTIC CORPORATION, INCORPORATED UNDER THE LAWS OF THIS STATE ON APRIL 27, 1906, APPEARS TO HAVE COMPLIED WITH ALL THE PROVISIONS OF THE GENERAL NOT FOR PROFIT CORPORATION ACT OF THIS STATE, AND AS OF THIS DATE, IS IN GOOD STANDING AS A DOMESTIC CORPORATION IN THE STATE OF ILLINOIS.



Authentication #: 1332501708

Authenticate at: <http://www.cyberdriveillinois.com>

*In Testimony Whereof, I hereto set
my hand and cause to be affixed the Great Seal of
the State of Illinois, this 21ST
day of NOVEMBER A.D. 2013 .*

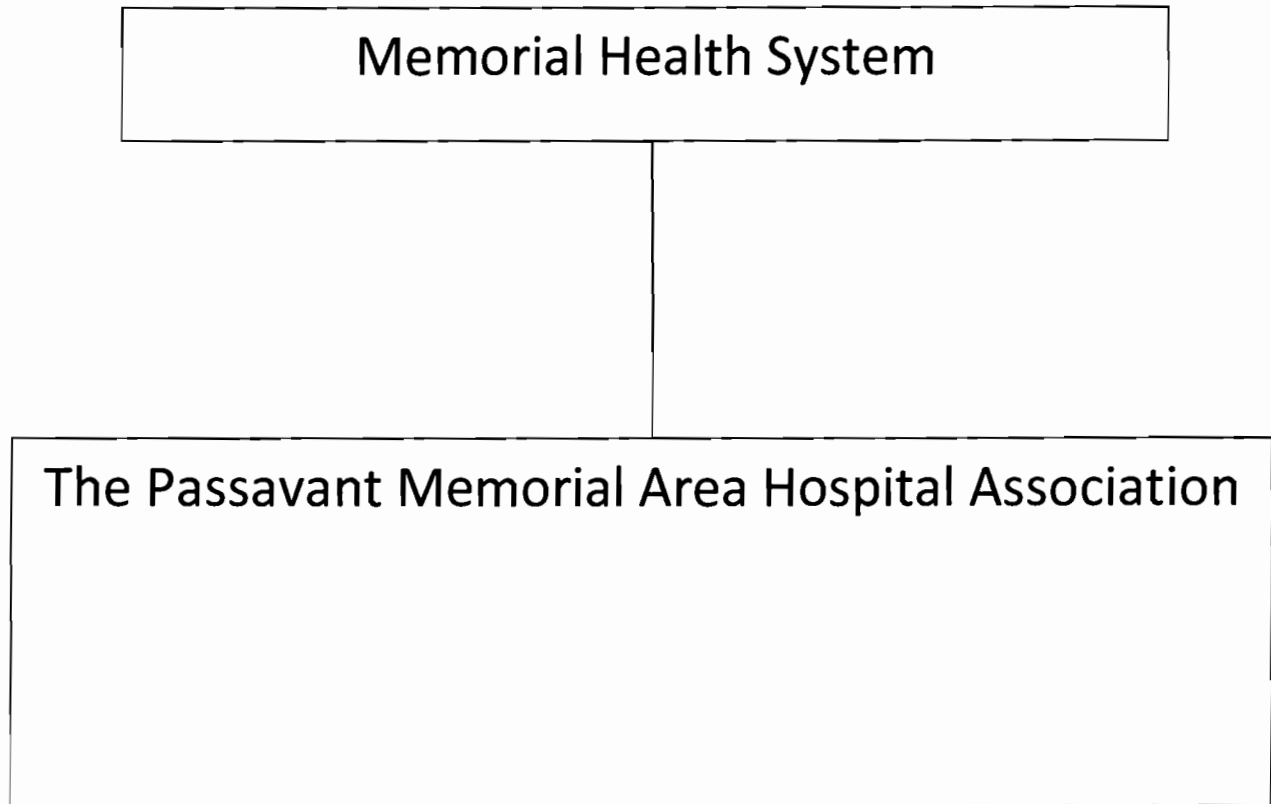
Jesse White

SECRETARY OF STATE

Before Transaction:

The Passavant Memorial Area Hospital Association

After Transaction:



Attachment #5

Transaction Documents

Included in Attachment #5 on the pages immediately following this page is a copy of the complete transaction document including schedules and exhibits which detail the terms and conditions of the proposed transaction. The "Affiliation Agreement" that follows is signed by both co-applicants (see two signature pages immediately following Article 15 which contains the Glossary of terms used in the agreement). Clauses stating that the transaction is contingent upon approval by the Illinois Health Facilities and Services Review Board appear in Articles 6.3.2, 7.3.2, 10.1.2 and 11.1.2.

The Affiliation Agreement includes 159 pages that follow.

CONFIDENTIAL

**AFFILIATION AGREEMENT
BY AND BETWEEN
MEMORIAL HEALTH SYSTEM,
THE PASSAVANT MEMORIAL AREA HOSPITAL ASSOCIATION,
PASSAVANT AREA HOSPITAL FOUNDATION,
PASSAVANT PHYSICIAN ASSOCIATION, INC. AND
JACKSONVILLE CRNA'S, INC.**

DECEMBER 31, 2013

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LIST OF EXHIBITS

<u>EXHIBIT</u>	<u>DESCRIPTION</u>
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B	Amended and Restated Bylaws of PAH Affiliates
B-1	Amended and Restated Bylaws of Passavant Area Hospital Foundation
B-2	Amended and Restated Bylaws of Passavant Physician Association, Inc.
B-3	Amended and Restated Bylaws of Jacksonville CRNAs, Inc.
C	Integration Task Force
D	Amended and Restated Bylaws of MHS

LIST OF SCHEDULES

<u>SCHEDULE</u>	<u>DESCRIPTION</u>
6.4.6	Employee Pension Plan Accounts
6.6	Interim Changes
6.8.2	Limitations on Licenses and Permits
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6.15	Insurance Coverage
6.17.1	Employee Benefit Plans
6.17.2	Benefit Plans Subject to Funding Rules
6.19	Accreditations
6.20	Material Contract Defaults
7.9.2	MHS Limitations on Licenses and Permits
7.12	MHS Interim Changes

AFFILIATION AGREEMENT

THIS AFFILIATION AGREEMENT (the "**Agreement**") is made and entered into on December 31, 2013 (the "**Execution Date**"), to be effective as of the Closing Date (as defined herein), by and between **MEMORIAL HEALTH SYSTEM**, an Illinois not-for-profit corporation ("**MHS**"), **THE PASSAVANT MEMORIAL AREA HOSPITAL ASSOCIATION D/B/A PASSAVANT AREA HOSPITAL**, an Illinois not-for-profit corporation ("**PAH**"), **PASSAVANT AREA HOSPITAL FOUNDATION**, an Illinois not-for-profit corporation ("**PAHF**"), **PASSAVANT PHYSICIAN ASSOCIATION, INC.**, an Illinois not-for-profit corporation ("**PPA**"), and **JACKSONVILLE CRNA'S, INC.**, an Illinois not-for-profit corporation ("**CRNA**"). MHS, PAH, PAHF, PPA and CRNA are each referred to herein as a "**Party**" and, collectively, as the "**Parties**" to this Agreement. PAHF, PPA and CRNA are referred to collectively as the "**PAH Affiliates**". The PAH Affiliates and PAH are referred to collectively as the "**PAH Entities**". ARTICLE 16 contains a glossary of all capitalized defined terms used in this Agreement.

RECITALS

A. MHS is the controlling member or shareholder of certain affiliated health care organizations including Memorial Medical Center (collectively, the "**MHS Affiliates**," which together with MHS are referred to collectively as the "**MHS Entities**").

B. PAH operates a general acute care hospital located in Jacksonville, Illinois, and the PAH Affiliates operate other affiliated health care businesses.

C. The MHS Entities and PAH Entities share a patient-centered culture committed to excellence, quality and transparency, and these entities' histories of sound governance and management, together with excellent physicians, nurses and other caregivers, have assured the delivery of exceptional care at each institution, resulting in their recognition as preferred hospitals and employers of choice that engage effectively with physicians and the community to achieve superior results.

D. MHS and PAH have engaged in discussions to explore the possibility of the PAH Entities affiliating with MHS to support and further their common and unifying health care missions and to better serve their respective communities.

E. As a result of such discussions, MHS and PAH entered into a Letter of Intent, dated October 4, 2013 ("**Letter of Intent**"), pursuant to which they set forth their preliminary understandings and agreements regarding the nature and terms of a potential affiliation whereby the PAH Entities would become part of the MHS system (the "**Affiliation**").

F. The Parties consider it to be consistent with their purposes, including, where applicable, their charitable purposes, and in the best interests of the communities they serve to become affiliated as described herein.

G. As contemplated by the Letter of Intent, the Parties wish to set forth the full and complete terms of their agreement with respect to the Affiliation between and among them and related matters.

NOW, THEREFORE, for and in consideration of the premises, and the agreements, covenants, representations and warranties hereinafter set forth, and other good and valuable consideration, the receipt and adequacy of which are forever acknowledged and confessed, the Parties agree as follows:

ARTICLE 1

AFFILIATION GOALS AND OBJECTIVES

The PAH Entities and MHS Entities share a mission of providing the highest quality health care services to the communities they serve in Central Illinois. The Parties believe that they will be in the best position to continue and strengthen the high-quality health care services they each deliver, and to meet the clinical, financial and technological demands of delivering health care in Central Illinois, by exploring initiatives that enhance the missions and clinical, operational, management and financial strengths of the PAH Entities and MHS Entities through the Affiliation. The Parties believe the Affiliation, among other things, will benefit the residents of Central Illinois by enabling them to undertake joint efforts to create a comprehensive and integrated delivery system that will better serve the health care needs of the residents of Central Illinois and, specifically, the residents of PAH's service area, through maintaining and enhancing the ability of PAH Entities to deliver state-of-the-art health care services in the communities they serve.

ARTICLE 2

IMPLEMENTATION OF AFFILIATION

2.1 Reorganization of PAH Entities. Effective as of the Closing Date, PAH shall amend its bylaws substantially in the form set forth as Exhibit A, pursuant to which MHS will become the sole member of PAH but the PAH Board of Governors ("**Governors**") will be retained as a nominating body. Effective as of the Closing Date, the PAH Entities shall amend the bylaws of the PAH Affiliates substantially in the form set forth in Exhibit B, pursuant to which PAH will be and remain the sole member of each PAH Affiliate with certain reserved powers over each such Affiliate.

2.2 Ownership. The Affiliation shall not affect the ownership, or result in the transfer or conveyance, of any asset owned as of the Closing Date by the PAH Entities. All assets, including all cash, cash equivalents and other assets (tangible or intangible, real or personal), owned or held in the name of the respective PAH Entities shall be and remain the property of the respective PAH Entity on the Closing Date.

2.3 Liabilities. All liabilities, indebtedness, commitments and other financial and operational obligations of the PAH Entities, whether known or unknown, fixed or contingent, recorded or unrecorded, existing as of the Closing Date or arising thereafter (each a "**PAH Liability**") and collectively, the "**PAH Liabilities**") shall be and remain the liabilities and obligations of the PAH Entities, respectively, from and after the Closing Date. The PAH Liabilities shall include, without limitation, liabilities, indebtedness, commitments, encumbrances, obligations, notes, loan agreements, indentures, mortgages, security agreements,

debt service reserve fund agreements, financing statements, subordination agreements, of the PAH Entities, existing as of the Closing Date or arising thereafter. The Affiliation will not cause any MHS Entity to become obligated upon or assume any PAH Liability, and will not cause any MHS Entity assets to become liable for or subject to any PAH Liability. Notwithstanding the above, a key purpose of the Affiliation is to obtain MHS's assistance in improving the health of the communities served by PAH, and actions taken pursuant to the respective entities' Governing Documents and this Agreement after the Closing Date may result in MHS providing financial assistance from MHS to PAH Entities.

2.4 Integration Task Force. Following the Execution Date, MHS and PAH will establish an Integration Task Force and work groups as set forth in Exhibit C to develop recommended plans, strategies, priorities, and timetables for post-closing integration, consistent with compliance with antitrust requirements. The Task Force will address, among others, the tasks and subject matter areas set forth on Exhibit C, which include capital planning, physician integration and recruitment, employee integration, information technology integration (including the matters set forth in Section 4.4 of this Agreement), analysis and prioritization of the operational initiatives set forth in Section 4.8 of this Agreement, capital finance planning, and streamlining and integration of management services. Any material recommendations of the Task Force must be mutually agreeable to MHS and to the PAH Board before they are finalized and implemented. The Task Force's work will continue through and after the Closing Date.

ARTICLE 3

GOVERNANCE

3.1 PAH Entity Boards. The individuals who are the members of the Boards of Directors of each PAH Entity (each, a "Board") immediately preceding the Closing Date shall be and remain the members of the Board of each respective PAH Entity as of the Closing Date. The Chair, Vice Chair, Treasurer, Secretary, and assistant officers of each PAH Entity shall retain such positions as of the Closing Date.

3.2 Post-Closing PAH Board. The amended bylaws of PAH to be effective as of the Closing Date (the "**Amended PAH Bylaws**") shall contain the following provisions concerning its Board:

3.2.1 Any vacancies in or replacements to the PAH Board will be filled through nomination by the Governors, recommendation by the PAH Board, and approval by MHS.

3.2.2 Members of the PAH Board may be removed with or without cause by the vote of at least two-thirds (2/3) of all of the PAH Board members then in office.

3.2.3 MHS may remove members of the PAH Board, but only for cause. A PAH director's breach of his or her fiduciary duty to PAH shall be the sole cause for removal.

3.3 Post-Closing PAH Affiliate Boards. The amended bylaws of the PAH Affiliates to be effective as of the Closing Date (collectively, the "**Amended PAH Affiliate Bylaws**") shall

provide that the PAH Board shall have the power to appoint and remove the Boards of each Affiliate.

3.4 MHS Board. Effective as of the Closing Date, MHS shall amend and restate its bylaws substantially in the form set forth in Exhibit D (collectively, the “**Amended MHS Bylaws**”) to add two directors who are residents of the PAH service area, nominated by the PAH Board and appointed by MHS. The Amended MHS Bylaws will provide that such directors are subject to the MHS Board member credentialing and approval process.

3.5 President/CEO of PAH. The current President and Chief Executive Officer of PAH (“**PAH President**”) intends to retire no later than the Closing Date. Between the Execution Date and Closing Date, the Parties desire to identify a new PAH President who shall reside full-time in the Jacksonville, Illinois area as soon as practicable following his/her hire date. The new PAH President shall be an employee of MHS and a member of the MHS leadership team with authority and responsibility for, among other things, PAH. The PAH President shall have a dual reporting relationship (i) to the MHS President and Chief Executive Officer (or his designee) and (ii) to the PAH Board. The PAH President shall be appointed by, and may be removed by, MHS, but only upon mutual agreement with the PAH Board.

3.6 Future Governing Document Amendments. Neither PAH nor MHS shall amend the Amended PAH Bylaws, Amended PAH Affiliate Bylaws, or the Amended MHS Bylaws to modify the provisions set forth in this ARTICLE 3, except as set forth in such amended bylaws.

ARTICLE 4

MHS POST-CLOSING COMMITMENTS

4.1 Employment of PAH Entity Employees. The Parties agree that as of the Closing Date, the employees in good standing of the PAH Entities as of such date (the “**Employees**”) shall continue to be employed by the applicable PAH Entity following the Closing Date for a period of not less than twelve (12) months. Such employment shall be in the same position and location, at the same pay rates and with the same employee benefits and seniority as such Employees have at the Closing Date. “Employees” shall not include individuals with written employment contracts, whose employment shall be governed by their respective contract terms. Nothing herein is intended to restrict the right of: (a) the PAH Entities to terminate any Employee or engage in staff reductions or consolidations prior to the Closing Date (to the extent such actions are consistent with the then current applicable policies and procedures and Applicable Law); or (b) the PAH Entities to terminate any Employee or engage in staff reductions or consolidations at and following the Closing Date (to the extent such actions are consistent with the then current applicable policies and procedures, including MHS system-wide policies, and Applicable Law). All current Employee benefit plans described in Schedule 6.17.1 shall remain in effect at and after the Closing Date until the same are amended, modified, replaced or terminated in accordance with the provisions of those benefit plans, as approved by MHS and the PAH Board.

4.2 Continued Operations. The Parties intend that PAH will continue to operate as a state-of-the-art, general acute care hospital serving the Jacksonville community. In its exercise of its reserved powers to approve budgets, plans, debt, and major expenditures, MHS will act in support of this objective.

4.3 Capital Expenditures. MHS will include in the annual and long-term capital budgets it approves for PAH expenditures a minimum annual routine capital expenditure amount equal to capital depreciation for the budgeted year plus ten percent, subject to PAH financial and operational performance and its system-wide budget.

4.4 IT Commitment. MHS will fund capital and cash fund requirements solely from MHS's funds for the conversion of PAH's hospital information technology systems and the physician information technology systems from McKesson to MHS's systems (including Cerner for inpatient and AllScripts for ambulatory). This systems conversion shall be planned as part of the Integration Task Force and implementation shall commence promptly following the Closing Date. If, and to the extent, other PAH software systems, such as outpatient, ED, lab, radiology, financial and billing, cannot be maintained efficiently and effectively with the systems conversion, such software systems shall be converted to MHS's systems. MHS will fund such software systems conversions solely from MHS's funds.

4.5 Hospital Services and Programs in PAH Service Area. PAH will have a right of first refusal for all hospital services or programs that the Parties desire to undertake in PAH's primary service area.

4.6 Quality Improvement. MHS will assist PAH with improving quality and patient satisfaction scores on the Medicare Value-Based Purchasing Programs.

4.7 Debt. MHS will assist PAH with renewing or replacing its outstanding bank qualified debt with Comerica Bank prior to December, 2015.

4.8 Operational Initiatives. Within twelve (12) months following the Closing Date, the Integration Task Force will complete an evaluation of the high priority needs previously identified by the PAH Board, including documentation of business need and examination of financial feasibility. The Integration Task Force's findings will inform the overall budgets and plans developed and approved by PAH and MHS pursuant to MHS's reserved powers, provided, however, that if the Integration Task Force does not document business need and financial feasibility of any of the high priority needs, MHS shall not be required to pursue them. The identified high priority needs are:

4.8.1 conversion of PAH to all private rooms;

4.8.2 the establishment of primary care clinics in outlying referral areas (e.g., Beardstown, Winchester, Roodhouse and Whitehall), consistent with the Physician Recruitment Plan (defined below);

4.8.3 expanded cancer care for patients in the community, including development of a Cancer Registry;

4.8.4 expansion of temporary pacemaker insertion services and electrocardiogram and echocardiogram interpretations;

4.8.5 addressing the issues outlined in the Community Health Needs Assessment of Morgan County 2013-2015 done in conjunction with the Morgan County Health Department;

4.8.6 the provision of inpatient dialysis at PAH;

4.8.7 a formal and regular infectious disease and nephrology consult arrangement at PAH; and

4.8.8 establishing a regulatory compliant compensation model to incentivize physicians employed by MHS to utilize PAH's clinical services and programs and work with Springfield Clinic to do the same.

4.9 Physician Recruitment. Within six (6) months following the Closing Date, the Integration Task Force will develop a "**Physician Recruitment Plan**," including documentation of business need and examination of financial feasibility, and alternative ways of meeting needs. The Physician Recruitment Plan will inform the overall budgets and plans developed and approved by PAH and MHS pursuant to MHS's reserved powers.

4.10 BJC Collaborative. PAH will be entitled to participate in services and other benefits provided by the BJC Collaborative to the same extent as other MHS affiliates. Opportunities for participation in the BJC Collaborative will be addressed as part of the Integration Task Force evaluation.

4.11 Branding. PAH will retain use of the "Passavant Area Hospital" name and logo unless and until the PAH Board approves otherwise.

4.12 Local Vendor Relationships. MHS will use commercially reasonable efforts to use local vendors, contractors and firms to purchase or otherwise obtain products and services, subject to the Parties' mutual goal of achieving efficiencies.

ARTICLE 5

OPERATIONAL ASPECTS OF THE AFFILIATION

5.1 Medical Staff; Physician Integration.

5.1.1 The Affiliation shall not affect or change the medical staff status or privileges held by individuals who are members of the medical staff of PAH as of the Closing Date. Members of PAH's medical staff will not be required to re-apply as a result of the closing of the Affiliation, except as otherwise required by PAH's medical staff bylaws with respect to expiration of medical staff appointments or credentials. Any amendments to the PAH medical staff bylaws must be approved by the PAH Board and the PAH Medical Staff.

5.1.2 The Parties will work together before and after the Closing Date through the Integration Task Force to determine how best to clinically integrate PAH's employed and affiliated physicians with MHS physician services so as to provide the best possible services to residents of PAH's service area while using physician resources most efficiently. It is anticipated that the physicians employed by PPA will continue to be employed by PPA pursuant to their employment agreements, and over time the physicians will be integrated into Memorial Physician Services or, if applicable and agreed upon by the Springfield Clinic, the Springfield Clinic.

5.1.3 As of the Execution Date, each active PAH physician medical staff member may apply to, and subject to meeting credentialing requirements, join as a participating physician in Health Alliance Medical Plan.

5.2 Charitable Assets and Donor-Restricted Funds. Following the Closing Date:

5.2.1 To the extent any property was given, devised, or bequeathed to PAH Entities for charitable purposes, such property will be administered by PAH Entities in accordance with those purposes.

5.2.2 Bequests, gifts and endowments of the PAH Entities that are restricted as to use or manner of investment shall continue to be so restricted, and PAH Entities shall honor donative intent with respect thereto.

5.2.3 Grants or contributions received on or after the Closing Date that are restricted for use by a PAH Entity or at a PAH Entity facility shall belong to or be the property of such PAH Entity.

5.3 Integration of Non-Clinical Operations. The Parties agree that integration of the non-clinical operations of the PAH Entities and the MHS Entities may present opportunities for cost savings and improved service and operating efficiencies. The Integration Task Force will consider whether and how PAH Entity non-clinical operations may be integrated with those of MHS. The Parties anticipate that MHS will provide certain management, administrative or other services to PAH Entities at the direction of senior management of MHS, with such services determined on a collaborative and mutually acceptable basis between MHS and the PAH Board. As services are provided to PAH Entities, MHS shall allocate the cost of such services to PAH Entities based upon a reasonable and equitable allocation methodology consistent with the methodology applied to all of the MHS Affiliates, provided, however, that MHS will only charge direct costs for a transition period of twelve (12) months following the Closing Date and that thereafter allocation will be as budgeted in consultation with the PAH Board; and provided, further, that MHS expenditures used to fulfill the IT commitments set forth in Section 4.4 will not be included in direct or indirect costs considered in establishing such charges.

ARTICLE 6

REPRESENTATIONS AND WARRANTIES OF PAH ENTITIES

As of the Execution Date and as of the Closing Date, the PAH Entities hereby jointly and severally represent and warrant as follows:

6.1 Due Organization; Good Standing; Power.

6.1.1 Each of PAH, PAHF and CRNA is an Illinois not-for-profit corporation, exempt from federal income taxation under Section 501(a) of the Code, as an organization described in Section 501(c)(3) of the Code and is not a “private foundation” within the meaning of Section 509(a) of the Code. PPA is an Illinois not-for-profit corporation.

6.1.2 Each of the PAH Entities is duly formed, validly existing and in good standing under the laws of Illinois, and has the corporate power and authority to own, operate or hold under lease its properties and assets and to carry on its business and operations as presently conducted. Each of the PAH Entities has registered with the proper governmental authorities all assumed names under which it operates its business(es) and continuously maintained all such filings in good standing.

6.2 Corporate Authorization.

6.2.1 The PAH Entities have the full corporate power and authority to enter into and to perform its respective obligations under this Agreement.

6.2.2 The execution, delivery and performance of this Agreement by the PAH Entities have been duly and properly authorized by all necessary corporate action in accordance with its Governing Documents.

6.2.3 This Agreement constitutes the valid and legally binding obligation of the PAH Entities, enforceable against it in accordance with its terms, except as enforceability may be limited by: (a) general principles of equity, regardless of whether enforcement is sought in a proceeding in equity or at law; and (b) bankruptcy, insolvency, reorganization, moratorium or other similar laws of general application now or hereafter in effect relating to or affecting the enforcement of creditors’ rights generally.

6.3 No Violation; Approvals.

6.3.1 The execution, delivery and performance of this Agreement shall not result in the creation of any lien, charge, or encumbrance of any kind or the termination or acceleration of any indebtedness or other obligation of any PAH Entity, and is not prohibited by, does not violate or conflict with any provision of, and does not constitute a default under or breach of any Material Contract, indenture, mortgage, material permit or license, approval or other commitment to which any PAH Entity is a party or is subject or by which any such corporation is bound, or any Applicable Law.

6.3.2 Except for filings required pursuant to the Hart-Scott-Rodino Antitrust Improvements Act (“**HSR Act**”) and the IHFSRB, no approval, authorization, registration, consent, order or other action of or filing that has not occurred or been obtained with or from any person, including any court, administrative agency or other governmental authority, is required for the execution and delivery by the PAH Entities of this Agreement or the consummation by the PAH Entities of the transactions contemplated or required hereby.

6.4 Financial Statements.

6.4.1 PAH has provided MHS with: (a) audited financial statements of each of the PAH Entities for the two years ended September 30, 2012 and 2011 and the audited consolidated financial statements of the PAH Entities for the year ended September, 2012 (the “**Audited Financial Statements**”); and (b) unaudited financial statements of the PAH Entities for the interim period from October 1, 2012 through the most recent month end date for which financial statements were available prior to the Execution Date (the “**Unaudited Financial Statements**”). From the Execution Date to the Closing Date, by the twenty-fifth business day of the following month, PAH shall provide MHS with monthly unaudited financial statements of the PAH Entities for the immediately preceding month (the “**Interim Financial Statements**”, and together with the Audited Financial Statements and the Unaudited Financial Statements, the “**PAH Financial Statements**”). As soon as available, PAH shall provide MHS with the audited consolidated financial statements of the PAH Entities for the year ended September, 2013.

6.4.2 The PAH Financial Statements are: (a) true and correct in all material respects and present fairly the financial position of the PAH Entities, respectively, and the results of the respective operations of the PAH Entities at the dates and for the periods indicated; and (b) are in conformity with GAAP, applied consistently for the periods specified, including the consistent use of assumptions, practices, procedures and terminology, except that the Unaudited Financial Statements and the Interim Financial Statements need not contain any of the footnotes or other year-end adjustments required to comply with GAAP.

6.4.3 From and after October 1, 2012, the PAH Entities have not made any changes to their accounting methods or practices, including methods or practices used to:

- (a) Establish reserves on any patient and notes and accounts receivable;
- (b) Establish estimates of any third-party settlements;
- (c) Determine the value of any other accounts that require subjective determinations; and
- (d) Establish malpractice, general liability or other self-insurance reserves, including claims incurred but not reported.

6.4.4 The PAH Entities have no material liabilities or obligations of any kind, whether contingent or absolute, direct or indirect, or matured or unmatured, that are not shown or provided for in the PAH Financial Statements provided to MHS prior to the Execution Date, other than: (a) claims covered by insurance and any individual liability or obligation of less than \$100,000, provided such liabilities and obligations in the aggregate do not exceed \$1,000,000; or (b) liabilities arising in the ordinary course of business that are reflected on the Interim Financial Statements.

6.4.5 The PAH Financial Statements accurately reflect in all material respects donor-restricted funds or assets of the PAH Entities.

6.4.6 Except as set forth on Schedule 6.4.6, prior to the Closing Date, no PAH Entity has taken, or caused or permitted to be taken, any action that would change the legal or beneficial ownership status of the accounts in which funds of or attributable to employee pension plans of all PAH Entities are invested or otherwise held.

6.5 Accounts Receivable. All accounts receivable of the PAH Entities reflected on the PAH Financial Statements represent and constitute bona fide indebtedness owing to the PAH Entities for services actually performed or for goods or supplies actually provided in the amounts indicated on the PAH Financial Statements, with no known set offs, deductions, compromises, or reductions, other than reasonable allowances for bad debts and contractual allowances in an amount consistent with historical policies and procedures of PAH and that are taken into consideration in the preparation of the PAH Financial Statements. PAH has made available to MHS a complete and accurate aging report of all such accounts receivable and a schedule of all accounts receivable, whether recorded or unrecorded, that have been assigned to collection agencies or are otherwise held or assigned for collection.

6.6 Interim Changes. Except for matters expressly permitted or authorized by this Agreement or except as set forth on Schedule 6.6, there has not been, after the date of the most recent Audited Financial Statements:

6.6.1 Any Material Adverse Change to the PAH Entities taken as a whole;

6.6.2 Any disposition by the PAH Entities of any property, rights or other assets owned by or employed in the PAH Entities, except for dispositions in the usual and ordinary course of the business;

6.6.3 Any amendment of the Governing Documents of PAH Entities;

6.6.4 Any change to the makeup or composition of the senior managers of PAH, or Boards of the PAH Entities, other than in the ordinary course of business;

6.6.5 Any new Material Contract having a dollar value greater than \$500,000, or any termination or material amendment of any Material Contract having a dollar value greater than \$500,000, not previously disclosed to MHS; and

6.6.6 Any adoption or amendment of any bonus, profit sharing, incentive or severance agreement or arrangement, or any Benefit Plan, involving any officer, director or Employee of the PAH Entities.

6.7 Legal Proceedings. Except as previously disclosed to MHS, there is no claim, action, suit, proceeding or investigation pending or, to the Knowledge of PAH, threatened against or affecting a PAH Entity that could reasonably be expected to result in a Material Adverse Change in the PAH Entities in the aggregate or the ability of any of such entities to perform their respective obligations under this Agreement.

6.8 Licenses and Permits.

6.8.1 Each of the PAH Entities holds and is in material compliance with all material governmental licenses, permits, certificates, consents and approvals as are necessary to run their operations as currently operated (the “**Licenses and Permits**”). The Licenses and Permits are current, unrestricted and valid. PAH has made available to MHS copies of each License and Permit.

6.8.2 To PAH’s Knowledge, except as set forth Schedule 6.8.2, there are no pending or threatened proceedings that are reasonably likely to result in the revocation, termination, suspension or limitation of any of its Licenses and Permits.

6.9 No Material Omissions.

6.9.1 The PAH Entities have responded in all material respects to all requests for information and documentation made by MHS in connection with its due diligence review of the business, operations, assets and liabilities of the PAH Entities. PAH has not omitted any material information relating to the businesses, operations, assets or liabilities of the PAH Entities in their respective responses to MHS’s requests. Since the delivery of such responses to MHS, none of the PAH Entities has received and not disclosed any information that would render untrue or misleading in any material respect any information previously disclosed to MHS in response to its requests for information.

6.9.2 The representations and warranties of PAH contained in this Agreement, and each Exhibit, Schedule, certificate or other document delivered at Closing by PAH pursuant to this Agreement, are accurate, correct and complete in all material respects, do not contain any untrue statement of a material fact, or omit to state a material fact necessary in order to make the statements and information contained therein not misleading.

6.10 Compliance with Law. Each of the PAH Entities is in compliance with all Applicable Laws, including, without limitation, all Health Care Laws, in all material respects.

6.11 Title to Owned Real Property and Other Assets.

6.11.1 Schedule 6.11.1 lists all real property owned by any PAH Entity and used in connection with their current operations by common address and property tax identification number (the “**Owned Real Property**”). Except as set forth on Schedule 6.11.1, one [or more] of the PAH Entities is the sole and exclusive owner of all right, title and interest in and has good and marketable fee simple title to the Owned Real Property free and clear of all liens, mortgages, security interests, options, pledges, charges, covenants, conditions, restrictions and other encumbrances and claims of any kind or character whatsoever, other than Permitted Encumbrances. PAH Entities have furnished MHS with true and complete copies of owner’s title insurance policies issued for each Owned Real Property and the recorded vesting deed for each Owned Real Property. There are no outstanding options, right of first refusal or rights of first offer to purchase any Owned Real Property or any portion thereof or interest therein. Except as described on Schedule 6.11.1, with respect to the Owned Real Property:

(a) No PAH Entity has received during the past three years notice of a material violation of any Applicable Law, and no PAH Entity has received notice of condemnation, lien, assessment or the like relating to any part of the Owned Real Property or the operation thereof;

(b) There are no tenants or other persons or entities occupying any space in the Owned Real Property, or claiming any possession, adverse or not, to any portion of the Owned Real Property, other than pursuant to written tenant leases with an PAH Entity;

(c) Each parcel of Owned Real Property is either: (i) exempt from real property or ad valorem taxation pursuant to Section 15-65 of the Property Tax Code (35 ILCS 200/15-65), and the PAH Entities have received no notice and have no Knowledge that the status of such Owned Real Property will change from exempt to taxable; or (ii) separately assessed for real estate tax purposes and is not combined with any land or real estate that is not a part of the Owned Real Property for real estate tax assessment purposes, and the PAH Entities have not received any notice of change in assessed value that is not reflected in Owned Real Property tax bills furnished to MHS;

(d) No portion of any Owned Real Property is located within an area that has been identified by the Federal Emergency Management Agency as an area having special flood or mudslide hazards as such term is used in the National Flood Insurance Act of 1968, as amended and supplemented by The Flood Disaster Protection Act of 1973, and in regulations, interpretations and rulings thereunder;

(e) All permanent certificates of occupancy and all other material licenses, permits, authorizations, consents, certificates and approvals required by all governmental authorities having jurisdiction and the requisite certificates of the local board of fire underwriters (or other body exercising similar functions) have been issued for the Owned Real Property (and all individual items constituting the Owned Real Property), have been paid for, are in full force and effect, and, to the Knowledge of PAH, will not be invalidated, violated or otherwise adversely affected by any change of control or ownership of any PAH Entity;

(f) PAH has made available to MHS complete copies of all engineering assessments and construction contracts that have been prepared by or at the direction of the PAH Entities within the last three years relating to any of the Owned Real Property and still in possession of the PAH Entities and there are to the Knowledge of PAH no facts or conditions affecting any PAH Entity that would, individually or in the aggregate, interfere in any material respect with the use or occupancy of the Owned Real Property improvements or any portion thereof in the operation of the business as currently conducted thereon;

(g) No PAH Entity has received any notice of any existing, proposed or contemplated plans to modify or realign any street or highway or any existing, proposed or contemplated eminent domain proceeding that would result in the taking of all or any part of the Owned Real Property or that would materially adversely affect the current use of any part of the Owned Real Property;

(h) The use or occupancy of the Owned Real Property or any portion thereof and the operation of business as currently conducted is not dependent on a "permitted non-conforming use" or "permitted non-conforming structure" or similar variance, exemption or approval from any governmental entity; and the current use and occupancy of the Owned Real Property and the operation of the business as currently conducted thereon does not violate in any material respect any easement, covenant, condition, restriction or similar provision in any instrument of record or other unrecorded agreement affecting such Owned Real Property. Upon consummation of the transactions contemplated by this Agreement, the owners of the Owned Real Property will be entitled to continue to use any Owned Real Property that is currently employed by the PAH Entities in the conduct of their operations as currently conducted;

(i) All water, oil, gas, electrical, steam, compressed air, telecommunications, sewer, storm and waste water systems and other utility services or systems for the Owned Real Property have been installed and are operational and sufficient for the operation of the business as currently conducted thereon. The PAH Entities have not received notice of discontinuance of or reduction in such services; and

(j) The Owned Real Property is subject to no easements, conditions, restrictions, ordinances, or other limitations that would make such property unusable for its current use or the title to such property unmarketable or materially restrict or impair the current use or operation of the business in a manner consistent with the current use, or that would require the removal of any improvements; except for such easements, conditions, restrictions, ordinances, or other limitations that individually would not materially impair the value or the continued use and operation of the Owned Real Property as presently conducted by the PAH Entities.

6.11.2 Except as previously disclosed to MHS: (a) the PAH Entities have not received any notice or complaint within the prior three (3) years or that is outstanding or unresolved alleging or asserting a material violation of any Environmental Law, an obligation to investigate, assess, abate, remove, or remediate any Hazardous Substances on any part or all of the Owned Real Property under or pursuant to any Environmental Law or that any of the PAH Entities are or may be liable as a potentially responsible party under CERCLA. To the Knowledge of PAH; (b) the PAH Entities have not possessed, managed, processed, released, handled or disposed of or discharged Hazardous Substances, except in material compliance with applicable Environmental Law; (c) prior owners, operators or occupants of the Owned Real Property have not caused or allowed any Hazardous Substances to be discharged, possessed, managed, processed, released, or otherwise handled on the Owned Real Property in material violation of any Environmental Law; (d) the PAH Entities are complying and, for the previous three (3) years, have complied in all material respects with all applicable Environmental Law and all Licenses and Permits issued pursuant to any Environmental Law; (e) the Owned Real Property does not contain asbestos containing material in a form or condition for which abatement, repair or removal is required by applicable Environmental Law; and (f) the PAH entities have not received any complaint, inquiry or report within the prior three (3) years or that is outstanding or unresolved alleging that the indoor air quality inside any buildings on the Owned Real Property is potentially harmful or unsafe or that there are potentially elevated levels of toxic mold or fungus present inside any buildings on the

Owned Real Property. PAH shall promptly notify MHS should it obtain Knowledge, prior to the Closing Date, of any lien, written notice, litigation, or threat of litigation relating to any actual or alleged violation of Environmental Law or any alleged or actual unauthorized release, spill, disposal or discard of any Hazardous Substance. Except as set forth on Schedule 6.11.2, to the Knowledge of PAH, none of the PAH Entities has sent, arranged for disposal or treatment, arranged with a transporter for transport for disposal or treatment, transported, or accepted for transport any Hazardous Substances, to a facility, site or location, that, pursuant to CERCLA or any similar state or local law: (i) has been placed or has been publicly proposed by authorities having jurisdiction to be placed, on the CERCLA National Priorities List or its state equivalent; or (ii) is subject to a claim, administrative order or other demand to take removal or remedial action by any person having jurisdiction and authority in the matter. Without in any way limiting the generality of the foregoing: (y) all current or former underground storage tanks located on the Owned Real Property and all information in PAH Entities' possession relating to the capacity, uses, dates of installation and contents of such underground storage tanks located on the Owned Real Property have been previously provided to MHS; and (z) all existing underground storage tanks used by the PAH Entities to store Hazardous Substances are in compliance in all material respects with applicable Environmental Law. The PAH Entities have provided to MHS all Phase I reports, Phase II reports, asbestos surveys, tank closure reports, indoor air assessments, environmental compliance audits, Occupational Safety and Health Administration compliance audits or similar environmental reports in the possession, custody or control of the PAH Entities with respect to the Owned Real Property or any other property currently or formerly owned or operated by any of the PAH Entities.

6.12 Title to Assets. Except as disclosed on Schedule 6.12, other than Owned Real Property that is provided for in Section 6.11.1, each of the PAH Entities has good and defensible title to all of its assets of every kind, character and description, whether personal, tangible or intangible, used in connection with the operation of the businesses of the respective PAH Entities, free and clear of all liens, mortgages, security interests, options, pledges, charges, covenants, conditions, restrictions and other encumbrances and claims of any kind or character whatsoever, other than Permitted Encumbrances.

6.13 Affiliates and Subsidiaries. Each of PAH's wholly controlled affiliates and subsidiaries are party to this Agreement.

6.14 Tax Exempt Status. The IRS has not taken, or, to the Knowledge of PAH, proposed to take, any action to revoke the tax-exemption of any of the tax-exempt PAH Entities, and has not determined in writing or, to the Knowledge of PAH, proposed to announce, that any of the PAH Entities is a "private foundation" within the meaning of Section 509(a) of the Code. There has been no change in the organization or operation of any of the tax-exempt PAH Entities that would result in a loss of a PAH Entity's status as an organization described in Section 501(c)(3) of the Code or that could cause a PAH Entity to be treated as a "private foundation" within the meaning of Section 509(a) of the Code.

6.15 Insurance. Schedule 6.15 sets forth an accurate, correct and complete list (including the name of the insurer, coverage, and expiration date) of all binders and policies of insurance maintained by the PAH Entities, under which a PAH Entity is a named insured or that

otherwise insure assets used primarily in connection with the operation of the PAH Entities (collectively, the "**Insurance Policies**"). Except as set forth on Schedule 6.15, the Insurance Policies are in full force and effect and shall remain in full force and effect through the Closing Date.

6.16 Taxes. The PAH Entities have filed, or shall file, all returns, declarations, and reports and all information returns and statements required to be filed or sent with respect to all Taxes for all periods preceding the Closing Date (collectively, the "**Returns**"). As of the time of filing, the Returns correctly reflected, and Returns prepared or being prepared but not yet filed as of the Execution Date, shall correctly reflect, the income, business, assets, operations, activities and status of the PAH Entities and any other information required to be shown therein. Each PAH Entity has timely paid or made provision for all Taxes shown as due and payable on its Returns required to be filed or sent prior to the Execution Date and has made provision for timely payment of all Taxes that shall be shown as due and payable on its Returns required to be filed or sent by it after the Execution Date and relating to any period prior to the Closing Date.

6.17 Employee Benefits.

6.17.1 Schedule 6.17.1 sets forth an accurate, correct and complete list of all "employee welfare benefit plans" (as defined in Section 3(1) of ERISA), "employee pension benefit plans" (as defined in Section 3(2) of ERISA), and all other employee benefit plan agreements and arrangements and employee benefit policies, whether funded or unfunded, qualified or nonqualified, subject to ERISA or not, maintained or contributed to (or required to be contributed to) by PAH Entities for the benefit of any of its officers, employees or other persons (all the foregoing being herein referred to as "**Benefit Plans**"). The PAH Entities have made available to MHS the following:

- (a) Each Benefit Plan and all amendments thereto;
- (b) The most recent annual reports on Form 5500, if required, filed with the IRS or the Department of Labor with respect to any Benefit Plan, including all schedules and attachments;
- (c) Each insurance contract relating to any Benefit Plan and any amendments thereto;
- (d) The most recent certified financial statements relating to each Benefit Plan, as applicable, and the most recent actuarial reports for any Benefit Plan that is a tax qualified defined benefit pension plan;
- (e) The summary plan description and all summaries of material modifications for each Benefit Plan;
- (f) All collective bargaining agreements or other such contracts, including any riders or amendments thereto; and

(g) Each determination letter, ruling letter or any outstanding ruling request on the tax exempt status of any qualified Benefit Plan or any voluntary employees' beneficiary association implementing a Benefit Plan.

6.17.2 All contributions to, and payments from, the Benefit Plans required to be made in accordance with the terms of the Benefit Plans and Applicable Law have been timely made. Except for those Benefit Plans disclosed on Schedule 6.17.2, no Benefit Plan is subject to the funding rules of Section 302 of ERISA or Section 412 of the Code.

6.17.3 All Benefit Plans (and all related trust agreements or annuity contracts or any funding instruments) have been administered in accordance with their terms and materially comply currently, and have materially complied in the past, both as to form and operation, with the provisions of applicable tax laws, the Code and Applicable Law. To the extent that any Benefit Plan is a tax qualified retirement plan, it has been maintained and administered in accordance with its terms and the provisions of applicable tax laws and the Code, where required for the Benefit Plan to be tax qualified under Sections 401(a) and 501(a) of the Code, and all other Applicable Laws.

6.17.4 All reports, returns and similar documents with respect to the Benefit Plans required to be filed with any government agency or distributed to any Benefit Plan participant have been duly and timely filed or distributed. To the Knowledge of PAH, there are no threatened or pending investigations by any governmental agency, termination proceedings or other claims (except claims for benefits payable in the normal operation of the Benefit Plans), suits or proceedings against or involving any Benefit Plan or asserting any rights or claims to benefits under any Benefit Plan that could reasonably be expected to give rise to any material liability, nor are there any facts that could reasonably be expected to give rise to any material liability in the event of any such investigation, claim, suit or proceeding.

6.17.5 To the Knowledge of PAH, no "prohibited transaction" (as defined in Section 4975 of the Code or Section 406 of ERISA) has occurred that involves the assets of any Benefit Plan and that could reasonably be expected to subject any of the PAH Entities, or any of their respective employees, or a trustee, administrator or other fiduciary of any trust created under any Benefit Plan, to the tax or penalty on prohibited transactions imposed by Section 4975 of the Code or the sanctions imposed under Title I of ERISA. No Benefit Plan that has been terminated has or may cause liability to any of the PAH Entities.

6.18 Payment Programs. PAH has provided to MHS a list of all of the private, commercial and governmental payment and procurement programs with which the PAH Entities are participating providers (including, without limitation, Medicare and Medicaid) (the "Payment Programs").

6.18.1 No PAH Entity is engaged in termination proceedings as to its respective participation in any Payment Program, nor has any PAH Entity received notice that its current participation in any Payment Program is subject to any contest, termination or suspension as a result of alleged violations or any material noncompliance with participation requirements;

6.18.2 No PAH Entity has taken or committed to any action, entered into any agreement, contract or undertaking, or taken or omitted to take any other action of any nature whatsoever that was or is in material violation of any applicable Payment Program condition of participation, contract, standard, policy, rule, regulation, procedure or other requirement;

6.18.3 All billing and collection practices of each PAH Entity and, of any billing and/or collection agent acting on behalf of any PAH Entity, have been in material compliance with all Health Care Laws and the conditions for participation, contracts, standards, policies, rules, regulations, manuals, procedures and requirements of all Payment Programs;

6.18.4 All cost reports and cost statements submitted by the PAH Entities to any Payment Program are true, accurate and complete in all material respects and have been prepared and submitted in accordance with cost and accounting principles consistently applied that comply with all applicable Payment Program conditions for participation, contracts, standards, policies, rules, regulations, manuals, procedures and requirements, including, without limitation, Payment Program interpretations and guidance;

6.18.5 PAH has provided to MHS copies of all open cost reports and a description of their status;

6.18.6 No PAH Entity has taken any of the following actions: submitted to any Payment Program any false, fraudulent, abusive or improper claim for payment, billed any Payment Program for any service not rendered or not rendered as claimed, or received and retained any payment or reimbursement from any Payment Program in excess of the proper amount allowed by Applicable Law and applicable contracts or agreements with the Payment Programs;

6.18.7 There is no audit, investigation, adverse action, or civil, administrative, or criminal proceeding pending or, to the Knowledge of PAH, threatened relating to participation in any Payment Program by any PAH Entity; and, to the Knowledge of PAH, there is no basis for any such adverse action by the Payment Program against any PAH Entity;

6.18.8 Except as previously disclosed to MHS, no Payment Program has requested or, to the Knowledge of PAH, threatened any recoupment, refund, or set off from any PAH Entity, or imposed any fine, penalty or other sanction on any PAH Entity; and

6.18.9 The PAH Entities have complied, or will comply, in a timely manner with any material notice, approval, application, submission, filing or other requirements of the Payment Programs with respect to the transactions contemplated by this Agreement, including, without limitation, any transfer or change of ownership requirements.

6.19 Accreditation. PAH has provided to MHS a list of PAH's current accreditations by various accreditation organizations, including, without limitation, Joint Commission (collectively, the "**Accreditations**"). Except as set forth on Schedule 6.19: (a) all of the PAH Entities' accreditations by various accreditation organizations (including Joint Commission)

have been duly obtained, are held by the respective PAH Entities, are current and valid, and are in full force and effect; (b) to the Knowledge of PAH, no event has occurred or other fact exists with respect to the Accreditations that allows, or after notice or lapse of time or both would allow, revocation, suspension, restriction, limitation or termination of any of the Accreditations or would result in any other impairment of the rights of the holder of any of the Accreditations; (c) no notice from any accreditation organization in respect to the revocation, suspension, restriction, limitation or termination of any Accreditations has been issued, received or, to the Knowledge of PAH, proposed or threatened; and (d) no statement of deficiencies, survey report, inspection report, notice of audit, audit results, complaint or other notice of noncompliance with the requirements, standards or other conditions of any Accreditation has been issued, received or, to the Knowledge of PAH, proposed or threatened by any accreditation organization, for which any actual or potential payment or other obligation exists for which a plan of correction has not been submitted.

6.20 No Defaults. Except as listed on Schedule 6.20, no PAH Entity is in breach or default under any material term or provision of any Material Contract.

6.21 Compliance Program. PAH has provided to MHS a copy of PAH's current compliance program materials. Except as previously disclosed to MHS, PAH: (a) is not a party to a Corporate Integrity Agreement with the Office of Inspector General of the United States Department of Health and Human Services; (b) has no reporting obligations pursuant to any settlement agreement entered into with any federal, state or local government entity; (c) to the Knowledge of PAH, has not been the subject of any government payer program investigation conducted by any federal or state enforcement agency within the past three years; (d) has not been a defendant in any unsealed qui tam/False Claims Act litigation within the past three years; (e) has not been served with or received, within the past three years, any search warrant, subpoena, civil investigative demand, contact letter, or, to PAH's Knowledge, telephone or personal contact by or from any federal or state enforcement agency (except in connection with medical services provided to third parties who may be defendants or the subject of investigation into conduct unrelated to the operation of the health care businesses conducted by the PAH Entities); and (f) has not received, to PAH's Knowledge, any complaints within the past three years from employees, independent contractors, vendors, physicians, or any other person that resulted in a claim being filed with a federal, state or local government entity alleging that PAH has violated any law or regulation. To the Knowledge of PAH, there are no material irregularities nor are there any reasonable grounds to anticipate the commencement of any investigation or inquiry, or the assertion of any claim or demand by any governmental entity related to any activity, practice or policy of PAH, any claim for payment or reimbursement made by PAH, or any payment or reimbursement received by PAH. For purposes of this Agreement, the term "compliance program" refers to provider programs of the type described in the compliance guidance published by the Office of Inspector General of the Department of Health and Human Services.

6.22 Exclusion from Health Care Programs. Except as previously disclosed to MHS, neither any PAH Entity nor any of its respective officers, directors, agents or managing employees (as such term is defined in 42 U.S.C. § 1320a 5(b)) nor any other employee, agent or independent contractor of any PAH Entity has been: (a) excluded from participating in any Federal Health Care Program (as defined in 42 U.S.C. § 1320a 7b(f)); (b) subject to sanction or

been indicted or convicted of a crime, or pled nolo contendere or to sufficient facts, in connection with any allegation of violation of any Federal Health Care Program requirement or Health Care Law; (c) debarred or suspended from any federal or state procurement or nonprocurement program by any government agency; or (d) designated a Specially Designated National or Blocked Person by the Office of Foreign Asset Control of the U.S. Department of Treasury.

6.23 Medical Staff Matters. PAH has provided to MHS true, correct, and complete copies of the bylaws and rules and regulations of the medical staff of PAH, as well as a list of all current members of the medical staff. Except as previously disclosed to MHS: (a) there are no adverse actions with respect to any medical staff members of PAH or any applicant thereto for which a medical staff member or applicant has requested a judicial review hearing that has not been scheduled or has been scheduled but has not been completed; (b) there are no pending or, to the Knowledge of PAH, threatened disputes with applicants, staff members, or health professional affiliates, and PAH knows of no basis therefor; and (c) all appeal periods in respect of any medical staff member or applicant against whom an adverse action has been taken have expired. Notwithstanding the foregoing provisions of this Section 6.23, PAH shall not be required to disclose any information pursuant to this Section 6.23 where such disclosure is prohibited by state law or where such disclosure would, in PAH's reasonable discretion, potentially jeopardize any applicable privilege that would protect the disclosure of such information to third parties.

6.24 Experimental Procedures. The PAH Entities have not performed or permitted the performance of any experimental or research procedures or studies involving PAH patients not authorized and conducted in accordance with the procedures of the applicable Institutional Review Board.

6.25 Intellectual Property; Computer Software. No proceedings are pending or, to the Knowledge of PAH, threatened that challenge the validity of the ownership by the PAH Entities of any trademarks, service marks, trade names, patents, copyrights, and applications therefore (whether registered or common law) currently owned or used by the PAH Entities ("**Intellectual Property**"). The PAH Entities have not licensed anyone to use such Intellectual Property and PAH has no Knowledge of the use or the infringement of any such Intellectual Property by any other person. To the Knowledge of PAH, the PAH Entities own (or possesses adequate and enforceable licenses or other rights to use) all Intellectual Property and all computer software programs and similar systems used in the conduct of their businesses.

6.26 No Survival. None of the representations and warranties contained in this ARTICLE 6 shall survive the Closing.

ARTICLE 7

REPRESENTATIONS AND WARRANTIES OF MHS

As of the Execution Date and as of the Closing Date, MHS hereby represents and warrants, on its own behalf and on behalf of the MHS Affiliates, as follows:

7.1 Due Organization; Good Standing; Power.

7.1.1 MHS is an Illinois not-for-profit corporation, exempt from federal income taxation under Section 501(a) of the Code, as an organization described in Section 501(c)(3) of the Code and is not a "private foundation" within the meaning of Section 509(a) of the Code.

7.1.2 MHS and the MHS Affiliates are duly formed, validly existing and in good standing under the laws of the State of Illinois and have the corporate power and authority to own, operate or hold under lease its properties and assets and to carry on their business and operations as presently conducted.

7.2 Corporate Authorization.

7.2.1 MHS has the full corporate power and authority to enter into and to perform its obligations under this Agreement.

7.2.2 The execution, delivery and performance of this Agreement by MHS has been duly and properly authorized by all necessary corporate action in accordance with its Governing Documents.

7.2.3 This Agreement constitutes the valid and legally binding obligation of MHS, enforceable against it in accordance with its terms, except as enforceability may be limited by: (a) general principles of equity, regardless of whether enforcement is sought in a proceeding in equity or at law; and (b) bankruptcy, insolvency, reorganization, moratorium or other similar laws of general application now or hereafter in effect relating to or affecting the enforcement of creditors' rights generally.

7.3 No Violation; Approvals.

7.3.1 The execution, delivery and performance of this Agreement shall not result in the creation of any lien, charge, or encumbrance of any kind or the termination or acceleration of any indebtedness or other obligation of MHS, and is not prohibited by, does not violate or conflict with any provision of, and does not constitute a default under or breach of any material contract, indenture, mortgage, material permit or license, approval or other commitment to which MHS is a party or is subject or by which any such corporation is bound, or any Applicable Law.

7.3.2 To the Knowledge of MHS, except for filings required pursuant to the HSR Act and the IHFSRB, no approval, authorization, registration, consent, order or other action of or filing that has not occurred or been obtained with or from any person, including any court, administrative agency or other governmental authority, is required for the execution and delivery by MHS of this Agreement or the consummation by MHS of the transactions contemplated or required hereby.

7.4 Tax Exempt Status. The IRS has not taken, or, to the Knowledge of MHS, proposed to take, any action to revoke the tax-exemption of any of the tax-exempt MHS Entities, and has not determined in writing or, to the Knowledge of MHS, proposed to announce, that any

of the MHS Entities is a “private foundation” within the meaning of Section 509(a) of the Code. MHS has no Knowledge of any change in the organization or operation of any of the tax-exempt MHS Entities that would result in a loss of an MHS Entity’s status as an organization described in Section 501(c)(3) of the Code or that could cause an MHS Entity to be treated as a “private foundation” within the meaning of 509(a) of the Code.

7.5 Compliance Program. MHS has provided to PAH a copy of MHS’s current compliance program materials. Except as previously disclosed to PAH, MHS: (a) is not a party to a Corporate Integrity Agreement with the Office of Inspector General of the United States Department of Health and Human Services; (b) does not have reporting obligations pursuant to any settlement agreement entered into with any federal, state or local government entity; (c) to the Knowledge of MHS, has not been the subject of any government payer program investigation conducted by any federal or state enforcement agency within the past three years; (d) has not been a defendant in any unsealed qui tam/False Claims Act litigation within the past three years; (e) has not been served with or received, within the past three years, any search warrant, subpoena, civil investigative demand, contact letter, or, to MHS’s Knowledge, telephone or personal contact by or from any federal or state enforcement agency (except in connection with medical services provided to third parties who may be defendants or the subject of investigation into conduct unrelated to the operation of the health care businesses conducted by the MHS Entities); and (f) has not received, to MHS’s Knowledge, any complaints within the past three years from employees, independent contractors, vendors, physicians, or any other person that resulted in a claim being filed with a federal, state or local government entity alleging that an MHS Entity has violated any law or regulation.

7.6 Exclusion from Health Care Programs. Except as previously disclosed to PAH, no MHS Entity nor any of its respective officers, directors, agents or managing employees (as such term is defined in 42 U.S.C. §1320a 5(b)) nor any other employee, agent or independent contractor of any MHS Entity has been: (a) excluded from participating in any Federal Health Care Program (as defined in 42 U.S.C. § 1320a 7b(f)); (b) subject to sanction or been indicted or convicted of a crime, or pled nolo contendere or to sufficient facts, in connection with any allegation of violation of any Federal Health Care Program requirement or Health Care Law; (c) debarred or suspended from any federal or state procurement or nonprocurement program by any government agency; or (d) designated a Specially Designated National or Blocked Person by the Office of Foreign Asset Control of the U.S. Department of Treasury.

7.7 Legal Proceedings. Except as previously disclosed to PAH, there is no claim, action, suit, proceeding or investigation pending or, to the Knowledge of MHS, threatened against or affecting an MHS Entity that could reasonably be expected to result in a Material Adverse Change in the MHS Entities in the aggregate or the ability of any of such entities to perform their respective obligations under this Agreement.

7.8 Financial Statements. MHS has provided PAH with copies of the MHS Financial Statements consolidating all MHS Affiliates. The MHS Financial Statements are: (a) true and correct in all material respects and present fairly the financial position of the MHS Entities, respectively, and the results of the respective operations of the MHS Entities at the dates and for the periods indicated and (b) are in conformity with GAAP, applied consistently for the periods specified, including the consistent use of assumptions, practices, procedures and

terminology, except that the MHS Unaudited Financial Statements and the MHS Interim Financial Statements need not contain any of the footnotes or other year-end adjustments required to comply with GAAP.

7.9 Licenses and Permits.

7.9.1 Each of the MHS Entities holds and is in material compliance with all Licenses and Permits. The Licenses and Permits are current, unrestricted and valid.

7.9.2 To MHS's Knowledge, except as set forth Schedule 7.9.2, there are no pending or threatened proceedings that are reasonably likely to result in the revocation, termination, suspension or limitation of any of its Licenses and Permits.

7.10 No Material Omissions.

7.10.1 The MHS Entities have responded in all material respects to all requests for information and documentation made by PAH in connection with its due diligence review of the business, operations, assets and liabilities of the MHS Entities. MHS has not omitted any material information relating to the businesses, operations, assets or liabilities of the MHS Entities in their respective responses to PAH's requests. Since the delivery of such responses to PAH, none of the MHS Entities has received and not disclosed any information that would render untrue or misleading in any material respect any information previously disclosed to PAH in response to its requests for information.

7.10.2 The representations and warranties of MHS contained in this Agreement, and each Exhibit, Schedule, certificate or other document delivered at Closing by MHS pursuant to this Agreement, are accurate, correct and complete in all material respects, do not contain any untrue statement of a material fact, or omit to state a material fact necessary in order to make the statements and information contained therein not misleading.

7.11 Compliance with Law. To the Knowledge of MHS, each of the MHS Entities is in compliance with all Applicable Laws, including, without limitation, all Health Care Laws, in all material respects.

7.12 Interim Changes. Except for matters expressly permitted or authorized by this Agreement or except as set forth on Schedule 7.12, there has not been, after the date of the most recent MHS Financial Statements:

7.12.1 Any Material Adverse Change to the MHS Entities taken as a whole;

7.12.2 Any amendment of the Governing Documents of the MHS Entities;
and

7.12.3 Any change to the MHS Chief Executive Officer or Chief Operating Officer or makeup or composition of the Boards of the MHS Entities, other than in the ordinary course of business.

7.13 No Survival. None of the representations and warranties contained in this ARTICLE 7 shall survive the Closing.

ARTICLE 8

PRE CLOSING COVENANTS OF PAH

PAH hereby agrees to keep, perform and fully discharge, or to cause to be kept, performed and fully discharged, as applicable, the following covenants and agreements, as applicable:

8.1 Interim Conduct of Business. From the Execution Date to the Closing Date:

8.1.1 PAH shall and shall cause each PAH Affiliate to:

(a) Preserve, protect and maintain its business, properties and assets;

(b) Operate its businesses as a going concern, consistent with prior practices and not other than in the ordinary course of business;

(c) Preserve the goodwill of all individuals and entities having business or other relations with it or them, including, without limitation, physicians, employees, patients, customers and suppliers; and

(d) Obtain all documents called for by this Agreement and required to facilitate the consummation of the transactions contemplated by this Agreement.

8.1.2 PAH shall promptly provide MHS with the Interim Financial Statements as soon as such statements are available.

8.1.3 Neither PAH nor any of the PAH Entities shall enter into a Material Contract, subject to Applicable Law, unless they provide MHS with twenty-one (21) days' prior notification and such Material Contract has been reviewed by legal counsel to PAH.

8.1.4 Unless they provide MHS with prior notification, neither PAH nor any of the PAH Entities shall:

(a) Make any changes, or permit any changes to be made, in the Governing Documents of the PAH Entities, except for changes expressly authorized by this Agreement; or

(b) Enter into any transaction or contractual obligation that could have a Material Adverse Change in the businesses of the PAH Entities, except for transactions expressly authorized by this Agreement.

8.2 Preserve Accuracy of Representations and Warranties. From the Execution Date to the Closing Date:

8.2.1 PAH shall take no action that would render any representation or warranty contained in ARTICLE 6 inaccurate or untrue as of the Closing Date.

8.2.2 PAH shall promptly notify MHS of any lawsuits, claims, administrative actions or other proceedings asserted or commenced against any PAH Entity, or its officers, directors or member involving in any material way the ability of PAH to consummate the transactions contemplated or required by this Agreement, or materially affecting a PAH Entity's business, properties or its assets.

8.2.3 PAH shall, and shall cause the PAH Affiliates to promptly notify MHS in writing of any facts or circumstances that come to their attention and that cause, or through the passage of time may cause, any of the representations and warranties made by them and contained in ARTICLE 6 to be untrue or misleading at any time from the Execution Date to the Closing Date.

8.3 Access to Information.

8.3.1 From the Execution Date to the Closing Date, PAH shall give MHS and their representatives full and free access, during normal business hours, to all properties, books, records and contracts and other materials pertaining to the businesses, properties and assets of the PAH Entities, as may be reasonably requested and appropriate in order for such Parties to perform its obligations hereunder (and in accordance with guidelines approved by the Parties' antitrust counsel), subject to reasonable advance notice and provided that MHS shall not exercise such rights of access in such manner as would unduly interfere with the operations of the PAH Entities' personnel or the activities of PAH's patients or guests.

8.3.2 PAH shall cooperate in keeping the MHS Entities fully informed and shall promptly notify the MHS Entities of any Material Adverse Change in the normal course of business or prospects of any PAH Entity.

8.4 Maintain Books and Accounting Practices. From the Execution Date to the Closing Date, PAH shall maintain the books of account of the PAH Entities in the usual, regular and ordinary manner in accordance with GAAP consistently applied and on a basis consistent with prior years, including, without limitation, the consistent use of assumptions, practices, procedures and terminology, and, except as otherwise required by GAAP, and PAH shall not make or cause to be made any material changes in the accounting methods or practices of the PAH Entities.

8.5 Compliance with Laws. From the Execution Date to the Closing Date, PAH shall, and shall cause each of the PAH Affiliates to:

8.5.1 Comply with all Applicable Laws affecting the PAH Entities; and

8.5.2 Keep, hold and maintain all certificates, certificates of need, certificates of exemption, accreditation, licenses and other permits necessary for the conduct and operation of the PAH Entities.

8.6 Third Party Authorizations. From the Execution Date to the Closing Date, PAH shall, and shall cause the PAH Affiliates to, obtain expeditiously all consents, approvals and authorizations of third parties, whether governmental or private, make all filings, and give all notices which may be necessary or appropriate under Applicable Laws and under all contracts, agreements and commitments to which a PAH Entity is a party or is bound, or to the extent necessary for the valid execution, delivery and performance of this Agreement by PAH.

ARTICLE 9

PRE-CLOSING COVENANTS OF MHS

MHS hereby agrees to keep, perform and fully discharge, or to cause to be kept, performed and fully discharged, as applicable, the following covenants and agreements, as applicable:

9.1 Interim Conduct of Business. From the Execution Date to the Closing Date, MHS shall and shall cause each MHS Affiliate to:

9.1.1 Preserve, protect and maintain its business, properties and assets;

9.1.2 Operate its businesses as a going concern, consistent with prior practices and not other than in the ordinary course of business;

9.1.3 Preserve the goodwill of all individuals and entities having business or other relations with it or them, including, without limitation, physicians, employees, patients, customers and suppliers; and

9.1.4 Obtain all documents called for by this Agreement and required to facilitate the consummation of the transactions contemplated by this Agreement.

9.2 Preserve Accuracy of Representations and Warranties. From the Execution Date to the Closing Date:

9.2.1 MHS shall take no action that would render any representation or warranty contained in ARTICLE 7 inaccurate or untrue as of the Closing Date.

9.2.2 MHS shall promptly notify PAH of any lawsuits, claims, administrative actions or other proceedings asserted or commenced against any MHS Entity, or its officers, directors or member involving in any material way the ability of MHS to consummate the transactions contemplated or required by this Agreement, or materially affecting an MHS Entity's business, properties or its assets.

9.2.3 MHS shall, and shall cause the MHS Affiliates to, promptly notify PAH in writing of any facts or circumstances that come to their attention and that cause, or through the passage of time may cause, any of the representations and warranties contained in ARTICLE 7 to be untrue or misleading at any time from the Execution Date to the Closing Date.

9.3 Access to Information. From the Execution Date to the Closing Date, MHS shall give PAH and its representatives access pertaining to the businesses, properties and assets of the MHS Entities, as may be reasonably requested (and in accordance with guidelines approved by the Parties' antitrust counsel).

9.4 Compliance with Laws. From the Execution Date to the Closing Date, MHS shall, and shall cause each of the MHS Affiliates to:

9.4.1 Comply with all Applicable Laws affecting the MHS Entities; and

9.4.2 Keep, hold and maintain all certificates, certificates of need, certificates of exemption, accreditation, licenses and other permits necessary for the conduct and operation of the MHS Entities.

9.5 Third Party Authorizations. From the Execution Date to the Closing Date, MHS shall obtain expeditiously all consents, approvals and authorizations of third parties, whether governmental or private, make all filings, and give all notices which may be necessary or appropriate under Applicable Laws and under all contracts, agreements and commitments to which MHS is a party or is bound, or to the extent necessary for the valid execution, delivery and performance of this Agreement by MHS.

ARTICLE 10

CONDITIONS PRECEDENT TO OBLIGATIONS OF PAH

The obligations of PAH to consummate the transactions contemplated by this Agreement are, at the option of PAH, subject to the satisfaction, on or prior to the Closing Date, of the following conditions:

10.1 Regulatory Approvals. All regulatory consents and approvals required for the consummation of the transactions contemplated or required by this Agreement shall have been obtained on or before the Closing Date, including, without limitation:

10.1.1 Hart-Scott-Rodino. The Parties shall have submitted their respective filings under the HSR Act and all required waiting periods under the HSR Act shall have expired.

10.1.2 Health Planning. The Parties shall have obtained a certificate of exemption from the IHFSRB to consummate the Affiliation.

10.2 Performance of Covenants. MHS shall have performed all of the obligations and complied with each and all of the covenants, agreements and conditions required to be performed or complied with by it on or prior to the Closing Date.

10.3 No Pending Action. No action or proceeding before any court or governmental body shall be pending or threatened wherein an unfavorable judgment, decree or order would prevent the carrying out of this Agreement or any of the transactions contemplated hereby,

declare unlawful the transactions contemplated by this Agreement or cause such transactions to be rescinded.

10.4 No Bankruptcy. MHS shall not: (a) be in receivership or dissolution; (b) have made any assignment for the benefit of creditors; (c) have admitted in writing its inability to pay its debts as they mature; (d) have been adjudicated bankrupt; or (e) have filed a petition in voluntary bankruptcy, a petition or answer seeking reorganization or an arrangement with creditors under the federal bankruptcy law or any other similar law or statute of the United States or any state, nor shall any such petition have been filed against any MHS Entity.

10.5 Consents. All consents, approvals and authorizations of third parties required for the consummation of the transactions contemplated or required by this Agreement shall have been obtained on or before the Closing Date.

10.6 Absence of Material Adverse Change. There shall have been no Material Adverse Change in the financial or operating condition of the MHS Entities taken as a whole.

10.7 Delivery of MHS Closing Documents. MHS shall have delivered, on or before the Closing Date, the MHS Closing Documents.

10.8 Delivery of Other Agreements. MHS shall have executed and delivered all other agreements determined by the Parties to be necessary or appropriate to be entered into as of the Closing Date, relating to the Affiliation.

ARTICLE 11

CONDITIONS PRECEDENT TO OBLIGATIONS OF MHS

The obligations of MHS to consummate the transactions contemplated by this Agreement are, at the option of MHS, subject to the satisfaction, on or prior to the Closing Date, of the following conditions:

11.1 Regulatory Approvals. All regulatory consents and approvals required for the consummation of the transactions contemplated or required by this Agreement shall have been obtained on or before the Closing Date, including, without limitation:

11.1.1 Hart-Scott-Rodino. The Parties shall have submitted their respective filings under HSR Act, and all required waiting periods under the HSR Act shall have expired.

11.1.2 Health Planning. The Parties shall have obtained a certificate of exemption from the IHFSRB to consummate the transactions contemplated hereby.

11.2 Performance of Covenants. PAH shall have performed all of the obligations and complied with each and all of the covenants, agreements and conditions required to be performed or complied with by it on or prior to the Closing Date.

11.3 No Pending Action. No action or proceeding before any court or governmental body shall be pending or threatened wherein an unfavorable judgment, decree or order would

prevent the carrying out of this Agreement or any of the transactions contemplated hereby, declare unlawful the transactions contemplated by this Agreement or cause such transactions to be rescinded.

11.4 No Bankruptcy. No PAH Entity shall: (a) be in receivership or dissolution; (b) have made any assignment for the benefit of creditors; (c) have admitted in writing its inability to pay its debts as they mature; (d) have been adjudicated bankrupt; or (e) have filed a petition in voluntary bankruptcy, a petition or answer seeking reorganization or an arrangement with creditors under the federal bankruptcy law or any other similar law or statute of the United States or any state; and nor shall any such petition have been filed against any PAH Entity.

11.5 Consents. All consents, approvals and authorizations of third parties, required for the consummation of the transactions contemplated by this Agreement shall have been obtained on or before the Closing Date.

11.6 Absence of Material Adverse Change. There shall have been no Material Adverse Change in the financial or operating condition of the MHS Entities taken as a whole.

11.7 Delivery of PAH Closing Documents. PAH shall have delivered, on or before the Closing Date, the PAH Closing Documents.

11.8 Delivery of Other Agreements. PAH shall have executed and delivered all other agreements determined by the Parties to be necessary or appropriate to be entered into as of the Closing Date, relating to the transactions contemplated by this Agreement.

ARTICLE 12

CLOSING

12.1 Closing Date; Closing. The Parties shall close the Affiliation and the other transactions contemplated by the Agreement on: (a) the first business day of the month immediately following receipt of all regulatory approvals and satisfaction of all conditions precedent to Closing set forth herein, at 12:01 a.m., Central Standard Time; or (b) such other date agreed to by the Parties following the receipt of all regulatory approvals and satisfaction of all conditions precedent to Closing set forth herein (the "**Closing Date**"). The delivery of the documents required to be delivered on the Closing Date by the respective Parties (the "**Closing**") shall occur on the business day immediately prior to the Closing Date, at the offices of McDermott Will & Emery LLP, 227 W. Monroe Street, Chicago, Illinois, or any other date or location agreed to by the Parties. All documents to be executed and actions to be taken, pursuant to this Agreement, at the Closing, shall be deemed to have been executed and to have been taken substantially concurrently, and no action shall be deemed to be complete until all are completed. Unless the Parties otherwise agree in writing, the Affiliation and other transactions contemplated herein to become effective as of the Closing Date, shall become so effective, provided that, as of the Closing Date, all of the Closing conditions (except for any Closing condition which has been waived in writing by the Party(ies) entitled to do so) have occurred, including the delivery by each Party of each of the Closing documents required to be delivered by such Party hereunder.

12.2 Pre Closing Actions. Prior to the Closing, the Parties shall take and cause to be taken all actions necessary or appropriate on their respective parts to implement the transactions contemplated herein on the Closing Date, including the following:

12.2.1 Actions by MHS. Prior to the Closing Date, the MHS Board shall approve the execution of any and all agreements and other documents and the taking of any and all other actions necessary or appropriate to consummate the transactions contemplated, including approval of the Amended MHS Bylaws.

12.2.2 Actions by PAH Entities. Prior to the Closing Date, the Boards of the PAH Entities shall approve the execution by PAH of any and all agreements and other documents, and the taking of any and all other actions necessary or appropriate to consummate the transactions contemplated or required by this Agreement to be taken by the PAH Entities on or before the Closing Date, including approval of the Amended PAH Bylaws.

12.3 Closing Document Deliveries. At the Closing, the Parties shall deliver the documents described below.

12.3.1 MHS Closing Documents. At the Closing, MHS shall deliver the following documents (the “**MHS Closing Documents**”):

(a) A certificate of the President and Chief Executive Officer of MHS, dated as of the Closing Date, certifying as to the continued accuracy and completeness of representations and warranties of MHS, and their respective performance of the covenants and conditions precedent, set forth in this Agreement;

(b) A certificate of the Secretary of MHS, dated as of the Closing Date, certifying as to the due adoption and continued effectiveness of, and attaching a copy of, the resolutions of the MHS Board approving the actions and transactions required or contemplated by this Agreement; and

(c) Such other instruments and documents as may be reasonably necessary to carry out the transactions contemplated by this Agreement and to comply with the terms hereof.

12.3.2 PAH Closing Documents. At the Closing, PAH shall deliver the following documents (the “**PAH Closing Documents**”):

(a) A certificate of the President and Chief Executive Officer of PAH, dated as of the Closing Date, certifying as to the continued accuracy and completeness of representations and warranties of the PAH Entities and their respective performance of the covenants and conditions precedent, set forth in this Agreement;

(b) A certificate of the Chief Financial Officer of PAH, dated as of the Closing Date, certifying as of the date thereof, as to the accuracy of the financial representations and warranties relating to the PAH Entities set forth at Sections 6.4 and 6.5;

(c) A certificate of the Secretary of PAH, dated as of the Closing Date, certifying as to the due adoption and continued effectiveness of, and attaching a copy of: (i) the resolutions of the PAH Board approving the actions and transactions required or contemplated by this Agreement, including the Amended PAH Bylaws; and (ii) in its capacity of member or shareholder of the PAH Entities, the resolutions approving the amended Bylaws for the PAH Entities and any transactions contemplated hereunder which are required for the PAH Entities, pursuant to the PAH Governing Documents in effect as of the Execution Date, to be approved by PAH; and

(d) Such other instruments and documents as may be reasonably necessary to carry out the transactions contemplated or required by this Agreement and to comply with the terms hereof.

12.4 Modification of Schedules. During the period from the Execution Date to the Closing Date, each Party shall update the Schedules it delivered at the Execution Date to ensure compliance with Section 8.2 or Section 9.2, as applicable.

ARTICLE 13

TERMINATION

13.1 Termination Upon Certain Events. Either MHS or PAH may, at or prior to the time set for Closing, terminate this Agreement under any one of the following circumstances:

13.1.1 Legal Proceeding. If at the time of Closing: (a) a bona fide action or proceeding shall be pending against any Party wherein an unfavorable judgment, decree or order would prevent or make unlawful the carrying out of the transactions contemplated by this Agreement; or (b) any governmental agency shall have notified any Party that the consummation of the transactions contemplated herein would constitute a violation of Applicable Law and that it has commenced or intends to commence proceedings to restrain the consummation of the transactions contemplated herein, and such agency has not withdrawn such notice prior to such termination; or (c) upon receipt of a "Request for Additional Information and Documentary Material" from the Department of Justice or Federal Trade Commission following submission of the Parties' Hart-Scott-Rodino pre-merger notification; or

13.1.2 Conditions Precedent to Closing. If the conditions of this Agreement to be complied with or performed by any other Party at or before the Closing shall not have been complied with or performed on or before the Closing Date or such later date upon which the Parties shall mutually agree, and such noncompliance or nonperformance shall have not been waived by the Party giving notice of termination; or

13.1.3 Material Adverse Change. If at any time prior to the Closing, there has been a Material Adverse Change to the businesses of either PAH or MHS, as applicable, and such change shall have not been waived by the Party giving notice of termination; or

13.1.4 Closing Date Deadline. If, for any reason, the Closing shall not have occurred on or before December 31, 2014.

13.2 Effect of Termination. If there has been a termination under Section 13.1, this Agreement shall be deemed terminated, and all further obligations of the Parties hereunder shall terminate, except those obligations specifically identified in this Agreement as surviving termination. Any termination under Section 13.1 shall be without liability to the Parties, except that such termination shall be without prejudice to the rights and remedies which any Party seeking to terminate this Agreement may have if a default shall be made by any other Party in the observance or in the due and timely performance by such Party of any of the covenants herein contained. Notwithstanding anything to the contrary, if a Party shall have made such default, the other Parties need not terminate this Agreement but may seek to specifically enforce the defaulting Party's obligations hereunder.

13.3 Withdrawal Right. For ten (10) years following the Closing Date, the PAH Board will have the right to unwind the Affiliation upon a sale of MHS and its affiliates, including PAH, to any entity that is not a 501(c)(3) organization under the Code (a "**For-Profit Transaction**").

13.3.1 MHS shall notify the PAH Board within thirty (30) days of entering into an exclusive letter of intent or other similar transaction document for a For-Profit Transaction ("**Notice of a For-Profit Transaction**"), provided that such event occurs before the tenth anniversary of the Closing Date.

13.3.2 If, upon receipt of Notice of a For-Profit Transaction, PAH desires to unwind the Affiliation, it shall, within sixty (60) days of Notice of a For-Profit Transaction, send to MHS a notice of its intent to unwind the Affiliation (a "**Withdrawal Notice**").

13.4 Withdrawal Procedure.

13.4.1 If PAH sends a Withdrawal Notice, the Parties shall take such actions as may be necessary or appropriate to effect an unwind simultaneously with consummation of the For-Profit Transaction (or such other date as the Parties may agree). If the For-Profit Transaction is not consummated, PAH shall not have a withdrawal right.

13.4.2 Following the Withdrawal Notice and until a withdrawal transaction is consummated, the Parties shall: (i) operate, and permit each other to operate exclusively in the ordinary course of their business, consistent with past practices and the terms of this Agreement; and (ii) take such actions as may be necessary or appropriate to preserve goodwill, including physician, employee and payor relationships.

13.4.3 Within fifteen (15) days following the Withdrawal Notice, PAH shall appoint to a committee (the "**Withdrawal Committee**") three (3) members of the PAH Board who do not serve on the MHS Board (the "**PAH Members**") and MHS shall appoint to the Withdrawal Committee three (3) members of MHS Board of Directors (the "**MHS Members**"). Within fifteen (15) days following its formation, the Withdrawal Committee shall select an Independent Restructuring Expert; provided, however that if the Withdrawal Committee cannot agree upon an Independent Restructuring Expert within such timeframe, then, the PAH Members (acting as a group) and the MHS Members (acting as a group) each shall select a Restructuring Expert, and the two Restructuring Experts so selected shall agree

upon a third Restructuring Expert (the three Restructuring Experts to comprise an “**Expert Panel**”). The Restructuring Expert (or Expert Panel, as applicable) shall assist the Withdrawal Committee to identify, agree upon and implement the actions that are necessary or appropriate to effect a Withdrawal Transaction within the time periods described herein, including, without limitation: (i) the equitable transfer of assets, including, without limitation, the equitable allocation of the ownership, and corresponding debt and financial obligations, relating to operations within the PAH primary service area, taking into account any transfers of fund balances or net assets between PAH and MHS; (ii) the transfer and equitable allocation of liabilities (including payroll, taxes, accounts payable and intercompany loans and accounts payable); (iii) the refunding by PAH of any bonds issued after the Closing Date to finance or refinance PAH or other facilities within the PAH primary service area; (iv) the transfer of professional and non-professional employees and contractors; (v) the assignment, termination, renewal, amendment or renegotiation of material contracts; (vi) the maintenance of payor relationships; (vii) the creation of new corporate entities and the application for tax exempt status; (viii) the securing of licenses and regulatory approvals; (ix) the implementation of amendments to governance documents; (x) the removal of officers and directors and the reconstitution of boards; (xi) the implementation of changes to signage, stationery and branding; and (xii) the provision of transition services to be valued at fair market value designed to replace centralized corporate services or functions that were consolidated at MHS, all for a sufficient period of time (but in no event more than one hundred eighty (180) days after the effective date of the Withdrawal Transaction) to allow PAH to develop such services and functions independently.

13.4.4 Within ninety (90) days following the Withdrawal Date, the Withdrawal Committee shall identify and agree upon the actions that are necessary or appropriate to effectuate a Withdrawal Transaction. If the Withdrawal Committee cannot identify or agree upon all actions necessary to effectuate the Withdrawal Transaction, the open action items shall be submitted to the Independent Restructuring Expert (or Expert Panel, as applicable) for resolution. Within thirty (30) days of submission, the Independent Restructuring Expert (or Expert Panel, as applicable) shall issue a report (the “**Withdrawal Report**”) which: (i) restates any agreed findings of the Withdrawal Committee; (ii) describes in detail any other actions that are necessary or appropriate to effect the Withdrawal Transaction within the time frames described herein (and the parties responsible therefore); (iii) sets forth the Independent Restructuring Expert’s (or Expert Panel’s, as applicable) conclusions, recommendations and findings with respect to all such actions; and (iv) allocates as between the Parties the costs associated with effecting the Withdrawal Transaction. The Parties shall be bound by the conclusions, recommendations and findings in the Withdrawal Report and shall take such actions described therein in order to effect a Withdrawal Transaction in accordance with the time periods described herein. Without limiting any other remedies available to the Parties at law or in equity, either Party shall be entitled to enforce the conclusions, recommendations and findings within the Withdrawal Report in a court of competent jurisdiction.

13.4.5 The costs of the Independent Withdrawal Expert (and, if applicable, the cost of the Expert Panel) shall be borne by MHS, and the costs of the Withdrawal Transaction shall be allocated between the Parties as agreed upon by the Withdrawal Committee or as specified in the Withdrawal Report.

13.4.6 In the event that a Withdrawal Transaction otherwise approved pursuant to this Section 13.4 cannot be effectuated by PAH because of the inability of PAH to refund any bonds or other obligations issued or incurred to finance or refinance PAH which are at the time secured by MHS commitments or guaranties within no more than ninety (90) days following the Withdrawal Date, MHS shall provide full contractual operational control of the assets subject to the Withdrawal Transaction to PAH, and PAH shall take all commercially reasonable actions necessary to assume the obligations to pay such bonds and other obligations to enter into such contractual arrangements as may be reasonably required by MHS to secure its obligations to pay such bonds and other obligations, including securing such payments under its financing documents by a first lien on the gross receipts, revenues and other assets of PAH and other operations attributable to PAH in the PAH primary service area and to pay the debt service and other payments of such bonds and other obligations as the same become due.

13.5 For-Profit Transaction Without Withdrawal

13.5.1 If PAH does not give a Withdrawal Notice, PAH shall be entitled to receive its pro rata share of the net proceeds of any For-Profit Transaction. Such proceeds shall be allocated in a manner that takes into account the net value of the PAH Entities (taking into account asset transfers and fund balances) compared to the net value of the MHS Entities as a whole.

ARTICLE 14

GENERAL PROVISIONS

14.1 Enforcement; Remedies.

14.1.1 The PAH Board shall be the sole body to have legal standing to enforce the commitments set forth in ARTICLES 4 and 5 (the "**Commitments**").

14.1.2 If the PAH Board believes that one or more Commitments has been materially breached, PAH shall give notice to MHS of its belief (the "**Commitment Notice**"). For thirty (30) days following the delivery of the Commitment Notice, the MHS President and CEO and the PAH Board Chair shall negotiate to resolve the issue in good faith.

14.1.3 In the event PAH believes the issue still exists after the 30-day meeting period, then PAH shall give MHS written notice to that effect. MHS and PAH shall engage in good faith efforts to settle the issue by non-binding mediation.

14.1.4 In the event PAH is unable to resolve the issue to its satisfaction following mediation, PAH's sole remedy shall be to seek a judicial order for MHS's specific performance of the Commitment.

14.2 No Shop Clause. PAH agrees that, from and after the Execution Date of this Agreement until the earlier to occur of the Closing or the termination of this Agreement, the PAH Entities will not, without the prior consent of MHS or except as otherwise permitted by this Agreement, explore, meet, discuss, negotiate, directly or indirectly, or enter into an agreement

with any third party for the purpose of discussing, organizing, formulating, designing, developing, investing in or implementing an arrangement that could lead to a change in control, sale of equity, lease of assets, sale of assets, joint operating agreement/joint operating company, merger, consolidation, liquidation, academic affiliation or any other business relationship similar to the transactions contemplated by this Agreement. PAH shall promptly notify MHS by telephone and thereafter confirm in writing, if any such discussions or negotiations are sought to be initiated with the PAH Entities or any such proposal or possible proposal is received directly or indirectly by any PAH Entity. In the event a PAH Entity or any of its representatives receives an unsolicited offer relating to a type of transaction described above, PAH shall promptly inform the person or organization making such unsolicited offer of the existence of the restrictions of this Section 14.2, but not the other contents of this Agreement (including MHS's identity unless such disclosure has been previously made to the public by joint press releases), and PAH shall reject such offer.

14.3 Performance of Undertakings. The Parties agree that the standard that shall apply to the Parties' performance of all covenants and undertakings contained in this Agreement and in any and every document executed and delivered hereunder is a commercially reasonable standard.

14.4 Consummation of Transactions. The Parties shall use, and cause their Affiliates to use, reasonable commercial efforts to consummate the transactions contemplated by this Agreement and shall take, or cause their Affiliates to take, no other action which is inconsistent with its obligations hereunder or which could materially delay the consummation of the transactions contemplated hereby.

14.5 Notice. Any notice, demand or communication required, permitted, or desired to be given hereunder will be deemed effectively given when personally delivered, when received by facsimile, email or overnight courier, or three (3) days after being deposited in the United States mail, with postage prepaid thereon, certified or registered mail, return receipt requested, addressed as follows:

Passavant:

Janet Terry, Chair
Chester A. Wynn, CPA, FHFMA
President & CEO
Passavant Area Hospital
1600 West Walnut Street
Jacksonville, Illinois 62650
Facsimile: 217.243.2206
E-mail Address: chet.wynn@passavanthospital.com

With a copy to:

Monte Dube
Partner
Proskauer Rose LLP
Three First National Plaza
70 West Madison, Suite 3800
Chicago, IL 60602-4342
Facsimile: 312.962.3551
E-mail Address: mdube@proskauer.com

Memorial:

Edgar J. Curtis
President and Chief Executive Officer
Memorial Health System
701 North First Street
Springfield, IL 62781
Facsimile:
E-mail Address: curtis.ed@mhsil.com

With a copy to:

Anna N. Evans
General Counsel and Vice President of Internal Audit
& Compliance
Memorial Health System
701 North First Street
Springfield, IL 62781
Facsimile: 217.788.5520
E-mail Address: evans.anna@mhsil.com

14.6 Cost of Transaction. Whether or not the transactions contemplated hereby shall be consummated, the Parties agree as follows: (a) MHS shall pay the fees, expenses, and disbursements of MHS and its agents, representatives, accountants, and legal counsel incurred in connection with the subject matter hereof and any amendments hereto; and (b) PAH shall pay the fees, expenses, and disbursements of PAH and its agents, representatives, accountants, and legal counsel incurred in connection with the subject matter hereof and any amendments hereto. Notwithstanding anything to the contrary, MHS shall pay any fees charged by any government agency in connection with notices or other filings as may be required under the HSR Act or associated with the certificate of exemption process with the IHFSRB.

14.7 No Brokerage. The Parties represent to each other that no broker has in any way been contacted in connection with the transactions herein contemplated. Each Party agrees to indemnify the other Parties from and against all loss, cost, damage or expense arising out of claims for fees or commissions of brokers employed or alleged to have been employed by such indemnifying Party.

14.8 Entire Agreement; Amendment. This Agreement, including all Schedules and Exhibits required hereunder, supersedes all previous agreements, oral or written, and constitutes the entire agreement among the Parties respecting the subject matter of this Agreement, and no Party shall be entitled to benefits other than those specified herein. Each Exhibit and Schedule referenced in this Agreement shall be considered a part hereof as if set forth herein in full. As

among the Parties, oral statements or prior written material which are not specifically incorporated or referenced herein shall not be of any force and effect. The Parties specifically acknowledge that in entering into and executing this Agreement, the Parties rely solely upon the representations and agreements contained in this Agreement and no others. This Agreement may be amended or modified only by an agreement in writing signed by all the Parties.

14.9 Non Assignment. This Agreement shall be binding upon and inure to the benefit of the Parties and their respective successors, assigns and legal representatives, but no Party may assign its rights in this Agreement or delegate its duties under this Agreement to a third party by any means without first obtaining the prior written consent of the other Parties.

14.10 No Third Party Beneficiaries. Except as expressly set forth herein, this Agreement shall not confer any rights or remedies upon any person or other third party other than the Parties and their respective successors and permitted assigns.

14.11 Third Party Authorizations. From the Execution Date to the Closing Date, each of the Parties shall use its reasonable best efforts to obtain expeditiously all consents, authorizations and other approvals of third parties necessary for the valid execution, delivery and performance of this Agreement by the Party.

14.12 Consents, Approvals and Discretion. Except as herein expressly provided to the contrary, whenever this Agreement requires any consent or approval to be given by a Party or a Party must or may exercise discretion, the Parties agree that such consent or approval shall not be unreasonably withheld or delayed and such discretion shall be reasonably exercised.

14.13 Additional Assurances. The provisions of this Agreement shall be self operative and shall not require further agreement by the Parties except as may be herein specifically provided to the contrary; provided, however, at the request of a Party, the other Party or Parties shall execute such additional instruments and take such additional actions as the requesting Party may deem necessary to effectuate this Agreement.

14.14 Severability. In the event any provision of this Agreement is held to be invalid, illegal or unenforceable, in whole or in part, for any reason and in any respect, such invalidity, illegality, or unenforceability shall in no event affect, prejudice or disturb the validity of any remaining provision of this Agreement, which shall be and remain in full force and effect, and binding and enforceable in accordance with its terms.

14.15 Governing Law. This Agreement will be governed by the laws of the State of Illinois without regard to that State's conflicts of laws principles. Any action or proceeding arising directly or indirectly in connection with, out of, or related to this Agreement may be commenced and maintained only in courts located in Morgan County, Illinois. The Parties, by their execution of this Agreement, consent and submit to the jurisdiction of any State or Federal court located within Morgan County, Illinois. Each Party waives any right that it may otherwise have to transfer or change the venue of any action or proceeding brought against it by the other Party and arising directly or indirectly in connection with, out of, or related to this Agreement.

14.16 Headings; Cross References. Headings of Articles and Sections in this Agreement and the table of contents hereof are solely for convenience or reference, do not

constitute a part hereof and shall not affect the meaning, construction or effect hereof. Unless indicated otherwise, references in this Agreement to Articles, Sections, Schedules and Exhibits are to articles, sections, schedules and exhibits of this Agreement.

14.17 Construction. Each Party has engaged separate independent legal counsel and independent advisors to provide advice and guidance to such Party. This Agreement and all documents or instruments delivered pursuant hereto shall be construed without regard to the identity of the person who drafted the various provisions of the same. Each and every provision of this Agreement and such other documents and instruments shall be construed as though the Parties participated equally in the drafting of the same. Consequently, the Parties acknowledge and agree that any rule of construction that a document is to be construed against the drafting Party shall not be applicable to this Agreement.

14.18 Waiver of Terms. The failure of any Party to insist, in any one or more instances, on performance of any of the terms, covenants and conditions of this Agreement shall not be construed as a waiver or relinquishment of any rights granted hereunder or thereunder or of the future performance of any such term, covenant or condition, but the obligations of the Parties with respect thereto shall continue in full force and effect. A waiver by one Party of the performance of any covenant, condition, representation or warranty of the other Party shall not invalidate this Agreement, nor shall such waiver be construed as a waiver of any other covenant, condition, representation or warranty. A waiver by any Party of the time for performing any act shall not constitute a waiver of the time for performing any other act or the time for performing an identical act required to be performed at a later time.

14.19 Counterparts; Signatures. The Parties agree that this Agreement may be executed in multiple originals, each of which shall be considered an original for all purposes and, collectively, shall be considered to constitute this Agreement. The Parties further agree that signatures transmitted by facsimile or in Portable Document Format (pdf) may be considered an original for all purposes, including, without limitation, the execution of this Agreement and enforcement of this Agreement.

14.20 Time is of the Essence. Time is hereby expressly made of the essence with respect to each and every term and provision of this Agreement and any other agreements determined by the Parties to be necessary or appropriate to be entered into in connection with the transactions contemplated by this Agreement.

14.21 Publicity and Public Relations; Confidentiality. Except as required by law, it is understood that all press releases or other public communications of any sort relating to this Agreement, and the method of the release for publication thereof, will be subject to the approval of both Parties, which approval will not be unreasonably withheld by either Party. Any communications necessary to effectively present the Affiliation to external constituencies served by the Parties and governmental bodies and officials will be mutually approved by the Parties. The Parties will coordinate on timing and content of communications with internal constituencies. The Confidentiality Agreement by and between MHS and PAH, dated July 30, 2013, and agreed to by MHS and PAH in the Letter of Intent (the "**Confidentiality Agreement**"), shall remain in full force and effect.

ARTICLE 15

GLOSSARY

15.1 Glossary. For convenience, set forth below is a glossary of defined terms used in this Agreement:

- 15.1.1 “**Accreditations**” shall have the meaning set forth in Section 6.19.
- 15.1.2 “**Affiliate**” shall mean any entity which is under the Control of, or which is under common Control with, the subject entity.
- 15.1.3 “**Affiliation**” shall have the meaning set forth in Recital E.
- 15.1.4 “**Agreement**” shall have the meaning set forth in the introductory paragraph.
- 15.1.5 “**Amended MHS Bylaws**” shall have the meaning set forth in Section 3.4.
- 15.1.6 “**Amended PAH Affiliate Bylaws**” shall have the meaning set forth in Section 3.3.
- 15.1.7 “**Amended PAH Bylaws**” shall have the meaning set forth in Section 3.2.
- 15.1.8 “**Applicable Law**” shall mean all applicable federal, state and local laws, statutes, ordinances, rules, regulations, codes and any judgment, decree, order, writ or injunction of any court or regulatory authority.
- 15.1.9 “**Audited Financial Statements**” shall have the meaning set forth in Section 6.4.1.
- 15.1.10 “**Benefit Plans**” shall have the meaning set forth in Section 6.17.1.
- 15.1.11 “**Board**” shall have the meaning set forth in Section 3.1.
- 15.1.12 “**CERCLA**” shall have the meaning set forth in Section 15.1.22.
- 15.1.13 “**Closing**” shall have the meaning set forth in Section 12.1.
- 15.1.14 “**Closing Date**” shall have the meaning set forth in Section 12.1.
- 15.1.15 “**Code**” shall mean the Internal Revenue Code of 1986, as amended.
- 15.1.16 “**Commitments**” shall have the meaning set forth in Section 14.1.
- 15.1.17 “**Commitment Notice**” shall have the meaning set forth in Section 14.1.2.

15.1.18 **“Confidentiality Agreement”** shall have the meaning set forth in Section 14.21.

15.1.19 **“Control”** shall mean possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of an entity whether through ownership of voting securities, by contract or otherwise.

15.1.20 **“CRNA”** shall have the meaning set forth in the introductory paragraph.

15.1.21 **“Employees”** shall have the meaning set forth in Section 4.1.

15.1.22 **“Environmental Law”** shall mean federal, state or local statutes and ordinances, and all rules and regulations promulgated thereunder, common law, orders, consent decrees, permits, and binding judicial and administrative interpretations thereof, pertaining or relating to: (a) pollution, (b) natural resources and the environment; (c) public and worker health and safety; and (d) the identification, reporting, generation, manufacture, processing, distribution, use, treatment, storage, disposal, emission, discharge, release, transport or other handling of any Hazardous Substances, including, without limitation, the Comprehensive Environmental Response, Compensation and Liability Act, as amended (**“CERCLA”**), and the Resource Conservation and Recovery Act, as amended (**“RCRA”**).

15.1.23 **“ERISA”** shall mean the Employee Retirement Income Security Act of 1974, as amended.

15.1.24 **“Execution Date”** shall mean December 31, 2013.

15.1.25 **“Expert Panel”** shall have the meaning set forth in Section 13.4.3.

15.1.26 **“For-Profit Transaction”** shall have the meaning set forth in Section 13.3.

15.1.27 **“GAAP”** shall mean Generally Accepted Accounting Principles.

15.1.28 **“Governing Documents”** shall mean the articles of incorporation, certificate of incorporation, bylaws, partnership agreement, operating agreement or other documents by and through which a business organization is formed and governed.

15.1.29 **“Hazardous Substances”** shall mean petroleum or petroleum products, polychlorinated biphenyls, asbestos containing materials, lead based paint, radioactive materials, toxic mold or fungus of any kind or species, medical wastes, and any substances, materials, chemicals, pollutants, constituents, wastes or noxious substances regulated by any Environmental Law.

15.1.30 **“Health Care Laws”** shall mean all federal, state and local laws, statutes, rules, regulations, ordinances and codes applicable to health care providers and facilities; federal and state health care program conditions of participation, standards, policies, rules, procedures and other requirements; and accreditation standards of any applicable

accrediting organization. Health Care Laws include, without limitation, the following laws: the federal (Title XIX of the Social Security Act) and state Medicaid programs and their implementing regulations, the Medicare Program (Title XVIII of the Social Security Act) and its implementing regulations, the federal False Claims Act (31 U.S.C. §§3729 et seq.), the Federal Health Care Program Anti Kickback Statute (42 U.S.C. §1320a 7b(b)), the Federal Physician Self Referral Law (42 U.S.C. §1395nn), the Federal Administrative False Claims Law (42 U.S.C. §1320a 7b(a)), the Health Insurance Portability and Accountability Act of 1996 (“**HIPAA**”) and the HIPAA Privacy Rule, the HIPAA Security Rule and the HIPAA Standards for Transactions and Code Sets (42 U.S.C. 1320d 1329d 8; 45 CFR Parts 160 and 164), the federal Confidentiality of Alcohol and Drug Abuse Patient Records Act (42 U.S.C. 290ee 3), the Rehabilitation Act, the Americans with Disabilities Act, the Occupational Safety and Health Administration statutes and regulations for blood borne pathogens and workplace risks, and any state and local laws that address the same or similar subject matter. Health Care Laws also include federal, state and local laws applicable to health care provider and facilities, including, without limitation, laws related to: federal and state health care program billing, cost reporting, revenue reporting, payment and reimbursement; federal and state health care program fraud, abuse, theft or embezzlement; procurement of health care services, human and social services, and other health related services; employee background checks and credentialing of employees; credentialing and licensure of facilities or providers of such services; zoning, maintenance, safety and operations of group homes, residential facilities and day programs, and other building health and safety codes and ordinances; certificate of need laws; state law restrictions on the corporate practice of medicine (or the corporate practice of any other health related profession); eligibility for federal and state health care program contracting, including any requirements limiting contracting to nonprofit or tax exempt entities; patient information and medical record confidentiality, including psychotherapy and mental health records; splitting of health care fees; patient brokering, patient solicitation, patient capping, and/or payment of inducements to recommend or refer, or to arrange for the recommendation or referral of, patients to health care providers or facilities; standards of care, quality assurance, risk management, utilization review, peer review, and/or mandated reporting of incidents, occurrences, diseases and events; advertising or marketing of health care services; and the enforceability of restrictive covenants on health care providers.

15.1.31 “**HIPAA**” shall have the meaning set forth in Section 15.1.30.

15.1.32 “**HSR Act**” shall have the meaning set forth in Section 6.3.2.

15.1.33 “**IHFSRB**” shall mean the Illinois Health Facilities and Services Review Board.

15.1.34 “**Insurance Policies**” shall have the meaning set forth in Section 6.15.

15.1.35 “**Intellectual Property**” shall have the meaning set forth in Section 6.25.

15.1.36 “**Interim Financial Statements**” shall have the meaning set forth in Section 6.4.1.

15.1.37 **"IRS"** shall mean the Internal Revenue Service.

15.1.38 **"Joint Commission"** shall mean The Joint Commission.

15.1.39 **"Knowledge", "known", "knowingly", "to the knowledge"** or any variant thereof shall, when qualifying any representation, warranty or other statement in this Agreement, mean and refers to:

(a) with respect to the PAH Entities or PAH: (i) all matters with respect to which the PAH President and CEO or the PAH Board has received written notice; or (ii) the actual knowledge of the President and CEO, Chief Financial Officer, and Director of Engineering, after performing a deliberate investigation of the applicable representations and warranties, and the facts underlying them, including having met with counsel to the applicable corporation to review such representations and warranties (including each Schedule referenced therein); or

(b) with respect to the MHS Entities or MHS: (i) all matters with respect to which the MHS President and CEO or the MHS Board has received written notice; or (ii) the actual knowledge of the President and CEO, Chief Financial Officer, and Chief Operating Officer, after performing a deliberate investigation of the applicable representations and warranties, and the facts underlying them, including having met with counsel to the applicable corporation to review such representations and warranties (including each Schedule referenced therein).

15.1.40 **"Letter of Intent"** shall have the meaning set forth in Recital E.

15.1.41 **"Licenses and Permits"** shall have the meaning set forth in Section 6.8.1.

15.1.42 **"Material Adverse Change"** shall mean any condition, change, event, violation, inaccuracy, circumstance or effect that:

(a) Individually or in the aggregate, could reasonably be expected to result in (i) liabilities with respect to Applicable Laws, including, without limitation, Health Care Laws, or Payment Programs, in excess of \$5,000,000 in the case of PAH Entities or \$15,000,000 in the case of MHS Entities; or (ii) the inability of an entity to remain tax-exempt, remain a licensed entity, operate as a health care facility, or be reimbursed by any Payment Program; or

(b) Could reasonably be expected to result in a change during any rolling 12 month period, in the assets, results of operation or the financial condition of the MHS Entities or the PAH Entities taken as a whole: (i) as to any reduction in the total net assets of the entity in an amount in the aggregate greater than ten percent of the group's total net assets as reflected on the group's interim unaudited balance sheet for the initial month of the twelve (12) month period; or (ii) as to any change in the financial condition of the group, has resulted in or is reasonably likely to result, on a normalized basis (i.e., after taking into account whether the effects of such change or event are reasonably likely to continue over such period), in a reduction in earnings before deductions for interest, taxes, depreciation and amortization of the Party over

the twelve (12) month period ending in the month in which the change or event occurs, in an amount greater than ten percent of the group's total net assets (as reflected on the Party's interim unaudited balance sheets for the initial month of that twelve (12) month period).

(c) Notwithstanding anything to the contrary, "Material Adverse Change" shall not include: (i) changes in the financial or operating performance due to or caused by the announcement of the transactions contemplated by this Agreement or seasonal changes; (ii) changes or proposed changes to any law, reimbursement rates or policies of governmental agencies or bodies that are generally applicable to hospitals or health care facilities; (iii) requirements, reimbursement rates, policies or procedures of third party payors or accreditation commissions or organizations that are generally applicable to hospitals or health care facilities; (iv) general business, industry or economic conditions, including such conditions related to the business of the Parties, that do not disproportionately affect the applicable Parties; (v) local, regional, national or international political or social conditions, including the engagement by the United States in hostilities, whether or not pursuant to the declaration of a national emergency or war, or the occurrence of any military or terrorist attack, that do not disproportionately affect the applicable Parties; (vi) changes in financial, banking or securities markets (including any disruption thereof and any decline in the price of any security or any market index) that do not disproportionately affect the applicable Parties; or (vii) changes in GAAP.

15.1.43 "**Material Contracts**" shall mean all contracts, leases (capital and operating), and other agreements entered into by or on behalf of any one or more of the PAH Entities which are in effect and have: (i) a dollar value or liability greater than \$250,000 in the aggregate; or (ii) a term of greater than one year.

15.1.44 "**MHS**" shall have the meaning set forth in the introductory paragraph to this Agreement.

15.1.45 "**MHS Affiliates**" shall have the meaning set forth in Recital A.

15.1.46 "**MHS Board**" shall mean the Board of Directors of MHS.

15.1.47 "**MHS Closing Documents**" shall have the meaning set forth in Section 12.3.1.

15.1.48 "**MHS Entities**" shall have the meanings set forth in Recital A.

15.1.49 "**MHS Financial Statements**" shall mean the audited consolidated financial statements of the MHS Entities for the two years ended in September 30, 2012 and 2011 and the unaudited financial statements of the MHS Entities from the interim period from October 1, 2012 through the most recent month-end date for which financial statements were available prior to the Execution Date.

15.1.50 "**MHS Members**" shall have the meaning set forth in Section 13.4.3.

15.1.51 "**Notice of a For-Profit Transaction**" shall have the meaning set forth in Section 13.3.1.

15.1.52 **“Owned Real Property”** shall have the meaning set forth in Section 6.11.1.

15.1.53 **“PAH”** shall have the meaning set forth in the introductory paragraph to this Agreement.

15.1.54 **“PAH Affiliate”** and **“PAH Affiliates”** shall have the meanings set forth in the introductory paragraph to this Agreement.

15.1.55 **“PAH Board”** shall mean the Board of Directors of PAH.

15.1.56 **“PAH Closing Documents”** shall have the meaning set forth in Section 12.3.2.

15.1.57 **“PAH Entity”** or **“PAH Entities”** shall have the meanings set forth in the introductory paragraph to this Agreement.

15.1.58 **“PAH Financial Statements”** shall have the meaning set forth in Section 6.4.1.

15.1.59 **“PAH Liability”** and **“PAH Liabilities”** shall have the meanings set forth in Section 2.3.

15.1.60 **“PAH Members”** shall have the meaning set forth in Section 13.4.3.

15.1.61 **“PAH Party”** and **“PAH Parties”** shall have the meaning set forth in the introductory paragraph.

15.1.62 **“PAH President”** shall have the meaning set forth in Section 3.5.

15.1.63 **“PAHF”** shall have the meaning set forth in the introductory paragraph.

15.1.64 **“Party”** and **“Parties”** shall have the meanings set forth in the introductory paragraph of this Agreement.

15.1.65 **“Payment Programs”** shall have the meaning set forth in Section 6.18.

15.1.66 **“Permitted Encumbrances”** shall mean (a) encumbrances for Taxes not yet due and payable or being diligently contested in good faith and for which appropriate reserves have been established in accordance with GAAP (provided that Permitted Encumbrances shall not apply to omitted or reassessed Taxes imposed due to incorrect, false or misleading real estate tax exemption applications or annual exemption certifications filed pursuant to 35 ILCS 200/15-10); (b) liens for inchoate mechanics’ and materialmen’s liens for construction in progress and workmen’s, repairmen’s, warehousemen’s and carriers’ liens arising in the ordinary course of the business; (c) easements, restrictive covenants, rights of way and other similar restrictions of record, which do not impair in any material respect the

value of its assets or the continued conduct of the business of a PAH Entity or its continued use of its assets in the manner currently used; (d) zoning, building and other similar restrictions which do not impair in any material respect the value the asset or the continued conduct of the business of a PAH Entity or its continued use of its assets in the manner currently used; (e) encumbrances, encroachments and other imperfections of title, licenses or encumbrances, if any, of record that do not impair in any material respect the value of the asset or the continued conduct of the business of a PAH Entity or its continued use of its assets in the manner currently used; (f) encumbrances arising under original purchase price conditional sales contracts and equipment leases with third parties entered into in the ordinary course of business; and (g) in the case of leased property, all matters, whether or not of record, affecting the title of the lessor (and any underlying lessor) of the leased property do not impair in any material respect the value of its asset or the continued conduct of the business of a PAH Entity or its continued use of its assets in the manner currently used.

15.1.67 **“Physician Recruitment Plan”** shall have the meaning set forth in Section 4.9.

15.1.68 **“PPA”** shall have the meaning set forth in the introductory paragraph.

15.1.69 **“RCRA”** shall have the meaning set forth in Section 15.1.22.

15.1.70 **“Returns”** shall have the meaning set forth in Section 6.16.

15.1.71 **“Taxes”** shall mean all federal, state, county, local and other taxes of every kind.

15.1.72 **“Unaudited Financial Statements”** shall have the meaning set forth in Section 6.4.1.

15.1.73 **“Withdrawal Committee”** shall have the meaning set forth in Section 13.4.3.

15.1.74 **“Withdrawal Notice”** shall have the meaning set forth in Section 13.3.2.

15.1.75 **“Withdrawal Report”** shall have the meaning set forth in Section 13.4.4.

[SIGNATURE PAGE FOLLOWS]

IN WITNESS WHEREOF, the Parties, acting through their duly authorized representatives, have executed this Affiliation Agreement as of the Execution Date.

MEMORIAL HEALTH SYSTEM

By: 
Edgar J. Curtis
President and Chief Executive Officer

**THE PASSAVANT MEMORIAL AREA
HOSPITAL ASSOCIATION**

By: _____
Janet M. Terry
Chair, Board of Directors

**PASSAVANT AREA HOSPITAL
FOUNDATION**

By: _____
Keith Lape, Ph.D.
President

**PASSAVANT PHYSICIAN ASSOCIATION,
INC.**

By: _____
Keith Bradbury
Chair

JACKSONVILLE CRNA'S, INC.

By: _____
Janet M. Terry
Chair, Board of Directors

IN WITNESS WHEREOF, the Parties, acting through their duly authorized representatives, have executed this Affiliation Agreement as of the Execution Date.

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By:

Edgar J. Curtis
President and Chief Executive Officer

**THE PASSAVANT MEMORIAL AREA
HOSPITAL ASSOCIATION**

By:

Janet M. Terry
Chair, Board of Directors

**PASSAVANT AREA HOSPITAL
FOUNDATION**

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Keith Lape, Ph.D.
President

**PASSAVANT PHYSICIAN ASSOCIATION,
INC.**

By:

Keith Bradbury
Chair

JACKSONVILLE CRNA'S, INC.

By:

Janet M. Terry
Chair, Board of Directors

Signature Page to the Affiliation Agreement

EXHIBIT A
AMENDED AND RESTATED BYLAWS OF PAH

See attached.

**AMENDED AND RESTATED BYLAWS
OF
THE PASSAVANT MEMORIAL AREA HOSPITAL ASSOCIATION**

[To be Effective as of Transaction Closing Date]

**ARTICLE I
NAME**

The name of the Corporation shall be The Passavant Memorial Area Hospital Association, an Illinois not-for-profit corporation, herein referred to as the “**Corporation.**”

**ARTICLE II
MISSION STATEMENT**

To improve the health of the people and communities we serve.

CARRYING OUT THE MISSION

The objects and purposes of the Corporation are to provide high quality health care in a service area centered in Jacksonville, Illinois, through the ownership and operation of a general hospital organized as a not-for-profit corporation (the “**Hospital**”). Provision shall be made for the proper care of the needy through income from endowments, gifts and other sources to the extent reasonably possible without jeopardizing the financing of the range and quality of services needed to care for all the patients.

CHARITABLE STATUS

The Corporation is organized exclusively for charitable, scientific and educational purposes as a not-for-profit corporation, and its activities shall be conducted for the aforesaid purposes in such a manner that no part of its net earnings will inure to the benefit of any member, director, officer or individual. No substantial part of the net earnings or activities of the Corporation shall be utilized in the carrying on of propaganda or otherwise attempting to influence legislation, and the Corporation shall not participate in or intervene in (including the publishing or distribution of statements) any political campaign on behalf of any candidate for public office. It shall not be its purpose to engage in carrying on propaganda or otherwise attempting to influence legislation.

The Corporation shall possess all powers which a corporation organized under the General Not-For-Profit Corporation Act of the State of Illinois, as the same from time to time may be amended, shall possess; including all powers which are not in conflict with the aforesaid purposes for which the Corporation is organized, including, but not limited to, the power to purchase, take, receive, lease as Lessee or Lessor, take by gift, devise or bequest, or otherwise

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acquire, own, hold, use, invest in and otherwise deal in and with any real or personal property or any interest therein situated in or out of the State of Illinois; to sell, convey, pledge, mortgage, assign and otherwise transfer or dispose of all or any part of its property and assets; from time to time to use, distribute, contribute, expend, donate, apply and appropriate all of its property and assets, and all proceeds and avails thereof, and income and profit derived there from, exclusively for charitable, educational, scholastic or scientific purposes, provided, however, the Corporation shall not engage in any business which would disqualify it from being exempt from taxation under Sections 501(a) or 501(c)(3) of the Internal Revenue Code.

In the event of the dissolution or liquidation of the Corporation, and after the payment of or other provision with respect to the Corporation's then existing debts, liabilities and obligations, all of the remaining assets of the Corporation shall be distributed to organizations which are described in Section 501(c)(3) of the Internal Revenue Code whose tax-exempt purposes are substantially similar to the Corporation's corporate purposes, or, if there are no such organizations, to such organizations, as selected by the Corporation's Board of Directors, which are operated exclusively for charitable, educational, scholastic or scientific purposes and which then qualify as tax-exempt organizations under Section 501(c)(3) of the Internal Revenue Code.

Anything herein contained to the contrary notwithstanding, no assets of the Corporation shall be donated, distributed, applied to, paid over or otherwise used or employed in any manner which would disqualify the Corporation from being exempt from taxation under Sections 501(a) or 501(c)(3) of the Internal Revenue Code.

ARTICLE III **MEMBERSHIP**

Section 1: Corporate Member

There shall be a Corporate Member of the Corporation which shall be Memorial Health System, an Illinois not-for-profit corporation, and any successor to such corporation resulting from merger, consolidation, or other corporate reorganization, herein referred to as the "**Corporate Member**." If at any time the Corporate Member shall cease to exist and there is no successor corporation, the Board of Directors of the Corporation (the "**Board of Directors**") shall exercise all powers of the Corporate Member until such time as the Board of Directors decides to elect a new Corporate Member.

Section 2: Powers and Rights of the Corporate Member

The Corporate Member shall elect the directors of the Corporation, from a slate of nominees proposed by the Board of Governors, taking into consideration the recommendations of the Board of Directors, and appoint the President and Chief Executive Officer of the Corporation (the "**President**"), upon mutual agreement with the Board of Directors, and shall have such other powers and authority as are set forth in the following:

A. Approval of all annual and long-term capital and operating budgets and strategic plans of the Corporation;

B. Approval of any amendment to the Bylaws or Articles of Incorporation of the Corporation;

C. Approval of any voluntary dissolution, merger, consolidation, sale or transfer of substantially all of the Corporation's assets (defined as 10% or more), or any creation of a subsidiary or affiliate corporation of the Corporation;

D. Removal of the President, upon mutual agreement with the Board of Directors;

E. Removal of any director of the Corporation for cause, which shall be defined as breach of his or her fiduciary duty to the Corporation;

F. Approval of capital expenditures in excess of \$1,000,000;

G. Approval of any guaranty of debt greater than \$250,000, including capital leases;

H. Approval of any agreement or transaction of material nature with another corporation controlled by or affiliated with the Corporate Member;

I. Approval of the selection of, or changes of, independent auditors;

J. Approval of the entry into, renewal of, or termination of contracts to provide covered healthcare services to beneficiaries of managed care contracts;

K. Approval of applications to the Illinois Health Facilities Planning Board for a permit or certificate of need for a proposed activity, whether or not involving a capital expenditure;

L. Approval of any sale or transfer of the Corporation's assets to a non-affiliated entity or third-party entity, if such assets have a value in excess of \$500,000;

M. Approval of any significant changes in the Corporation's insurance specifications or limits;

N. Approval of any contract between the Corporation and a third party which involves the provision of goods and/or services having a value in excess of \$1,000,000 for capital or \$1,500,000 in aggregate for operating and capital budgets which had not been previously approved by the Corporate Member in an annual capital or operating budget;

O. Approval of the borrowing of any sum, the principal of which exceeds \$250,000, or which has a stated term of greater than one year, or which is secured by a mortgage of all or

any portion of the Corporation's real property or the creation of a security interest in the Corporation's assets, including personal property and revenues, for the benefit of the lender, lessor or vendor, or the defeasance, advance payment or cancellation of any outstanding debt of the category described herein;

P. Approval of any contract for physician services having a value in excess of \$400,000;

Q. Approval of the sale of any of the Corporation's real property or interest therein or purchases of any additional real estate; and

R. Approval of any new or changes to existing long-term or master institutional plans.

ARTICLE IV **MEETINGS OF THE CORPORATE MEMBER**

Section 1: Corporate Member Meetings

The Corporate Member of the Corporation shall meet at such times as the Corporate Member may deem to be necessary to facilitate the conduct of the Corporation's business and affairs, and the Corporate Member may designate any such meeting as the Corporate Member's annual meeting as the Corporate Member of the Corporation, or, alternatively, the Corporate Member may dispense with the holding of an annual meeting without any further action on the part of the Corporate Member.

Section 2: Agenda of Annual Corporate Member and Special Meetings

(a) Annual Meeting

The agenda for annual meetings shall be as follows:

- (1) Call to order.
- (2) Presentation and approval of minutes of the last annual meeting and of any special meetings held since that meeting.
- (3) Presentation of the annual report of the Board of Directors.
- (4) Transaction of other business that may properly be brought before the meeting.
- (5) Adjournment.

(b) Special Meetings

The agenda for special meetings shall be as follows:

- (1) Call to order.
- (2) Reading of the official call for the meetings.
- (3) Transaction of the business for which the meeting is called.
- (4) Adjournment.

ARTICLE V
BOARD OF GOVERNORS

Section 1: Composition

There shall be a Board of Governors which shall be comprised of the individuals set forth below, herein referred to as the “**Board of Governors.**”

(a) Members from Churches

Certain members of the Board of Governors shall be appointed by each of the churches situated in the area comprising Morgan County; Scott County; Cass County; that part of Greene County situated in Township 12 North, Range 10 West; Township 12 North, Range 11 West; Township 12 North, Range 12 West; Township 12 North, Range 13 West; Township 11 North, Range 10 West; Township 11 North, Range 11 West; Township 11 North, Range 12 West; Township 11 North, Range 13 West; and the City of Greenfield; and that part of Macoupin County situated in Township 12 North, Range 8 West; Township 12 North, Range 9 West; Township 11 North, Range 8 West; and Township 11 North, Range 9 West (collectively, the “**Churches**”).

The number of representatives from each of the Churches shall be as follows:

- (1) One (1) from each Church having a membership of two hundred (200) or fewer.
- (2) Two (2) from each Church having a membership of more than two hundred (200) but not more than five hundred (500).
- (3) Three (3) from each Church having a membership of more than five hundred (500) but not more than one thousand (1,000).

- (4) Four (4) from each Church having a membership in excess of one thousand (1,000).

(b) Members from Organizations

Six (6) members of the Board of Governors shall be appointed by the following organizations (collectively, the “**Organizations**”), with each Organization appointing two (2) such representatives:

- (1) The Passavant Memorial Area Hospital Auxiliary;
- (2) The Passavant Memorial Area Hospital Alumnae Association; and
- (3) The Passavant Memorial Area Hospital Active Medical Staff.

(c) Members from the Board of Directors

Four (4) members of the Board of Governors shall be the Chairman, Chairman-Elect, Secretary and Treasurer of the Board of Directors, with each serving as the Chairman, Chairman-Elect, Secretary and Treasurer, respectively, of the Board of Governors.

Section 2: Election and Term of Office

Members of the Board of Governors from the Churches and Organizations shall hold office for a term of one (1) year or until their successors are duly elected, and their election certified by the Church or Organization that they represent on the Board of Governors. Each Church and Organization shall certify the membership and the name(s) of their representative(s) to the Secretary of the Board of Directors at least thirty (30) days prior to such the annual meeting of the Board of Governors. The Chair, Chairman-Elect, Secretary and Treasurer of the Board of Governors shall hold office so long as they continue to hold their respective positions on the Board of Directors.

Section 3: Meetings

The 2014 annual meeting of the Board of Governors was held in February 2014. Beginning in 2015 and continuing thereafter, the annual meeting of the Board of Governors shall be held each calendar year on a date between October 1st and October 31st, as selected by the Board of Directors. Special meetings may be called at any time by the Chair of the Board of Directors or upon petition of at least twenty (20) members of the Board of Governors. The call of a special meeting shall state the purposes of the meeting, and the business of the special meeting shall be limited to the stated purpose. Notices stating the hour, date and place of all meeting of the Board of Governors shall be sent to each member of the Board of Governors at least ten (10) days prior to such meeting.

Section 4: Powers

The Board of Governors shall approve a slate of qualified nominees for every vacancy of the Board of Directors. A qualified nominee shall: (i) be a resident of the area served by the Corporation, (ii) be willing to accept the responsibilities required as a director of the Corporation, and (iii) be available to actively participate in the activities of the Board of Directors. The nominees approved by the Board of Governors will be presented to the Board of Directors for review and recommendation and, subsequently, to the Corporate Member for election to the Board of Directors.

At least ninety (90) days prior to the annual meeting of the Board of Governors, the Chairman of the Board of Directors shall appoint, with the approval of the Executive Committee of the Board of Directors, a committee to select a suggested slate of nominees for presentation to the Board of Governors for approval. This committee shall consist of three (3) Governors who are not members of the Board of Directors and two (2) members of the Board of Directors who also may be, but are not required to be, members of the Board of Governors.

For the avoidance of doubt, the Board of Governors shall have no formal duties, responsibilities or obligations other than as set forth in this Section 4.

ARTICLE VI **BOARD OF DIRECTORS**

Section 1: Composition

The Board of Directors shall consist of sixteen (16) directors, at least one (1) of whom shall be an active member of the Medical Staff. Additionally, the President and the President of the Medical Staff shall be *ex officio* directors with full voting rights.

Section 2: Election and Term of Office

The term of office of each director, other than the *ex officio* directors, shall be four (4) years. The *ex officio* directors shall serve for as long as they hold their respective offices. The non-*ex officio* directors shall serve no more than two (2) successive terms. Provided however, if during his/her term of office as a director, he/she concurrently serves in the office of Chairman, or Chairman-Elect, the number of years he/she serves as an officer shall be added to the number of years he/she may consecutively serve as a director. Each director shall serve from the close of the annual meeting of the Board of Directors which he/she was elected until the close of the annual meeting of the Board of Directors at which his/her four-year term expires. Directors shall be eligible for re-election after having been off the Board of Directors for at least one (1) year as measured by the period between annual meetings. If either or both of the President and/or the President of the Medical Staff cease to hold such positions for any reason, they shall automatically cease to be *ex officio* directors without further action. The individuals replacing them shall serve as *ex officio* directors in their stead. The other sixteen (16) directors shall be

elected by the Corporate Member, as their terms expire or as vacancies arise in their positions. The Corporate Member shall elect each director from the slate of individuals presented to it by the Board of Governors, taking into consideration the recommendations of the Board of Directors; provided, however, if one or more of the individuals nominated for a position are not acceptable to the Corporate Member and a position remains unfilled, then the Board of Directors shall submit new slates for the unfilled position until individuals acceptable to the Corporate Member are elected. The non-*ex officio* directors shall serve staggered terms such that approximately one-fourth (1/4) of the non-*ex officio* directors are elected each year.

Section 3: Powers

A. Recommend approval of all annual and long-term capital and operating budgets and strategic plans of the Corporation;

B. Recommend approval of any amendment to the Bylaws or Articles of Incorporation of the Corporation;

C. Recommend approval of any voluntary dissolution, merger, consolidation, sale or transfer of substantially all of the Corporation's assets (defined as 10% or more), or any creation of a subsidiary or affiliate corporation of the Corporation;

D. Advise the Corporate Member on the performance of the President;

E. Remove the President, upon mutual agreement with the Corporate Member;

F. Recommend approval to the Corporate Member of capital expenditures (including budgeted capital expenditures) of the Corporation which are greater than \$1,000,000;

G. Recommend approval to the Corporate Member of any guaranty of debt greater than \$250,000, including capital leases;

H. Recommend approval of any agreement or transaction of material nature with another corporation controlled by or affiliated with the Corporate Member;

I. Recommend approval of the selection of, or changes of, independent auditors;

J. Recommend approval of the entry into, renewal of, or termination of contracts to provide covered healthcare services to beneficiaries of managed care contracts;

K. Recommend approval for the Corporation to make an application to the Illinois Health Facilities Planning Board for a permit or certificate of need for a proposed activity, whether or not involving a capital expenditure;

L. Recommend approval of any sale or transfer of the Corporation's assets to a non-affiliated entity or third-party entity, if such assets have a value in excess of \$500,000;

M. Recommend approval of any significant changes in the Corporation's insurance specifications or limits;

N. Recommend approval to the Corporate Member of any contract between the Corporation and a third party, which involves the provision of goods and/or services having a value in excess of \$1,000,000 for capital or \$1,500,000 in aggregate for operating and capital budgets which had not been previously approved by the Corporate Member in an annual capital or operating budget;

O. Recommend approval to the Corporate Member of the borrowing of any sum, the principal of which exceeds \$250,000, or which has a stated term of greater than one year, or which is secured by a mortgage of all or any portion of the Corporation's real property or the creation of a security interest in the Corporation's assets, including personal property and revenues, for the benefit of the lender, lessor or vendor, or the defeasance, advance payment or cancellation of any outstanding debt of the category described herein;

P. Recommend approval of any contract for physician services having a value in excess of \$400,000;

Q. Recommend approval of the sale of any of the Corporation's real property or interest therein or purchases of any additional real estate; and

R. Recommend approval of any new or changes to existing long-term or master institutional plans.

The matters specified herein, subject to Corporate Member approval, shall, after being reviewed and adopted by the Board of Directors, be submitted to the Corporate Member for approval. Except for the matters specifically enumerated herein, the Board of Directors has full authority and the exclusive prerogative to act in matters affecting the Corporation.

Section 4: Annual Meeting

An annual meeting of the Board of Directors shall be held on a date to be selected by the Corporate Member, which shall be held in the initial quarter of each calendar year, on a date between January 1st and March 31st. At each annual meeting, the Corporate Member shall announce its election of individuals to serve in those director positions the terms of which have expired and its appointment of the President. The Board of Directors shall then elect the Corporation's remaining officers and conduct such other business as it deems appropriate. The Secretary shall provide to each director at least ten (10) days' notice of the annual meeting; provided, however, that any director may waive such notice by attendance at the meeting or by signing a waiver of notice.

Section 5: Regular Meetings

Regular meetings of the Board of Directors shall be held at least quarterly. Such meetings shall be held at such time as designated by the President by announcement at the preceding regular meeting, by written notice, or by passage of a resolution by the Board of Directors setting a fixed time for said meeting.

Section 6: Special Meetings

Special meetings of the Board of Directors may be called by the Chairman of the Board, the President, or the Corporate Member or at the request of any four (4) directors. It shall be the duty of the Chairman of the Board to provide at least twenty-four (24) hours' notice to all directors of a special meeting; provided, however, that any director may waive such notice by attendance at the meeting or by signing a waiver of such notice.

Section 7: Notice

Notice for any meeting of the Board of Directors shall be given in writing by personal delivery, by mail, and/or electronic mail to each director to the address shown for such director in the records of the Corporation and to the Corporate Member. If mailed, such notice shall be deemed to be delivered when deposited in the United States mail in a sealed envelope so addressed with postage thereon prepaid. Neither the business to be transacted nor the purpose of any meeting need be specified in the notice unless specifically required by law or by these Bylaws.

Section 8: Attendance

The Chairman of the Board will meet with any member who is absent from three consecutive meetings of the Board of Directors. Continued absence may result in a request to resign from the Board of Directors.

Section 9: Quorum

A majority of the Board of Directors shall constitute a quorum for the transaction of business at any meeting of the Board of Directors, provided that if less than a majority of the directors are present those directors present may adjourn the meeting from time to time without further notice.

Section 10: Manner of Acting

The act of the majority of the directors present at a meeting at which a quorum is present shall be the act of the Board of Directors except where otherwise provided by law or by these Bylaws. If a director abstains from voting, that director's abstention will not be counted as being

a vote in favor of or against a particular motion; consequently, contrary to *Robert's Rules of Order*, the effect is not the same as if the abstaining director voted on the prevailing side.

Section 11: Informal Action

Unless specifically prohibited by the Articles of Incorporation or by these Bylaws, any action required to be taken at a meeting of the Board of Directors, or any committee thereof, or any other action which may be taken at a meeting of the Board of Directors, or any committee thereof, may be taken without a meeting if a consent in writing setting forth the action to be taken shall be signed by all directors or committee members entitled to vote with respect to the subject matter thereof. Any such consent signed by all directors or committee members shall have the same effect as a unanimous vote and may be stated as such in any document filed with the Secretary of State of the State of Illinois. Further, any meeting of the Board of Directors, or any committee thereof, may be held by telephone conference as long as each of the directors or committee members participating therein subsequently signs the minutes thereof.

Section 12: Compensation

Directors shall not be paid compensation for their services as directors, but may be reimbursed for bona fide expenses incurred arising out of such services rendered. However, nothing herein contained shall be construed to prohibit payment of compensation to an individual who serves as a director for services rendered to the Corporation in another capacity.

Section 13: Vacancies

Vacancies occurring on the Board of Directors shall be filled by the Corporate Member from among individuals nominated by the Board of Directors. Any director so elected shall hold office for the unexpired term of his predecessor in office.

Section 14: Removal

Notwithstanding the provisions of Section 2(E) of this Article III, the Board of Directors may remove any member of the Board of Directors, with or without cause, at any time by the affirmative vote of two-thirds (2/3) of the members of the Board of Directors then in office.

ARTICLE VII OFFICERS

Section 1: Officers

The officers of the Corporation shall be a Chairman of the Board, a Chairman-Elect of the Board, a President, a Secretary, and a Treasurer. The Board of Directors may appoint such other officers as it shall deem desirable. The Chairman of the Board, Chairman-Elect of the Board, an Immediate Past Chairman of the Board, if available, Secretary, and Treasurer must be members of the Board of Directors.

Section 2: Election, Term of Office, Removal, and Vacancies

All officers shall be elected at the annual meeting of the Board of Directors and shall hold office for a period of one (1) year or until their successors shall have been duly elected. All officers, other than the President, shall be elected by the Board of Directors. The President shall be elected by the Corporate Member from candidates approved by the Board of Directors. The Corporate Member shall present to the Board of Directors a minimum of two (2) candidates to serve as President, and shall provide the Board of Directors appropriate opportunity to interview the candidates and review their credentials. To assist the Board of Directors in evaluating each candidate's qualifications, the Corporate Member shall, if the Board of Directors so requests, assemble a candidate review committee composed of officers selected by the Corporate Member from the officers of the Corporation and Passavant Area Hospital Foundation. To the extent the Board of Directors does not approve either of the candidates, the Corporate Member shall continue to present candidates until the Board of Directors finds one (1) of which it approves. In the event the Board of Directors indicates a preference among the candidates it approves, the Corporate Member shall appoint the preferred candidate unless in the exercise of its best judgment it believes that factors warrant the appointment of one of the other approved candidates. These factors may include the candidate's salary requirements, availability to begin employment, and compatibility with the Corporate Member's management philosophy. To the extent the Corporate Member reelects the Corporation's then current President to serve another term, it need not comply with the above-described candidate review process. The Board of Directors alone shall have the right to remove any officer of the Corporation other than the President. The Board of Directors and the Corporate Member shall each have the right to remove the President, upon mutual agreement. Vacancies in an officer position shall be filled by the Board of Directors; provided, however, a vacancy in the President's position shall only be filled by the Corporate Member. The Corporate Member shall fill the vacancy pursuant to the above-described candidate review process.

Section 3: Chairman of the Board

The Chairman of the Board shall preside at all meetings of the Board of Directors. The Chairman of the Board shall appoint all committees of the Board of Directors not otherwise provided for.

Section 4: Chairman-Elect of the Board

The Board of Directors shall elect a Chairman-Elect of the Board who shall be assigned such duties by the Board of Directors as it shall from time to time determine. The Chairman-Elect of the Board shall perform the duties of the Chairman of the Board in the event of the absence of the Chairman of the Board.

Section 5: President

The President shall be the Chief Executive Officer of the Corporation, shall be subject to the direction and control of the Board of Directors, and shall have the general supervision, direction, and control of the business and affairs of the Corporation and its officers, agents, and employees. The President shall advise and make recommendations to the Board of Directors relating to the operation of the Corporation and long-range planning. The President shall be a voting member of each committee of the Board of Directors other than the Board Evaluation Committee.

The President may sign with the Secretary or other proper officer of the Corporation authorized by the Board of Directors any deeds, bonds, contracts, or other instruments which the Board of Directors has authorized to be executed.

The President shall also prepare and present to the Corporate Member periodic and regular reports of the operation and condition of the Corporation, including financial reports. The President shall represent the Corporation in all matters relating to the Corporate Member.

In addition, the authority and duties of the President shall include:

(a) Adhere to, be guided by, and endeavor to assure compliance with the philosophy, mission, values and ethics of the Corporation, as established by the Corporate Member, these Bylaws, the bylaws of the Corporate Member, and the bylaws of the Medical Staff.

(b) Integrate the philosophy of the Corporation, as established by the Corporate Member, into the total operation of the Hospital.

(c) Prepare and recommend plans and regulations for the departmental organization of hospital personnel and for the coordination and supervision thereof.

(d) Select, employ, direct and discharge administrative staff; and develop, recommend and supervise personnel policies, practices, and salary schedules.

(e) Supervise the activities of those who relate to him directly in the organizational structure and coordinate these activities with those of the Medical Staff.

(f) Supervise the preparation of and submit to the Board for review the annual hospital budget in accordance with the policies of the Corporate Member.

(g) Supervise business affairs to ensure that funds are collected and expended to the best possible advantage, and submit and recommend for Board approval schedules of rates and charges for Hospital services together with plans and procedures for the raising of additional funds, as necessary, from outside sources in accordance with the policies of the Corporate Member.

(h) Maintain physical properties in a functional, safe, attractive and economical condition in a manner consistent with corporate goals.

(i) Formulate and implement hospital policies in cooperation with the Board.

(j) Serve on the Board and on all committees thereof ex-officio with vote except as otherwise provided herein.

(k) Send appropriate notices or waivers of notice regarding Board meetings, and prepare agendas and other materials for all meetings of the Board.

(l) Attend meetings of the Corporate Member Board, and its committees, when requested.

(m) Attend all meetings of the Medical Staff and serve on committees thereof ex-officio without a vote.

(n) Function as an agent of the Board in assisting the Medical Staff with its organization and medico-administrative problems and responsibilities.

(o) Function as agent of the Board in serving as liaison and channel of communications between the Board and any of its committees and the Medical Staff.

(p) Annually perform an evaluation of the performance of the Medical Staff President.

(q) Annually prepare and provide goals and objectives for approval of the Board, and submit quarterly progress reports to the Board and to the Corporate Member.

(r) Work continually with other health care professionals in order that high quality care may be rendered to the patients at all times.

(s) Function as agent of the Corporation in all its relationships with other health related agencies and corporations interfacing with the Hospital.

(t) Cooperate with the Corporate Member and its subsidiaries, and support system-wide programs.

(u) Provide a mechanism for the orientation and regular ongoing education of directors.

(v) Perform other duties that may be necessary or in the best interest of the Corporation.

(w) Prepare and distribute to the Corporate Member reports of Board deliberations within eight (8) business days after the date of the Board meeting at which such deliberations took place.

The President shall perform all duties incident to the office of President and such other duties as may be prescribed by the Board of Directors.

Section 6: Treasurer

The Treasurer shall be responsible for the custody of the funds of the Corporation. The Treasurer shall ensure that a true and accurate accounting of the financial transactions of the Corporation is made and that reports of such transactions are presented to the Board of Directors.

Section 7: Secretary

The Secretary shall prepare an agenda for and keep minutes of meetings of the Corporation and the Board of Directors; see that all notices are duly given in accordance with the provisions of these Bylaws, or as required by law; and be custodian of the corporate records and of the seal of the Corporation and see that the seal of the Corporation is affixed to all documents as required. The Secretary shall sign all documents as required by the office and shall perform such duties as may be assigned by the President and the Chairman of the Board.

**ARTICLE VIII
COMMITTEES OF THE BOARD OF DIRECTORS**

Section 1: Committees

Committees of the Board of Directors shall be standing or special. Standing committees shall be an executive committee, a governance committee, a finance and investment committee, an institutional planning committee, and such other standing committees as the Board of Directors may authorize. Any committee that considers issues affecting the discharge of Medical Staff responsibilities will have one or more physician members appointed by the Chairman of the Board. Any standing committee duties and responsibilities, excluding issues relating to the Medical Staff, may be executed by the Executive Committee.

Section 2: Executive Committee

The executive committee shall consist of the Chairman of the Board, the Chairman-Elect of the Board, the President, the Treasurer, the Secretary, and the immediate past Chairman of the

Board provided he/she has remaining years on the Board of Directors.

The executive committee shall have power to transact all regular business of the Corporation during the interim between meetings of the Board of Directors provided that the committee shall refer all matters of major importance to the Board of Directors and will inform the full board of any such action at the next scheduled board meeting. Included will be expedited credentialing of new Medical Staff members as recommended by the Medical Executive Committee. The members of the committee shall act as the representatives of the Board of Directors on the joint conference committee. It shall also act as a general reviewing committee on matters placed on the agenda of the Board of Directors' meeting. The executive committee shall meet monthly.

Section 3: Governance Committee

The governance committee shall consist of the Secretary of the Board of Directors, who shall serve as the chairperson of the governance committee, and at least six (6) additional members appointed by the Chairman of the Board. Non-voting members of the committee shall include the Chairman of the Board, the Chairman-Elect of the Board, the President, the Medical Staff President or designee, and the President and Chief Executive Officer of the Corporate Member, or his designee (the "**Corporate Member President**"). The governance committee shall meet at least quarterly.

The governance committee shall be responsible for director development, board self-evaluation, review of these Bylaws, policies and procedures review, legislative initiatives, review of the quality of patient care provided by the Hospital, continuing education for the Board of Directors, and other issues as may be assigned by the Chairman of the Board. All recommendations and actions taken by the governance committee shall be reported at the next meeting of the Board of Directors.

Section 4: Finance and Investment Committee

The finance and investment committee shall consist of the Treasurer, at least six (6) additional members of the Board of Directors appointed by the Chairman of the Board and the Corporate Member President. The Chairman of the Board shall serve as a non-voting member of the committee. The Treasurer shall be the chairperson of the committee. The committee shall meet at least quarterly.

The finance and investment committee shall consider and report upon matters of budget and shall control and report upon all other fiscal matters as directed by the Board of Directors; cause to be prepared and submitted to the Board of Directors, at its last regular meeting before the end of the fiscal year, a budget showing expected receipts and income and expense for the ensuing fiscal year; review investment policy and strategy; and report to the Board of Directors on the Corporation's investment performance on at least a semi-annual basis.

Section 5: Institutional Planning Committee

The institutional planning committee shall consist of the Chairman-Elect of the Board, who shall serve as the chairperson of the institutional planning committee, and at least six (6) additional members appointed by the Chairman of the Board. Non-voting members of the committee shall include the Chairman of the Board, the President, the Medical Staff President or designee, and the Corporate Member President. The institutional planning committee shall meet at least quarterly.

The institutional planning committee shall: (i) be responsible for the review and updating of the strategic plan of the Hospital consistent with the Hospital's roles, objectives, and goals; (ii) function as a hearing committee for any patient complaints that may be lodged against the Hospital; (iii) shall be responsible for addressing physical plant concerns; and (iv) shall be responsible for other issues as may be assigned by the Chairman of the Board. All recommendations and actions taken by the institutional planning committee shall be reported at the next meeting of the Board of Directors

Section 6: Special Committees and Task Force Groups

Special committees and task force groups may be appointed by the Chairman of the Board with the concurrence of the Board of Directors for such special tasks as circumstances warrant. Such special committees shall limit their activities to the accomplishment of the tasks for which they were created and appointed, and shall have no power to act except as is specifically conferred by action of the Board of Directors. Upon completion of the tasks for which they were appointed, such special committees shall stand discharged.

ARTICLE IX

Medical Staff

Section 1: General

The Medical Staff is a policy formulating body in areas relating directly to the quality of patient care, subject to approval of the Board of Directors.

The Medical Staff Executive Committee shall make recommendations to the Board of Directors concerning: (1) appointments, reappointments and other changes in staff status; (2) granting of clinical privileges; (3) disciplinary actions; (4) all matters relating to professional competence; and (5) such specific matters as may be referred to it by the Board of Directors.

All applications for Medical Staff privileges will be presented to the Board of Directors after review and approval by the appropriate specialty department chair and the Executive Committee of the Medical Staff. The Board of Directors will review the qualifications and references of the applicant along with the recommendations of the department chair and

Executive Committee of the Medical Staff. The Board of Directors will accept, defer or reject the application.

In the event the Board of Directors reaches a tentative conclusion that it does not concur with a recommendation of the Executive Committee of the Medical Staff or if the Board of Directors tentatively rejects an application (whether or not the Executive Committee of the Medical Staff recommended its approval), there shall be a conference of the Executive Committee of the Medical Staff and the Executive Committee of the Board of Directors. The Executive Committee of the Board of Directors shall report the substance of such meeting to the Board of Directors, who shall then make the final decision on the matter.

Reappointments to the Medical Staff shall be reviewed at the December meeting of the Board of Directors each year. All reappointments must be recommended to the Board of Directors by the Executive Committee of the Medical Staff.

Each application for appointment to the Medical Staff must contain a request for the specific clinical privileges desired by the applicant. Evaluation of all requests shall be based upon the applicant's education, training, experience, demonstrated competence, references and other relevant information.

Physicians, dentists and podiatrists employed by the Hospital, either full or part time, must be members of the Medical Staff, achieving that status by the same procedure provided for other Medical Staff members. The Hospital reserves the right, in its sole discretion, to enter into exclusive contracts for the provision of services at the Hospital. Such contracts may serve to exclude other staff members from exercising privileges in certain areas.

The Code of Ethics as adopted by the American Medical Association, the American Dental Association and the American Podiatry Association shall govern the professional conduct of all members of the Medical Staff. A signed application form shall constitute an agreement that, when appointed, the member will strictly abide by the Principles of Medical Ethics of the American Medical Association, the Code of Ethics of the American Dental Association or the Code of Ethics of the American Podiatry Association, whichever is applicable.

Section 2: Medical Staff Governance

It shall be the duty of the Active and Associate Medical Staff to formulate its own Bylaws and to formulate rules regarding its membership and membership upon the subordinate staff, including Honorary, Consulting, Associate, Affiliate and Courtesy Staff, for such duties and privileges as may from time to time be required or conferred by the Board of Directors; and such Bylaws, Rules and Regulations shall be submitted by the Active and Associate Medical Staff to the Board of Directors and become effective upon approval by the Board of Directors.

Section 3: Review Process and Hearings

The Medical Staff shall have a review procedure when any practitioner making reapplication to the Medical Staff is notified of a recommendation that adversely affects the practitioner's reappointment. The individual shall be entitled to a hearing and an appellate review procedure with regard to said recommendation, as provided in the Medical Staff Bylaws.

In instances where the activities or professional conduct of any practitioner with clinical privileges are considered to be lower than the standards or aims of the Medical Staff, or inconsistent with approved hospital policy, corrective action may be requested by any officer of the Medical Staff, by the chair of the department, by the chair of any standing committee of the Medical Staff, by the President of the Corporation or by the Board of Directors. Hearing and appellate review procedures shall be available to the affected practitioner, as provided in the Medical Staff Bylaws.

There shall be an appellate review mechanism for adverse actions taken by the Board of Directors as set forth in the Medical Staff Bylaws.

**ARTICLE X
AFFILIATED ORGANIZATIONS**

Section 1: Auxiliary

(a) The purpose of The Passavant Memorial Area Hospital Auxiliary (the "**Auxiliary**") shall be to advance and promote the welfare of the hospital through ways approved by the Board of Directors. This purpose shall be accomplished by interpreting to the public the functions, services and needs of the Hospital; by services to the Hospital and its patients; by raising funds in a manner satisfactory to the Board of Directors and in harmony with the planning of the community.

(b) The bylaws of the Auxiliary shall be subject to approval by the Board of Directors.

(c) Upon request by the Board of Directors, the president of the Auxiliary shall attend meetings of the Board of Directors to report on actions of the Auxiliary for approval by the Board of Directors.

(d) A report of the Auxiliary shall be presented to the Board of Governors at its annual meeting.

Section 2: Other Affiliated Organizations

Other volunteer groups and organizations, working for the benefit of the Hospital and its services, may from time to time be approved by resolution of the Board of Directors.

ARTICLE XI
CONTRACTS, CHECKS, DEPOSITS, AND FUNDS

Section 1: Contracts

The Board of Directors may, subject to approval by the Corporate Member if so required by these Bylaws, authorize any officer or officers, agent or agents of the Corporation, in addition to the officers so authorized by these Bylaws, to enter into any contract or execute and deliver any instrument in the name of and on behalf of the Corporation; and such authority may be general or confined to specific instances.

Section 2: Checks, Drafts, Etc.

All checks, drafts, or other orders for the payment of money, notes, or other evidence of indebtedness issued in the name of the Corporation shall be signed by such officer or officers, agent or agents of the Corporation in such manner as shall from time to time be determined by resolution of the Board of Directors, subject to approval by the Corporate Member if so required by these Bylaws.

Section 3: Deposits

All funds of the Corporation shall be deposited from time to time to the credit of the Corporation in such banks, trust companies, or other depositories as the Board of Directors may select.

ARTICLE XII
INDEMNIFICATION

Section 1. Statutory Indemnification

The Hospital will indemnify the officers, directors, employees and agents of the Hospital as and to the extent permitted under the "General Not For Profit Corporation Act of 1986," as amended, or other applicable statutes of the State of Illinois.

Section 2. Indemnification Against Litigation

The Hospital will indemnify any person who was or is a party, or is threatened to be named as a party, to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action or suit by or in the right of the

Hospital), by reason of the fact that he or she is or was an officer, director, employee or agent of the Hospital, or is or was serving at the request of the Hospital as an officer, director, employee or agent of another corporation, limited liability company, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him or her in connection with such action, suit or proceeding, if he or she acted in good faith and in a manner he or she reasonably believed to be in, or not opposed to, the interests of the Hospital and, with respect to any criminal action or proceeding, had no reasonable cause to believe that his or her conduct was unlawful. The termination of any action, suit or proceeding by judgment, order, settlement, conviction or a plea of nolo contendere, or an equivalent plea, will not create, per se, a presumption that the person did not act in good faith and in a manner he or she reasonably believed to be in, or not opposed to, the interests of the Hospital and, with respect to any criminal action or proceeding, had reasonable cause to believe his or her conduct was unlawful.

Section 3. Indemnification Against Derivative Suits

The Hospital will indemnify any person who was or is a party, or is threatened to be named as a party, to any threatened, pending or completed action or suit by or in the right of the Hospital to procure a judgment by reason of the fact that he or she is or was an officer, director, employee or agent of the Hospital, or is or was serving at the request of the Hospital as an officer, director, employee or agent of another corporation, limited liability company, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees) actually and reasonably incurred by him or her in connection with the defense or settlement of such action or suit, if he or she acted in good faith and in a manner he or she reasonably believed to be in, or not opposed to, the interests of the Hospital; however, there will be no indemnification by the Hospital if that person has been adjudged negligent or guilty of misconduct in the performance of his or her duty to the Hospital, unless, and to the extent, the court where the action or suit was instituted determines, on application, that, despite the adjudication of negligence or misconduct, and in view of all the circumstances presented to the court, such person is fairly and reasonably entitled to be indemnified against such expenses as the court deems proper.

Section 4. Expenses

As and to the extent an officer, director, employee or agent of the Hospital has been successful, on the merits or otherwise, in the defense of any action, suit or proceeding referred to in Section 2 or Section 3 of this Article XII, or in defense of any claim or issue in that action, suit or proceeding, he or she will be indemnified against expenses (including attorneys' fees) actually and reasonably incurred by him or her in connection with the action, suit or proceeding.

Section 5. Determination of Indemnification

Any indemnification under or pursuant to this Article XII (unless ordered by a court) must be authorized by the Hospital in a specific case, after a determination that indemnification

of the officer, director, employee or agent is proper under the standard of conduct which is prescribed by this Article XII. Indemnification must be determined by a majority vote of a quorum consisting of directors who were not parties to the action, suit or proceeding or, if such a quorum is not obtainable, or, even if obtainable, a quorum of disinterested directors so resolves, by independent legal counsel (compensated by the Hospital) in a formal opinion, in writing, addressed to the Hospital, which is accepted by the directors.

Section 6. Advance of Expenses

Expenses incurred in defending an action, suit or proceeding, whether civil, criminal, administrative or investigative, may be paid by the Hospital in advance of the final disposition of such action, suit or proceeding, as authorized pursuant to Section 5 of this Article XII, after the Hospital has received an agreement by or on behalf of the officer, director, employee or agent to repay, at the request of the Hospital, any amounts so advanced.

Section 7. Insurance

The Hospital may purchase and maintain insurance on behalf of any person who is or was an officer, director, employee or agent of the Hospital, or is or was serving at the request of the Hospital as an officer, director, employee or agent of another corporation, limited liability company, partnership, joint venture, trust or other enterprise, to cover any liability asserted against him or her and incurred by him or her in any such capacity, or arising by virtue of his or her status as an officer, director, employee or agent.

Section 8. Notice of Indemnification

Any indemnification of any officer, director, employee or agent pursuant to any of the preceding provisions of this Article XII, including any payment or reimbursement of expenses, must be reported, in writing, to the Corporate Member within the ten (10) day period which follows the occurrence of that indemnification.

ARTICLE XIII **BOOKS, RECORDS, AND ACCOUNTS**

The Corporation shall keep or cause to be kept correct and complete books and records of account and shall also keep minutes of the proceedings of the Board of Directors and its committees and/or membership, all of which shall be kept separate and apart from the books, records, accounts, and minutes of its subsidiaries and affiliates. In addition, the Corporation shall annually cause a certified audit of its accounts to be made and shall cause to be filed the necessary reports, tax returns, or other documents as may be required by law on its own behalf.

ARTICLE XIV
FISCAL YEAR

The fiscal year of the Corporation shall end on the 30th day of September of each year.

ARTICLE XV
SEAL

The Board of Directors shall provide a corporate seal which shall be in the form of a circle and shall have inscribed thereon the name of the Corporation and the words, "**Corporate Seal, Illinois.**"

ARTICLE XVI
WAIVER OF NOTICE

Whenever any notice whatever is required to be given under the provisions of the General Not-for-Profit Corporation Act of the State of Illinois or under the provisions of the Articles of Incorporation or the Bylaws of the Corporation, a waiver thereof in writing signed by the person or persons entitled to such notice, whether before or after the times stated therein, shall be deemed equivalent to the giving of such notice.

ARTICLE XVII
OFFICES

The Corporation shall have and continuously maintain in this State a registered office and registered agent whose office is identical with such registered office, and may have other offices within or without the State of Illinois as the Board of Directors may from time to time determine.

ARTICLE XVIII
AMENDMENTS

At any regular meeting of the Board of Directors or at a special meeting of the Board of Directors, if notice thereof is contained in the notice for a special meeting, at which a quorum is present at either, these Bylaws or the Articles of Incorporation may be repealed and/or amended either in whole or in part by resolution of not less than a majority of the members of the Board of Directors. No amendment of these Bylaws or the Articles of Incorporation shall be effective until and unless approved by the Corporate Member. Notwithstanding the foregoing, the Corporate Member shall have the ability to alter, amend, modify, or repeal these Bylaws or the Articles of Incorporation, in whole or in part, whenever in its discretion it deems appropriate; provided, however, that the provisions of Article V, of Article VI, and of Article VII, Section 2 of these Bylaws, and this Article XVIII of these Bylaws, may not be amended by the Corporate Member without the concurrence of the Board of Directors.

ARTICLE XIX
SELF-EVALUATION

The Board of Directors shall complete a self-evaluation and collective evaluation annually in an effort to review its performance and report the results of the evaluation at a regularly scheduled meeting of the Board of Directors.

ARTICLE XX
BYLAW REVIEW

These Bylaws shall be reviewed annually by the Board of Directors; provided, however, that such review may be delegated to the governance committee. Recommendations for revisions will be made by the Board of Directors to the Corporate Member for consideration and approval.

ARTICLE XXI
CODE OF ETHICS AND CONFLICTS OF INTEREST POLICY

The Hospital expects and demands ethical conduct and compliance with all laws by the Hospital's officers, directors, employees and other agents, and the Hospital relies on the good faith of such officers, directors, employees and agents in the exercise of their duties and responsibilities to the Hospital. The purposes of the Hospital's Code of Ethics and Conflicts of Interest Policy are to: (a) memorialize the Hospital's commitment to ethical and legally compliant conduct; (b) offer guidance to the Hospital's officers, directors, employees and agents, through the implementation of this Code of Ethics and Conflicts of Interest Policy, to promote the avoidance of circumstances and situations which are, or which appear to be, in conflict with their duties and responsibilities to the Hospital in order to protect the Hospital's interests when the Hospital is contemplating entering into a transaction or arrangement which could benefit the private interests of an officer, director, employee or other agent of the Hospital; and (c) articulate the Hospital's policies to be followed when assessing ethical conduct and potential conflicts of interest. This Code of Ethics and Conflicts of Interest Policy is intended to supplement, without replacing, any applicable state laws or regulations governing ethical conduct and/or conflicts of interest which are applicable to nonprofit and charitable corporations.

Chairman

Secretary

February 14, 1974
Date Adopted

Adopted February 14, 1974
Amended August 16, 1979
Amended February 14, 1980
Amended February 9, 1984
Amended February 13, 1986
Amended February 12, 1987
Reviewed August 21, 1989
Amended February 14, 1991
Amended February 11, 1993
Amended February 10, 1994
Amended February 8, 1996
Amended February 13, 1997
Amended February 12, 1998
Amended February 10, 2000
Amended February 8, 2001
Amended February 13, 2003
Amended February 12, 2009
Amended February 11, 2010
Amended February 7, 2013
Amended and Restated _____, 2014

EXHIBIT B
AMENDED AND RESTATED BYLAWS OF PAH AFFILIATES

EXHIBIT B-1

**AMENDED AND RESTATED BYLAWS OF
PASSAVANT AREA HOSPITAL FOUNDATION**

See attached.

AMENDED AND RESTATED BYLAWS
OF
PASSAVANT AREA HOSPITAL FOUNDATION

ARTICLE I
Offices

The Foundation shall continuously maintain in the State of Illinois a registered office and a registered agent whose business office is identical with such registered office and may have other offices within or without the state.

ARTICLE II
Purposes

SECTION 1. GENERAL PURPOSE. Any purpose that would qualify for tax-deductible gifts under Section 170(c) of the United States Internal Revenue Code 26 U.S.C. Sec. 170(c), as now or hereafter amended. Any such purpose that is deemed to be charitable under subsection (a)(1) of this Section.

SECTION 2. SPECIFIC PURPOSE. Without limiting the general purpose stated in Section 1, herein, the specific purpose of the Foundation will be to establish and maintain relationships that generate philanthropic support to enhance The Passavant Memorial Area Hospital Association's (referred to herein as the "Hospital") ability to provide excellence in health care.

ARTICLE III
Members

SECTION 1. MEMBERS. The sole member of the Foundation shall be The Passavant Memorial Area Hospital Association, and any successor to such corporation resulting from merger, consolidation, or other corporate reorganization (the "Corporate Member"). If at any time the Corporate Member shall cease to exist and there is no successor corporation, the Board of Trustees may elect a new member or, at its discretion, amend these Bylaws and the Articles of Incorporation as it deems appropriate.

SECTION 2. POWERS AND RIGHTS OF MEMBERS. The power and authority of the Corporate Member concerning the affairs of the Foundation are as set forth in the following:

- A. Approval of all annual and long-term capital and operating budgets and strategic plans of the Foundation;
- B. Approval of any amendment to the Bylaws or Articles of Incorporation of the Foundation;

C. Approval of any voluntary dissolution, merger, consolidation, sale or transfer of substantially all of the Foundation's assets (defined as 10% or more), or any creation of a subsidiary or affiliate corporation of the Foundation;

D. Removal of the President, upon mutual agreement with the Board of Trustees;

E. Appointment of trustees of the Foundation in accordance with Section 2 of Article IV of these Bylaws;

F. Removal of any trustee of the Foundation with or without cause;

G. Approval of capital expenditures in excess of \$1,000,000;

H. Approval of any guaranty of debt greater than \$250,000, including capital leases;

I. Approval of any agreement or transaction of material nature with another corporation controlled by or affiliated with the Corporate Member;

J. Approval of the selection of, or changes of, independent auditors;

K. Approval of the entry into, renewal of, or termination of contracts to provide covered healthcare services to beneficiaries of managed care contracts;

L. Approval of applications to the Illinois Health Facilities Planning Board for a permit or certificate of need for a proposed activity, whether or not involving a capital expenditure;

M. Approval of any sale or transfer of the Foundation's assets to a non-affiliated entity or third-party entity, if such assets have a value in excess of \$500,000;

N. Approval of any significant changes in the Foundation's insurance specifications or limits;

O. Approval of any contract between the Foundation and a third party which involves the provision of goods and/or services having a value in excess of \$1,000,000 for capital or \$1,500,000 in aggregate for operating and capital budgets which had not been previously approved by the Corporate Member in an annual capital or operating budget;

P. Approval of the borrowing of any sum, the principal of which exceeds \$250,000, or which has a stated term of greater than one year, or which is secured by a mortgage of all or any portion of the Foundation's real property or the creation of a security interest in the Foundation's assets, including personal property and revenues, for the benefit of the lender, lessor or vendor, or the defeasance, advance payment or cancellation of any outstanding debt of the category described herein;

Q. Approval of any contract for physician services having a value in excess of \$400,000;

R. Approval of the sale of any of the Foundation's real property or interest therein or purchases of any additional real estate; and

S. Approval of any new or changes to existing long-term or master institutional plans.

SECTION 3. ANNUAL MEETING. The annual meeting of the Foundation shall be held at a time determined by the Hospital Board of Directors. The purpose of the annual meeting shall be the election of the Board of Trustees of the Foundation, the presentation by the Executive Director of the Foundation of the annual report of the Foundation to the Hospital Board of Directors as to the preceding year's status and activities, and the transaction of such other business as may come before the meeting.

SECTION 4. NO MEMBERSHIP CERTIFICATES. No membership certificates of the Foundation shall be required.

ARTICLE IV Board of Trustees

SECTION 1. GENERAL POWERS. The affairs of the Foundation shall be managed by or under the direction of its Board of Trustees.

SECTION 2. NUMBER, TENURE, AND QUALIFICATIONS. The number of trustees shall be a minimum of eleven (11) and a maximum of fifteen (15) as determined by resolution of the Board of Directors of the Hospital from time to time. Each trustee shall hold office until his or her successor shall have been elected and qualified. Trustees shall be residents of the geographic service area of the Hospital.

A. *Permanent Trusteeships.* Four (4) of the trustees shall be permanent trustees who must be members of the Hospital's Board of Directors as selected by the Hospital's Board of Directors from time to time. Such directors will likewise possess full voting rights as a trustee of the Foundation.

B. *Elected Trusteeships.* The remaining trustees shall be elected annually at the Annual Meeting. The Board of Trustees shall nominate trustees for the coming year and submit that list to the Hospital's Board of Directors no later than 60 days before the Annual Meeting. Additionally, the Board of Trustees, for any vacancy created by reason of an increase in the number of trustees, death, incapacity, removal, resignation, or any other reason, shall submit its nominee(s) to the Hospital's Board of Directors, which shall vote upon the approval of the nomination within 60 days of submission of the nomination.

C. *Ex-Officio (Non-Voting) Trustees:* The President and Chief Financial Officer of the Hospital and the Executive Director of the Foundation shall serve as ex-

officio, non-voting, trustees of the Foundation, by virtue of his or her office, so long as he or she is serving in that capacity.

SECTION 3. REGULAR MEETINGS. A regular annual meeting of the Board of Trustees shall be held as set forth in Article III, the Board of Trustees may provide, by resolution, the time and place for the holding of additional regular meetings of the board without other notice than such resolution.

SECTION 4. SPECIAL MEETINGS. Special meetings of the Board of Trustees may be called by or at the request of the president or any two trustees. The person or persons authorized to call special meetings of the board may fix any place within the Hospital's service area as the place for holding any special meeting of the board called by them.

SECTION 5. NOTICE. Notice of any special meeting of the Board of Trustees shall be given at least 2 days previous thereto by written notice to each trustee at his or her electronic mail (e-mail) address or postal address as shown by the records of the Foundation except that no special meeting of trustees may remove a trustee unless written notice of the proposed removal is delivered to all trustees at least 20 days prior to such meeting. If mailed, such notice shall be deemed to be delivered when deposited in the United States mail in a sealed envelope so addressed, with postage thereon prepaid. If e-mailed, the notice shall be deemed delivered at the date and time affixed on the e-mail message at the time of sending. Notice of any special meeting of the Board of Trustees may be waived in writing signed by the person or persons entitled to the notice either before or after the time of the meeting. The attendance of a trustee at any meeting shall constitute a waiver of notice of such meeting, except when a trustee attends a meeting for the express purpose of objecting to the transaction of any business because the meeting is not lawfully called or convened. Neither the business to be transacted at, nor the purpose of, any regular or special meeting of the board need be specified in the notice or waiver of notice of such meeting, unless specifically required by law or by these bylaws.

SECTION 6. QUORUM. A majority of the voting members of the Board of Trustees shall constitute a quorum for the transaction of business at any meeting of the Board of Trustees, provided that if less than a majority of the trustees are present at said meeting, a majority of the trustees present may adjourn the meeting to another time without further notice.

SECTION 7. MANNER OF ACTING. The act of a majority of the trustees present at a meeting at which a quorum is present shall be the act of the Board of Trustees, unless the act of a greater number is required by statute, these bylaws, or the articles of incorporation. No trustee may act by proxy on any matter. It shall require the affirmative vote of seventy-five percent (75%) of the trustees in office at a duly called meeting to voluntarily dissolve the Foundation or to determine the manner of distributing funds upon dissolution regardless of the reason for the dissolution.

SECTION 8. RESIGNATION AND REMOVAL OF TRUSTEES. A trustee may resign at any time upon written notice to the Board of Trustees. A trustee may be removed with or without cause by the Corporate Member, or as otherwise specified by statute.

SECTION 9. INFORMAL ACTION BY TRUSTEES. The authority of the Board of Trustees may be exercised without a meeting if a consent in writing, setting forth the action taken, is signed by all of the trustees entitled to vote.

SECTION 10. COMPENSATION. The trustees shall not be compensated for their service to the Foundation as a trustee. By resolution of the Board of Trustees, the trustees may be paid their reasonable expenses, if any, of attendance at each meeting of the board and for such expenses incurred in the course of their duties.

SECTION 11. PRESUMPTION OF ASSENT. A trustee of the Foundation who is present at a meeting of the Board of Trustees at which action on any Foundation matter is taken shall be conclusively presumed to have assented to the action taken unless his or her dissent shall be entered in the minutes of the meeting or unless he or she shall file his or her written dissent to such action with the person acting as the secretary of the meeting before the adjournment thereof or shall forward such dissent by registered or certified mail to the secretary of the Foundation immediately after the adjournment of the meeting. Such right to dissent shall not apply to a trustee who voted in favor of such action.

ARTICLE V Officers

SECTION 1. OFFICERS. The officers of the Foundation shall be a president, two or more vice presidents (the number thereof to be determined by the Board of Trustees), a treasurer, a secretary, and such other officers as may be elected or appointed by the Board of Trustees. Officers whose authority and duties are not prescribed in these bylaws shall have the authority and perform the duties prescribed, from time to time, by the Board of Trustees. Any two or more offices may be held by the same person.

SECTION 2. ELECTION AND TERM OF OFFICE. All officers of the Foundation, except the Executive Director which position is discussed further herein at Section 9, shall be elected annually by the Board of Trustees at the regular annual meeting of the Board of Trustees. If the election of officers shall not be held at such meeting, such election shall be held as soon thereafter as conveniently may be. Vacancies may be filled or new offices created and filled at any meeting of the Board of Trustees. Each officer shall hold office until his or her successor shall have been duly elected and shall have qualified, until his or her death, or until he or she shall resign or shall have been removed in the manner hereinafter provided. Election of an officer shall not of itself create contract rights.

SECTION 3. REMOVAL. Any officer elected or appointed by the Board of Trustees may be removed by the Board of Trustees whenever in its judgment the best interests of the Foundation would be served thereby, but such removal shall be without prejudice to the contract rights, if any, of the person so removed.

SECTION 4. PRESIDENT. The president shall be the principal executive officer of the Foundation. Subject to the direction and control of the Board of Trustees, he or she shall be in charge of the business and affairs of the Foundation; he or she shall see that the resolutions and directives of the Board of Trustees are carried into effect except in those instances in which that

responsibility is assigned to some other person by the Board of Trustees; and, in general, he or she shall discharge all duties incident to the office of president and such other duties as may be prescribed by the Board of Trustees. He or she shall preside at all meetings of the members and of the Board of Trustees. Except in those instances in which the authority to execute is expressly delegated to another officer or agent of the Foundation or a different mode of execution is expressly prescribed by the Board of Trustees or these bylaws, he or she may execute for the Foundation any contracts, deeds, mortgages, bonds, or other instruments that the Board of Trustees has authorized to be executed, and he or she may accomplish such execution either individually or with the secretary, any assistant secretary, or any other officer thereunto authorized by the Board of Trustees, according to the requirements of the form of the instrument.

He or she may vote all securities that the Foundation is entitled to vote except as and to the extent such authority shall be vested in a different officer or agent of the Foundation by the Board of Trustees.

SECTION 5. VICE PRESIDENTS. There shall be two vice presidents – one for stewardship and gifts, and one for nominations. Each shall serve as chair of the standing committee of the same name as created by these bylaws. The vice presidents shall assist the president in the discharge of his or her duties as the president may direct and shall perform such other duties as from time to time may be assigned to him or her by the president or the Board of Trustees. In the absence of the president or in the event of his or her inability or refusal to act, the vice president, in the order named above, shall perform the duties of the president and, when so acting, shall have all the powers of and be subject to all the restrictions on the president. Except in those instances in which the authority to execute is expressly delegated to another officer or agent of the Foundation or a different mode of execution is expressly prescribed by the Board of Trustees or these bylaws, the vice president (or any of them if there is more than one) may execute for the Foundation any contracts, deeds, mortgages, bonds, or other instruments that the Board of Trustees has authorized to be executed, and he or she may accomplish such execution either individually or with the secretary, any assistant secretary, or any other officer thereunto authorized by the Board of Trustees, according to the requirements of the form of the instrument.

SECTION 6. TREASURER. The treasurer shall be the principal accounting and financial officer of the Foundation. He or she shall (a) have charge of and be responsible for the maintenance of adequate books of account for the Foundation; (b) have charge and custody of all funds and securities of the Foundation, and be responsible therefor, and for the receipt and disbursement thereof; and (c) perform all the duties incident to the office of treasurer and such other duties as from time to time may be assigned to him or her by the president or by the Board of Trustees. If required by the Board of Trustees, the treasurer shall give a bond for the faithful discharge of his or her duties in such sum and with such surety or sureties as the Board of Trustees shall determine.

SECTION 7. SECRETARY. The secretary shall (a) record the minutes of the meetings of the members and of the Board of Trustees in one or more books provided for that purpose; (b) see that all notices are duly given in accordance with the provisions of these bylaws or as required by law; (c) be a custodian of the corporate records; (d) keep a register of the post office address of each member which shall be furnished to the secretary by such member; and

(e) perform all duties incident to the office of secretary and such other duties as from time to time may be assigned to him or her by the president or by the Board of Trustees.

SECTION 8. ASSISTANT TREASURERS AND ASSISTANT SECRETARIES. The assistant treasurers and assistant secretaries shall perform such duties as shall be assigned to them by the treasurer or the secretary, respectively, or by the president or the Board of Trustees. If required by the Board of Trustees, the assistant treasurers shall give bonds for the faithful discharge of their duties in such sums and with such sureties as the Board of Trustees shall determine.

SECTION 9. EXECUTIVE DIRECTOR. The Executive Director is an officer of the Foundation and shall be the manager of the Foundation's daily operations and shall carry out such functions and duties as directed by the Board of Trustees. The Executive Director shall be an employee of the Hospital and be employed upon such terms and conditions as the Hospital may, in its discretion, deem advisable. The cost of the Executive Director's salary and benefits may be invoiced to the Foundation for reimbursement at such time or times that the Hospital deems appropriate. The Executive Director shall report to the President of the Hospital and the Executive Committee of the Foundation. His or her performance evaluations shall be conducted by the President and CEO of the Hospital upon eliciting input from the Executive Committee of the Foundation.

SECTION 10. SALARIES. The salary of the Executive Director shall be fixed from time to time by the President of the Hospital and upon the advice of the Board of Trustees of the Foundation. No other officer shall receive compensation for their services to the Foundation as an officer.

ARTICLE VI

Committees, Commissions, and Advisory Boards

SECTION 1. COMMITTEES. The Board of Trustees, by resolution adopted by a majority of the trustees in office, may designate one or more committees, each of which will consist of two or more trustees and such other persons as the Board of Trustees designates, provided that a majority of each committee's members are trustees. The committees, to the extent provided in said resolution and not restricted by law, shall have and exercise the authority of the Board of Trustees in the management of the Foundation; but the designation of such committees and the delegation thereto of authority shall not operate to relieve the Board of Trustees, or any individual trustee, of any responsibility imposed on it, him, or her by law. Required standing committees shall include a board nominating committee; an executive, finance & investment committee; a stewardship and gifts committee, and such other standing committees as the Board of Trustees may authorize.

A. Board Nominating Committee

The President of the Foundation shall appoint, on an annual basis, a board nominating committee, which shall be comprised of two (2) or more trustees. To the extent any of the individuals nominated are not acceptable to the Corporate Member, the board nominating

committee shall submit new names until an individual acceptable to the Corporate Member for such position(s) is(are) elected.

B. Executive, Finance & Investment Committee

The executive, finance & investment committee (hereinafter referred to as the executive committee) shall consist of the President, the Vice President for Stewardship and Gifts, the Vice President for Nominations, the Treasurer, the Secretary, and the Executive Director of the Foundation; and the President and the Chief Financial Officer of the Hospital. The executive committee shall have the power to transact all regular business of the Foundation during the interim between meetings of the Board of Trustees, provided any action taken shall not conflict with the policies of the Board of Trustees, and the committee shall refer all matters of major importance to the Board of Trustees. The executive committee shall be responsible for monitoring and reporting to the Board of Trustees and management of funds in accordance with the policies, Rules and Regulations which are adopted and prescribed by the Board of Trustees of the Foundation. The President of the Foundation shall chair this committee. The Foundation shall follow the investment policy of the Hospital, as amended from time to time.

C. Stewardship and Gifts Committee

The stewardship and gifts committee shall explore, review, recommend, and assist in the implementation of programs intended to produce financial support in the major areas of giving: wills and bequests; life income agreements; life insurance; annuities; short and long term trusts; and gifts of stocks, bonds, securities, and real estate. The committee shall also identify individuals and organizations who have the capacity to become annual, major or planned gift donors. Additionally, the stewardship and gifts committee shall annually review stewardship policies and donor communication tools. The committee shall explore and recommend stewardship practices that enhance donor relationship with the Foundation. The committee shall appropriately acknowledge gifts to the Foundation.

SECTION 2. COMMISSIONS OR ADVISORY BODIES. Commissions or advisory bodies not having and exercising the authority of the Board of Trustees in the Foundation may be designated or created by the Board of Trustees and shall consist of such persons as the Board of Trustees designates. A commission or advisory body may or may not have trustees as members, as the Board of Trustees determines. The commission or advisory body may not act on behalf of the Foundation or bind it to any actions but may make recommendations to the Board of Trustees or to the officers of the Foundation.

SECTION 3. TERM OF OFFICE. Each member of a committee, advisory board, or commission shall continue as such until the next annual meeting of the members of the Foundation and until his or her successor is appointed, unless the committee, advisory board, or commission shall be sooner terminated, or unless such member resigns, is removed from such committee, advisory board, or commission by the Board of Trustees, or ceases to qualify as a member thereof.

SECTION 4. CHAIR. The Vice President of the Foundation for each of the standing committees prescribed by these bylaws shall serve as chair of the standing committee. The

President of the Foundation shall appoint a chair of all other such committees, advisory boards, or commissions unless another person is appointed by the Board of Trustees.

SECTION 5. VACANCIES. Vacancies in the membership of any committee, advisory board, or commission may be filled by appointments made in the same manner as provided in the case of the original appointments.

SECTION 6. QUORUM. Unless otherwise provided by the resolution of the Board of Trustees designating a committee, advisory board, or commission, a majority of the whole committee, advisory board, or commission shall constitute a quorum, and the act of a majority of the members present at a meeting at which a quorum is present shall be the act of the committee, advisory board, or commission.

SECTION 7. RULES. Each committee, advisory board, or commission may adopt rules for its own government not inconsistent with these bylaws or with rules adopted by the Board of Trustees.

SECTION 8. INFORMAL ACTION. The authority of a committee may be exercised without a meeting if a consent in writing, setting forth the action taken, is signed by all the members entitled to vote.

ARTICLE VII

Contracts, Checks, Deposits, and Funds

SECTION 1. CONTRACTS. The Board of Trustees may authorize any officer or officers or agent or agents of the Foundation, in addition to the officers so authorized by these bylaws, to enter into any contract or execute and deliver any instrument in the name of and on behalf of the Foundation, and such authority may be general or confined to specific instances.

SECTION 2. CHECKS, DRAFTS, ETC. All checks, drafts, or other orders for the payment of money, notes, or other evidences of indebtedness issued in the name of the Foundation shall be signed by such officer or officers or agent or agents of the Foundation and in such manner as shall from time to time be determined by resolution of the Board of Trustees. In the absence of such determination by the Board of Trustees, such instruments shall be signed by the treasurer or an assistant treasurer and countersigned by the president or a vice president of the Foundation.

SECTION 3. DEPOSITS. All funds of the Foundation shall be deposited from time to time to the credit of the Foundation in such banks, trust companies, or other depositories as the Board of Trustees may select.

SECTION 4. GIFTS. The Board of Trustees may accept on behalf of the Foundation any contribution, gift, bequest, or devise for the general purposes or for any special purpose of the Foundation.

ARTICLE VIII

Books and Records

The Foundation shall keep correct and complete books and records of account. It shall also keep minutes of the proceedings of its members, Board of Trustees, and committees having any of the authority of the Board of Trustees and shall keep at the registered or principal office a record giving the names and addresses of the members entitled to vote. All books and records of the Foundation may be inspected by any member, or his or her agent or attorney, for any proper purpose at any reasonable time.

ARTICLE IX Fiscal Year

The fiscal year of the Foundation shall coincide with that of the corporate member.

ARTICLE X Waiver of Notice

Whenever any notice is required to be given under the provisions of the General Not-For-Profit Foundation Act of Illinois or under the provisions of the articles of incorporation or the bylaws of the Foundation, a waiver thereof in writing, signed by the person or persons entitled to such notice, whether before or after the time stated therein, shall be deemed equivalent to the giving of such notice. Attendance at any meeting shall constitute waiver of notice thereof unless the person at the meeting objects to the holding of the meeting because proper notice was not given.

ARTICLE XI Indemnification

SECTION 1. INDEMNIFICATION IN ACTIONS OTHER THAN BY OR IN THE RIGHT OF THE FOUNDATION. The Foundation may indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending, or completed action, suit, or proceeding, whether civil, criminal, administrative, or investigative (other than an action by or in the right of the Foundation) by reason of the fact that he or she is or was a trustee, officer, employee, or agent of the Foundation, or is or was serving at the request of the Foundation as a trustee, officer, employee, or agent of another Foundation, partnership, joint venture, trust, or other enterprise, against expenses (including attorneys' fees, judgments, fines, and amounts paid in settlement actually and reasonably incurred by such person in connection with such action, suit, or proceeding, if such person acted in good faith and in a manner he or she reasonably believed to be in, or not opposed to, the best interests of the Foundation and, with respect to any criminal action or proceeding, had no reasonable cause to believe his or her conduct was unlawful. The termination of any action, suit, or proceeding by judgment, order, settlement, or conviction or upon a plea of nolo contendere or its equivalent shall not, of itself, create a presumption that the person did not act in good faith and in a manner he or she reasonably believed to be in or not opposed to the best interests of the Foundation or, with respect to any criminal action or proceeding, that the person had reasonable cause to believe that his or her conduct was unlawful.

SECTION 2. INDEMNIFICATION IN ACTIONS BY OR IN THE RIGHT OF THE FOUNDATION. The Foundation may indemnify any person who was or is a party or is

threatened to be made a party to any threatened, pending, or completed action or suit by or in the right of the Foundation to procure a judgment in its favor by reason of the fact that such person is or was a trustee, officer, employee, or agent of the Foundation, or is or was serving at the request of the Foundation as a trustee, officer, employee, or agent of another Foundation, partnership, joint venture, trust, or other enterprise, against expenses (including attorneys' fees) actually and reasonably incurred by such person in connection with the defense or settlement of such action or suit, if such person acted in good faith and in a manner he or she reasonably believed to be in, or not opposed to, the best interests of the Foundation, provided that no indemnification shall be made in respect of any claim, issue, or matter as to which such person shall have been adjudged to be liable for negligence or misconduct in the performance of his or her duty to the Foundation, unless, and only to the extent that the court in which such action or suit was brought shall determine upon application that, despite the adjudication of liability, but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses as the court shall deem proper.

SECTION 3. RIGHT TO PAYMENT OF EXPENSES. To the extent that a trustee, officer, employee, or agent of the Foundation has been successful, on the merits or otherwise, in the defense of any action, suit, or proceeding referred to in Sections 1 and 2 of this Article, or in defense of any claim, issue, or matter therein, such person shall be indemnified against expenses (including attorneys' fees) actually and reasonably incurred by such person in connection therewith.

SECTION 4. DETERMINATION OF CONDUCT. Any indemnification under Sections 1 and 2 of this Article (unless ordered by a court) shall be made by the Foundation only as authorized in the specific case, upon a determination that indemnification of the trustee, officer, employee, or agent is proper in the circumstances because he or she has met the applicable standard of conduct set forth in Sections 1 or 2 of this Article. Such determination shall be made (a) by the Board of Trustees by a majority vote of a quorum consisting of trustees who were not parties to such action, suit, or proceeding; (b) if such a quorum is not obtainable, or even if obtainable, if a quorum of disinterested trustees so directs, by independent legal counsel in a written opinion; or (c) by the members entitled to vote, if any.

SECTION 5. PAYMENT OF EXPENSES IN ADVANCE. Expenses incurred in defending a civil or criminal action, suit, or proceeding may be paid by the Foundation in advance of the final disposition of such action, suit, or proceeding, as authorized by the Board of Trustees in the specific case, upon receipt of an undertaking by or on behalf of the trustee, officer, employee, or agent to repay such amount, unless it shall ultimately be determined that he or she is entitled to be indemnified by the Foundation as authorized in this Article.

SECTION 6. INDEMNIFICATION NOT EXCLUSIVE. The indemnification provided by this Article shall not be deemed exclusive of any other rights to which those seeking indemnification may be entitled under any bylaw, agreement, vote of members or disinterested trustees, or otherwise, both as to action in his or her official capacity and as to action in another capacity while holding such office, and shall continue as to a person who has ceased to be a trustee, officer, employee, or agent, and shall inure to the benefit of the heirs, executors, and administrators of such a person.

SECTION 7. INSURANCE. The Foundation may purchase and maintain insurance on behalf of any person who is or was a trustee, officer, employee, or agent of the Foundation, or who is or was serving at the request of the Foundation as a trustee, officer, employee, or agent of another Foundation, partnership, joint venture, trust, or other enterprise, against any liability asserted against such person and incurred by such person in any such capacity, or arising out of his or her status as such, whether or not the Foundation would have the power to indemnify such person against such liability under the provisions of this Article.

SECTION 8. NOTICE TO MEMBERS. If the Foundation has paid indemnity or has advanced expenses under this Article to a trustee, officer, employee, or agent, the Foundation shall report the indemnification or advance in writing to any members entitled to vote with or before the notice of the next meeting of the members entitled to vote.

SECTION 9. REFERENCES TO FOUNDATION. For purposes of this Article, references to "the Foundation" shall include, in addition to the surviving Foundation, any merging Foundation (including any Foundation having merged with a merging Foundation) absorbed in a merger that, if its separate existence had continued, would have had the power and authority to indemnify its trustees, officers, employees, or agents, so that any person who was a trustee, officer, employee, or agent of such merging Foundation, or was serving at the request of such merging Foundation as a trustee, officer, employee, or agent of another Foundation, partnership, joint venture, trust, or other enterprise, shall stand in the same position under the provisions of this Article with respect to the surviving Foundation as such person would have with respect to such merging Foundation if its separate existence had continued.

SECTION 10. OTHER REFERENCES. For purposes of this Article, references to "other enterprises" shall include employee benefit plans; references to "fines" shall include any excise taxes assessed on a person with respect to an employee benefit plan; and references to "serving at the request of the Foundation" shall include any service as a trustee, officer, employee, or agent of the Foundation that imposes duties on or involves services by such trustee, officer, employee, or agent with respect to an employee benefit plan, its participants, or beneficiaries. A person who acted in good faith and in a manner he or she reasonably believed to be in the best interests of the participants and beneficiaries of an employee benefit plan shall be deemed to have acted in a manner "not opposed to the best interests of the Foundation" as referred to in this Article.

ARTICLE XII Conflict of Interest

SECTION 1. FAIRNESS OF TRANSACTION. If a transaction is fair to the Foundation at the time it is authorized, approved, or ratified, the fact that a trustee of the Foundation is directly or indirectly a party to the transaction is not grounds for invalidating the transaction.

SECTION 2. VALIDITY OF TRANSACTION. In a proceeding contesting the validity of a transaction described in Section 1 of this Article, the person asserting validity has the burden of proving fairness unless the material facts of the transaction and the trustee's interest or relationship were disclosed or known to the Board of Trustees and the board or committee

authorized, approved, or ratified the transaction by the affirmative votes of a majority of disinterested trustees even though the disinterested trustees were less than a quorum.

SECTION 3. QUORUM. The presence of a trustee who is directly or indirectly a party to the transaction described in Section 1 of this Article or a trustee who is otherwise not disinterested may be counted in determining whether a quorum is present but may not be counted when the Board of Trustees or a committee then takes action on the transaction.

SECTION 4. INDIRECT PARTY. For purposes of this Article, a trustee is "indirectly" a party to a transaction if the other party to the transaction is a family member of the trustee or an entity in which the trustee has a material financial interest or of which the trustee is an officer, trustee, or general partner. The term "family member" is defined to only include the trustee's, spouse, civil union partner, parents, brothers, sisters, children, and the spouses/civil union partners of any of these family members.

ARTICLE XIII Amendments

The power to alter, amend, or repeal the bylaws or adopt new bylaws shall be vested in the Board of Trustees unless otherwise provided in the articles of incorporation or the bylaws. Such action may be taken at a regular or special meeting for which written notice of the purpose shall be given. No amendment of these Bylaws or the Articles of Incorporation shall be effective until and unless approved by the Corporate Member. Notwithstanding the foregoing, the Corporate Member shall have the ability to alter, amend, modify, or repeal these Bylaws or the Articles of Incorporation, in whole or in part, whenever in its discretion it deems appropriate. The bylaws may contain any provisions for the regulation and management of the affairs of the Foundation not inconsistent with law or the articles of incorporation.

The undersigned certify that the foregoing bylaws were adopted by resolution of the Board of Directors of The Passavant Memorial Area Hospital Association effective as of the ____ day of _____, 20__.

Chairman of the Board of Directors
Passavant Memorial Area
Hospital Association

Attest:

Secretary

EXHIBIT B-2

**AMENDED AND RESTATED BYLAWS OF
PASSAVANT PHYSICIAN ASSOCIATION, INC.**

See attached.

Amended and Restated Bylaws

Passavant Physician Association, Inc.

Article 1

Name

Section 1.1.

The name of the Corporation is Passavant Physician Association, Inc.

Article 2

Purposes

Section 2.1.

The Corporation is organized for charitable, educational and scientific purposes, but only to the extent and in such manner that such purposes constitute exclusively charitable, educational and scientific purposes within the meaning of Sections 501(c)(3) and 170 (c)(2)(B) of the Internal Revenue Code of 1986, as amended, or the corresponding provisions of any subsequent Federal tax law (hereinafter referred to as the "Code").

More specifically, the purposes of the Corporation shall include:

(a) To conduct health care and health care related activities which support and benefit the operation of health care facilities in Jacksonville, Illinois, and elsewhere, in which the treatment of patients shall be provided in accordance with professional standards which are consistent with reasonably maintainable goals.

(b) To otherwise operate exclusively for charitable, scientific and educational purposes within the meaning of Section 501(c)(3) of the Code, in the course of which operation:

(1) No part of the net earnings of the Corporation shall inure to the benefit of, or be distributable to, its members, directors, officers or other persons, except that the Corporation shall be authorized and empowered to pay reasonable compensation for services rendered and to make payments and distributions in furtherance of the purposes set forth herein.

(2) No substantial part of the activities of the Corporation shall be the carrying on of propaganda, or otherwise attempting to influence legislation, and the Corporation shall not participate in, or intervene in (including the publishing or distribution of statements) any political campaign on behalf of or in opposition to any candidate for public office.

(3) Notwithstanding any other provisions of these Bylaws, the Corporation shall not carry on any other activities not permitted to be carried on: (a) by a corporation exempt from Federal income tax under Section 501(c)(3) of the Code; or (b) a corporation, contributions to which are deductible under Section 170(c)(2) of the Code.

In the event of the dissolution of the Corporation, the Board of Directors of the Corporation (the "Board") shall, after paying or making provision for the payment of all of the liabilities of the Corporation, distribute all of the assets of the Corporation to the Corporate Member (as set forth in Section 3.1 of these Bylaws), if then in existence and if qualified as an exempt organization under Section 501(c)(3) of the Code, otherwise in such manner, or to such organization or organizations organized and operated exclusively for charitable, educational or scientific purposes as shall at the time qualify as an exempt organization or organizations under Section 501(c)(3) of the Code, and as shall be affiliated with Memorial Health System, an Illinois not-for-profit corporation, and as the Board shall determine. Any such assets not so disposed of shall be disposed of by a court of competent jurisdiction of the county in the state in which the principal office of the Corporation is then located, exclusively for such purposes or to such organization or organizations, as said court shall determine, which are organized and operated exclusively for such purposes.

Article 3

Membership

Section 3.1. Corporate Member. The Corporate Member of the Corporation shall be The Passavant Memorial Area Hospital Association, an Illinois not-for-profit corporation. The Corporation shall have no other members.

Section 3.2. Powers of Corporate Member. The Corporate Member of the Corporation shall have such powers as are provided for in the Articles of Incorporation, these Bylaws and the laws of the state of Illinois, including, but not limited to, the exclusive power to:

- (a) Remove the President, upon mutual agreement with the Board of Directors;
- (b) Appoint directors of the Corporation in accordance with Section 7.2 of these Bylaws; and
- (c) Remove any director of the Corporation with or without cause.

In addition, the Corporate Member reserves the powers set forth in Section 5.1 and Article 11 of these Bylaws. The Board of Directors of the Corporate Member or such representative as the Corporate Member may designate in writing to the Secretary of the Corporation may exercise the powers of the Corporate Member.

Section 3.3. Transfer of Membership. Membership in the Corporation is not transferable or assignable.

Article 4

Meetings of the Corporate Member

Section 4.1. Annual Meeting. Beginning with the year 2014, the annual meeting of the Corporate Member shall be held in the initial quarter of each calendar year, on a date between January 1st and March 31st, or such other date, time and place as may be determined by the Corporate Member. The purpose of the annual meeting shall be to elect Directors, to hear the reports of the officers of the Corporation and to transact such other business as may come before the meeting.

Section 4.1. Special Meetings. Special meetings of the Corporate Member may be called by the Chairman of the Corporation or the Corporate Member. The person or persons authorized to call special meetings may fix the date, time and place for holding the special meetings.

Article 5

Board of Directors

Section 5.1. General Powers. Subject to the authority of the Corporate Member as provided in this Section, the Board shall manage the business and affairs of the Corporation and shall exercise in the name of and on behalf of the Corporation all of the rights and privileges legally exercisable by the Corporation as a corporate entity except as otherwise may be provided by law, the Articles of Incorporation, and these Bylaws. The power and authority of the Board to exercise the following specific powers are conditioned upon the advance approval of the Corporate Member:

- (a) Adopt, or permit the adoption of, any annual or long-term capital or operating budgets or strategic plans of the Corporation;
- (b) Adopt, or permit the adoption of, any amendment to the Bylaws or Articles of Incorporation of the Corporation;
- (c) Adopt, or permit the adoption of, any voluntary dissolution, merger, consolidation, sale or transfer of substantially all of the Corporation's assets (defined as 10% or more), or any creation of a subsidiary or affiliate corporation of the Corporation;
- (d) Approve, or permit the approval of, capital expenditures in excess of \$1,000,000;
- (e) Approve, or permit the approval of, any guaranty of debt greater than \$250,000, including capital leases;

(f) Authorize or permit the Corporation to enter into any agreement or transaction of material nature with another corporation controlled by or affiliated with the Corporate Member;

(g) Approve, or permit the approval of, the selection of, or changes of, independent auditors;

(h) Authorize or permit the entry into, renewal of, or termination of contracts to provide covered healthcare services to beneficiaries of managed care contracts;

(i) Approve, or permit the approval of, applications to the Illinois Health Facilities Planning Board for a permit or certificate of need for a proposed activity, whether or not involving a capital expenditure;

(j) Approve, or permit the approval of, any sale or transfer of the Corporation's assets to a non-affiliated entity or third-party entity, if such assets have a value in excess of \$500,000;

(k) Approve, or permit the approval of, any significant changes in the Corporation's insurance specifications or limits;

(l) Authorize or permit the Corporation to enter into any contract between the Corporation and a third party which involves the provision of goods and/or services having a value in excess of \$1,000,000 for capital or \$1,500,000 in aggregate for operating and capital budgets which had not been previously approved by the Corporate Member in an annual capital or operating budget;

(m) Approve, or permit the approval of, the borrowing of any sum, the principal of which exceeds \$250,000, or which has a stated term of greater than one year, or which is secured by a mortgage of all or any portion of the Corporation's real property or the creation of a security interest in the Corporation's assets, including personal property and revenues, for the benefit of the lender, lessor or vendor, or the defeasance, advance payment or cancellation of any outstanding debt of the category described herein;

(n) Authorize or permit the Corporation to enter into any contract for physician services having a value in excess of \$400,000;

(o) Approve, or permit the approval of, the sale of any of the Corporation's real property or interest therein or purchases of any additional real estate; and

(p) Adopt, or permit the adoption of, any new or changes to existing long-term or master institutional plans.

For the purposes of these Bylaws, the terms "affiliate" and "subsidiary" shall include any corporation, association, partnership, trust, joint venture or other entity controlling, controlled by or under common control with the Corporation.

Section 5.2. Number, Election and Qualifications. The number of Directors constituting the Board of the Corporation shall be not fewer than three (3) and not more than seven (7). Each Director shall be elected by the Corporate Member, as prescribed in Section 3.2 of these Bylaws. The number of Directors may be increased or decreased from time to time by amendment of these Bylaws; provided, however, no change in the number of Directors shall have the effect of shortening the term of an incumbent Director. Each Director holding office as of [April 1], 2014 shall continue to hold office for the remainder of his four (4)-year term, until his successor is elected and qualified or until his death, disqualification, resignation or removal. Thereafter, each Director shall hold office for a one (1)-year term, until his successor is elected and qualified or until his death, disqualification, resignation or removal. Directors shall consist of persons distinguished by their achievement and good judgment who have expertise in areas which will aid the Corporation in the development of programs and policies.

Section 5.3. Removal. The Corporate Member alone may remove a Director. Removal as a Director also shall constitute removal as an officer of the Corporation and as a member of all committees of the Board.

Section 5.4. Vacancies. The Corporate Member alone may fill a vacancy in the office of a Director due to death, resignation, disqualification, removal or otherwise. Director vacancies shall be filled in the manner prescribed for election of Directors. The Director elected to fill a vacancy shall hold office until the next annual meeting of the Corporate Member.

Section 5.5. Resignation. Any Director may resign his office at any time by filing a written resignation with the Secretary of the Corporation, which resignation shall become effective upon the date specified therein, or, if no date is specified therein, upon receipt by the Corporation at its principal place of office.

Section 5.6. Compensation. Directors as such shall not receive any stated salaries for their services, but by resolution of the Board, a fixed sum and expenses for attendance may be allowed for attendance at each regular or special meeting of the Board. Nothing herein contained shall be construed to preclude any Director from serving the Corporation in any other capacity and receiving compensation therefore.

Section 5.7. Conflict of Interest. Any possible conflict of interest on the part of a Director shall be disclosed to the Board. When any such interest becomes a matter of action for the Board, such Director shall not vote or use personal influence on the matter, and shall not be counted in the quorum for a meeting at which action by the Board is to be taken on the interest. The Director may, however, briefly state a position on the matter, and answer pertinent questions of members of the Board. The minutes of all actions taken on such matters shall clearly reflect that these requirements have been met.

Article 6

Meetings of the Board

Section 6.1. Annual Meeting. The annual meeting of the Board shall be the first regular meeting of the Board following the annual meeting of the Corporate Member and shall be held within ninety days of the annual meeting of the Corporate Member for the purpose of electing officers, appointing members of Board committees, and transacting such other business as may come before the meeting. No notice of the annual meeting of the Board shall be necessary.

Section 6.2. Regular Meetings. The Board shall hold regular meetings at such date, time and place as may be determined by resolution of the Board.

Section 6.3. Special Meetings. Special meetings may be called by the Chairman of the Corporation, the Corporate Member or at the written request of three-fifths of the entire Board.

Section 6.4. Voting. In all matters brought before the Board, each Director shall have one vote.

Section 6.5. Quorum. At any annual, regular, or special meeting, a majority of the Directors in office shall constitute a quorum. A Director may be noted as present at a meeting only if the Director is present in person.

Section 6.6. Manner of Acting. Unless otherwise required by law, the Articles of Incorporation or these Bylaws, the act of the majority of Directors present at a meeting at which a quorum is present shall be the act of the Board. Voting by proxy shall not be permitted.

Section 6.7. Notice and Waiver. Directors shall be given notice of each special meeting of the Board. Such notice shall set forth the date, time, place and purpose of the meeting and shall be signed by the Secretary of the Corporation. Notice shall be delivered to each Director not less than twenty-four hours prior to the meeting. A Director may waive notice by the execution of a written waiver, either before or after the holding of the meeting. Such waiver shall be filed with or entered upon the records of the Corporation. The attendance of a Director at a meeting without protest at the commencement of the meeting shall be deemed to be a waiver by him of notice.

Section 6.8. Informal Action by Directors. Any action required to be taken at a meeting of the Board, or any other action which may be taken at a meeting of the Board, may be taken without a meeting if a written consent, setting forth the action so taken, shall be signed by all of the Directors.

Article 7

Officers

Section 7.1. Number. The officers of the Corporation shall be a Chairman, a Vice Chairman, a President, a Treasurer and a Secretary, each of whom shall be elected or appointed

by the Board of Directors. The Board of Directors may appoint other officers, if it deems it necessary, who shall have such authority and shall perform such duties as from time to time may be prescribed by the Board of Directors. Any two (2) or more offices may be held by the same person.

Section 7.2. Election and Term of Office. The officers of the Corporation shall be elected by the Board of Directors at its annual meeting, to hold office for a term of one (1) year. If the election of officers is not held at that annual meeting, the election shall be held as soon thereafter as practicable. Vacancies may be filled or new offices filled at any meeting of the Board of Directors. Each officer shall hold office until his successor shall have been duly elected and shall have qualified or until his death or until he shall resign or shall have been removed in the manner hereinafter provided.

Section 7.3. Removal. Any officer or agent of the Corporation may be removed by the Board of Directors whenever in its judgment the best interests of the Corporation would be served thereby, but such removal shall be without prejudice to the contract rights, if any, of the person so removed. Election or appointment of an officer or agent shall not of itself create contract rights.

Section 7.4. Resignation. Any officer may resign at any time by giving written notice to the Board of Directors, or the President or Secretary of the Corporation. Any such resignation shall take effect at the date of the receipt of such notice or at any later time specified therein, and, unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

Section 7.5. Vacancies. A vacancy in any office because of death, resignation, removal, disqualification or otherwise may be filled by the Board of Directors for the unexpired portion of the term.

Section 7.6. Bonds. If the Board of Directors by resolution shall so require, any officer or agent of the Corporation shall give bond to the Corporation in such amount and with such surety as the Board of Directors may deem sufficient, conditioned upon the faithful performance of their respective duties and offices.

Section 7.7. Chairman. The Chairman shall preside at all meetings of the Board of Directors. Except as otherwise provided in Article 8 of these Bylaws, he shall appoint all committees, with the approval of the Board of Directors. The President shall report to the Chairman on all matters. He may sign, with the Secretary or any other proper officer of the Corporation thereunto authorized by the Board of Directors, any deeds, mortgages, bonds, contracts or other instruments which the Board of Directors has authorized to be executed, except in cases where the signing and execution thereof shall be expressly delegated by the Board of Directors or by these Bylaws to some other officer or agent of the Corporation or shall be required by law to be otherwise signed or executed.

Section 7.8. Vice Chairman. In the absence of the Chairman or in the event of his inability or refusal to act, the Vice Chairman shall perform the duties of the Chairman. The Vice Chairman shall perform such other duties as from time to time may be assigned to him by the Board of Directors or by the President.

Section 7.9. President. The President shall be the chief executive officer of the Corporation and shall in general supervise and control all of the business and affairs of the Corporation. He shall preside at all meetings of the Board of Directors. He may sign, with the Secretary or any other proper officer of the Corporation thereunto authorized by the Board of Directors, any deeds, mortgages, bonds, contracts or other instruments which the Board of Directors has authorized to be executed, except in cases where the signing and execution thereof shall be expressly delegated by the Board of Directors or by these Bylaws to some other officer or agent of the Corporation or shall be required by law to be otherwise signed or executed; and in general shall perform all duties incident to the office of President and such other duties as may be prescribed by the Board of Directors from time to time.

Section 7.10. Treasurer. The Treasurer shall: (a) have charge and custody of and be responsible for all funds and securities of the Corporation; receive and give receipts for moneys due and payable to the Corporation from any source whatsoever and deposit all such moneys in the name of the Corporation in such banks, trust companies or other depositories as shall be selected by the Board of Directors; and (b) in general, perform all duties incident to the office of Treasurer and all other duties as from time to time may be assigned to him by the Board of Directors or the President. If required by the Board of Directors, the Treasurer shall give a bond for the faithful discharge of his duties in the sum and with a surety or sureties as the Board of Directors shall determine. The Treasurer shall be elected from among the members of the Board of Directors.

Section 7.11. Secretary. The Secretary shall: (a) keep the minutes of the Board of Directors' meetings in one or more books provided for that purpose; (b) see that all notices are duly given in accordance with the provisions of these Bylaws or as required by law; (c) be custodian of the corporate records and, if the Corporation has a corporate seal, of the seal of the Corporation and see that the seal of the Corporation is affixed to all documents, the execution of which on behalf of the Corporation under its seal is duly authorized in accordance with the provisions of these Bylaws; (d) keep a register of the post office address of each Director; and (e) in general, perform all duties incident to the office of Secretary and all other duties as from time to time may be assigned to him by the Board of Directors or the President. The Secretary shall be elected from among the members of the Board of Directors.

Section 7.12. Salaries. The salaries of the officers, if any, shall be fixed from time to time by the Board of Directors, and no officer shall be prevented from receiving such salary by reason of the fact that he is also a Director of the Corporation. No salaried officer may receive any per diem compensation as a Director.

Article 8

Committees

Section 8.1. Classes of Committees. Committees of the Board of Directors shall be standing or special. Standing committees shall be authorized by the Board. Special committees may be established by the Board for such special tasks as circumstances warrant. With the exception of an Executive Committee, if one is established by the Board, no committee, whether standing or special, may act on behalf of the Corporation or bind the Corporation to any action but may make recommendations to the Board or to the officers of the Corporation. All committees shall keep a record of proceedings and the minutes of meetings shall be submitted to the Board.

Section 8.2. Appointments. Except as otherwise provided in this Article with respect to the Executive Committee, the chairmen and members of all committees shall be appointed by the Chairman of the Corporation, with the approval of the Board, for one-year terms following each annual meeting. Except as may be directed by these Bylaws or by the Board, committee members need not be Directors.

Section 8.3. Executive Committee. The Board of Directors, by resolution adopted by a majority of the Directors in office, may appoint an Executive Committee. The Executive Committee shall have two or more Directors, a majority of its membership shall be Directors and all committee members shall serve at the pleasure of the Board of Directors. The Executive Committee may exercise the authority of the Board of Directors in the management of the Corporation during intervals between meetings of the Board; provided, however, it may not: adopt a plan for distribution of the assets of the Corporation, or for dissolution; approve or recommend to the Corporate Member any act required by law or these Bylaws to be approved by the Corporate Member; fill vacancies on the Board or any of its committees; elect, appoint or remove any officer or Director or member of any committee, or fix the compensation of any member of a committee; adopt, amend, or repeal these Bylaws or the Articles of Incorporation of the Corporation; amend, alter, repeal or take any action inconsistent with any resolution or action of the Board; adopt a plan of merger or consolidation with another corporation, or authorize the sale, lease, exchange or mortgage of all or substantially all of the property or assets of the Corporation; or take any other action prohibited by law.

Article 9

Indemnification

Section 9.1. Actions Other Than by or in the Right of the Corporation. The Corporation shall indemnify any person who was or is a party, or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action by or in the right of the Corporation) by reason of the fact that he is or was a Director, officer, employee or agent of the Corporation, or who is or was serving at the request of the Corporation as a director, officer,

partner or trustee of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by such person in connection with such action, suit or proceeding, if such person acted in good faith and in a manner he reasonably believed to be in, or not opposed to, the best interests of the Corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful. The termination of any action, suit or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent, shall not, of itself, create a presumption that the person did not act in good faith and in a manner which he reasonably believed to be in or not opposed to the best interests of the Corporation or, with respect to any criminal action or proceeding, that the person had reasonable cause to believe that his conduct was unlawful.

Section 9.2. Actions by or in the Right of the Corporation. The Corporation shall indemnify any person who was or is a party, or is threatened to be made a party to any threatened, pending or completed action or suit by or in the right of the Corporation to procure a judgment in its favor by reason of the fact that such person is or was a Director, officer, employee or agent of the Corporation, or is or was serving at the request of the Corporation as a director, officer, partner or trustee of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees) actually and reasonably incurred by such person in connection with the defense or settlement of such action or suit, if such person acted in good faith and in a manner he reasonably believed to be in, or not opposed to, the best interests of the Corporation, provided that no indemnification shall be made in respect of any claim, issue or matter as to which such person shall have been adjudged to be liable for negligence or misconduct in the performance of his duty to the Corporation, unless, and only to the extent that the court in which such action or suit was brought shall determine upon application that, despite the adjudication of liability, but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses as the court shall deem proper.

Section 9.3. Indemnification Against Expenses. To the extent that a Director, officer, employee or agent of the Corporation has been successful, on the merits or otherwise, in the defense of any action, suit or proceeding referred to in Sections 9.1 and 9.2, or in defense of any claim, issue or matter therein, such person shall be indemnified against expenses (including attorneys' fees) actually and reasonably incurred by such person in connection therewith.

Section 9.4. Authorization of Indemnification. Any indemnification under Sections 9.1 and 9.2 (unless ordered by a court) shall be made by the Corporation only as authorized in the specific case, upon a determination that indemnification of the Director, officer, employee or agent is proper in the circumstances because he has met the applicable standard of conduct set forth in Sections 9.1 or 9.2. Such determination shall be made (1) by the Board by a majority vote of a quorum consisting of Directors who were not parties to such action, suit or proceeding, or (2) if such a quorum is not obtainable, or even if obtainable, if a quorum of disinterested Directors so directs, by independent legal counsel in a written opinion, or (3) by the Corporate Member.

Section 9.5. Payment of Expenses in Advance. Expenses incurred in defending a civil or criminal action, suit or proceeding may be paid by the Corporation in advance of the final disposition of such action, suit or proceeding, as authorized by the Board in the specific case, upon receipt of an undertaking by or on behalf of the Director, officer, employee or agent to repay such amount, unless it shall ultimately be determined that he is entitled to be indemnified by the Corporation as authorized in this Article.

Section 9.6. Provisions Not Exclusive. The indemnification provided by this Article shall not be deemed exclusive of any other rights to which those seeking indemnification may be entitled under any bylaw, agreement, vote of the Corporate Member or disinterested Directors, or otherwise, both as to action in his official capacity and as to action in another capacity while holding such office, and shall continue as to a person who has ceased to be a Director, officer, employee or agent, and shall inure to the benefit of the heirs, executors and administrators of such a person.

Section 9.7. Insurance. The Corporation may purchase and maintain insurance on behalf of any person who is or was a Director, officer, employee or agent of the Corporation, or who is or was serving at the request of the Corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, against any liability asserted against such person and incurred by such person in any such capacity, or arising out of his status as such, whether or not the Corporation would have the power to indemnify such person against such liability under the provisions of the Article.

Section 9.8. Notice to Corporate Member. Any indemnification of any director, officer, employee, partner, trustee or agent in accordance with this Article, including any payment or reimbursement of expenses, shall be reported in writing to the Corporate Member within ten days of such indemnification.

Article 10

Miscellaneous

Section 10.1. Corporate Seal. The Board shall provide a corporate seal which shall have inscribed thereon the name of the Corporation and the words "Corporate Seal, Illinois."

Section 10.2. Fiscal Year. The fiscal year of the Corporation shall end on the last day of September of each year.

Section 10.3. Loans. No loan shall be contracted on behalf of the Corporation and no evidence of indebtedness shall be issued in its name unless authorized by a resolution of the Board which was adopted after having obtained the written approval of the Corporate Member, if such approval is required by these Bylaws.

Section 10.4. Loans to Directors or Officers. No loans shall be made by the Corporation to its Directors or officers. Directors who knowingly vote for or assent to the

making of a loan to a Director or officer, and officers participating in the making of such loan, shall be jointly and severally liable to the Corporation for the amount of such loan until the repayment thereof.

Section 10.5. Gifts. The Board may accept on behalf of the Corporation any contribution, gift, bequest or devise for the general purposes or for any special purpose of the Corporation.

Section 10.6. Waiver of Notice. Anything herein contained to the contrary notwithstanding, whenever any notice whatsoever is required or permitted to be given by law, waiver thereof, in writing, signed by the person or persons entitled to such notice, whether before or after the time stated therein, shall be equivalent to the giving of such notice.

Section 10.7. Books and Records. The Corporation shall keep correct and complete books and records of accounts and shall also keep minutes of the proceedings of the Corporate Member, the Board, and committees having any of the authority of the Board. All books and records of the Corporation may be inspected by the Corporate Member or its agent or attorney for any proper purpose at any reasonable time.

Section 10.8. Contracts. The Board after having obtained the written approval of the Corporate Member, if such approval is required by these Bylaws, may authorize any officer or agent of the Corporation to enter into any contract or execute and deliver any instrument in the name of and on behalf of the Corporation.

Section 10.9. Checks, Drafts, etc. All checks, drafts, or other orders for the payment of money, notes, or other evidences of indebtedness issued in the name of the Corporation may be signed by such officers, agents and employees authorized to do so in accordance with resolutions of the Board then in effect which were adopted after having obtained the written approval of the Corporate Member, if such approval is required by these Bylaws.

Section 10.10. Bonds. Any officer, agent or employee who may be authorized by the Board to handle funds of the Corporation shall give a bond in such sum and with such surety and in such form as shall be provided by the Board for the faithful performance of the duties of his office, the premium on any such bond to be paid by the Corporation.

Section 10.11. Depositories. All corporate funds not otherwise employed shall be deposited to the credit of the Corporation in such banks or other depositories as the Board may designate.

Section 10.12. Rules of Order. The rules of standard parliamentary procedure shall govern the conduct of meetings of the Corporate Member, the Board, and the committees of the Board, where such rules are not inconsistent with these Bylaws or with any special rules of order the Corporation may adopt.

Article 11

Amendment of Bylaws

The Corporate Member may at any time alter, amend or repeal these Bylaws or adopt new Bylaws and such alteration, amendment or repeal of these Bylaws or adoption of new Bylaws shall be effective without the approval of the Board. The Board may alter or amend these Bylaws provided that a copy of the proposed change was presented at a previous regular meeting of the Board, and provided further that the Corporate Member shall have first approved such alteration or amendment by written consent.

EXHIBIT B-3

**AMENDED AND RESTATED BYLAWS OF
JACKSONVILLE CRNA'S, INC.**

See attached.

Amended and Restated Bylaws

Jacksonville CRNA's, Inc.

Article 1

Name

Section 1.1.

The name of the Corporation is Jacksonville CRNA's, Inc.

Article 2

Purposes

Section 2.1.

The Corporation is organized for charitable, educational and scientific purposes, but only to the extent and in such manner that such purposes constitute exclusively charitable, educational and scientific purposes within the meaning of Sections 501(c)(3) and 170 (c)(2)(B) of the Internal Revenue Code of 1986, as amended, or the corresponding provisions of any subsequent Federal tax law (hereinafter referred to as the "Code").

More specifically, the purposes of the Corporation shall include:

(a) To provide the services of certified registered nurse anesthetists to patients at Passavant Area Hospital, Jacksonville, Illinois.

(b) To otherwise operate exclusively for charitable, scientific and educational purposes within the meaning of Section 501(c)(3) of the Code, in the course of which operation:

(1) No part of the net earnings of the Corporation shall inure to the benefit of, or be distributable to, its members, directors, officers or other persons, except that the Corporation shall be authorized and empowered to pay reasonable compensation for services rendered and to make payments and distributions in furtherance of the purposes set forth herein.

(2) No substantial part of the activities of the Corporation shall be the carrying on of propaganda, or otherwise attempting to influence legislation, and the Corporation shall not participate in, or intervene in (including the publishing or distribution of statements) any political campaign on behalf of or in opposition to any candidate for public office.

(3) Notwithstanding any other provisions of these Bylaws, the Corporation shall not carry on any other activities not permitted to be carried on: (a) by a

corporation exempt from Federal income tax under Section 501(c)(3) of the Code; or (b) a corporation, contributions to which are deductible under Section 170(c)(2) of the Code.

In the event of the dissolution of the Corporation, the Board of Directors of the Corporation (the "Board") shall, after paying or making provision for the payment of all of the liabilities of the Corporation, distribute all of the assets of the Corporation to the Corporate Member (as set forth in Section 3.1 of these Bylaws), if then in existence and if qualified as an exempt organization under Section 501(c)(3) of the Code, otherwise in such manner, or to such organization or organizations organized and operated exclusively for charitable, educational or scientific purposes as shall at the time qualify as an exempt organization or organizations under Section 501(c)(3) of the Code, and as shall be affiliated with Memorial Health System, an Illinois not-for-profit corporation, and as the Board shall determine. Any such assets not so disposed of shall be disposed of by a court of competent jurisdiction of the county in the state in which the principal office of the Corporation is then located, exclusively for such purposes or to such organization or organizations, as said court shall determine, which are organized and operated exclusively for such purposes.

Article 3

Membership

Section 3.1. Corporate Member. The Corporate Member of the Corporation shall be The Passavant Memorial Area Hospital Association, an Illinois not-for-profit corporation. The Corporation shall have no other members.

Section 3.2. Powers of Corporate Member. The Corporate Member of the Corporation shall have such powers as are provided for in the Articles of Incorporation, these Bylaws and the laws of the state of Illinois, including, but not limited to, the exclusive power to:

- (a) Remove the President, upon mutual agreement with the Board of Directors;
- (b) Appoint directors of the Corporation in accordance with Section 7.2 of these Bylaws; and
- (c) Remove any director of the Corporation with or without cause.

In addition, the Corporate Member reserves the powers set forth in Section 5.1 and Article 11 of these Bylaws. The Board of Directors of the Corporate Member or such representative as the Corporate Member may designate in writing to the Secretary of the Corporation may exercise the powers of the Corporate Member.

Section 3.3. Transfer of Membership. Membership in the Corporation is not transferable or assignable.

Article 4

Meetings of the Corporate Member

Section 4.1. Annual Meeting. Beginning with the year 2014, the annual meeting of the Corporate Member shall be held in the initial quarter of each calendar year, on a date between January 1st and March 31st, or such other date, time and place as may be determined by the Corporate Member. The purpose of the annual meeting shall be to elect Directors, to hear the reports of the officers of the Corporation and to transact such other business as may come before the meeting.

Section 4.1. Special Meetings. Special meetings of the Corporate Member may be called by the Chairman of the Corporation or the Corporate Member. The person or persons authorized to call special meetings may fix the date, time and place for holding the special meetings.

Article 5

Board of Directors

Section 5.1. General Powers. Subject to the authority of the Corporate Member as provided in this Section, the Board shall manage the business and affairs of the Corporation and shall exercise in the name of and on behalf of the Corporation all of the rights and privileges legally exercisable by the Corporation as a corporate entity except as otherwise may be provided by law, the Articles of Incorporation, and these Bylaws. The power and authority of the Board to exercise the following specific powers are conditioned upon the advance approval of the Corporate Member:

- (a) Adopt, or permit the adoption of, any annual or long-term capital or operating budgets or strategic plans of the Corporation;
- (b) Adopt, or permit the adoption of, any amendment to the Bylaws or Articles of Incorporation of the Corporation;
- (c) Adopt, or permit the adoption of, any voluntary dissolution, merger, consolidation, sale or transfer of substantially all of the Corporation's assets (defined as 10% or more), or any creation of a subsidiary or affiliate corporation of the Corporation;
- (d) Approve, or permit the approval of, capital expenditures in excess of \$1,000,000;
- (e) Approve, or permit the approval of, any guaranty of debt greater than \$250,000, including capital leases;

(f) Authorize or permit the Corporation to enter into any agreement or transaction of material nature with another corporation controlled by or affiliated with the Corporate Member;

(g) Approve, or permit the approval of, the selection of, or changes of, independent auditors;

(h) Authorize or permit the entry into, renewal of, or termination of contracts to provide covered healthcare services to beneficiaries of managed care contracts;

(i) Approve, or permit the approval of, applications to the Illinois Health Facilities Planning Board for a permit or certificate of need for a proposed activity, whether or not involving a capital expenditure;

(j) Approve, or permit the approval of, any sale or transfer of the Corporation's assets to a non-affiliated entity or third-party entity, if such assets have a value in excess of \$500,000;

(k) Approve, or permit the approval of, any significant changes in the Corporation's insurance specifications or limits;

(l) Authorize or permit the Corporation to enter into any contract between the Corporation and a third party which involves the provision of goods and/or services having a value in excess of \$1,000,000 for capital or \$1,500,000 in aggregate for operating and capital budgets which had not been previously approved by the Corporate Member in an annual capital or operating budget;

(m) Approve, or permit the approval of, the borrowing of any sum, the principal of which exceeds \$250,000, or which has a stated term of greater than one year, or which is secured by a mortgage of all or any portion of the Corporation's real property or the creation of a security interest in the Corporation's assets, including personal property and revenues, for the benefit of the lender, lessor or vendor, or the defeasance, advance payment or cancellation of any outstanding debt of the category described herein;

(n) Authorize or permit the Corporation to enter into any contract for physician services having a value in excess of \$400,000;

(o) Approve, or permit the approval of, the sale of any of the Corporation's real property or interest therein or purchases of any additional real estate; and

(p) Adopt, or permit the adoption of, any new or changes to existing long-term or master institutional plans.

For the purposes of these Bylaws, the terms "affiliate" and "subsidiary" shall include any corporation, association, partnership, trust, joint venture or other entity controlling, controlled by or under common control with the Corporation.

Section 5.2. Number and Election. The number of Directors constituting the Board of the Corporation shall be five (5). The Directors of the Corporation shall be members of the Board of Directors of the Corporate Member and shall be elected at the annual meeting of the Corporate Member, for terms of one (1) year and until new directors are elected. The Directors may be the Chairman, Chairman-Elect, an Immediate Past Chairman, if available, Secretary, and Treasurer of the Board of Directors of the Corporate Member. Each member of the Board of Directors of the Corporate Member shall be entitled to one (1) vote for each director to be elected, and the five (5) candidates receiving the largest number of votes shall be declared elected. Cumulative voting shall not be allowed.

Section 5.3. Removal. The Corporate Member alone may remove a Director. Removal as a Director also shall constitute removal as an officer of the Corporation and as a member of all committees of the Board.

Section 5.4. Vacancies. The Corporate Member alone may fill a vacancy in the office of a Director due to death, resignation, disqualification, removal or otherwise. Director vacancies shall be filled in the manner prescribed for election of Directors. The Director elected to fill a vacancy shall hold office until the next annual meeting of the Corporate Member.

Section 5.5. Resignation. Any Director may resign his office at any time by filing a written resignation with the Secretary of the Corporation, which resignation shall become effective upon the date specified therein, or, if no date is specified therein, upon receipt by the Corporation at its principal place of office.

Section 5.6. Compensation. Directors as such shall not receive any stated salaries for their services, but by resolution of the Board, a fixed sum and expenses for attendance may be allowed for attendance at each regular or special meeting of the Board. Nothing herein contained shall be construed to preclude any Director from serving the Corporation in any other capacity and receiving compensation therefore.

Section 5.7. Conflict of Interest. Any possible conflict of interest on the part of a Director shall be disclosed to the Board. When any such interest becomes a matter of action for the Board, such Director shall not vote or use personal influence on the matter, and shall not be counted in the quorum for a meeting at which action by the Board is to be taken on the interest. The Director may, however, briefly state a position on the matter, and answer pertinent questions of members of the Board. The minutes of all actions taken on such matters shall clearly reflect that these requirements have been met.

Article 6

Meetings of the Board

Section 6.1. Annual Meeting. The annual meeting of the Board shall be the first regular meeting of the Board following the annual meeting of the Corporate Member and shall be held within ninety days of the annual meeting of the Corporate Member for the purpose of

electing officers, appointing members of Board committees, and transacting such other business as may come before the meeting. No notice of the annual meeting of the Board shall be necessary.

Section 6.2. Regular Meetings. The Board shall hold regular meetings at such date, time and place as may be determined by resolution of the Board.

Section 6.3. Special Meetings. Special meetings may be called by the Chairman of the Corporation, the Corporate Member or at the written request of three-fifths of the entire Board.

Section 6.4. Voting. In all matters brought before the Board, each Director shall have one vote.

Section 6.5. Quorum. At any annual, regular, or special meeting, a majority of the Directors in office shall constitute a quorum. A Director may be noted as present at a meeting only if the Director is present in person.

Section 6.6. Manner of Acting. Unless otherwise required by law, the Articles of Incorporation or these Bylaws, the act of the majority of Directors present at a meeting at which a quorum is present shall be the act of the Board. Voting by proxy shall not be permitted.

Section 6.7. Notice and Waiver. Directors shall be given notice of each special meeting of the Board. Such notice shall set forth the date, time, place and purpose of the meeting and shall be signed by the Secretary of the Corporation. Notice shall be delivered to each Director not less than twenty-four hours prior to the meeting. A Director may waive notice by the execution of a written waiver, either before or after the holding of the meeting. Such waiver shall be filed with or entered upon the records of the Corporation. The attendance of a Director at a meeting without protest at the commencement of the meeting shall be deemed to be a waiver by him of notice.

Section 6.8. Informal Action by Directors. Any action required to be taken at a meeting of the Board, or any other action which may be taken at a meeting of the Board, may be taken without a meeting if a written consent, setting forth the action so taken, shall be signed by all of the Directors.

Article 7

Officers

Section 7.1. Number. The officers of the Corporation shall be a Chairman, a Vice Chairman, a President, a Treasurer and a Secretary, each of whom shall be elected or appointed by the Board of Directors. The Board of Directors may appoint other officers, if it deems it necessary, who shall have such authority and shall perform such duties as from time to time

may be prescribed by the Board of Directors. Any two (2) or more offices may be held by the same person.

Section 7.2. Election and Term of Office. The officers of the Corporation shall be elected by the Board of Directors at its annual meeting, to hold office for a term of one (1) year. If the election of officers is not held at that annual meeting, the election shall be held as soon thereafter as practicable. Vacancies may be filled or new offices filled at any meeting of the Board of Directors. Each officer shall hold office until his successor shall have been duly elected and shall have qualified or until his death or until he shall resign or shall have been removed in the manner hereinafter provided.

Section 7.3. Removal. Any officer or agent of the Corporation may be removed by the Board of Directors whenever in its judgment the best interests of the Corporation would be served thereby, but such removal shall be without prejudice to the contract rights, if any, of the person so removed. Election or appointment of an officer or agent shall not of itself create contract rights.

Section 7.4. Resignation. Any officer may resign at any time by giving written notice to the Board of Directors, or the President or Secretary of the Corporation. Any such resignation shall take effect at the date of the receipt of such notice or at any later time specified therein, and, unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

Section 7.5. Vacancies. A vacancy in any office because of death, resignation, removal, disqualification or otherwise may be filled by the Board of Directors for the unexpired portion of the term.

Section 7.6. Bonds. If the Board of Directors by resolution shall so require, any officer or agent of the Corporation shall give bond to the Corporation in such amount and with such surety as the Board of Directors may deem sufficient, conditioned upon the faithful performance of their respective duties and offices.

Section 7.7. Chairman. The Chairman shall preside at all meetings of the Board of Directors. Except as otherwise provided in Article 8 of these Bylaws, he shall appoint all committees, with the approval of the Board of Directors. The President shall report to the Chairman on all matters. He may sign, with the Secretary or any other proper officer of the Corporation thereunto authorized by the Board of Directors, any deeds, mortgages, bonds, contracts or other instruments which the Board of Directors has authorized to be executed, except in cases where the signing and execution thereof shall be expressly delegated by the Board of Directors or by these Bylaws to some other officer or agent of the Corporation or shall be required by law to be otherwise signed or executed.

Section 7.8. Vice Chairman. In the absence of the Chairman or in the event of his inability or refusal to act, the Vice Chairman shall perform the duties of the Chairman. The Vice

Chairman shall perform such other duties as from time to time may be assigned to him by the Board of Directors or by the President.

Section 7.9. President. The President shall be the chief executive officer of the Corporation and shall in general supervise and control all of the business and affairs of the Corporation. He shall preside at all meetings of the Board of Directors. He may sign, with the Secretary or any other proper officer of the Corporation thereunto authorized by the Board of Directors, any deeds, mortgages, bonds, contracts or other instruments which the Board of Directors has authorized to be executed, except in cases where the signing and execution thereof shall be expressly delegated by the Board of Directors or by these Bylaws to some other officer or agent of the Corporation or shall be required by law to be otherwise signed or executed; and in general shall perform all duties incident to the office of President and such other duties as may be prescribed by the Board of Directors from time to time.

Section 7.10. Treasurer. The Treasurer shall: (a) have charge and custody of and be responsible for all funds and securities of the Corporation; receive and give receipts for moneys due and payable to the Corporation from any source whatsoever and deposit all such moneys in the name of the Corporation in such banks, trust companies or other depositories as shall be selected by the Board of Directors; and (b) in general, perform all duties incident to the office of Treasurer and all other duties as from time to time may be assigned to him by the Board of Directors or the President. If required by the Board of Directors, the Treasurer shall give a bond for the faithful discharge of his duties in the sum and with a surety or sureties as the Board of Directors shall determine. The Treasurer shall be elected from among the members of the Board of Directors.

Section 7.11. Secretary. The Secretary shall: (a) keep the minutes of the Board of Directors' meetings in one or more books provided for that purpose; (b) see that all notices are duly given in accordance with the provisions of these Bylaws or as required by law; (c) be custodian of the corporate records and, if the Corporation has a corporate seal, of the seal of the Corporation and see that the seal of the Corporation is affixed to all documents, the execution of which on behalf of the Corporation under its seal is duly authorized in accordance with the provisions of these Bylaws; (d) keep a register of the post office address of each Director; and (e) in general, perform all duties incident to the office of Secretary and all other duties as from time to time may be assigned to him by the Board of Directors or the President. The Secretary shall be elected from among the members of the Board of Directors.

Section 7.12. Salaries. The salaries of the officers, if any, shall be fixed from time to time by the Board of Directors, and no officer shall be prevented from receiving such salary by reason of the fact that he is also a Director of the Corporation. No salaried officer may receive any per diem compensation as a Director.

Article 8

Committees

Section 8.1. Classes of Committees. Committees of the Board of Directors shall be standing or special. Standing committees shall be authorized by the Board. Special committees may be established by the Board for such special tasks as circumstances warrant. With the exception of an Executive Committee, if one is established by the Board, no committee, whether standing or special, may act on behalf of the Corporation or bind the Corporation to any action but may make recommendations to the Board or to the officers of the Corporation. All committees shall keep a record of proceedings and the minutes of meetings shall be submitted to the Board.

Section 8.2. Appointments. Except as otherwise provided in this Article with respect to the Executive Committee, the chairmen and members of all committees shall be appointed by the Chairman of the Corporation, with the approval of the Board, for one-year terms following each annual meeting. Except as may be directed by these Bylaws or by the Board, committee members need not be Directors.

Section 8.3. Executive Committee. The Board of Directors, by resolution adopted by a majority of the Directors in office, may appoint an Executive Committee. The Executive Committee shall have two or more Directors, a majority of its membership shall be Directors and all committee members shall serve at the pleasure of the Board of Directors. The Executive Committee may exercise the authority of the Board of Directors in the management of the Corporation during intervals between meetings of the Board; provided, however, it may not: adopt a plan for distribution of the assets of the Corporation, or for dissolution; approve or recommend to the Corporate Member any act required by law or these Bylaws to be approved by the Corporate Member; fill vacancies on the Board or any of its committees; elect, appoint or remove any officer or Director or member of any committee, or fix the compensation of any member of a committee; adopt, amend, or repeal these Bylaws or the Articles of Incorporation of the Corporation; amend, alter, repeal or take any action inconsistent with any resolution or action of the Board; adopt a plan of merger or consolidation with another corporation, or authorize the sale, lease, exchange or mortgage of all or substantially all of the property or assets of the Corporation; or take any other action prohibited by law.

Article 9

Indemnification

Section 9.1. Actions Other Than by or in the Right of the Corporation. The Corporation shall indemnify any person who was or is a party, or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action by or in the right of the Corporation) by reason of the fact that he is or was a Director, officer, employee or agent of the Corporation, or who is or was serving at the request of the Corporation as a director, officer,

partner or trustee of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by such person in connection with such action, suit or proceeding, if such person acted in good faith and in a manner he reasonably believed to be in, or not opposed to, the best interests of the Corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful. The termination of any action, suit or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent, shall not, of itself, create a presumption that the person did not act in good faith and in a manner which he reasonably believed to be in or not opposed to the best interests of the Corporation or, with respect to any criminal action or proceeding, that the person had reasonable cause to believe that his conduct was unlawful.

Section 9.2. Actions by or in the Right of the Corporation. The Corporation shall indemnify any person who was or is a party, or is threatened to be made a party to any threatened, pending or completed action or suit by or in the right of the Corporation to procure a judgment in its favor by reason of the fact that such person is or was a Director, officer, employee or agent of the Corporation, or is or was serving at the request of the Corporation as a director, officer, partner or trustee of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees) actually and reasonably incurred by such person in connection with the defense or settlement of such action or suit, if such person acted in good faith and in a manner he reasonably believed to be in, or not opposed to, the best interests of the Corporation, provided that no indemnification shall be made in respect of any claim, issue or matter as to which such person shall have been adjudged to be liable for negligence or misconduct in the performance of his duty to the Corporation, unless, and only to the extent that the court in which such action or suit was brought shall determine upon application that, despite the adjudication of liability, but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses as the court shall deem proper.

Section 9.3. Indemnification Against Expenses. To the extent that a Director, officer, employee or agent of the Corporation has been successful, on the merits or otherwise, in the defense of any action, suit or proceeding referred to in Sections 9.1 and 9.2, or in defense of any claim, issue or matter therein, such person shall be indemnified against expenses (including attorneys' fees) actually and reasonably incurred by such person in connection therewith.

Section 9.4. Authorization of Indemnification. Any indemnification under Sections 9.1 and 9.2 (unless ordered by a court) shall be made by the Corporation only as authorized in the specific case, upon a determination that indemnification of the Director, officer, employee or agent is proper in the circumstances because he has met the applicable standard of conduct set forth in Sections 9.1 or 9.2. Such determination shall be made (1) by the Board by a majority vote of a quorum consisting of Directors who were not parties to such action, suit or proceeding, or (2) if such a quorum is not obtainable, or even if obtainable, if a quorum of disinterested Directors so directs, by independent legal counsel in a written opinion, or (3) by the Corporate Member.

Section 9.5. Payment of Expenses in Advance. Expenses incurred in defending a civil or criminal action, suit or proceeding may be paid by the Corporation in advance of the final disposition of such action, suit or proceeding, as authorized by the Board in the specific case, upon receipt of an undertaking by or on behalf of the Director, officer, employee or agent to repay such amount, unless it shall ultimately be determined that he is entitled to be indemnified by the Corporation as authorized in this Article.

Section 9.6. Provisions Not Exclusive. The indemnification provided by this Article shall not be deemed exclusive of any other rights to which those seeking indemnification may be entitled under any bylaw, agreement, vote of the Corporate Member or disinterested Directors, or otherwise, both as to action in his official capacity and as to action in another capacity while holding such office, and shall continue as to a person who has ceased to be a Director, officer, employee or agent, and shall inure to the benefit of the heirs, executors and administrators of such a person.

Section 9.7. Insurance. The Corporation may purchase and maintain insurance on behalf of any person who is or was a Director, officer, employee or agent of the Corporation, or who is or was serving at the request of the Corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, against any liability asserted against such person and incurred by such person in any such capacity, or arising out of his status as such, whether or not the Corporation would have the power to indemnify such person against such liability under the provisions of the Article.

Section 9.8. Notice to Corporate Member. Any indemnification of any director, officer, employee, partner, trustee or agent in accordance with this Article, including any payment or reimbursement of expenses, shall be reported in writing to the Corporate Member within ten days of such indemnification.

Article 10

Miscellaneous

Section 10.1. Corporate Seal. The Board shall provide a corporate seal which shall have inscribed thereon the name of the Corporation and the words "Corporate Seal, Illinois."

Section 10.2. Fiscal Year. The fiscal year of the Corporation shall end on the last day of September of each year.

Section 10.3. Loans. No loan shall be contracted on behalf of the Corporation and no evidence of indebtedness shall be issued in its name unless authorized by a resolution of the Board which was adopted after having obtained the written approval of the Corporate Member, if such approval is required by these Bylaws.

Section 10.4. Loans to Directors or Officers. No loans shall be made by the Corporation to its Directors or officers. Directors who knowingly vote for or assent to the

making of a loan to a Director or officer, and officers participating in the making of such loan, shall be jointly and severally liable to the Corporation for the amount of such loan until the repayment thereof.

Section 10.5. Gifts. The Board may accept on behalf of the Corporation any contribution, gift, bequest or devise for the general purposes or for any special purpose of the Corporation.

Section 10.6. Waiver of Notice. Anything herein contained to the contrary notwithstanding, whenever any notice whatsoever is required or permitted to be given by law, waiver thereof, in writing, signed by the person or persons entitled to such notice, whether before or after the time stated therein, shall be equivalent to the giving of such notice.

Section 10.7. Books and Records. The Corporation shall keep correct and complete books and records of accounts and shall also keep minutes of the proceedings of the Corporate Member, the Board, and committees having any of the authority of the Board. All books and records of the Corporation may be inspected by the Corporate Member or its agent or attorney for any proper purpose at any reasonable time.

Section 10.8. Contracts. The Board after having obtained the written approval of the Corporate Member, if such approval is required by these Bylaws, may authorize any officer or agent of the Corporation to enter into any contract or execute and deliver any instrument in the name of and on behalf of the Corporation.

Section 10.9. Checks, Drafts, etc. All checks, drafts, or other orders for the payment of money, notes, or other evidences of indebtedness issued in the name of the Corporation may be signed by such officers, agents and employees authorized to do so in accordance with resolutions of the Board then in effect which were adopted after having obtained the written approval of the Corporate Member, if such approval is required by these Bylaws.

Section 10.10. Bonds. Any officer, agent or employee who may be authorized by the Board to handle funds of the Corporation shall give a bond in such sum and with such surety and in such form as shall be provided by the Board for the faithful performance of the duties of his office, the premium on any such bond to be paid by the Corporation.

Section 10.11. Depositories. All corporate funds not otherwise employed shall be deposited to the credit of the Corporation in such banks or other depositories as the Board may designate.

Section 10.12. Rules of Order. The rules of standard parliamentary procedure shall govern the conduct of meetings of the Corporate Member, the Board, and the committees of the Board, where such rules are not inconsistent with these Bylaws or with any special rules of order the Corporation may adopt.

Article 11

Amendment of Bylaws

The Corporate Member may at any time alter, amend or repeal these Bylaws or adopt new Bylaws and such alteration, amendment or repeal of these Bylaws or adoption of new Bylaws shall be effective without the approval of the Board. The Board may alter or amend these Bylaws provided that a copy of the proposed change was presented at a previous regular meeting of the Board, and provided further that the Corporate Member shall have first approved such alteration or amendment by written consent.

EXHIBIT C

INTEGRATION TASK FORCE

The Integration Task Force to be formed as of the Execution Date will be made up of the following members:

PAH Task Force Members

Chester Wynn
David Bolen

MHS Task Force Members

Ed Curtis
Doug Rahn
Bob Kay
Kevin England
Raj Govindaiah
Travis Dowell
Bob Scott
Aimee Allbritton
David Graham
Jerry Miller

The Integration Task Force will be aided in its mission by appointing individuals to Work Groups. The Integration Task Force will appoint Work Group members and such members will meet to provide to the Integration Task Force expected time frames and deliverables for their activities. Work Groups may include:

- Capital Planning
- Physician Integration and Recruitment
- Employee Integration
- Information Technology Integration
- Operational Initiatives Analysis
- Capital Finance Planning
- Management Services Integration

EXHIBIT D

AMENDED AND RESTATED BYLAWS OF MHS

See attached.

Bylaws
Memorial Health System

Article I

Name and Office

Section 1.01. Name and Office

The name of the Corporation is Memorial Health System, an Illinois Not-For-Profit Corporation, and its principal location and office shall be in the City of Springfield, in the County of Sangamon, in the State of Illinois.

Article II

Purposes and Powers

Section 2.01. Purposes and Powers

a. The purposes for which the Corporation is organized are to establish, acquire, support, erect, maintain, own and equip health care providers and institutions, including, without limiting the foregoing, hospitals, nursing homes, skilled nursing facilities, intermediate care facilities and ambulatory care centers; to conduct, sponsor, support, promote, develop, own and operate charitable, educational, scientific and scholastic programs and activities and other activities and programs ancillary to and in support of the foregoing; to foster, promote, support, develop, encourage, maintain, receive and accept funds, gifts and contributions for and on behalf of such activities; and to establish, conduct, sponsor, acquire, own, maintain and operate such other entities and activities which, in the opinion of the Board of Directors and at its discretion, will support the foregoing, exclusively for the benefit of and to carry out some or all of the purposes of organizations described in either Section 509(a)(1) or 509(a)(2) of the Internal Revenue Code of 1986, as amended, or any subsequent law of the United States (the "**Internal Revenue Code**"). In no instance, however, will the Corporation engage in the practice of medicine.

b. No part of the net earnings of the Corporation shall inure to the benefit of any private individual; no part of the income of the Corporation shall be distributed to its members, directors or officers, provided, however, that the payment of reasonable compensation for services rendered shall not be deemed a distribution of income; no substantial part of the activities of the Corporation shall consist of carrying on propaganda or otherwise attempting to influence legislation. The Corporation shall not participate in, or intervene in (including the publication or distribution of statements), any political campaign on behalf of any candidate for public office.

c. The Corporation shall possess all powers which a corporation organized under the General Not-For-Profit Corporation Act of the State of Illinois, as the same from time to time may be amended, shall possess; including all powers which are not in conflict with the aforesaid purposes for which the Corporation is organized, including, but not limited to, the power to purchase, take, receive, lease as Lessee or

Lessor, take by gift, devise or bequest, or otherwise acquire, own, hold, use, invest in and otherwise deal in and with any real or personal property or any interest therein situated in or out of the State of Illinois; to sell, convey, pledge, mortgage, assign and otherwise transfer or dispose of all or any part of its property and assets; from time to time to use, distribute, contribute, expend, donate, apply and appropriate all of its property and assets, and all proceeds and avails thereof, and income and profit derived there from, exclusively for charitable, educational, scholastic or scientific purposes, provided, however, the Corporation shall not engage in any business which would disqualify it from being exempt from taxation under Sections 501(a) or 501(c)(3) of the Internal Revenue Code.

d. In the event of the dissolution or liquidation of the Corporation, and after payment of just debts and liabilities, all remaining assets shall be distributed to Memorial Medical Center, an Illinois not-for-profit corporation, or to its successors and assigns, if then in existence, and if such successors and assigns are organizations described in Section 501(c)(3) of the Internal Revenue Code, and if not then to such organization or organizations organized and operated exclusively for charitable, educational, scholastic or scientific purposes as shall at the time qualify as an exempt organization or organizations under Section 501(c)(3) of the Internal Revenue Code, as determined by the Board of Directors.

e. Anything herein contained to the contrary notwithstanding, no assets of the Corporation shall be donated, distributed, applied to, paid over or otherwise used or employed in any manner which would disqualify the Corporation from being exempt from taxation under Sections 501(a) or 501(c)(3) of the Internal Revenue Code.

Article III

Members

Section 3.01. Individual Members

Any individual who meets the criteria for membership approved by the Board of Directors from time to time may become a Member of the Corporation upon election by the Board of Directors at any meeting, for a term of no more than six (6) years, commencing immediately upon the close of such meeting. There shall be no restriction upon successive terms of membership. The Membership shall be organized into six (6) groups, and the number of Members of the Corporation shall never be less than forty (40) nor more than one hundred and eight (108). Each year at the close of the last regular meeting of the Board of Directors prior to the annual meeting of the Membership the term of membership of each Member assigned to one (1) group of Members shall expire in order that the terms of membership shall be staggered by group. At such meeting of the Board of Directors, Members may be elected or re-elected and assigned to the group whose term is expiring or assigned to any other group. Members shall have no voting rights with respect to the management, control or operation of the affairs and properties of the Corporation other than (i) the power to elect the directors at the annual meeting of the

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Membership (the "Member Elected Directors"), as follows: not more than fifteen (15) directors of the Board of Directors; and (ii) the power to remove a Member Elected Director under Section 4.03 of these Bylaws.

Section 3.02. Annual Meeting

The annual meeting of the Members of the Corporation shall be held immediately prior to the scheduled annual meeting of the Corporation's Board of Directors. The business to be transacted at the annual meeting of the Members will consist of the following activities: (i) the induction of the new Members who were elected by the Board of Directors of the Corporation at the regular meeting of the Board of Directors which immediately preceded the Members' annual meeting; (ii) the receipt of the Corporation's reports concerning the prior year's operations; and (iii) the election of the new Member Elected Directors, as contemplated under Section 3.01, from the slate of nominees then presented to the Members by the Corporation's Governance Committee.

Section 3.03. Quorum, Manner of Acting and Proxies

At the annual meeting of the Membership any action, which is permitted to be taken under Section 3.02, may be taken by a majority of those Members present in person or by proxy. A quorum shall be twenty percent (20%) of the Membership. Any Member may vote by proxy given to another Member in a form approved by the Board of Directors which bears a date not more than three (3) months prior to the annual meeting.

Section 3.04. Notice of Annual Meeting of the Membership

Notice of the annual meeting of the Membership shall be given not less than twenty (20) days nor more than forty-five (45) days prior to the annual meeting of the Membership to each Member listed on the Membership Roster at the address therein contained. Such notice shall contain the slate of approved nominees as Member Elected Directors of the Corporation and a statement that any Member wishing to propose additional nominees must submit the names to the Chairman in writing, and the written nomination notice must be:

a. endorsed by an additional twenty-five (25) Members as evidenced by their signatures on the nomination notice to the Chairman; and

b. received by the Chairman no later than ten (10) days after the date of such notice of the annual meeting for such additional nominees to be presented to the Membership.

Article IV

Board of Directors

Section 4.01. General Powers

The management, control and operation of the affairs and properties of the Corporation shall vest and be in the directors of the Corporation. The Board of Directors shall exercise authority over the affairs and properties of subsidiary or affiliate corporations of the Corporation only to the extent expressly provided in the Articles of Incorporation or Bylaws of such subsidiaries or affiliates. Except as may be so provided, the trustees or directors of the Corporation's subsidiaries and/or affiliates shall have and exercise full power over the affairs and properties of such subsidiaries and affiliates as permitted by such Articles of Incorporation and Bylaws and as permitted by law.

Section 4.02. Election, Number and Qualifications

The Board of Directors shall consist of not more than nineteen (19) directors, of which not more than fifteen (15) shall be Member Elected Directors. The Members shall elect the Member Elected Directors at the annual meeting of the Membership from (i) the slate of nominees prepared by the Governance Committee and included in the notice of the annual meeting, and (ii) the list of additional nominees, if any, submitted by the Members in accordance with Section 3.04. Each nominee for the position of Member Elected Director shall be representative of the community at large and shall be a Member of the Corporation, except that nominees who are Physicians need not be Members of the Corporation. One director shall be elected by the Board of Directors at its annual meeting immediately following the annual meeting of the Membership (the "Lincoln Board Elected Director"). The Lincoln Board Elected Director shall be elected by the Board of Directors from a slate of nominees prepared by the Abraham Lincoln Board Nominating Committee (provided, however, that such committee shall prepare additional slate(s) if the Board of Directors chooses not to elect the director from the slate(s) presented), which director (i) must be a resident of either Logan or Eastern Mason county at the time of his nomination and (ii) must have served a minimum of three (3) years on the Boards of Directors of Abraham Lincoln Healthcare System, Inc. ("Lincoln System"), the Abraham Lincoln Memorial Hospital ("Lincoln Hospital"), Abraham Lincoln Healthcare Foundation ("Lincoln Foundation"), or Lincoln Health Services, Inc. ("Lincoln Services"). Two directors shall be elected by the Board of Directors at its annual meeting immediately following the annual meeting of the membership from a slate of nominees prepared by The Passavant Memorial Area Hospital Association ("PAH") Board (the "Passavant Board Elected Directors", and together with the Lincoln Board Elected Director, the "Board Elected Directors"). Such nominees shall be residents of the PAH service area. The PAH Board shall prepare additional slate(s) if the Board of Directors chooses not to elect a director from the slate(s) presented, until such seats are filled. One director shall be the President of the Corporation who shall be ex officio with vote. No person shall be eligible for election as a Member Elected Director or a Board Elected Director

(collectively, an "Elected Director") unless he satisfies the criteria for membership on the Board of Directors adopted from time to time by the Board of Directors.

The Board of Directors may also include one (1) or more emeritus members. The Board of Directors, at its discretion, may appoint as emeritus members (i) the former President of the Corporation if the former President served in the position of President of the Corporation for twenty (20) or more years before his retirement and (ii) former members of the Board of Directors if the former members served as members of the Board of Directors for fifteen (15) or more years before their retirement.

An emeritus member shall serve in an advisory capacity only. He shall have the right to attend meetings of the Board of Directors and participate in its deliberations, subject to the policies and procedures, and rules and regulations, of the Board of Directors. However, he shall not be required to attend meetings of the Board of Directors, and shall not possess any of the rights or privileges of membership on the Board of Directors, including, but not limited to, the right to vote, the right to call or adjourn meetings of the Board of Directors, or the right to be counted in determining the existence of a quorum. He shall not be responsible for any decision or action of the Board of Directors.

An emeritus member shall serve on the Board of Directors as an emeritus member from the date on which he is appointed until his death or resignation or until his removal by the Board of Directors. An emeritus member, however, shall not be considered to be or classified as an Elected Director under this Section 4.02.

Section 4.03. Terms of Office, Vacancies and Removal

Each Member Elected Director shall serve from the close of the annual meeting of the Membership of the Corporation at which he was elected until the close of the next annual meeting of the Membership of the Corporation. Each Board Elected Director shall serve from the close of the annual or subsequent meeting of the Board of Directors at which he was elected until the close of the next annual meeting of the Board of Directors. No Elected Director may serve more than nine (9) consecutive one (1) year terms in office as an Elected Director; provided however, if during his term of office as an Elected Director, he concurrently serves in the office of Chairman, First Vice Chairman, Second Vice Chairman and/or immediate Past Chairman, the number of years he serves as an officer shall be added to the number of years he may consecutively serve as an Elected Director. If an Elected Director ceases to be eligible for reelection due to the term limitation contained in this Section 4.03, after an absence of one (1) year, he shall be eligible for reelection to the Board of Directors.

If a director shall die, resign, be removed, fail to satisfy any qualifications necessary to serve as a director, or otherwise be unable to serve, the remaining directors shall elect a replacement to serve for the remainder of his term; provided, however, that: (i) if such director is a Lincoln Board Elected Director then the

remaining directors shall elect such replacement from a slate of nominee(s) prepared by the Lincoln Board Nominating Committee in accordance with the procedures set forth in Section 6.04; and (ii) if such director is a Passavant Board Elected Director, then the remaining directors shall elect such replacement from a slate of nominee(s) prepared by the PAH Board. If three-fourths (3/4) of the other directors vote to remove an Elected Director for any reason, such resolution shall be presented to the Membership for its approval by a majority of the Members present at an annual or special meeting of the Membership; provided, however, that removal of a Board Elected Director shall not require such Membership approval. At any annual or special meeting, the Members may remove any Member Elected Director for any reason, without a prior resolution concerning removal by the Board of Directors, by a vote of three-fourths (3/4) of the entire Membership of the Corporation.

Section 4.04. Annual Meeting

The annual meeting of the Board of Directors shall be held within ninety (90) days following January 1st of each year, following the annual meeting of the Membership, at such time, place and hour as shall be fixed and determined by the President of the Corporation. The purposes of the annual meeting shall be the election of the Board Elected Directors, the election of officers and the transaction of such other business as may come before the meeting.

Section 4.05. Regular Meetings

Regular meetings of the Board of Directors shall be held on such dates as established at the annual meeting of the Board of Directors and at such time and place as so established. Such meetings shall be canceled or held at a different time or at a different place as designated by the President of the Corporation by announcement at the preceding Board meeting, by written notice to the directors by the President, or by the passage of a resolution of the Board of Directors setting a new time or place for said meeting.

Section 4.06. Special Meetings and Notices

Special meetings of the Board of Directors may be called by or at the request of the President or any three (3) directors. Notice of any special meeting of the Board of Directors shall be given in writing at least five (5) days prior thereto, by written notice delivered personally or sent by mail to each director to his address as shown in the records of the Corporation. If mailed, such notice should be deemed to be delivered when deposited in the United States mail in a sealed envelope so addressed with postage thereon prepaid. Any director may waive notice of any meeting. The attendance of the director at any meeting shall constitute a waiver of notice of such meeting except if a director attends a meeting for the express purpose of objecting to the transaction of any business because the meeting is not lawfully called or convened. Neither the business to be transacted nor the purpose of any regular or special meeting of the Board need be specified in the notice or waiver of notice of such meeting unless specifically required by law or by these Bylaws.

Section 4.07. Quorum

A majority of the entire Board of Directors shall constitute a quorum for the transaction of business at any meeting of the Board, provided that if less than a majority of the directors are present, those directors present may adjourn the meeting from time to time without further notice.

Section 4.08. Manner of Acting

The act of the majority of the directors present at a meeting at which a quorum is present shall be the act of the Board of Directors except where otherwise provided by law or by these Bylaws. If a director abstains from voting, that director's abstention will not be counted as being a vote in favor of or against a particular motion; consequently, contrary to *Robert's Rules of Order*, the effect is not the same as if the abstaining director voted on the prevailing side.

Section 4.09. Informal Action

Unless specifically prohibited by the Articles of Incorporation or by these Bylaws, any action required to be taken at a meeting of the Board of Directors, or any other action which may be taken at a meeting of the Board of Directors, may be taken without a meeting if a consent in writing setting forth the action to be taken shall be signed by all directors entitled to vote with respect to the subject matter thereof. Any such consent signed by all directors shall have the same effect as a unanimous vote and may be stated as such and the document filed with the Secretary of State of Illinois.

Section 4.10. Compensation

Directors shall not be paid compensation for their services as directors. However, nothing herein contained shall be construed from prohibiting payment of compensation to an individual who serves as a director for services rendered to the Corporation in another capacity.

Section 4.11. Attendance

a. Each Elected Director shall be expected to attend and participate in all meetings of the Board of Directors and of all committees thereof to which he is appointed, and in all meetings of all boards of directors of the Corporation's subsidiaries and affiliates to which he is elected, and of all committees thereof to which he is appointed.

b. If during a three-year period an Elected Director is unable to attend at least sixty percent (60%) of all of the meetings held which are referred to in Section 4.11a above, he shall be ineligible for reelection to the Board of Directors unless the

Executive Committee waives the attendance requirement as applied to him for the term of office next succeeding the term of office then ending.

c. Due to his status as an ex officio member of all committees of the Board of Directors, the Chairman of the Board of Directors shall not be required to satisfy the attendance requirements for committee meetings set forth in this Section 4.11.

Article V

Officers

Section 5.01. Officers

The officers of the Corporation shall be a Chairman, a First Vice Chairman, a Second Vice Chairman, a President, a Treasurer and a Secretary. The Board may elect such other officers, including one or more Vice Presidents, Assistant Secretaries or Assistant Treasurers, as it shall deem desirable. All officers, except Vice Presidents, Assistant Treasurers and Assistant Secretaries, shall be members of the Board of Directors.

Section 5.02. Election and Term of Office

The officers of the Corporation shall be elected by the Board of Directors at the annual meeting of the Board of Directors from a slate of nominees prepared by the Governance Committee. All officers shall serve for one (1) year following the close of the annual meeting of the Board of Directors until the close of the next annual meeting of the Board of Directors. If an officer who must be a director is not reelected as a director by the Members, his term of office shall terminate at the close of the annual meeting of the Membership at which he was not reelected as a director.

Section 5.03. Chairman of the Board

The Chairman of the Board shall preside at all meetings of the Board of Directors and the Membership. He shall appoint all committees of the Board not otherwise provided for upon the approval of such appointments by the Board.

Section 5.04. Vice Chairman of the Board

The First Vice Chairman of the Board shall be assigned such duties by the Chairman as he shall from time to time determine. The First Vice Chairman of the Board shall perform the duties of the Chairman of the Board in the event of his absence or inability. The Second Vice Chairman shall perform such duties as assigned by the Chairman.

Section 5.05. President

The President shall be the Chief Executive Officer of the Corporation. The Board of Directors shall delegate to the President the necessary authority and responsibility for the administration of the affairs of the Corporation subject only to such Bylaws as may be adopted and such resolutions as may be issued by the Board of Directors. He shall advise and make recommendations to the Board of Directors relating to the operation of the Corporation and long range planning. The President shall be a voting member of each committee of the Board except the Leadership Compensation Committee. He shall present a report at each annual meeting of the Board of Directors covering the operations during the preceding fiscal year. He may sign with the Secretary or other proper officer of the Corporation authorized by the Board of Directors any deeds, bonds, contracts or other instruments which the Board of Directors has authorized to be executed. He shall perform all duties incident to the office of President and such other duties as may be prescribed by the Board of Directors. He shall vote, as proxy for the Corporation, all shares of stock owned by the Corporation, and he shall otherwise represent the Corporation at all meetings of subsidiaries and affiliates.

Section 5.06. Vice Presidents

The Board of Directors may in its discretion elect one or more Vice Presidents. Of the Vice Presidents, the Board may designate some as Senior Vice Presidents. All Vice Presidents shall be accountable to the President, and the President shall assign the duties of each Vice President, in accordance with a chart of organization which may but need not be approved by the Board of Directors.

Section 5.07. Treasurer

The Treasurer shall be responsible for the custody of the funds and securities of the Corporation, shall advise the Board of Directors respecting its financial condition and the handling of its monies and investments, and shall perform such additional duties as may be assigned to him by the President.

Section 5.08. Secretary

The Secretary shall sign documents of the Corporation as required and shall keep or cause to be kept the minutes of the Board of Directors in one or more books provided for that purpose; see that all notices are duly given in accordance with the provisions of these Bylaws, or as required by law; be custodian of the corporate records and of the seal of the Corporation and see that the seal of the Corporation is affixed to all documents as required. He shall sign all documents as required by his office and shall perform such duties as may be assigned to him by the President.

Section 5.09. **Assistant Treasurer**

An Assistant Treasurer may be elected by the Board of Directors. He shall, in general, perform such duties as the Treasurer and the Board of Directors may from time to time assign to him and shall perform the duties of the Treasurer during his absence.

Section 5.10. **Assistant Secretary**

The Board of Directors may elect an Assistant Secretary to perform the detail work of the office of Secretary. When so authorized, the Assistant Secretary may sign with the President or any officer so designated by the Board of Directors any document so required to be executed in the ordinary course of business. He shall perform the duties of the Secretary during his absence.

Section 5.11. **Removal**

Any officer who is also a director may be removed from office for any reason only by a vote of three-fourths (3/4) of the entire Board of Directors. All other officers may be removed on a majority vote of the directors in attendance at a regular meeting of the Board of Directors.

Article VI

Committees of the Board of Directors

Section 6.01. **General**

The Board of Directors may authorize the creation of both standing and special committees. Standing committees shall be an Executive Committee, Governance Committee, Lincoln Board Nominating Committee, Finance and Audit Committee, Strategic Planning and Development Committee, Personnel Committee, Quality and Safety Management Committee, Leadership Compensation Committee, Community Benefit Committee and such other standing committees as the Board of Directors may authorize.

The Chairman of the Board of Directors shall appoint, with the approval of the Board of Directors, the chairmen and members of all committees of the Board of Directors. The term of appointment shall be one (1) year, commencing on the close of the annual meeting of the Board of Directors. All members of the Executive Committee and the Governance Committee shall be directors. Except for the Lincoln Board Nominating Committee, a majority of the members of all other committees shall be directors. The Chairman of the Board and the President shall be ex officio voting members of all committees; provided, however, that as to the Leadership Compensation Committee, the Chairman of the Board shall be an ex officio voting member and the President shall not be a member. Non-director members of committees (other than the Executive Committee and the Governance

Committee) may be selected from the Members of the Corporation, the medical staffs of the Corporation's affiliated hospitals and the community at large. The chairman of each standing committee shall be a director.

Section 6.02. Executive Committee

a. **Composition.** At a minimum, the Executive Committee shall consist of the Chairman of the Board of Directors, the President and four (4) other directors as follows (if the persons have been reelected to the Board of Directors): the immediate past Chairman of the Board; the First and Second Vice Chairmen and one (1) or two (2) directors (if the immediate Past Chairman is not then serving as a director). Meetings of the Executive Committee shall be chaired by the Chairman of the Board.

b. **Duties.** The Executive Committee shall:

- (1) Have the power of the Board of Directors during intervals between meetings of the Board of Directors except that no action shall be taken which shall conflict with law or the express policies of the Board of Directors, except in emergencies;
- (2) Assure that the Leadership Compensation Committee of the Memorial Health System Board of Directors, which bears oversight responsibility for the uniform review and approval of compensation and executive-level benefits for all executive employees of Memorial Health System and the Corporation, has appropriately carried out such oversight responsibility with respect to executive employees of the Corporation;
- (3) Recommend changes in the organizational structure of the Corporation and the establishment of or changes in related and subsidiary organizations; and
- (4) Review other matters of major significance to the Corporation.

Section 6.03. Governance Committee

a. **Composition.** At a minimum, the Governance Committee shall consist of the Chairman, First and Second Vice Chairmen, President and Immediate Past Chairman of the Board and one additional member appointed by the Chairman.

b. **Duties.** The Governance Committee shall:

- (1) Submit nominations to the Corporate Member for the persons to be elected as directors at the last regular meeting of the Board of Directors prior to the annual meeting of the Corporate Member; and

- (2) Submit nominations to the directors for the persons to be elected as the officers of the Corporation at each annual meeting of the Board of Directors.
- (3) Review the responsibilities of all Board Committees at least annually.
- (4) Develop and administer an annual Board of Directors' self-evaluation process to include an evaluation of the Board as a whole, the individual members of the Board and the Board's Committees.
- (5) Develop and oversee a Board education plan based upon the needs of the overall Board and individual members.
- (6) Define the role of Board members and annually review the application of the Conflict of Interest Policy.

Section 6.04. Lincoln Board Nominating Committee

The Lincoln Board Nominating Committee shall consist of the individuals who serve on the Lincoln Hospital Board of Directors. The Lincoln Board Nominating Committee shall annually submit a slate of nominees to the Board of Directors of persons to be elected and reelected to the Board of Directors as a Lincoln Board Elected Director. In addition, if there is a vacancy in a Lincoln Board Elected Director position, the Lincoln Board Nominating Committee shall submit a slate to the Board of Directors of nominee(s) to fill such vacancy. If, for any reason, the Board of Directors chooses not to elect the nominee(s) on a slate presented to it, the Lincoln Board Nominating Committee shall submit additional slate(s) until the Board of Directors elects the necessary number of individuals.

Section 6.05. Finance and Audit Committee

a. **Composition.** The Finance and Audit Committee shall consist of such number of members as the Board of Directors may designate from time to time. At a minimum, the members shall include the Chairman of the Board, the President and the Treasurer.

b. **Duties.** The Finance and Audit Committee shall:

- (1) Recommend to the Board of Directors financial policies and plans for the Corporation;
- (2) Recommend to the Board of Directors long-range financial plans, including capital and operating requirements;

- (3) Consider the Corporation's fiscal budget for capital and operating requirements and recommend adoption of said budget by the Board of Directors; this budget may encompass the entire fiscal year or a portion thereof;
- (4) Maintain financial evaluation and controls through consideration of financial and statistical reports on operations and recommend the adoption of these reports by the Board of Directors;
- (5) Receive reports and recommendations from management, or external consultants, who have been employed by the Corporation, such as certified public accountants and legal counsel, on matters of financial management, such as accounting systems, definition of accounting periods, appraisals and financial policies and present appropriate recommendations to the Board of Directors;
- (6) Consider appropriate debt structure as proposed by the President of the Corporation and recommend action to the Board of Directors;
- (7) Recommend to the Board of Directors investment policies and practices to govern the sound management and preservation of the Corporation's endowment;
- (8) Recommend to the Board of Directors insurance policies and programs, except that coverage that relates to fringe benefits of employees;
- (9) Recommend to the Board of Directors the appointment of depositories and a certified public accountant for the Corporation;
- (10) Monitor, in conjunction with the Corporation's designated Compliance Officer, the Corporation's adherence to and compliance with the federal, state and local laws and regulations which are applicable to the Corporation's business operations; and
- (11) Assure appropriate insurance coverage for general and professional liability exposures.

Section 6.06. Strategic Planning and Development Committee

a. **Composition.** The Strategic Planning and Development Committee shall consist of such number of members as the Board of Directors may designate from time to time. The members shall include the Chairman of the Board and the President, at a minimum.

b. **Duties.** The Strategic Planning and Development Committee shall:

- (1) Review and evaluate the short-range and long-range and annual goals of the System and recommend appropriate action to the Board of Directors;
- (2) Recommend to the Board of Directors long-range plans for the orderly development of the System within the framework of approved mission, vision, strategic plan, goals and projected future requirements of the System;
- (3) Conduct an annual evaluation of the Corporation's accomplishments in comparison with present goals and plans and past trends and recommend action as necessary to the Board of Directors;
- (4) Conduct a continuing review of the long-range plans adopted for the Corporation and recommend modifications in such plans to the Board of Directors as necessary to reflect past and current experience and other factors;
- (5) Determine the need for additions to or modification of physical facilities and equipment in cooperation with the Finance and Audit Committee which is responsible for projections of operating costs and revenues to be generated;
- (6) Recommend to the Board of Directors policies concerning the use and preservation of the physical plant;
- (7) Monitor construction projects and keep the Board of Directors informed of progress; and
- (8) Recommend to the Board of Directors policies and programs concerned with paramedical educational programs supported by the Corporation and with the treatment of students.

Section 6.07. Personnel Committee

a. **Composition.** The Personnel Committee shall consist of such number of members as the Board of Directors may designate from time to time. At a minimum, the members shall include the Chairman of the Board and the President.

b. **Duties.** The Personnel Committee shall:

- (1) Recommend to the Board of Directors general policies regarding human resources administration;

- (2) Review, evaluate and recommend to the Board of Directors management proposals regarding the compensation of all non-executive Corporation employees generally, including:
 - (i) Compensation budgeting;
 - (ii) Compensation planning;
 - (iii) Wage and salary structures;
 - (iv) Incentive pay plans;
 - (v) Pay for performance plans;
 - (vi) Modifications to compensation programs;
 - (vii) Benefit plans; and
 - (viii) Other issues related to employee compensation.
- (3) Provide ongoing review of the Corporation's human resources' programs;
- (4) Evaluate pertinent human resources/labor relations' issues and recommend appropriate course of action to the Board of Directors;
- (5) Assure that an adequate number of qualified personnel are available to carry out the Corporation's programs through the development of recruitment strategies.

Section 6.08. Quality and Safety Management Committee

a. **Composition.** The Quality and Safety Management Committee shall consist of such number of members as the Board of Directors may designate from time to time. At a, minimum, the members shall include the Chairman of the Board, the President, the President-elect of the Medical Staff.

b. **Duties.** The Quality and Safety Management Committee shall:

- (1) Ensure that credentials are reviewed and privileges granted and renewed based on the demonstrated clinical competence of the health care practitioner involved and recommend appropriate action by the Board of Directors;
- (2) Make certain the Quality Assurance program effectively identifies, assesses and resolves patient care problems;

- (3) Monitor the Corporation's liability experience and take required action to reduce exposure to loss;
- (4) Undertake such additional duties or projects in the area of Quality Control as shall be deemed appropriate by the Chairman or the Board of Directors.
- (5) Report to the Board of Directors the status of patient safety and quality of care including recommendations for improvement.
- (6) Report to the Board of Directors the status of patient satisfaction initiatives including recommendations for improvement.
- (7) Review accreditation and disaster planning.

Section 6.09. Community Benefit Committee

a. **Composition.** At a minimum, the Community Benefit Committee shall consist of the President and at least two other members of the Board.

b. **Duties.** The Community Benefit Committee shall:

- (1) Be responsible for overseeing and making recommendations with respect to all forms of benefit provided to the community by MHS and its affiliates, consistent with the tax-exempt purposes of MHS and its exempt affiliates.
- (2) The Committee shall oversee the annual community needs assessment process and recommend to the Board the annual Community Benefit Plan and budget.

Section 6.10. Leadership Compensation Committee

a) **Composition.** At a minimum, the Leadership Compensation Committee shall consist of such number of directors and/or nondirector members as the Board of Directors may designate from time to time, provided that the requirements of Section 6.01 are satisfied. Directors and nondirectors shall not be appointed to, nor serve on, the Leadership Compensation Committee to the extent that membership on the Leadership Compensation Committee by any such director or nondirector would prevent the Leadership Compensation Committee from being treated as an 'authorized body' for purposes of qualifying for the rebuttable presumption of reasonableness under Section 4958 of the Internal Revenue Code and the Treasury Regulations thereunder.

b) **Duties.** The Leadership Compensation Committee shall:

- (1) Review and approve all forms of compensation and benefits provided to executive-level employees or physician leaders of the Corporation or of

Memorial Medical Center, or, if applicable, any other affiliate (to the extent authorized in the such Bylaws);

(2) Shall take such steps as may be necessary or advisable to assure that no participating member of the Leadership Compensation Committee has a conflict of interest with respect to the deliberation and approval of any executive or physician leader's compensation or benefit arrangement; shall select and use third-party professional advisors (who may also act as professional advisors with respect to the Corporation); and

(3) Shall report to the Board of Directors, and to the Memorial Medical Center Board of Directors, or, if applicable, any other affiliate Board, on the manner in which the Leadership Compensation Committee has carried out its responsibilities, provided that such reports shall be provided in such detail as may be determined for this purpose by the Chairman of the Board.

The Leadership Compensation Committee shall serve in an independent and autonomous capacity which shall not require any action by the Board of Directors to carry out its prescribed duties herein.

Article VII

Contracts, Checks, Deposits and Funds

Section 7.01. Contracts

The Board may authorize any officer or officers, agent or agents of the Corporation, in addition to the officers so authorized by these Bylaws, to enter into any contract or execute and deliver any instrument in the name of and on behalf of the Corporation and such authority may be general or confined to specific instances.

Section 7.02. Checks, Drafts, Etc.

All checks, drafts or other orders for the payment of money, notes or other evidence of indebtedness issued in the name of the Corporation shall be signed by such officer or officers, agent or agents of the Corporation in such manner as shall from time to time be determined by resolution of the Board.

Section 7.03. Deposits

All funds of the Corporation shall be deposited from time to time to the credit of the Corporation in such banks, trust companies or other depositories as the Board may select.

Article VIII

Books, Records and Accounts

Section 8.01. General

The Corporation shall keep or cause to be kept correct and complete books and records of account and shall also keep minutes of the proceedings of the Board of Directors and its committees (as otherwise required by these Bylaws) and/or Membership, all of which shall be kept separate and apart from the books, records, accounts and minutes of its subsidiaries and affiliates. In addition, the Corporation shall annually cause a certified audit of its accounts to be made and shall cause to be filed the necessary reports, tax returns, or other documents as may be required by law on its own behalf.

Article IX

Miscellaneous

Section 9.01. Fiscal Year

The fiscal year of the Corporation shall end on the 30th day of September each year.

Section 9.02. Seal

The Board of Directors shall provide a corporate seal which shall be in the form of a circle and shall have inscribed thereon the name of the Corporation and the words, "Corporate Seal, Illinois."

Section 9.03. Waiver of Notice

Whenever any notice whatever is required to be given under the provisions of the General Not-For-Profit Corporation Act of the State of Illinois or under the provisions of the Articles of Incorporation or the Bylaws of this Corporation, a waiver thereof in writing signed by the person or persons entitled to such notice, whether before or after the time stated therein, shall be deemed equivalent to the giving of such notice.

Section 9.04. Offices

The Corporation shall have and continuously maintain in this state a registered office and registered agent whose office is identical with such registered office and may have other offices within or without the State of Illinois as the Board of Directors may from time to time determine.

Article X

Amendments

Section 10.01. Procedure

At any regular meeting of the Board of Directors or at a special meeting of the Board of Directors if notice thereof is contained in the notice for a special meeting, at which a quorum is present at either, these Bylaws or the Articles of Incorporation may be repealed and/or amended either in whole or in part by resolution of not less than a three-fourths (3/4) majority of the directors then in office. Amendments to provisions of Sections 4.02 and 4.03 pertaining to the Passavant Board Elected Directors shall also require approval of the PAH Board.

Article XI

Indemnification

Section 11.01. Statutory Indemnification

The Corporation will indemnify the Members, officers, directors, employees and agents of the Corporation as and to the extent permitted under the "General Not For Profit Corporation Act of 1986," as amended, or other applicable statutes of the State of Illinois.

Section 11.02. Indemnification Against Litigation

The Corporation will indemnify any person who was or is a party, or is threatened to be named as a party, to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action or suit by or in the right of the Corporation), by reason of the fact that he or she is or was a Member, officer, director, employee or agent of the Corporation, or is or was serving at the request of the Corporation as a Member, officer, director, employee or agent of another corporation, limited liability company, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him or her in connection with such action, suit or proceeding, if he or she acted in good faith and in a manner he or she reasonably believed to be in, or not opposed to, the interests of the Corporation and, with respect to any criminal action or proceeding, had no reasonable cause to believe that his or her conduct was unlawful. The termination of any action, suit or proceeding by judgment, order, settlement, conviction or a plea of nolo contendere, or an equivalent plea, will not create, per se, a presumption that the person did not act in good faith and in a manner he or she reasonably believed to be in, or not opposed to, the interests of the Corporation and, with respect to any criminal action or proceeding, had reasonable cause to believe his or her conduct was unlawful.

Section 11.03. Indemnification Against Derivative Suits

The Corporation will indemnify any person who was or is a party, or is threatened to be named as a party, to any threatened, pending or completed action or suit by or in the right of the Corporation to procure a judgment by reason of the fact that he or she is or was a Member, officer, director, employee or agent of the Corporation, or is or was serving at the request of the Corporation as a Member, officer, director, employee or agent of another corporation, limited liability company, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees) actually and reasonably incurred by him or her in connection with the defense or settlement of such action or suit, if he or she acted in good faith and in a manner he or she reasonably believed to be in, or not opposed to, the interests of the Corporation; however, there will be no indemnification by the Corporation if that person has been adjudged negligent or guilty of misconduct in the performance of his or her duty to the Corporation, unless, and to the extent, the court where the action or suit was instituted determines, on application, that, despite the adjudication of negligence or misconduct, and in view of all the circumstances presented to the court, such person is fairly and reasonably entitled to be indemnified against such expenses as the court deems proper.

Section 11.04. Expenses

If a Member, officer, director, employee or agent of the Corporation has been successful, on the merits or otherwise, in the defense of any action, suit or proceeding referred to in Section 11.02 or Section 11.03 of this Article XI, or in defense of any claim or issue in that action, suit or proceeding, he or she will be indemnified against expenses (including attorneys' fees) actually and reasonably incurred by him or her in connection with the action, suit or proceeding. The person being indemnified pursuant to the provisions of this Article XI may select and engage, in consultation with the Corporation, the legal counsel who will then serve as his or her representative in the defense of the action, suit or proceeding involving that person, or, alternatively, he or she may allow the Corporation to select and engage his or her legal counsel.

Section 11.05. Advance of Expenses

Expenses incurred in defending an action, suit or proceeding, whether civil, criminal, administrative or investigative, may be paid by the Corporation in advance of the final disposition of such action, suit or proceeding, if the Corporation has received an agreement by or on behalf of the Member, officer, director, employee or agent to repay, at the subsequent request of the Corporation, any amounts so advanced by the Corporation if such expenses are not payable by the Corporation pursuant to Section 11.04 of this Article XI.

Section 11.06. Insurance

The Corporation may purchase and maintain insurance on behalf of any person who is or was a Member, officer, director, employee or agent of the Corporation, or is or was serving at the request of the Corporation as a Member, officer, director, employee or agent of another corporation, limited liability company, partnership, joint venture, trust or other enterprise, to cover any liability asserted against him or her and incurred by him or her in any such capacity, or arising by virtue of his or her status as an officer, director, employee or agent.

Article XII

Code of Ethics and Conflicts of Interest Policy

The Corporation expects and demands ethical conduct and compliance with all laws by the Corporation's Members, officers, directors, employees and other agents, and the Corporation relies on the good faith of such Members, officers, directors, employees and agents in the exercise of their duties and responsibilities to the Corporation. The purposes of the Corporation's Code of Ethics and Conflicts of Interest Policy are to: (a) memorialize the Corporation's commitment to ethical and legally compliant conduct; (b) offer guidance to the Corporation's Members, officers, directors, employees and agents, through the implementation of this Code of Ethics and Conflicts of Interest Policy, to promote the avoidance of circumstances and situations which are, or which appear to be, in conflict with their duties and responsibilities to the Corporation in order to protect the Corporation's interests when the Corporation is contemplating entering into a transaction or arrangement which could benefit the private interests of a Member, officer, director, employee or other agent of the Corporation; and (c) articulate the Corporation's policies to be followed when assessing ethical conduct and potential conflicts of interest. This Code of Ethics and Conflicts of Interest Policy is intended to supplement, without replacing, any applicable state laws or regulations governing ethical conduct and/or conflicts of interest which are applicable to nonprofit and charitable corporations.

SCHEDULE 6.4.6
Employee Pension Plan Accounts

None.

SCHEDULE 6.6

Interim Changes

6.6.3:

The Bylaws of PAH were amended on February 7, 2013. A copy of the amended PAH Bylaws has been provided to MHS.

The Articles of Incorporation and Bylaws of PPA were revised in its dissolution and reincorporation on January 24, 2013. Copies of the documents have been provided to MHS.

6.6.6:

The PAH money purchase plan and tax-sheltered annuity plan were each amended October 1, 2012 and August 26, 2013.

PAH adopted a 457(b) plan in November, 2012.

SCHEDULE 6.8.2

Limitations on Licenses and Permits

None.

SCHEDULE 6.11.1

Owned Real Property and Leases

List of Real Property Used in Connection with Business:

Parcel ID	Owner	Property Address (when available)	City	State
08-13-200-013	Passavant Memorial Area Hospital Assoc.			IL
08-13-201-005	Passavant Memorial Area Hospital Assoc.	551 N. Westgate Ave.	Jacksonville	IL
09-18-100-001	Passavant Memorial Hospital	620 N. Westgate Ave.	Jacksonville	IL
09-18-100-003	Passavant Memorial Area Hospital Assoc.	1600 W. Walnut St.	Jacksonville	IL
09-18-100-004	Passavant Memorial Area Hospital Assoc.			IL
09-18-301-008	Passavant Memorial Area Hospital Assoc.	1515 W. Walnut St.	Jacksonville	IL
09-18-301-012	Passavant Memorial Area Hospital Assoc.	1515 W. Walnut St.	Jacksonville	IL
09-18-301-019	Passavant Memorial Area Hospital Assoc.	1515 W. Walnut St.	Jacksonville	IL

Real Property Leases:

Lease Agreement, dated October 1, 2011, by and between Passavant Area Hospital and Prairie Cardiovascular Consultants, Ltd.

Lease Agreement, dated May 23, 2005, by and between Passavant Area Hospital Association and Open MRI of Jacksonville, LLC

Agreement, dated March 1, 1992, by and between the Passavant Memorial Area Hospital Association and Joshua D. Warach, M.D. ("Warach Lease")

Second Addendum to Warach Lease, dated September 1, 1994, by and between Joshua D. Warach, M.D., S.C. and Passavant Area Hospital

Lease Agreement, dated February 15, 2013, by and between Passavant Area Hospital and Central Illinois Kidney and Dialysis Associates

Lease Agreement, effective as of July 23, 2008, by and between Passavant Area Hospital Association and Philip James Abraham, M.D.

Lease Agreement, dated May 23, 2005, by and between Passavant Area Hospital and Orthopaedic Center of Illinois, Ltd. ("OCI Lease")

Amendment to OCI Lease, dated September 1, 2008 by and between Passavant Area Hospital and Orthopaedic Center of Illinois, Ltd.

Lease Agreement, dated January 1, 2013, by and between Passavant Area Hospital and Central Illinois Hematology Oncology Center, P.C.

Ground Lease Agreement, dated January 1, 2012, by and between Memorial Health System and The Passavant Memorial Area Hospital Association

Other Encumbrances on Owned Real Property:

Reciprocal Easement Agreement, dated January 1, 2012, by and between Memorial Health System and The Passavant Memorial Area Hospital Association

Pre-Annexation Agreement, dated June 27, 2011, by and between the City of Jacksonville and The Passavant Memorial Area Hospital Association

Underground Electric Easement, dated May 24, 2012, granted by Passavant Memorial Area Hospital Association unto Ameren Illinois Company d/b/a Ameren Illinois

Overhead and Underground Electric Easement, dated July 3, 2013, granted by Passavant Memorial Area Hospital Association unto Ameren Illinois Company d/b/a Ameren Illinois

SCHEDULE 6.11.2

Compliance with Environmental Law

None.

SCHEDULE 6.12

Title Exceptions

Security Interest in Collateral identified in UCC-1 Financing Statement 011726313, filed on 1/17/2007 by Comerica Bank

Security Interest in Collateral identified in UCC-1 Financing Statement 014293922, filed on 5/14/2009 by Central Products, LLC

Security Interest in Collateral identified in UCC-1 Financing Statement 014320857, filed on 5/26/2009 by Bank of America, N.A., with Illinois Finance Authority described as an additional secured party.

Security Interest in Collateral identified in UCC-1 Financing Statement 014944729, filed on 1/19/2010 by MB Financial Bank, N.A.

Security Interest in Collateral identified in UCC-1 Financing Statement 017126156, filed on 3/21/2012 by Jacksonville Savings Bank

Security Interest in Collateral identified in UCC-1 Financing Statement 018059096, filed on 3/11/2013 by B. Braun Medical Inc.

Security Interest in Collateral identified in UCC-1 Financing Statement 018539667, filed on 8/26/2013 by Industrial Services of America, Inc.

Security Interest in Collateral identified in UCC-1 Financing Statement 013503206, filed on 8/4/2008 by Telarent Leasing Corporation.¹

Security Interest in Collateral identified in UCC-1 Financing Statement 012849850, filed on 1/8/2008 by Cisco Systems Capital Corporation¹

Security Interest in Collateral identified in UCC-1 Financing Statement 018802597, filed on 11/27/2013 by Everbank Commercial Finance, Inc.¹

Security Interest in Collateral identified in UCC-1 Financing Statement 018789159, filed on 11/22/2013 by Everbank Commercial Finance, Inc.¹

¹ Under investigation by PAH to determine whether it can or should be removed.

SCHEDULE 6.15

Insurance Coverage

Type of Coverage	Name of Insurer	Expiration Date
Business Automobile	Society Insurance	5/18/2014
Property	Fireman's Fund Insurance Company	12/31/2014
Medical Professional, General Liability	Illinois Provider Trust	12/31/2014
ER Physicians	ISMIE	7/1/2014
PPA Physicians	ISMIE	7/1/2014
Workers Comp	Illinois Compensation Trust	12/31/2014
Directors and Officers Liability	Travelers	10/1/2014
Heliport Liability	Global Aerospace, Inc	10/1/2014
Employee Dishonesty	Travelers	8/25/2015
Fiduciary Liability (pension & benefits)	Travelers	10/1/2014

SCHEDULE 6.17.1

Employee Benefit Plans

Vision Insurance (Avesis)

Dental Insurance (Delta Dental)

Health Program TPA (Blue Cross Blue Shield of Illinois)

Basic Life and AD&D (UNUM)

Supplemental Life (UNUM)

Supplemental AD&D (UNUM)

Passavant Memorial Area Hospital Association Employees' Pension Plan and Passavant Memorial Area Hospital Association Tax Deferred Annuity Plan

Passavant Memorial Area Hospital Association 457(b) Plan

Paid time off

PAH maintains both a short-term disability plan and long-term disability plan. The short term is self-funded as is the long-term plan until the employee has been off six months. After six months the plan is supported by a fully insured product currently written by UNUM.

SCHEDULE 6.17.2

Benefit Plans Subject to Funding Rules

None.

SCHEDULE 6.19

Accreditations

None.

SCHEDULE 6.20

Material Contract Defaults

None.

SCHEDULE 7.9.2

MHS Limitations on Licenses and Permits

No exceptions.

SCHEDULE 7.12

MHS Interim Changes

No exceptions.

Attachment #6

Financial Information

Included in Attachment #6 on the pages immediately following this page are documents demonstrating sufficient funds to finance the transaction and to operate the facility for 36 months.

- 1) Evidence of Memorial Health System's A+ bond rating from Standard and Poor's. (7 pages)
- 2) Evidence of Memorial Health System A1 bond rating from Moody's Investor Services. (7 pages)
- 3) Latest audited financial statement for Memorial Health System for Fiscal Years 2013, 2012 and 2011. (64 pages)
- 4) Latest audited financial statement for The Passavant Memorial Area Hospital Association's for Fiscal Years 2012 and 2011. (47 pages)

RatingsDirect®

Illinois Finance Authority Memorial Health System; Hospital

Primary Credit Analyst:

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Related Criteria And Research

Illinois Finance Authority

Memorial Health System; Hospital

Credit Profile

Illinois Fin Auth, Illinois

Memorial Hlth Sys, Illinois

Series 2009

Long Term Rating

A+/Stable

Affirmed

Rationale

Standard & Poor's Ratings Services affirmed its 'A+' long-term rating on the Illinois Finance Authority's \$148.195 million series 2009 hospital revenue bonds, issued on behalf of Memorial Health System. The outlook is stable.

The rating continues to be based on our opinion of Memorial's return to solid operations, stable management, and good balance sheet for the rating. However, Memorial is contemplating an expansion of the main campus in Springfield. Initial plans call for the project to require approximately \$110 million of new debt. For Memorial to be able to maintain its rating going forward, we expect performance to be no weaker than the forecast that was prepared by management.

During fiscal 2012, Memorial also issued two direct note obligations, 2012A and 2012B, which will allow Memorial to borrow up to a total of \$90 million by the end of fiscal 2013. All pro forma calculations assume that the full \$90 million is outstanding as of this analysis.

More specifically, the rating reflects our opinion of Memorial's:

- Good pro forma maximum annual debt service coverage (MADS) of 4.2x for the first quarter of fiscal 2013 ended Dec. 31;
- Good balance sheet, with 223 days' cash on hand, pro forma leverage of 38%, and cash to pro forma debt of 136% at Dec. 31, 2012; and
- Stable management team, which continues to implement and update its plan to help improve Memorial.

Partly offsetting our view of the above strengths is a possible future debt issuance by Memorial that would negatively affect the balance sheet.

Memorial is located in Springfield. Its major components are Memorial Medical Center (MMC), a teaching tertiary hospital with 500 licensed beds; Memorial Medical Center Foundation; Abraham Lincoln Memorial Hospital (ALMH), a critical access hospital located in Lincoln; Abraham Lincoln Healthcare Foundation; Taylorville Memorial Hospital (TMH), a critical access hospital located in Taylorville; Taylorville Memorial Hospital Foundation Inc.; Memorial Physician Services; Memorial Properties (formerly known as Healthcare Network Properties LLC); Memorial Home Services, which provides post-acute care services to residents of central Illinois; Mental Health Centers of Central

Illinois; and Memorial Health Ventures. Only Memorial and MMC are members of the obligated group.

Outlook

The stable outlook reflects our anticipation of management's ability to meet its 2013 budget, which calls for a 3% operating margin and liquidity similar to current levels.

If Memorial moves forward with its contemplated debt issuance in fiscal 2014, we would expect cash to debt to be no less than 150% and leverage to be no greater than 40% for Memorial to maintain its current rating or outlook.

Finally, unless the operations of Memorial soften again to a margin below 3%, or liquidity on the balance sheet deteriorates to less than 200 days, we anticipate maintaining the rating without a debt issuance. We do not anticipate raising the rating during the 18 month outlook period.

Enterprise Profile

Market share and utilization

In the Springfield market, MMC competes with St. John's Hospital, which is a part of Hospital Sisters Services Inc. MMC continues to lead the market with a 58.1% share in 2012.) This market share remains a positive for Memorial. It should be noted that the trauma designation switches annually between MMC and St. John's and was with MMC in fiscal 2012. For fiscal 2012, Memorial's acute admissions were again relatively flat at 26,155. However, Memorial did see increases in emergency room visits, outpatient visits, inpatient surgeries, and outpatient surgeries.

Memorial Health System And Subsidiaries

	Three month interims ended Dec. 31, 2012	--Fiscal year ended Sept. 30--		
		2012	2011	2010
Inpatient admissions	6,890	26,155	26,238	26,180
Patient days	32,921	116,073	115,836	133,031
Observation days	1,110	3,909	4,149	5,230
Emergency room visits	24,710	102,912	98,463	96,967
Outpatient visits	120,620	484,667	475,139	582,114
Home health visits	10,961	43,734	45,438	43,350
Inpatient surgeries	2,357	9,153	8,942	8,944
Outpatient surgeries	3,664	14,433	13,912	14,299
Births	438	1,978	1,999	1,962
Psychiatric/behavioral health admissions	318	1,365	1,273	1,335
Rehabilitation admissions	110	433	435	397
Medicare case mix index	1.754	1.724	1.712	1.678

Management

Memorial's management team has remained stable. For fiscal 2012, management was able to take full advantage of the new Abraham Lincoln Memorial Hospital, six updated outpatient operating rooms, and the location of trauma services

back at MMC. This, along with the continued growth of the medical group, its relationship with Southern Illinois University School of Medicine (SIUSM), and other initiatives, allowed Memorial to exceed its budget for fiscal 2012.

During fiscal 2013, Memorial became a member of the BJC Collaborative. The Collaborative members include Memorial, BJC HealthCare, CoxHealth, and St. Luke's Health System. The members combined have more than 4,500 beds and revenues of almost \$7 billion. The newly formed collaborative will allow the members to focus on lowering health care costs and deploying clinical programs and services to improve access to patients among other things.

Management has announced plans to expand MMC. The plan would include new patient rooms, operating rooms and support areas, a new Memorial Center for Learning and Innovation building, a new main entrance and lobby renovation, and upgrades of MMC's infrastructure.

Financial Profile

In accordance with our methodology explained in our report "New Bad Debt Accounting Rules Will Alter Some U.S. Not-for-Profit Health Care Ratios But Won't Affect Ratings" published Jan. 19, 2012 on RatingsDirect, we recorded Memorial's 2012 audit and first quarter of fiscal 2013 to include the adoption of Financial Accounting Standards Board ASU 2011-07 in 2012 but not in prior periods. The new accounting treatment means that Memorial's fiscal 2012 and subsequent financial statistics are directly comparable neither with the results for 2011 and prior years, nor with the 2011 median ratios. For an explanation of how the change in accounting for bad debt affects each financial measure, including the direction and size of the change, please see the above report.

Operations

Fiscal 2012 saw Memorial return to strong operations after a soft fiscal 2011. For the year, Memorial posted an operating margin of 7.1% compared with 2.6% in fiscal 2011. Management stated that the good operating results were driven by its strong relationship with the Springfield Clinic and its solid primary care network, while the leadership team also watched the expense base. For fiscal 2012, Memorial had 4.2x pro forma debt service coverage. For the first quarter of fiscal 2013, Memorial posted an operating margin of 5.1% compared with 1.1% for the same time period in fiscal 2012. Memorial continues to build off of the strategies that were implemented in fiscal 2012. While the operations for the first quarter are strong, we believe that Memorial should have no problems exceeding its budgeted 3% operating margin for fiscal 2013.

Balance sheet

The balance sheet for Memorial is good in our view with 223 days of cash at the end of the first quarter of fiscal 2013. As of Dec. 31, 2012, Memorial's pro forma leverage was good at 38%, and cash to pro forma debt declined to 136% when assuming that Memorial has exhausted \$90 million of the two lines issued in 2012.

Series 2012 debt

Memorial entered into a series 2012A obligation for a line of credit, up to \$60,000 with a commitment principal reduction amount, decreasing the principal to no more than \$30,000 due in September 2013. Beginning Oct. 1, 2014, the 2012A obligation will convert into a term loan of up to \$30,000, with quarterly principal and interest payments amortized over 20 years, with a maturity of Sept. 17, 2019. The interest rate is variable -- daily LIBOR plus 0.83%, with

an applicable spread of 0.0% to 0.4% based upon the current credit rating as issued by Standard & Poor's. Total draws against the line of credit as of Dec. 18, 2012 were \$30,000.

Memorial also entered into a Series 2012B Direct Note Obligation to borrow \$60,000 on Sept. 13, 2013, with a final maturity date of Oct. 1, 2033. The interest rate is a fixed rate of 4.26% (or monthly equivalent coupon yield of 4.22%) per annum. An earnest money reserve of 2%, or \$1,200, was established on Sept. 12, 2012 and pledged as additional security for the completion of the Series 2012 B obligation.

The proceeds from the Series 2012A and 2012B Direct Note Obligations will be used to construct, equip, and pay for any related financing costs for two medical office buildings that will be leased to employed and nonemployed physicians. One of the buildings will be located on the campus of Passavant Area Hospital in Jacksonville, Ill., and the other facility will be at MMC.

Future capital plans

Memorial has plans to spend approximately \$142 million on capital projects for the expansion of MMC. Currently, Memorial is contemplating issuing approximately \$110 million of debt in fiscal 2014 to help fund the projects. Based on the forecast provided to Standard & Poor's, Memorial does not plan to materially impact the balance sheet going forward. Its forecast does not anticipate leverage of greater than 38%, liquidity of less than 225 days, or cash to debt of less than 130%. Memorial's forecast runs through fiscal 2018. Once the debt issuances are finalized, Standard & Poor's will incorporate the plans into our rating. However, if Memorial is unable to perform up to the level of its forecast, there will be a strong likelihood of a negative outlook or rating action.

Memorial Health System And Subsidiaries

	--Fiscal year ended Sept. 30--			
	Three month interim ended Dec. 31, 2012*	2012*	2011	2010
Financial performance				
Net patient revenue (\$000s)	169,718	694,498	647,862	639,923
Total operating revenue (\$000s)	189,452	754,814	736,065	717,104
Total operating expenses (\$000s)	179,709	701,626	717,015	676,762
Operating income (\$000s)	9,743	53,188	19,050	40,342
Operating margin (%)	5.14	7.05	2.59	5.63
Net non-operating income (\$000s)	3,141	13,502	7,897	(510)
Excess income (\$000s)	12,884	66,690	26,947	39,832
Excess margin (%)	6.69	8.68	3.62	5.56
Operating EBIDA margin (%)	12.57	14.85	9.54	11.83
EBIDA margin (%)	14.00	16.35	10.50	11.77
Net available for debt service (\$000s)	26,958	125,621	78,102	84,406
Maximum annual debt service (\$000s)§	25,770	25,770	17,404	17,404
Maximum annual debt service coverage (x)§	4.18	4.87	4.49	4.85
Liquidity and financial flexibility				
Unrestricted cash and investments (\$000s)	411,563	389,595	323,356	354,305
Unrestricted days' cash on hand	223.2	217.6	174.7	202.4

Memorial Health System And Subsidiaries (cont.)				
Unrestricted cash/total long-term debt (%)	199.4	183.4	146.3	156.4
Average age of plant (years)	7.8	7.1	7.6	8.6
Capital expenditures/depreciation and amortization (%)	215.2	106.7	199.5	214.5
Debt and liabilities				
Total long-term debt (\$000s)	206,446	212,400	220,990	226,570
Long-term debt/capitalization (%)	29.1	30.4	33.2	35.8
Contingent liabilities (\$000s)§	97,005	69,795	77,340	81,659
Contingent liabilities/total long-term debt (%)	47.0	32.9	35.0	36.0
Debt burden (%)	3.33	3.34	2.33	2.40
Defined benefit plan funded status (%)	N.A.	71.52	74.71	67.20
Pro forma ratios§				
Unrestricted days' cash on hand	223.20			
Unrestricted cash/total long-term debt (%)	136.19			
Long-term debt/capitalization (%)	37.55			

*FASB 2011-07 adopted related to the treatment of bad debt. Standard & Poor's recorded bad debt expense as if FASB 2011-07 was adopted related to the treatment of bad debt beginning in fiscal 2012. §Pro forma assumes \$30 million is outstanding on 2012A and \$60 million on 2012B. N.A.—Not available.

Related Criteria And Research

USPF Criteria: Not-For-Profit Health Care, June 14, 2007

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MOODY'S

INVESTORS SERVICE

Rating Update: Moody's affirms Memorial Health System's (IL) A1 Outlook remains stable

Appendix 6

moody's letter

A1 MHS Rating

Global Credit Research - 01 Feb 2013

Affects approximately \$148 million of rated debt outstanding

ILLINOIS FINANCE AUTHORITY
Hospitals & Health Service Providers
IL

Opinion

NEW YORK, February 01, 2013 –Moody's Investors Service has affirmed Memorial Health System's (MHS) A1 bond rating on approximately \$148 million of Series 2009 fixed rate revenue bonds issued through the Illinois Finance Authority. The outlook remains stable. MHS also has approximately \$157 million of debt that does not carry an underlying rating from Moody's, including the Series 1985C, Series 1999A, Series 2003, and Series 2004 variable rate demand obligation (VRDO) bonds. The Series 1985C, Series 2003, and Series 2004 VRDOs bonds are supported by letters of credit (LOC) from JPMorgan Chase (expiring January 15, 2016). The Series 1999A VRDO bonds are supported by an LOC from PNC Bank (expiring January 15, 2016). After fiscal year end (FYE) 2012, as expected, MHS committed to issuing up to \$90 million of private placement direct loan bonds, including \$30 million of variable rate debt (direct loan with PNC) and \$60 million of fixed rate debt (direct loan with SunLife).

MHS is a three hospital network located in central Illinois. The three MHS hospitals are: (1) Memorial Medical Center (MMC), a 25,500 admission tertiary/quaternary academic medical center (AMC) located in Springfield, IL; (2) Taylorville Memorial Hospital (TMH), a 1,500 admission critical access hospital located in Taylorville, IL; and (3) Abraham Lincoln Memorial Hospital (ALMH), a 1,000 admission critical access hospital located in Lincoln, IL. MMC is one of two primary teaching hospitals for the Southern Illinois University (SIU) School of Medicine.

SUMMARY RATING RATIONALE: The affirmation of the A1 rating and stable outlook reflect MHS's leading market position in a broad service area, adequate balance sheet ratios, and its track record of profitability and particularly strong margins in fiscal year (FY) 2012. While we do not expect the strong performance in FY 2012 to be sustained, we believe MHS will continue to maintain good margins at the A1 rating level. As expected, after FYE 2012, MHS committed to issuing up to \$90 million of new debt, which stresses the system's debt coverage ratios. MHS management also is considering issuing an additional \$110-\$130 million of new debt within the next year. Unless MHS unexpectedly maintains FY 2012 operating margins and builds cash reserves considerably, if MHS moves forward with additional debt in late 2013/2014, this may pressure MHS's rating.

STRENGTHS

*Sizeable tertiary/quaternary AMC health system with affiliation as one of two leading teaching hospitals for the SIU medical school.

*Market share leader in broad nine county primary service area (PSA). MHS has only one sizeable competitor of note in the PSA (St. John's Hospital Springfield, a member of A1 rated Hospital Sisters Health System).

*Springfield is the capital of Illinois and home of SIU, which provide economic stability. The median household income in Sangamon County is in-line with the national average and the county's unemployment rate is just below the state and national averages (according to US Census Bureau and US Bureau of Labor Statistics).

*Track record of generating good operating results, with particularly strong margins in FY 2012 (14.2% adjusted operating cash flow margin). We note that since FY 2004, MHS has recorded an operating cash flow margin of at least 9.5%.

*Even with the debt issuance after FYE 2012, MHS's adjusted debt coverage ratios are adequate at the A1 rating level (2.7 times debt-to-cash flow, 5.0 times peak debt service coverage, 126% cash-to-direct debt, and 41% debt-to-total operating revenue).

*Low average age of plant of 7.1 years at FYE 2012 (all ratings median is 10.5 years).

*One of four members of the BJC Collaborative, which was formed in fall 2012. In addition to MHS, members include BJC Health System, Saint Luke's Health System of Kansas City, and CoxHealth of Springfield, MO.

CHALLENGES

*Despite MHS's leading market position in the PSA, St. John's Hospital represents significant competition, including for high-end tertiary services.

*MHS management is considering issuing another \$110-\$130 million of additional new debt in late 2013 or early 2014, which would stress debt coverage ratios, particularly considering that operating margins in future years are not expected to match the strong results in FY 2012.

*Underfunded defined benefit pension plan (72% pension funded ratio compared to a projected benefit obligation of \$394 million at FYE 2012). The plan was frozen in December 2011 and no new participants are permitted after that date.

*Medicaid as a percent of gross revenues has increased somewhat in recent years from 10.7% in FY 2007 to 13.1% in FY 2012.

DETAILED CREDIT DISCUSSION

LEGAL SECURITY: The Series 2009 bonds are a joint and several obligation of the obligated group, secured by a security interest in certain pledged revenues. The MHS parent and MMC are the only current members of the obligated group. The bond documents do not include a mortgage pledge or a debt service reserve fund.

INTEREST RATE DERIVATIVES: MHS currently has three floating-to-fixed interest rate swaps in place in connection with the Series 2003, Series 2004, and Series 1985C VRDO bonds. As of audited FYE 2012 (September 30 year end), the total notional amount of the swaps was \$59.6 million and the net termination value of the swaps was a negative \$9.7 million to MHS. The fixed rates MHS pays range from 3.49% to 4.99%. On the two swaps associated with the Series 2003 and Series 1985C VRDO bonds, MHS receives 70% of LIBOR. On the swap associated with the Series 2004 VRDO bonds, MHS receives 100% of LIBOR. Piper Jaffray is the counterparty on all three swaps.

RECENT DEVELOPMENTS/RESULTS

MHS operates one of two tertiary acute care systems in a nine county PSA centered on Springfield, IL (Sangamon County), the state's capital. Based on data provided by MHS management, factoring all patients from all patient origins, MMC captured 57.8% market share in calendar year 2011 compared to 42.2% share for St. John's Hospital Springfield (a member of A1 rated Hospital Sisters Health System). St. John's also offers an array of tertiary services. MHS's market share generally has trended up over the last two decades. In 1993, St. John's was the market leader with 52.8% share, while MMC captured 40.9% share, and much smaller Doctor's Hospital (which closed in 2003) captured 6.3%. We note, however, that MMC's market share dropped from 59.2% in 2010. Out-migration is limited. The closest markets with hospitals offering similar services to those available in Springfield are Peoria, IL (72 miles north of Springfield) and St. Louis, MO (98 miles southwest of Springfield).

Competition from entrepreneurial physicians is limited in Springfield due to the presence of large physician practices in the market, including the SIU faculty. The Springfield Clinic is the largest multi-specialty physician group in the area and is located adjacent to MMC. While Springfield Clinic physicians admit to both MMC and St. John's, according to MHS management MHS receives more than three-quarters of the clinic's volumes.

Demographic indicators in the Springfield area are reasonably good. Springfield is the state capital of Illinois and is the home of SIU, which provide stability to the local economy. According to US Census Bureau data, the median household income level in Sangamon County is just below the state average and just above the national average. Based on US Bureau of Labor Statistics data, the unemployment rate in the county is just below the state and national averages. We note that the State of Illinois is by far the biggest employer in the area. Given the state's fiscal challenges (the State of Illinois' general obligation rating is A2) and pressures to balance the budget, the state may look to downsize employment levels in the Springfield area and reduce employee benefits, which ultimately would contribute to increasing uncompensated care and deteriorating payer mix at area healthcare providers.

MHS has a track record of profitable operations, with particularly strong margins in FY 2012. In audited FY 2012 (September 30 year end), MHS recorded adjusted operating income of \$47.5 million (6.3% operating margin,

adjusted to reclassify a \$5.1 million one-time CMS rural floor settlement from operating revenue to non-operating) and operating cash flow of \$106.4 million (14.2% operating cash flow margin). In FY 2011, MHS recorded operating income of \$19.1 million (2.6% margin) and operating cash flow of \$70.2 million (9.5% margin). We note that bad debt is classified as an operating expense in FY 2011 and as a deduction from operating revenue in FY 2012.

MHS management attributes the improved performance in FY 2012 to a number of factors, including: (a) good cost management due to reduced clinical variation and the fact that MHS no longer has one-time costs associated with opening the major new projects at the critical access hospitals in FY 2011 (we note that the system's cost management in FY 2012 is particularly impressive even though pension expenses increased from a budgeted \$8.8 million to \$16.4 million); (b) while inpatient admissions were generally flat in FY 2012, MHS realized a 3.7% increase in outpatient surgeries and 1.1% increase in total outpatient visits; (c) unusual to the Springfield market, MMC and St. John's rotate Level I trauma center status, and MMC has the trauma status during even calendar years, so given MHS's September 30 fiscal year end, MHS had nine months of trauma designation during FY 2012 (management estimates that Level I trauma status was worth approximately \$8 million profit to MHS in FY 2012); and (d) MHS received \$6.7 million of electronic medical record (EMR) meaningful use funding in FY 2012, after not receiving funding in prior years. We note that in addition to the increased pension expense, MHS also faced additional headwinds in FY 2012 due to reduced funding from the State of Illinois, in the form of state employee health plan savings and Medicaid reimbursement cutbacks.

In future years, while MHS management expects to maintain good operating margins, the strong results in FY 2012 are not expected to continue. Between FY 2013 and FY 2018, management projects MHS to maintain an operating cash flow margin between 11% and 12%. For FY 2013, beyond an expected \$14 million increase in pension expense, management has targeted approximately \$18 million of expense savings and process improvements. Note that MMC will have only three months of trauma status in FY 2013, which will result in approximately \$5 million of reduced funding in FY 2013 compared to FY 2012.

In addition to expense savings identified internally, in fall 2012, MHS - along with Aa2 rated BJC Health System, A1 rated Saint Luke's Health System of Kansas City, and A2 rated CoxHealth of Springfield, MO - formed the BJC Collaborative. The purpose of the collaborative is to generate economies of scale and cost savings in areas such as joint purchasing/supply costs, information technology, legal services, and population health management. MHS management notes that the collaborative does not require material funding from any of the partners, and that there is no near-term plans for this to evolve into a merger among the parties.

Due to good operating performance and investment returns, MHS's absolute unrestricted cash and investments increased to \$390 million at FYE 2012 from \$323 million at FYE 2011. We note that MHS's cash position improved despite the system's continued increase in accounts receivables to 74 days at FYE 2012 from 62 days at FYE 2011 and 53 days at FYE 2010 (which is due to the State of Illinois delaying payment on Medicaid and state employee health plans). As a result of cash growth, MHS's cash on hand improved to a good 218 days at FYE 2012 from 175 days at FYE 2011 (A1 median is 204 days). According to management, at FYE 2012 MHS's unrestricted cash and investments were allocated among approximately 58% cash and fixed income, 40% equities, and 1.7% other investments (including real estate), and that 99% of unrestricted cash and investments could be liquidated within one month.

Factoring the Series 2012A and Series 2012B bonds issued after FYE 2012, MHS's Moody's adjusted pro forma debt ratios are adequate at the A1 rating level. Based on FY 2012 results (adjusted to include the Series 2012A&B debt), MHS's adjusted debt-to-cash flow measures 2.7 times (A1 median is 3.1 times), adjusted maximum annual debt service (MADS) coverage measures 5.0 times (A1 median is 5.1 times), debt-to-total operating revenue measures 41% (A1 median is 37%), cash-to-direct debt measures 126% (A1 median is 147%), and monthly liquidity-to-demand debt measures 242% (A1 median is 334%). Factoring MHS's operating leases and underfunded defined benefit pension plan (which was frozen in December 2011), MHS's cash-to-comprehensive debt measures 97% (A1 median is 117%).

Between FY 2013 and FY 2018, MHS has approximately \$450 million of capital spending plans, over half of which is targeted in the first two years of the projection period. Over the six years, this translates to an average capital spending ratio of 1.3 times (the all ratings median is 1.2 times). Key current capital projects include the construction of a medical office building (MOB) on the campus of Passavant Area Hospital in Jacksonville, FL (which is expected to be complete in April 2013, ahead of schedule according to management) and a new MOB in Springfield with the Springfield Clinic (which is expected to be complete in spring 2014). Future capital being considered is focused on expanding the MMC flagship campus, and would include projects such as new surgery capacity, adding three floors to MMC, constructing a new Center for Learning and Innovation (which is an MHS project that will in part benefit the SIU School of Medicine), renovate the main lobby, and support infrastructure

work. The MMC expansion projects are estimated to cost nearly \$140 million and would be constructed in phases between spring 2013 through early 2016. The \$90 million PNC and SunLife direct Series 2012A&B loans were issued after FYE 2012 to finance the MOB projects. To support the financing of the possible MMC expansion projects, MHS management is considering issuing an additional \$110-\$130 million of new debt within the next year.

OUTLOOK

The stable outlook reflects MHS's leading market position in a broad service area, adequate balance sheet ratios, and track record of profitability and particularly strong margins in FY 2012. While we do not expect the strong performance in FY 2012 to be sustained, we believe MHS will continue to maintain good margins at the A1 rating level. The additional \$110-\$130 million of new debt being considered may pressure MHS's rating, unless MHS unexpectedly maintains FY 2012 operating margins and builds cash reserves considerably.

WHAT COULD MAKE THE RATING GO UP

Material cash flow growth and maintenance of elevated operating margins resulting in significantly improved balance sheet ratios and debt coverage; continued market share growth; limited new debt

WHAT COULD MAKE THE RATING GO DOWN

Sustained weaker operating margins; thinner balance sheet and debt coverage ratios; material sustained market share loss; increase in debt as contemplated without maintenance of elevated operating margins and strengthening of balance sheet position

KEY INDICATORS

Assumptions & Adjustments:

- Based on Memorial Health System and Subsidiaries consolidated financial statements
- First number reflects audited FY 2011 for the year ended September 30, 2011
- Second number reflects pro forma on audited FY 2012 for the year ended September 30, 2012
- Pro forma factors \$90 million of Series 2012A&B direct loans issued after FYE 2012
- \$5.7 million CMS rural floor settlement removed from operating revenue
- Investment returns normalized at 6% unless otherwise noted
- Comprehensive debt includes direct debt, operating leases, and pension obligation, if applicable
- Monthly liquidity to demand debt ratio is not included if demand debt is de minimis

*Inpatient admissions: 27,946; 27,953

*Observation stays: 4,149; 3,909

*Medicare % of gross revenues: 48.0%; 47.5%

*Medicaid % of gross revenues: 12.8%; 13.1%

*Total operating revenues (\$): \$736 million; \$749 million

*Revenue growth rate (%) (3 yr CAGR): 6.5%; 5.2%

*Operating margin (%): 2.6%; 6.0%

*Operating cash flow margin (%): 9.5%; 14.2%

*Debt to cash flow (x): 2.84 times; 2.66 times

*Days cash on hand: 175 days; 217 days

*Maximum annual debt service (MADS) (\$): \$19.3 million; \$25.8 million

*MADS coverage with reported investment income (x): 4.04 times; 4.65 times

*Moody's-adjusted MADS Coverage with normalized investment income (x): 4.65 times; 5.01 times

*Direct debt (\$): \$226 million; \$308 million

*Cash to direct debt (%): 143%; 126%

*Comprehensive debt: \$284 million; \$402 million

*Cash to comprehensive debt (%): 114%; 97%

*Monthly liquidity to demand debt (%): 418%; 242%

RATED DEBT

Issued through the Illinois Finance Authority (debt outstanding as of September 30, 2012):

-Series 2009 Fixed Rate Revenue Bonds (\$148.2 million outstanding), rated A1

CONTACTS

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Underwriter: Nessler Shems, Piper Jaffray & Co., (617) 654-0771

PRINCIPAL METHODOLOGY

The principal methodology used in this rating was Not-For-Profit Healthcare Rating Methodology published in March 2012. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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CONSOLIDATED FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

Memorial Health System and Subsidiaries
Years Ended September 30, 2013, 2012, and 2011
With Report of Independent Auditors

Ernst & Young LLP

 **ERNST & YOUNG**

Memorial Health System and Subsidiaries
Consolidated Financial Statements and Supplementary Information
Years Ended September 30, 2013, 2012, and 2011

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Report of Independent Auditors

The Board of Directors
Memorial Health System

We have audited the accompanying consolidated financial statements of Memorial Health System and Subsidiaries (MHS), which comprise the consolidated balance sheets as of September 30, 2013, 2012, and 2011, and the related consolidated statements of operations and changes in net assets and cash flows for the three years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Memorial Health System and Subsidiaries at September 30, 2013, 2012, and 2011, and the consolidated results of their operations and their cash flows for the three years then ended in conformity with U.S. generally accepted accounting principles.

Supplementary Information

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

Ernst & Young LLP

December 10, 2013

Memorial Health System and Subsidiaries

Consolidated Balance Sheets
(In Thousands)

	2013	September 30 2012	2011
Assets			
Current assets:			
Cash and cash equivalents	\$ 142,064	\$ 97,488	\$ 71,240
Short-term investments	128,996	110,951	99,525
Assets whose use is limited – current portion	5,613	5,559	16,461
Receivables:			
Patient accounts receivable, net of allowance for uncollectible accounts of \$23,325, \$23,692, and \$22,096 as of September 30, 2013, 2012, and 2011, respectively	113,893	130,689	106,139
Receivables from third-party payors	7,931	16,835	11,638
Other	22,808	14,298	23,700
Inventories	11,912	10,754	11,088
Prepaid expenses	13,181	10,566	7,913
Total current assets	446,398	397,140	347,704
Assets whose use is limited:			
Board-designated funds	213,643	181,156	152,591
Self-insurance trusts	20,383	20,351	17,857
Bond trustee assets	1,563	1,555	1,614
Other restricted assets	–	1,200	–
Donor restricted assets	10,065	9,697	8,694
Deferred compensation investments	20,023	19,769	19,064
Total assets whose use is limited	265,677	233,728	199,820
Property, plant, and equipment	794,819	709,460	677,803
Less accumulated depreciation	379,178	344,307	315,613
Net property, plant, and equipment	415,641	365,153	362,190
Other assets:			
Investments in partnerships	5,282	4,679	4,919
Unamortized bond issuance costs	3,234	3,749	3,999
Beneficial interest in remainder trust	35,391	26,460	21,082
Other	10,700	10,810	10,229
Total other assets	54,607	45,698	40,229
Total assets	\$ 1,182,323	\$ 1,041,719	\$ 949,943

	2013	September 30 2012	2011
Liabilities and net assets			
Current liabilities:			
Long-term debt – current portion	\$ 7,596	\$ 5,590	\$ 5,420
Accounts payable	51,145	43,469	35,561
Accrued payroll	29,029	28,355	26,324
Interest payable	4,362	4,266	4,292
Payables to third-party payors	30,979	33,699	28,509
Other	18,120	11,541	14,734
Total current liabilities	141,231	126,920	114,840
Long-term debt – less current portion	261,803	212,400	220,990
Other liabilities:			
Deferred compensation and benefits	21,001	20,654	19,798
Self-insurance accrued expenses	17,067	19,398	18,858
Accrued employee benefits	13,470	13,234	11,087
Pension obligation	28,558	112,108	75,651
Other	9,864	12,991	12,441
Total other liabilities	89,960	178,385	137,835
Total liabilities	492,994	517,705	473,665
Net assets:			
Unrestricted	642,497	486,305	445,194
Temporarily restricted	41,671	32,754	26,145
Permanently restricted	5,161	4,955	4,939
Total net assets	689,329	524,014	476,278

Total liabilities and net assets	<u>\$ 1,182,323</u>	<u>\$ 1,041,719</u>	<u>\$ 949,943</u>
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See accompanying notes.

Memorial Health System and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets
(In Thousands)

	Years Ended September 30		
	2013	2012	2011
Revenues:			
Net patient service revenues	\$ 659,196	\$ 671,257	\$ 622,139
Provision for uncollectible accounts	(13,367)	(18,071)	(19,030)
	645,829	653,186	603,109
Hospital access improvement revenue	32,741	23,241	25,723
Capitation revenues	53,091	49,341	64,688
Other revenues	28,338	29,046	23,515
Total revenues	759,999	754,814	717,035
Expenses:			
Salaries and wages	262,739	256,421	255,388
Employee benefits	87,381	73,946	86,264
Physician fees	55,949	50,290	41,696
Utilities	11,449	11,768	11,996
Pharmaceutical supplies	23,757	22,941	21,708
Patient service supplies	82,432	89,309	87,892
Supplies and other	86,794	94,176	94,151
Hospital provider assessment	19,014	12,192	12,221
Purchased medical services	31,785	31,655	35,516
Depreciation and amortization	47,443	48,252	41,259
Interest expense and other financing costs	10,665	10,676	9,894
Total expenses	719,408	701,626	697,985
Income from operations	40,591	53,188	19,050
Nonoperating gains (losses):			
Interest and dividends	5,680	5,594	6,137
Realized gain (loss) on investments, net	9,768	9,747	2,712
Unrealized gain (loss) on investments, net	21,367	26,874	(16,040)
Change in fair value of interest rate swap	2,937	(511)	(110)
Contributions	1,983	2,092	2,096
Other revenue (expense), net	(3,674)	(3,931)	(3,048)
Total nonoperating gains (losses), net	38,061	39,865	(8,253)
Excess of revenues over expenses	78,652	93,053	10,797

Memorial Health System and Subsidiaries

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

	Years Ended September 30		
	2013	2012	2011
Unrestricted net assets:			
Excess of revenues over expenses	78,652	93,053	10,797
Change in pension and post-employment obligations	77,088	(53,021)	28,674
Net assets released from restrictions for property acquisitions	3	820	44
Other	449	259	92
Increase in unrestricted assets	156,192	41,111	39,607
Temporarily restricted net assets:			
Contributions	1,122	1,779	1,350
Change in fair value of beneficial interest in perpetual trusts	9,925	6,375	770
Gain (loss) on investments, net	718	1,144	(52)
Net assets released from restrictions and other	(2,848)	(2,689)	(1,980)
Increase in temporarily restricted assets	8,917	6,609	88
Permanently restricted net assets – contributions and other	206	16	42
Increase in net assets	165,315	47,736	39,737
Net assets, beginning of year	524,014	476,278	436,541
Net assets, end of year	<u>\$ 689,329</u>	<u>\$ 524,014</u>	<u>\$ 476,278</u>

See accompanying notes.

Memorial Health System and Subsidiaries

Consolidated Statements of Cash Flows
(In Thousands)

	Years Ended September 30		
	2013	2012	2011
Cash flows from operating activities:			
Change in net assets	\$ 165,315	\$ 47,736	\$ 39,737
Adjustments to reconcile change in net assets to net cash provided by operating activities:			
Non-cash contribution	(112)	—	—
Change in unrealized losses on interest rate swaps	(2,937)	511	110
Restricted contributions	(1,190)	(1,795)	(1,392)
Increase in beneficial interest in perpetual trust	(9,925)	(6,375)	(770)
Depreciation and amortization	47,445	48,255	41,261
Loss on disposal of assets	252	138	1,067
Provision for uncollectible accounts	13,367	18,071	19,030
Change in pension obligation	(77,088)	53,021	(28,674)
Changes in assets and liabilities:			
Accounts receivable	3,430	(42,622)	(36,181)
Inventory and other assets	(12,251)	7,020	(2,505)
Investments classified as trading, net	(50,197)	(34,468)	25,796
Receivable from/payable to third-party payors	6,184	(7)	(7,101)
Accounts payable and other current liabilities	15,021	6,722	(14,412)
Self-insurance and other long-term liabilities	(8,399)	(12,982)	3,702
Net cash provided by operating activities	<u>88,915</u>	<u>83,225</u>	<u>39,668</u>
Cash flows from investing activities:			
Acquisition of property and equipment	(98,200)	(51,496)	(82,331)
Proceeds on sale of property	529	653	122
Change in investment in partnerships	(603)	239	1,863
Net change in other assets	341	(482)	1,824
Net cash used in investing activities	<u>(97,933)</u>	<u>(51,086)</u>	<u>(78,522)</u>

Memorial Health System and Subsidiaries

Consolidated Statements of Cash Flows (continued)
(In Thousands)

	Years Ended September 30		
	2013	2012	2011
Cash flows from financing activities:			
Restricted contributions and gain	1,190	1,795	1,392
Repayment of long-term debt	(8,591)	(8,420)	(5,564)
Issuance of long-term debt	60,000	—	—
Proceeds from short-term borrowings	60,000	—	—
Repayment of short-term borrowings	(60,000)	—	—
Payment of bond issuance cost and discount	—	(263)	—
Distributions from beneficial interest in remainder trust	995	997	802
Net cash provided by (used in) financing activities	<u>53,594</u>	<u>(5,891)</u>	<u>(3,370)</u>
Net increase (decrease) in cash and cash equivalents	44,576	26,248	(42,224)
Cash and cash equivalents, beginning of year	<u>97,488</u>	<u>71,240</u>	<u>113,464</u>
Cash and cash equivalents, end of year	<u>\$ 142,064</u>	<u>\$ 97,488</u>	<u>\$ 71,240</u>
Supplemental disclosure of cash flow information:			
Cash paid for interest	\$ 11,060	\$ 10,702	\$ 10,989

See accompanying notes.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

September 30, 2013

1. Organization

Memorial Health System (Parent) is incorporated as a not-for-profit corporation under the laws of the state of Illinois and is a tax-exempt organization as described in Section 501(c)(3) of the Internal Revenue Code (the Code). Memorial Health System and Subsidiaries (MHS) comprise the following corporations and their subsidiaries:

Memorial Health System

Sole corporate member of:

- Memorial Medical Center (MMC)
 - Memorial Medical Center Foundation (MMCF)
- Memorial Physician Services (MPS)
 - HealthCare Network Properties, LLC d/b/a Memorial Properties (MP)
- Memorial Home Services NFP (MHSvc)
 - Memorial Home Services of Central Illinois, Inc. (MHSCI)
- The Abraham Lincoln Memorial Hospital (ALMH)
- Abraham Lincoln Healthcare Foundation (ALHF)
- Mental Health Centers of Central Illinois (MHCCI)
- Memorial Health Ventures (MHV)
- Taylorville Memorial Hospital (TMH)
 - TMH Foundation, Inc. (TMHF)

All significant intercompany transactions and balances have been eliminated in the consolidated financial statements.

2. Summary of Significant Accounting Policies

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with a maturity of three months or less when purchased, excluding amounts whose use is limited by board designation or other arrangements under trust agreements. MHS places its cash and cash equivalents with institutions with high credit quality. However, at certain times, such cash and cash equivalents are in excess of government-provided insurance limits. MHS routinely invests in money market mutual funds. These funds generally invest in highly liquid U.S. government and agency obligations. MHS's cash and cash equivalents are invested in financial instruments that potentially subject MHS to concentrations of credit risk.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Short-Term Investments

Short-term investments primarily comprise cash and cash equivalents, corporate obligations, government obligations, certificates of deposit, mutual funds, and corporate equity securities that are classified as current assets because such amounts are available to meet MHS's operating cash requirements.

Accounts Receivable

MHS provides health care services through inpatient and outpatient care facilities located in central Illinois and grants credit to patients, substantially all of whom are local residents. MHS generally does not require collateral or other security in extending credit to patients; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits payable under their health insurance programs, plans, or policies, including, but not limited to, Medicare, Medicaid, health maintenance organizations, and commercial insurance policies.

The allowance for uncollectible accounts is based upon management's assessment of expected amounts to be collected, considering historical business and economic conditions, trends in health care coverage, and other collection indicators. Periodically throughout the year, management assesses the adequacy of the allowance for uncollectible accounts based upon its review of accounts receivable payor composition and aging. This review takes into consideration recent write-off experience by payor category, payor agreement rate changes, and other factors. The results of these evaluations are used to make any modifications to the provision for uncollectible accounts to establish an appropriate allowance for uncollectible accounts. After satisfaction of amounts due from insurance, MHS follows established guidelines for placing certain past-due patient balances with collection agencies.

Inventories

Inventories, consisting primarily of medical supplies and drugs, are stated at the lower of cost or market value. Cost is determined using the average cost method.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Assets Whose Use Is Limited

Assets whose use is limited primarily include designated assets set aside by the Board of Directors (Board) for future capital improvements, over which the Board retains control and may, at its discretion, subsequently use for other purposes. The classification may also include amounts set aside under revocable self-insurance trust agreements, assets held by trustees under indenture agreements, assets restricted as to use by donors, cash restricted as to withdraw or use, and deferred compensation investments. Amounts designated to help meet the current liabilities of MHS have been classified as the current portion of assets whose use is limited in the consolidated balance sheets.

Investment securities are recorded at fair value, based on the valuation methodologies used in the Fair Value Measurement and Disclosures Topic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC). The cost of securities sold is based on the specific identification method. MHS classifies its investment portfolio as trading, with unrealized gains and losses included in excess of revenues over expenses.

Realized and unrealized gains and losses on investments, interest, and dividends from all other investments are reported as nonoperating gains (losses) unless the income is restricted by donor or law.

Property, Plant, and Equipment

Property, plant, and equipment are recorded at cost or, if donated, at fair value at the date of receipt. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets as follows:

Land improvements	5–25 years
Buildings and improvements	10–40 years
Equipment	3–10 years

Leasehold improvements are depreciated over the corresponding lease term and included in depreciation expense.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Beneficial Interest in Trust

MMC is the beneficiary of an irrevocable trust held and administered by a third-party trustee. The income from this trust is distributed annually, and the principal will be distributed at some future date. The proceeds from the trust are restricted by the donor to be used for general maintenance and support of MMC. MMC's beneficial interest in the trust of \$35,391, \$26,460, and \$21,082 as of September 30, 2013, 2012, and 2011, respectively, is equal to the estimated fair value of the underlying trust assets (primarily Illinois farm land) and is recognized by MMC as temporarily restricted net assets. Trust distributions were \$995, \$997, and \$802 in 2013, 2012, and 2011, respectively, and are included in unrestricted contributions within the consolidated statements of operations and changes in net assets.

TMHF is the discretionary income beneficiary of a trust. The principal of this trust is not controlled by TMHF, nor will it revert to TMHF upon dissolution, and accordingly, it is not reflected in the accompanying consolidated financial statements. The market value of assets held in the trust totaled \$622, \$618, and \$568 as of September 30, 2013, 2012, and 2011, respectively. Trust distributions were \$31, \$26, and \$23 in 2013, 2012, and 2011, respectively, and were included in unrestricted contributions within the consolidated statements of operations and changes in net assets.

Other Assets

Other assets primarily consist of cash surrender value of life insurance policies, noncomplete agreement clauses in physician acquisition contracts, and reinsurance recoveries. Under the terms of the agreements, vesting to the physicians in the cash surrender values occurs over various terms.

Deferred Compensation Investments

MHS has several nonqualified deferred compensation plans available to select employees. Contributions to the plans are invested in mutual funds and are payable to the employees upon vesting, retirement, or resignation. Deferred compensation investments at fair value and deferred compensation liabilities have been recorded in the accompanying consolidated balance sheets.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Accrued Employee Benefits

Employee benefits consist of the accrual for the paid sick time program and the accrual for post-employment benefits, which consists of three liabilities: the continuation of medical benefits to employees on long-term disability, postretirement health care benefits for certain employee groups that meet special qualifications, and sick time paid at retirement. MHS accrues these benefits based on actuarial estimates.

Net Assets

MHS's net assets are classified as restricted and unrestricted based on the existence or absence of donor-imposed restrictions. Restricted net assets comprise temporarily restricted net assets, whose use by MHS has been limited by donors to a specific time period or for a particular purpose, and permanently restricted net assets, which must be maintained by MHS in perpetuity with the related investment income expendable to support the donor-designated purpose. The general nature of the donor restrictions is to support MHS's mission and health education programs, and to assist in capital purchasing.

MHS's endowments consist of approximately 37 individual donor-restricted funds established for a variety of purposes. Net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

MHS has a policy of appropriating for distribution each year 5% of its endowment funds' average fair value of investments over the prior 36 months as of September 30 of the preceding fiscal year in which the distribution is planned. In establishing this policy, MHS considered the long-term expected return on its endowments. Accordingly, over the long term, MHS expects the current spending policy to allow its endowment to grow at an average of the long-term rate of inflation. This is consistent with MHS's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specific term as well as to provide additional real growth through new gifts and investment return.

Net Patient Service Revenues

Patient service revenue is reported net of contractual allowances and discounts at estimated net realizable amounts from patients, third-party payors, and others for services rendered and includes estimated retroactive adjustments due to future audits, reviews, investigations, and significant regulatory actions.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

MHS has agreements with third-party payors that provide for payments at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenues are reported at the estimated net realizable amount from patients, third-party payors, and others for services rendered. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and these amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, or investigations. MHS's net patient service revenue (net of contractual allowances and discounts) increased by approximately \$4,671, \$1,855, and \$7,736 in 2013, 2012, and 2011, respectively, as the result of these retroactive adjustments.

During 2012, MMC recognized as part of net patient service revenue \$5,675 for the Medicare Rural Floor Budget Neutrality Act Settlement (the Settlement). The Settlement with Centers for Medicare and Medicaid Services involved approximately 2,200 hospitals nationwide and was reached to resolve a challenge made by the plaintiff hospitals for underpayment of inpatient Medicare services dating back to 1999.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Noncompliance with Medicare and Medicaid laws and regulations can make MHS subject to significant regulatory action, including substantial fines and penalties, as well as exclusion from the Medicare and Medicaid programs.

The provision for bad debts is based upon management's judgmental assessment of historical and expected net collections considering business and general economic conditions in its service area, trends in health care coverage, and other collection indicators. Throughout the year, management assesses the adequacy of the allowance for uncollectible accounts based upon its review of accounts receivable payor composition and aging, taking into consideration recent write-off experience by payor category, payor agreement rate changes, and other factors. The results of these assessments are used to make modifications to the provision for bad debts and to establish an appropriate allowance for uncollectible accounts receivable. For third-party payors, the provision is determined by analyzing the anticipated residual patient balances and contractually due amounts from payors who are known to be having financial difficulties. For uninsured patients, the provision is based on an analysis of past experience related to patients

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

unwilling to pay the discounted patient balances. The difference between the standard rate charged (less the discounted rate) and the amount actually collected after the reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Capitation Revenues

MHS has entered into risk-based contracts to provide medical services. Under these arrangements, MHS receives capitation payments based on the demographic characteristics of covered members in exchange for providing certain medical services to those members. MHS has engaged in stop-loss insurance contracts to protect against future significant losses for catastrophic cases.

Purchased medical services represent payments made to non-MHS and out-of-network providers for covered medical claims. MHS estimates its liability for covered medical claims, including claims incurred but not reported as of the balance sheet dates, based upon historical costs incurred and payment-processing experience. The liability for covered medical claims is included in other current liabilities in the accompanying consolidated balance sheets.

Asset Impairment

MHS considers whether indicators of impairment are present and, if present, performs the necessary tests to determine whether the carrying values of an asset are appropriate. Impairment write-downs are recognized in depreciation expense at the time the impairment is identified.

Charity Care

In support of its mission, MHS provides care to patients who lack financial resources and are deemed to be financially indigent. Traditional charity care includes cost of services provided to persons who MHS determines cannot afford health care because of inadequate resources. The charges for services provided to charity patients are not reported as net patient service revenue.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Derivative Financial Instruments

MHS uses interest rate swap instruments as part of a risk management strategy to manage exposure to fluctuations in interest rates and to manage the overall cost of its debt. Derivatives are used to hedge identified and approved exposures and are not used for speculative purposes. All derivatives are recognized as either assets or liabilities and are measured at fair value. MHS uses pricing models for various types of derivative instruments that take into account the present value of estimated future cash flows. Gains and losses resulting from changes in the fair value of derivatives are reflected in nonoperating gains (losses) in the consolidated statements of operations and changes in net assets.

Derivatives provide counterparty credit risk. This is the risk that contractual obligations of the other parties to the agreements will not be fulfilled. Concentrations of credit risk relate to groups of counterparties that have similar economic or industry characteristics. Such concentration would cause the counterparties' ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. In addition, MHS is subject to the market risk associated with changes in the value of the underlying financial instrument.

Donor-Restricted Gifts

Unconditional promises to give cash and other assets to MHS are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received or the condition is met. Gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. A donor restriction expires when a stipulated time restriction ends or the purpose restriction is accomplished. At that time, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions.

Donor-restricted contributions whose restrictions are met within the same year as they are received are reported as unrestricted contributions in the accompanying consolidated financial statements.

Performance Indicator

MHS's performance indicator (excess of revenues over expenses) includes all changes in unrestricted net assets other than net assets released from restrictions for property acquisitions and pension and post-employment liability adjustments.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Summary of Significant Accounting Policies (continued)

Operating and Nonoperating Gains (Losses)

MHS's primary mission is to improve the health of the people and communities it serves through a broad range of general and specialized health care services, including inpatient acute care, outpatient services, physician services, and other health care services. Activities directly associated with the furtherance of this purpose are considered to be operating activities. Other activities that result in gains or losses peripheral to MHS's primary mission are considered to be nonoperating. Nonoperating activities include interest, dividends, realized and unrealized gains and losses on investments, change of fair value of interest rate swaps, contributions, and other revenues and expenses not related to patient care.

Income Taxes

The authoritative guidance in ASC 740, *Income Taxes*, creates a single model to address uncertainty in tax positions and clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. Under the requirements of this guidance, tax-exempt organizations could be required to record an obligation as the result of a tax position they have historically taken on various tax exposure items.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Functional Expenses

MHS's accounting policies conform to U.S. generally accepted accounting principles applicable to health care organizations. Substantially all expenses are related to providing health care services to the community.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

3. Income Taxes

Each of MHS's subsidiaries, excluding those described in the following paragraph, is a separately incorporated not-for-profit corporation as described under Section 501(c)(3) of the Code and is tax-exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. They do, however, operate certain programs that may result in unrelated business income. Upon review as required by ASC 740, no tax provision was recorded for the years ended September 30, 2013, 2012, or 2011.

MP is a limited liability company whose sole member is MPS. MP is considered a disregarded entity for tax purposes and is exempt from income tax as part of its member, MPS. MHSCI is a taxable for-profit corporation whose sole member is MHSvc.

4. Revenues

Net Patient Service Revenues

MHS provides health care services through inpatient, outpatient, and ambulatory care facilities. Certain patients receive services that are covered by governmental and third-party payments, including Medicare and Medicaid (60.5%, 59.5%, and 60.6% of gross patient service revenues charges in 2013, 2012, and 2011, respectively) at contractual rates generally below MHS's established rates.

The following is the mix of net patient service revenues before the provision for uncollectible accounts by major payor source:

	Years Ended September 30		
	2013	2012	2011
Medicare	\$ 253,120	\$ 257,937	\$ 243,874
Medicaid	47,858	55,661	50,364
Managed care	170,744	158,143	149,026
BlueCross BlueShield	134,972	134,464	121,568
Other commercial payors	37,496	51,822	42,144
Patients	15,006	13,230	15,163
Total	<u>\$ 659,196</u>	<u>\$ 671,257</u>	<u>\$ 622,139</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

4. Revenues (continued)

Gross patient service revenues from Medicare were approximately \$956,082, \$912,721, and \$832,986 in 2013, 2012, and 2011, respectively. MHS is paid for services rendered to Medicare program beneficiaries generally under prospectively determined rates. Those rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. MMC's payment classification of patients under the prospective system is subject to audit by the program's professional review organization. TMH and ALMH are both designated as critical access hospitals and receive cost-based reimbursement for the majority of their Medicare services. MHSvc is reimbursed under the prospective payment system for substantially all Medicare beneficiaries.

Inpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Outpatient and home health services rendered to Medicaid program beneficiaries are reimbursed upon a per visit, per diem rate or on a fee-for-service basis. Gross patient service revenues rendered under Medicaid agreements were approximately \$246,150, \$251,774, and \$223,485 for 2013, 2012, and 2011, respectively.

Patient accounts receivable are stated at net realizable value. MHS evaluates the collectability of its accounts receivable based on the length of time the receivable is outstanding, major payor sources of revenue, historical collection experience, and trends in health care insurance programs to estimate the appropriate allowance for uncollectible accounts and provision for uncollectible accounts. For receivables associated with services provided to patients who have third-party coverage, MHS analyzes contractually due amounts and provides an allowance for uncollectible accounts and a provision for uncollectible accounts. For receivables associated with self-pay patients, MHS records a significant provision for uncollectible accounts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. Accounts receivable are charged to the allowance for uncollectible accounts when they are deemed uncollectible.

The allowance for uncollectible accounts as a percentage of accounts receivable increased from 15.3% in 2012 to 17.0% in 2013 primarily due to the reduction of Medicaid receivables due to accelerated payments received in 2013 that had a minimal estimated allowance for uncollectible accounts. MHS' combined allowance for uncollectible accounts and charity care cover 85%, 90%, and 90% of self-pay and patient responsibility accounts receivable at September 30, 2013, 2012, and 2011, respectively.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

4. Revenues (continued)

The following is the mix of net receivables by major payor source:

	2013	September 30 2012	2011
Medicare	22.8%	20.6%	23.0%
Medicaid	9.5	22.7	12.2
Managed care	44.2	33.8	41.3
BlueCross BlueShield	13.7	10.5	13.1
Other commercial payors	8.0	10.5	8.3
Patients	1.8	1.9	2.1
Total	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

Hospital Access Improvement Revenue

On November 21, 2006, the Centers for Medicare and Medicaid Services (CMS) approved the state of Illinois' Hospital Assessment Program (the Program). The Program was initially effective from July 1, 2005 through June 30, 2008. On December 4, 2008, CMS approved the state of Illinois' Program for an additional five years and was effective from July 1, 2008 through June 30, 2013. Subsequently, on June 14, 2012, the state of Illinois approved a 15-month extension to the Program through December 31, 2014. MHS recognized Illinois hospital assessment revenue of \$22,716, \$23,241, and \$25,723 for the years ended September 30, 2013, 2012, and 2011, respectively, and assessment expense of \$12,033, \$12,055, and \$12,033 for the years ended September 30, 2013, 2012, and 2011, respectively.

In addition to the original Program, the state of Illinois General Assembly approved a program to enhance the Program (Enhanced Program). CMS approved the Enhanced Program on September 30, 2013, to be retrospectively effective at June 10, 2013, and it terminates on December 31, 2014. MHS recognized additional revenue of \$10,025 and expense of \$6,801 for the year ended September 30, 2013. A corresponding receivable of \$10,025 and payable of \$6,801 are reflected in other receivables and accounts payable in the accompanying September 30, 2013, balance sheet.

In connection with the Program, contributions of \$180, \$137, and \$188 for 2013, 2012, and 2011, respectively, were also made to the Illinois Hospital & Research Education Foundation for the Program, which was reflected as hospital assessment expense in the consolidated statements of operations and changes in net assets. The net impact of the assessment was to increase excess of revenues over expenses by \$13,727, \$11,049, and \$13,502 for the years ended September 30, 2013, 2012, and 2011, respectively.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

4. Revenues (continued)

Capitation Revenues

MMC and Springfield Clinic, LLP formed a network on July 1, 1999. The purpose of the network is to work cooperatively with and assist Health Alliance Medical Plans (HAMP) to arrange for, develop, and maintain a network of participating providers and to provide covered services to plan members in the service area. MMC has an agreement with the network to provide medical services to over 26,250 members of the network. MMC receives a monthly capitation payment based on the number of members, regardless of services provided by MMC or other providers. As of September 30, 2013, 2012, and 2011, MHS has recognized a liability for covered medical claims of \$1,950, \$1,490, and \$1,040, respectively.

Other Revenues

The American Recovery and Reinvestment Act of 2009 provides for Medicare and Medicaid incentive payments beginning in calendar year 2011 for eligible hospitals and professionals who implement and achieve meaningful use of certified electronic health record (EHR) technology. MHS utilized a grant accounting model to recognize revenues for Medicare and Medicaid EHR revenues of \$3,684 and \$1,260, respectively, for the year ended September 30, 2013, and Medicare and Medicaid EHR revenues of \$4,895 and \$1,833, respectively, for the year ended September 30, 2012. Medicare and Medicaid EHR revenue is recorded in other revenues in the consolidated statements of operations and changes in net assets. Also recorded in other revenues are cafeteria sales revenue, rental income, and prompt pay interest penalties received from the state of Illinois.

5. Community Benefits

MHS is dedicated to delivering high quality, patient-centered care in support of its mission to improve the health of the people and communities it serves. MHS strives to be a national leader for excellence in patient care and provide quality health care to every patient who comes through its doors, regardless of their ability to pay. Community benefit represents the unpaid costs of public means tested programs, traditional charity care, and other forms of community support such as academic support to the Southern Illinois University School of Medicine, community health improvement activities, and contributions to health-related community activities.

Charity care is provided to those who are eligible based on MHS's charity policy. In addition to the charity care responsibilities, MHS provides numerous other community benefits. These community benefits include medical education and research, community health education, screenings, support groups, counseling services, research, and in-kind support. To address the need for health care providers, a number of programs are offered for young people who may be interested in a career in health care. Medicare, a national social insurance program administered by the federal government, provides reimbursement using a prospective payment system (PPS).

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

5. Community Benefits (continued)

PPS pays MHS a set amount for each episode of care provided to a patient, regardless of the actual cost of care. MHS recognized this unpaid cost of providing care to Medicare patients as a part of its total service to the community.

MHS calculates the unpaid cost of services by payor using an activity-based costing methodology. Direct costs related to patient care are added to indirect costs, which have been allocated based upon relative value units of each procedure. The sum of direct and indirect costs is offset by any net revenues to determine the unpaid costs by payor. Services provided to Medicaid and charity care patients represent the most significant levels of uncompensated care. MHS calculates the cost of other community benefits by identifying specific expenditures incurred by the health system that directly benefited the community.

The following is a summary of management's estimate of the costs of MHS's community benefit services:

	Years Ended September 30					2012	2011
	2013						
	MMC	ALMH	TMH	All Other Affiliates	Total		
					Total	Total	Total
Unpaid cost of Medicaid	\$ 18,466	\$ 5,113	\$ 3,060	\$ 3,062	\$ 29,701	\$ 25,884	\$ 30,368
Unpaid cost of charity care	15,421	1,852	1,665	716	19,654	18,354	18,233
Other community benefits	23,978	126	200	165	24,469	20,401	18,655
Community benefit	57,865	7,091	4,925	3,943	73,824	64,639	67,256
Unpaid cost of Medicare	29,400	—	—	5,128	34,528	25,009	40,360
Subtotal	87,265	7,091	4,925	9,071	108,355	89,648	107,616
Illinois hospital assessment, net	(10,180)	(1,960)	(1,587)	—	(13,727)	(11,049)	(13,502)
Total service to the community	\$ 77,085	\$ 5,131	\$ 3,338	\$ 9,071	\$ 94,625	\$ 78,599	\$ 94,114

The Illinois hospital assessment payment is designed to improve access to hospital services for state residents by improving the overall adequacy of payments for all hospitals as well as providing more equity in payments among hospitals. The program has also brought to Illinois federal matching funds for the Medicaid program.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

6. Assets Whose Use Is Limited and Short-Term Investments

MHS's investments are exposed to various kinds and levels of risk. Fixed income securities expose MHS to interest rate risk, credit risk, and liquidity risk. As interest rates change, the value of many fixed income securities is affected. Credit risk is the risk that the obligor of the security will not fulfill its obligations. Liquidity risk is affected by the willingness of market participants to buy and sell given securities. Equity securities expose MHS to market risk, performance risk, and liquidity risk. Market risk is the risk associated with major movements of the equity markets, both foreign and domestic. Performance risk is the risk associated with a company's operating performance. Liquidity risk as previously defined tends to be higher for foreign equities and equities related to small capitalization companies.

The composition of assets whose use is limited and short-term investments, all at fair market value, is set forth in the following table:

	2013	September 30 2012	2011
Cash and cash equivalents	\$ 33,713	\$ 44,182	\$ 49,987
Certificates of deposit	3,480	3,524	7,380
U.S. Treasury obligations	29,380	37,601	36,799
Government obligations	15,223	6,665	13,818
Corporate obligations	49,417	59,142	57,062
Corporate equities	127,301	111,628	78,307
International equities	13,949	5,482	5,961
Investment in real estate	2,768	2,502	2,110
Mutual funds	124,301	78,762	63,540
Accrued interest receivable and other	754	750	842
Assets whose use is limited and short-term investments	<u>\$ 400,286</u>	<u>\$ 350,238</u>	<u>\$ 315,806</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

7. Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Fair Value Measurements and Disclosures Topic of the FASB Accounting Standards Codification establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement).

Certain of MHS's financial assets and financial liabilities are measured at fair value on a recurring basis, including money market, fixed income, equity instruments, mutual funds, and interest rate swap agreements. The three levels of the fair value hierarchy and a description of the valuation methodologies used for instruments measured at fair value are as follows:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities as of the reporting date. Level 1 primarily consists of financial instruments such as money market securities and listed equities.

Level 2 – Pricing inputs other than quoted prices included in Level 1, which are either directly observable or can be derived or supported from observable data as of the reporting date. Level 2 inputs may include quoted prices for similar assets and liabilities in non-active markets or pricing models whose inputs are observable for substantially the full term of the asset or liability. Instruments in this category include certain U.S. government agency and sponsored entity debt securities and interest rate swap agreements.

Level 3 – Pricing inputs include those that are significant to the fair value of the financial asset or financial liability and are not observable from objective sources. These inputs may be used with internally developed methodologies that result in management's best estimate of fair value.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

7. Fair Value Measurements (continued)

The fair value of financial assets and financial liabilities measured at fair value on a recurring basis was determined using the following inputs at September 30, 2013:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 33,713	\$ —	\$ —	\$ 33,713
Certificates of deposit	—	3,480	—	3,480
U.S. Treasury obligations	29,655	—	—	29,655
Government obligations	—	15,223	—	15,223
Corporate obligations	—	49,896	—	49,896
Corporate equities:				
Consumer discretionary	19,104	—	—	19,104
Consumer staples	9,685	—	—	9,685
Energy	12,831	—	—	12,831
Financial	20,843	—	—	20,843
Health care	17,804	—	—	17,804
Industrials	15,781	—	—	15,781
Information technology	22,052	—	—	22,052
Materials	6,049	—	—	6,049
Telecommunication services	1,161	—	—	1,161
Utilities	1,858	—	—	1,858
Other equities	123	10	—	133
International equities	13,949	—	—	13,949
Investment in real estate	—	—	2,768	2,768
Mutual funds	93,329	30,972	—	124,301
Assets whose use is limited and short-term investments	297,937	99,581	2,768	400,286
Beneficial interest in remainder trust	325	—	35,066	35,391
Total assets	<u>\$ 298,262</u>	<u>\$ 99,581</u>	<u>\$ 37,834</u>	<u>\$ 435,677</u>
Liabilities				
Interest rate swaps	\$ —	\$ 6,738	\$ —	\$ 6,738
Total liabilities	<u>\$ —</u>	<u>\$ 6,738</u>	<u>\$ —</u>	<u>\$ 6,738</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

7. Fair Value Measurements (continued)

The fair value of financial assets and financial liabilities measured at fair value on a recurring basis was determined using the following inputs at September 30, 2012:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 44,182	\$ —	\$ —	\$ 44,182
Certificates of deposit	—	3,524	—	3,524
U.S. Treasury obligations	37,829	—	—	37,829
Government obligations	—	6,665	—	6,665
Corporate obligations	—	59,664	—	59,664
Corporate equities:				
Consumer discretionary	17,375	—	—	17,375
Consumer staples	6,112	—	—	6,112
Energy	10,999	—	—	10,999
Financial	16,386	—	—	16,386
Health care	16,467	—	—	16,467
Industrials	14,479	—	—	14,479
Information technology	19,068	—	—	19,068
Materials	6,037	—	—	6,037
Telecommunication services	2,033	—	—	2,033
Utilities	2,672	—	—	2,672
International equities	5,482	—	—	5,482
Investment in real estate	—	—	2,502	2,502
Mutual funds	41,080	37,682	—	78,762
Assets whose use is limited and short-term investments	240,201	107,535	2,502	350,238
Beneficial interest in remainder trust	318	504	25,638	26,460
Total assets	<u>\$ 240,519</u>	<u>\$ 108,039</u>	<u>\$ 28,140</u>	<u>\$ 376,698</u>
Liabilities				
Interest rate swaps	\$ —	\$ 9,676	\$ —	\$ 9,676
Total liabilities	<u>\$ —</u>	<u>\$ 9,676</u>	<u>\$ —</u>	<u>\$ 9,676</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

7. Fair Value Measurements (continued)

The fair value of financial assets and financial liabilities measured at fair value on a recurring basis was determined using the following inputs at September 30, 2011:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 49,987	\$ —	\$ —	\$ 49,987
Certificates of deposit	—	7,380	—	7,380
U.S. Treasury obligations	37,085	—	—	37,085
Government obligations	—	13,818	—	13,818
Corporate obligations	—	57,618	—	57,618
Corporate equities:				
Consumer discretionary	10,834	—	—	10,834
Consumer staples	4,572	—	—	4,572
Energy	7,703	—	—	7,703
Financial	10,401	—	—	10,401
Health care	11,505	—	—	11,505
Industrials	11,685	—	—	11,685
Information technology	14,437	—	—	14,437
Materials	2,972	—	—	2,972
Telecommunication services	2,029	—	—	2,029
Utilities	1,855	—	—	1,855
Other equities	314	—	—	314
International equities	5,961	—	—	5,961
Investment in real estate	—	—	2,110	2,110
Mutual funds	37,798	25,742	—	63,540
Assets whose use is limited and short-term investments	209,138	104,558	2,110	315,806
Beneficial interest in remainder trust	701	—	20,381	21,082
Total assets	<u>\$ 209,839</u>	<u>\$ 104,558</u>	<u>\$ 22,491</u>	<u>\$ 336,888</u>
Liabilities				
Interest rate swaps	\$ —	\$ 9,165	\$ —	\$ 9,165
Total liabilities	<u>\$ —</u>	<u>\$ 9,165</u>	<u>\$ —</u>	<u>\$ 9,165</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

7. Fair Value Measurements (continued)

No transfers into or out of Level 1 or Level 2 occurred between October 1, 2011 and September 30, 2013.

Following is a description of MHS's valuation methodologies for assets and liabilities measured at fair value. Fair value for Level 1 is based upon quoted market prices. The fair value of Level 2 securities was determined through evaluated bid prices provided by third-party pricing services where quoted market prices were not available. The fair values of the interest rate swap contracts are determined based on the present value of expected future cash flows using discount rates appropriate with the risks involved. The valuations reflect a credit spread adjustment to the LIBOR discount curve in order to reflect the credit value adjustment for "nonperformance" risk. The credit spread adjustment is derived from other comparably rated entities' bonds priced in the market.

The carrying values of cash, cash equivalents, accounts receivable, and current liabilities are reasonable estimates due to the short-term nature of these financial instruments.

Due to the volatility of the stock market, there is a reasonable possibility of changes in fair value and additional gains and losses in the near term subsequent to September 30, 2013.

The table below sets forth a summary of changes in the fair value of MHS's Level 3 assets for the period from October 1, 2010 to September 30, 2013.

	<u>Investments in Real Estate</u>
Fair value at October 1, 2010	\$ 22,337
Unrealized gain	154
Fair value at September 30, 2011	22,491
Unrealized gain	5,649
Total as of September 30, 2012	28,140
Unrealized gain	9,694
Total as of September 30, 2013	<u>\$ 37,834</u>

	<u>Years Ended September 30</u>		
	<u>2013</u>	<u>2012</u>	<u>2011</u>
Unrealized gains related to Level 3 financial instruments held	\$ 23,739	\$ 14,045	\$ 8,396

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

8. Property, Plant, and Equipment

The following is a summary of property, plant, and equipment:

	2013	September 30 2012	2011
Land	\$ 28,508	\$ 27,041	\$ 26,753
Land improvements	39,344	37,347	34,735
Buildings	402,390	369,429	357,376
Equipment	262,165	246,683	240,818
Construction in progress	62,412	28,960	18,121
	<u>794,819</u>	<u>709,460</u>	<u>677,803</u>
Less accumulated depreciation	379,178	344,307	315,613
Property, plant, and equipment, net	<u>\$ 415,641</u>	<u>\$ 365,153</u>	<u>\$ 362,190</u>

Capitalized interest was \$491, \$187, and \$1,173 for the years ended September 30, 2013, 2012, and 2011, respectively.

9. Investments in Partnerships

Investments in partnerships are accounted for using the equity method when the ownership interest is 20% or greater. The cost method is used for other investments in partnerships. Income from these investments in partnerships was \$1,581, \$2,131, and \$2,920 for the years ended September 30, 2013, 2012, and 2011, respectively, and is reflected in other revenue in the consolidated statements of operations and changes in net assets. Investments in partnerships include the following entities:

	Ownership	Ownership at September 30	September 30 2013	September 30 2012	2011
Rutledge Joint Ventures, LLC	MHV	50.0%	\$ 2,812	\$ 2,704	\$ 2,455
Orthopaedic Surgery Center of Illinois, LLC	MHV	50.0	926	1,090	1,282
Jacksonville Joint Ventures, LLC	MHSCI	50.0	661	733	642
Mid-America Solutions, LLC	MHS	12.5	500	—	—
Lincoln Land Health Information Exchange, LLC	MHS	27.3	177	—	—
Lincolnland Lithotripsy, LLC	MMC	8.8	100	100	100
Memorial Employee Assistance Services, LLC	MHCCI	50.0	58	31	47
BJC Collaborative, LLC	MHS	25.0	25	—	—
WTA Laser, LLC	MHV	28.0	23	21	13
Miller Street Properties	MPS	—	—	—	380
Investments in partnerships			<u>\$ 5,282</u>	<u>\$ 4,679</u>	<u>\$ 4,919</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

9. Investments in Partnerships (continued)

Rutledge Joint Ventures, LLC

MHV and Heritage Enterprises, Inc. participate in a 50/50 joint venture in Rutledge Joint Ventures, LLC d/b/a Heritage Manor. Heritage Enterprises, Inc. is responsible for the management of the operations and accounting for the skilled nursing and subacute care facility.

Orthopaedic Surgery Center of Illinois, LLC

MHV and a group of orthopedic surgeons participate in a 50/50 joint venture, Orthopaedic Surgery Center of Illinois, LLC. An operating lease has been executed between MHS and the joint venture.

Jacksonville Joint Ventures, LLC

MHSCI and Passavant Area Hospital participate in a 50/50 joint venture, Jacksonville Joint Ventures, LLC d/b/a Passavant Home Services. The joint venture's purpose is to provide medical equipment, respiratory therapy, and intravenous infusion services in the home.

Mid-America Solutions, LLC

Mid-America Solutions, LLC operates as a health care supply purchasing and management organization to provide opportunities to reduce labor and non-labor costs associated with purchasing, receiving, and distributing supplies and related items and services, as well as to reduce facility-wide supply inventory and storage costs.

Lincoln Land Health Information Exchange, LLC

MHS is a founding member of the Lincoln Land Health Information Exchange, LLC (the Exchange) along with other Springfield based health care organizations. The purpose of the Exchange is to improve the efficiency, effectiveness, and reliability of health care information exchange between providers and settings through a shared technology infrastructure.

Lincolnland Lithotripsy, LLC

Lincolnland Lithotripsy, LLC provides medical equipment and medical equipment management, primarily by furnishing mobile lithotripter equipment and supplies. MMC has executed an equipment and service lease with the entity.

Memorial Employee Assistance Services, LLC

Memorial Employee Assistance Services, LLC is a partnership between MHCCI and Chestnut Global Partners (Chestnut). MHCCI is responsible for providing the clinical staffing and support, and Chestnut is responsible for administration and infrastructure. Chestnut and MHCCI each have a 50% interest. The primary purpose of the joint venture is to provide specialized employee assistance programming to businesses in Springfield and the surrounding area.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

9. Investments in Partnerships (continued)

BJC Collaborative, LLC

The BJC Collaborative, LLC (Collaborative) was formed in 2012 between MHS, BJC Healthcare, CoxHealth, and Saint Luke's Health System in order to achieve even higher quality care for the patients served by the independent not-for-profit health care organizations. The Collaborative's objective is to implement clinical programs and services to improve access and quality of care for patients, lower health care costs, and create additional operating efficiencies.

WTA Laser, LLC

WTA Laser, LLC is a joint venture between six individual community urologists and MHV. MHV owns a 28% interest in the joint venture, and the other six urologists each have a 12% interest. WTA Laser, LLC owns and leases equipment used in the treatment of diseases of the urinary tract and prostate and, in particular, purchases laser equipment used for photo-selective vaporization of the prostate.

Miller Street Properties

Miller Street Properties was a general partnership between MPS and three other health care professionals. The partnership was real estate situated in the city of Springfield with the principal place of business at 340 West Miller Street. The partnership had 18 units, of which MPS owned 6, for a 33.3% interest. MHS purchased the property and the partnership was dissolved on September 20, 2012.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

10. Long-Term Obligations

Long-term obligations are as follows:

	<u>2013</u>	<u>September 30 2012</u>	<u>2011</u>
<u>Obligated Group:</u>			
Revenue Bonds (Series 2009) issued December 22, 2009, secured by pledged revenues of the MHS Obligated Group at an annual fixed effective interest rate of 5.38%, 5.38%, and 5.37% as of September 30, 2013, 2012, and 2011, respectively.	\$ 86,952	\$ 87,366	\$ 87,881
Direct Note Obligation 2012C in the amount of \$60,000 was drawn upon on September 13, 2013, with a stated annual fixed interest rate of 4.26% as of September 30, 2013.	60,000	-	-
Variable Rate Demand Revenue Bonds (Series 2003) at average annual variable interest rates of 0.13%, 0.15%, and 0.19% as of September 30, 2013, 2012, and 2011, respectively, swapped at 70% of LIBOR through October 1, 2022, secured by a letter of credit that expires January 15, 2016.	24,740	26,345	27,865
Taxable Variable Rate Demand Revenue Bonds (Series 2004) at average annual variable interest rates of 0.16%, 0.19%, and 0.23% as of September 30, 2013, 2012, and 2011, respectively, swapped at 100% of LIBOR through October 1, 2024, secured by a letter of credit, which expires on January 15, 2016.	17,095	18,280	19,405
Variable Rate Demand Revenue Bonds (Series 1985C) at average annual variable interest rates of 0.15%, 0.16%, and 0.21% as of September 30, 2013, 2012, and 2011, respectively, swapped at 70% of LIBOR through January 1, 2016, secured by a letter of credit, which expires on January 15, 2016.	9,000	12,000	15,000
Obligated Group debt subtotal	<u>197,787</u>	<u>143,991</u>	<u>150,151</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

10. Long-Term Obligations (continued)

	2013	September 30 2012	2011
<u>Other Entities:</u>			
Indenture issued to Abraham Lincoln Memorial Hospital as part of the revenue bonds (Series 2009) that were issued on December 22, 2009, secured by pledged revenues of the MHS Obligated Group at an annual fixed effective rate of 5.38%, 5.38%, and 5.37% for September 30, 2013, 2012, and 2011, respectively.	\$ 42,380	\$ 42,581	\$ 42,832
Indenture issued to Taylorville Memorial Hospital as part of the revenue bonds (Series 2009) that were issued on December 22, 2009, secured by pledged revenues of the MHS Obligated Group at an annual fixed effective rate of 5.38%, 5.38%, and 5.37% for September 30, 2013, 2012, and 2011, respectively.	18,162	18,248	18,357
Variable Rate Loan program notes (Series 1999A) at an average variable interest rate of 0.20%, 0.23%, and 0.27% as of September 30, 2013, 2012 and 2011, respectively, due January 1, 2018, secured by a letter of credit, which expires on January 15, 2016, and by company assets (MP), and is guaranteed by the Obligated Group.	11,070	13,170	15,070
Total long-term obligations	269,399	217,990	226,410
Less current installments of long-term obligations	7,596	5,590	5,420
Long-term obligations – less current installments	<u>\$ 261,803</u>	<u>\$ 212,400</u>	<u>\$ 220,990</u>

Of MHS's debt, 96% is under a Master Trust Indenture (MTI) dated December 1, 2009. Currently, the Parent and MMC are the corporations that are Obligated Group members under the MTI. The MTI requires the Obligated Group to maintain debt covenants, including meeting a minimum debt service coverage ratio.

MHS maintains letters of credit with JP Morgan Chase Bank supporting the Series 1985, Series 2003, and Series 2004 bonds. As of September 30, 2013, the letters of credit are available up to \$71,000, and had related debt and interest outstanding against them of \$52,268. These letters of credit were available up to \$71,000 as of September 30, 2012, with related debt and interest of \$66,581 as well as credit available of \$75,000 at September 30, 2011, with \$64,290 of related debt and interest outstanding against them. These letters of credit expire on January 15, 2016. If

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

10. Long-Term Obligations (continued)

the bonds are not remarketed, the principal on the term loans would generally be payable 24 months after the failed remarketing.

MP maintains a letter of credit supporting the Series 1999A bonds. As of September 30, 2013, the letter of credit is available up to \$34,200, and as of September 30, 2012 and 2011, the letter of credit was available up to \$36,200 for each period. As of September 30, 2013, 2012, and 2011, the letter of credit had \$11,325, \$13,473, and \$15,417 of related debt and interest outstanding against it, respectively. The letter of credit expires on January 15, 2016. If the bonds are not remarketed, the principal is due at expiration of the letter of credit.

MMC and the Parent have entered into a guaranty agreement of the Series 1999A variable rate debt acquired by MP. This guaranty expires with the maturity of the bonds, and will not exceed the sum of \$13,473.

During fiscal year 2012, the Memorial Health System's Master Trust Indenture (MTI), dated December 1, 2009, was amended for the issuance of the Series 2012A and 2012B Direct Note Obligations.

On September 13, 2013 the Obligated Group exercised its authority within the 2012B Direct Note Obligation, dated September 18, 2012, a draw, referenced as 2012C Direct Note Obligation, in the amount of \$60,000, with a final maturity date of October 1, 2033 and a fixed interest rate of 4.26% (or monthly equivalent coupon yield of 4.22%) per annum. With the subject proceeds from the 2012C obligation, the Obligated Group paid the outstanding principal balance within the 2012A obligation in the amount of \$60,000.

In October 2013, the Obligated Group executed the 2013A Direct Note Obligation in the amount of \$90,000. Beginning January 1, 2015, the 2013A obligation will convert to a \$30,000 term loan with quarterly principal and interest payments, amortized over a 20-year period with a maturity date of January 1, 2020. The interest rate is a variable rate of daily LIBOR plus 0.83% with an applicable spread of 0.0% to 0.4% based upon the current rating as issued by Standard & Poor's and/or Moody's. The proceeds from the 2013A obligation will be used to finance a portion of improvements to its hospital located in Springfield, Illinois.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

10. Long-Term Obligations (continued)

Aggregate maturities of long-term obligations at September 30, 2013, are as follows:

<u>Period Ending</u> <u>September 30</u>	
2014	\$ 7,596
2015	8,039
2016	17,327
2017	8,283
2018	8,957
Thereafter	219,197
Total	<u>\$ 269,399</u>

Interest expense, excluding interest rate swap activity, is \$8,028, \$7,912, and \$6,993 for the years ended September 30, 2013, 2012, and 2011, respectively.

The valuation for the estimated fair value of long-term debt is completed by a third-party service and takes into account a number of factors including, but not limited to, any one or more of the following: (i) general interest rate and market conditions; (ii) macroeconomic and/or deal specific credit fundamentals; (iii) valuations of other financial instruments that may be comparable in terms of rating, structure, maturity, and/or covenant protection; (iv) investor opinions above the respective deal parties; (v) size of the transaction; (vi) cash flow projections, which in turn are based on assumptions about certain parameters that include, but are not limited to, default, recovery, prepayment, and reinvestment rates; (vii) administrator reports, asset manager estimates, broker quotations, and/or trustee reports; and (viii) comparable trades, where observable. Based on the inputs in determining the estimated fair value of debt this liability would be considered Level 2. The estimated fair value of long-term debt, based on quoted market prices for the same or similar issues was approximately \$275,169, \$233,235, and \$230,496, respectively, which includes consideration of third-party credit enhancements, of which there is no impact.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

11. Derivatives

MHS has interest rate related derivative instruments to manage its exposure on its variable-rate debt instruments and does not enter into derivative instruments for any purpose other than risk management purposes. Interest rate swap contracts between MHS and a third party (counterparty) provide for the periodic exchange of payments between the parties based on changes in a defined index and a fixed rate and expose MHS to market risk and credit risk. Credit risk is the risk that contractual obligations of the counterparties will not be fulfilled. Concentrations of credit risk relate to groups of counterparties that have similar economic or industry characteristics, which could cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. Counterparty credit risk is managed by requiring high credit standards for MHS's counterparties. The counterparties to these contracts are financial institutions that carry investment-grade credit ratings. MHS does not anticipate nonperformance by its counterparties. Market risk is the adverse effect on the value of a financial instrument that results from a change in interest rates. The market risk associated with interest rate changes is managed by established and monitoring parameters which limit the types and degree of market risk that may be undertaken. Management also mitigates risk through periodic reviews of MHS's derivative positions in the context of its blended cost of capital.

The following is a summary of the outstanding positions under these interest rate swap agreements at September 30, 2013:

<u>Expiration Date</u>	<u>MHS Pays</u>	<u>MHS Receives</u>	<u>Notional Amount</u>
October 1, 2024	4.99%	LIBOR	\$17,095
October 1, 2022	3.69%	70% of LIBOR	\$24,740
January 1, 2016	3.49%	70% of LIBOR	\$15,000

The objective of these interest swaps is to mitigate interest rate fluctuations and synthetically fix the interest rate of the related bond series. MMC and MHS have entered into an interest rate swap agreement to convert the 1985C, 2003, and 2004 series variable rate debt to a fixed rate basis, thus reducing the impact of interest rate changes on future interest expense. The accumulated unrealized derivative loss of \$638, \$737, and \$836 is included in unrestricted net assets at September 30, 2013, 2012, and 2011, respectively, and is being amortized into excess of revenues over expenses over the remaining term of the bonds that are being hedged. The net amount reclassified was \$99 for each of the years ended September 30, 2013, 2012, and 2011, and was included as nonoperating losses in the accompanying consolidated statements of operations and changes in net assets.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

11. Derivatives (continued)

The fair values of derivative instruments at September 30, 2013, 2012, and 2011, are as follows:

Derivatives Not Designated as Hedging Instruments	Balance Sheet Location	2013	September 30 2012	2011
Interest rate swaps	Other long-term liabilities	\$ 6,739	\$ 9,676	\$ 9,165

The effects of derivative instruments on the consolidated statements of operations and changes in net assets for the years ended September 30, 2013, 2012, and 2011, are as follows:

Derivatives Not Designated as Hedging Instruments	Location of Loss on Derivatives Recognized in Excess of Revenues Over Expenses	Amount of Gain (Loss) on Derivatives Recognized in Excess of Revenues Over Expenses Year Ended September 30		
		2013	2012	2011
Interest rate swaps	Change in fair value of interest rate swap	\$ 2,937	\$ (511)	\$ (110)
	Interest expense and other financing costs	(2,200)	(2,290)	(2,405)

12. Liability Programs

MHS is involved in litigation arising in the ordinary course of business. Claims alleging professional or general liability have been asserted against MHS and are currently in various stages of litigation. MHS is self-insured for claims of up to \$1,000 individually and \$6,000 in the aggregate and has commercial claims-made excess insurance coverage for \$25,000 per claim and \$25,000 in the aggregate. Professional liability coverage is provided on a first dollar basis through insured programs for MPS and MHCCI.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

12. Liability Programs (continued)

Accruals related to the estimated self-insurance liability and the corresponding charge to expense are actuarially determined for asserted and unasserted claims using historical claims experience and other relevant industry and hospital-specific factors and trends, discounted at an interest rate of 4.0% at September 30, 2013, 2012, and 2011. The general and professional liability was \$15,770, \$15,817, and \$15,277 at September 30, 2013, 2012, and 2011, respectively, including tail coverage on the claims-made policy. Excess insurance receivables are \$3,858, \$3,910, and \$4,046 at September 30, 2013, 2012, and 2011, respectively. Amounts charged to supplies and other expense in the consolidated statements of operations and changes in net assets are as follows:

	Years Ended September 30		
	2013	2012	2011
Self-insurance	\$ 438	\$ 1,590	\$ 1,559
Insured	2,273	2,577	2,589
Total	<u>\$ 2,711</u>	<u>\$ 4,167</u>	<u>\$ 4,148</u>

MHS maintains a revocable general and professional liability trust fund of \$14,293, \$13,649, and \$12,527 at September 30, 2013, 2012, and 2011, respectively.

MHS also provides for workers' compensation through a self-insurance trust or through insured programs. The funding level for this trust and estimation of the related liability are actuarially determined. Amounts charged to expense for this coverage for the years ended September 30, 2013, 2012, and 2011, were \$1,595, \$1,511, and \$2,735, respectively, and are included in employee benefits in the consolidated statements of operations and changes in net assets. The workers' compensation liability was \$5,080, \$5,628, and \$6,246 at September 30, 2013, 2012, and 2011, respectively. The excess insurance receivable is \$503, \$550, and \$631 at September 30, 2013, 2012, and 2011, respectively.

13. Pension Plans

Defined Benefit Plan

The MHS defined benefit pension plan (MHS Pension) covers substantially all of the employees of MHS, MMC, MPS, and MHSCI who began employment prior to January 1, 2012. The benefits are based on years of service and the employee's compensation during the highest five consecutive years of the last 10 years of employment. Contributions are made to the plans to meet the target funding level established by management and have exceeded the net pension cost each year.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

13. Pension Plans (continued)

On December 31, 2011, MHS Pension was frozen and no new participants were permitted after that date. Unvested participants on December 31, 2011, are still eligible to vest assuming service period requirements are met. A new defined contribution retirement savings plan (the Defined Contribution Plan) began on January 1, 2012. All eligible employees of MHS, MMC, MPS, and MHSvc are included in the defined contribution plan.

MHS also has a supplemental retirement benefit plan (MHS Restoration) covering MHS and MMC executives, which was frozen to new participants on December 31, 2009. Eligible participants in the MHS Restoration as of January 1, 2010, will continue to accrue benefits. The MPS Pension Restoration Plan covered physicians and was frozen for both new participation and benefits accruals as of December 31, 2011. Both restoration plans were designed to cover participants whose annual compensation exceeds the Internal Revenue Service cap limits for pension plan contributions and are unfunded.

The following table sets forth the benefit obligation and assets of MHS's defined benefit plans' funded status as recognized in MHS's consolidated balance sheets:

	2013	September 30 2012	2011
Change in benefit obligation:			
Benefit obligation – beginning of year	\$ 393,689	\$ 299,130	\$ 315,932
Service cost	233	3,819	11,202
Interest cost	17,478	16,366	18,107
Plan changes	–	–	633
Actuarial (gain) loss	(36,808)	83,382	20,715
Curtailments	–	–	(58,912)
Benefits paid	(10,230)	(9,008)	(8,547)
Benefit obligation – end of year	364,362	393,689	299,130
Change in plan assets:			
Fair value of plan assets – beginning of year	281,580	223,479	212,310
Actual gain (loss) on assets	44,652	39,579	(5,290)
Employer contribution	20,083	27,530	25,006
Benefits paid	(10,230)	(9,008)	(8,547)
Fair value of plan assets – end of year	336,085	281,580	223,479
Funded status	\$ (28,277)	\$ (112,109)	\$ (75,651)

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

13. Pension Plans (continued)

Amounts recognized in unrestricted net assets consist of the following:

	September 30		
	2013	2012	2011
Unrecognized actuarial losses	\$ 78,186	\$ 154,323	\$ 103,005
Unrecognized prior service cost	(20)	(32)	(155)
Accumulated adjustments to unrestricted net assets	<u>\$ 78,166</u>	<u>\$ 154,291</u>	<u>\$ 102,850</u>

Changes in plan assets and benefit obligations recognized in unrestricted net assets include the following:

	Years Ended September 30		
	2013	2012	2011
Current actuarial (gains) losses	\$ (59,715)	\$ 61,760	\$ 44,003
Prior service cost	—	—	633
Amortization of losses	(16,422)	(10,442)	(14,387)
Amortization of prior service cost	12	12	(9)
Recognition due to curtailment	—	111	(1,074)
Curtailment gains used to offset net loss	—	—	(58,912)
	<u>\$ (76,125)</u>	<u>\$ 51,441</u>	<u>\$ (29,746)</u>

The prior service cost and actuarial loss included in unrestricted net assets expected to be recognized in net periodic pension cost during the fiscal year ending September 30, 2014, are \$(13) and \$5,964, respectively.

Components of net periodic benefit cost are as follows:

	Years Ended September 30		
	2013	2012	2011
Service cost	\$ 233	\$ 3,819	\$ 11,202
Interest cost	17,478	16,366	18,107
Expected return on plan assets	(21,745)	(17,957)	(17,997)
Amortization of net loss and prior service cost	16,410	10,429	14,396
Curtailment and settlement charges	—	(77)	1,074
Net periodic benefit cost	<u>\$ 12,376</u>	<u>\$ 12,580</u>	<u>\$ 26,782</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

13. Pension Plans (continued)

No plan assets are expected to be returned to MHS during the year ending September 30, 2014.

The accumulated benefit obligation was \$361,857, \$391,358, and \$296,266 at September 30, 2013, 2012, and 2011, respectively.

Assumptions

Weighted average assumptions used to determine benefit obligations are as follows:

	September 30		
	2013	2012	2011
Discount rate	5.25%	4.50%	5.55%
Expected long-term return on plan assets	7.25%	7.50%	8.00%
Rate of compensation increase	N/A	N/A	4.00%

The effects of the changes in actuarial assumptions from 2012 to 2013 decreased the projected benefit obligation and the accumulated benefit obligation by \$(41,489) and \$(41,165), respectively, at September 30, 2013. The effects of the changes in actuarial assumptions from 2011 to 2012 increased the projected benefit obligation and the accumulated benefit obligation by \$82,334 and \$82,145, respectively, at September 30, 2012. The effects of the changes in actuarial assumptions from 2010 to 2011 decreased the projected benefit obligation and increased the accumulated benefit obligation by \$(40,858) and \$13,409, respectively, at September 30, 2011.

Weighted average assumptions used to determine net periodic benefit costs are as follows:

	Years Ended September 30		
	2013	2012	2011
Discount rate	4.50%	5.55%	5.80%
Expected long-term return on plan assets	7.50%	8.00%	8.00%
Rate of compensation increase	N/A	N/A	4.00%

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

13. Pension Plans (continued)

The weighted average asset allocation by asset category is as follows:

	Target Asset Allocation	2013	September 30 2012	2011
Equity securities	58.0%	61.3%	61.7%	55.5%
Debt securities	32.0	26.8	34.3	40.9
Balanced fund	10.0	9.5	—	—
Cash and cash equivalents	—	2.4	4.0	3.6
Total	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

The fair value of plan assets measured at fair value was determined using the following inputs at September 30, 2013:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 7,629	\$ —	\$ —	\$ 7,629
U.S. Treasury obligations	38,744	—	—	38,744
Government obligations	—	22,374	—	22,374
Corporate obligations	—	29,297	—	29,297
Corporate equities:				
Industrials	21,481	—	—	21,481
Consumer discretionary	19,318	—	—	19,318
Consumer staples	5,201	—	—	5,201
Energy	8,599	—	—	8,599
Financial	29,898	—	—	29,898
Materials	3,928	—	—	3,928
Information technology	19,330	—	—	19,330
Utilities	1,326	—	—	1,326
Health care	11,443	—	—	11,443
Telecommunications	448	—	—	448
Other	1,028	—	—	1,028
International equities	6,475	—	—	6,475
Mutual funds	77,646	31,920	—	109,566
Total assets	<u>\$ 252,494</u>	<u>\$ 83,591</u>	<u>\$ —</u>	<u>\$ 336,085</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

13. Pension Plans (continued)

The fair value of plan assets measured at fair value was determined using the following inputs at September 30, 2012:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 12,292	\$ —	\$ —	\$ 12,292
U.S. Treasury obligations	34,154	—	—	34,154
Government obligations	—	32,376	—	32,376
Corporate obligations	—	30,382	—	30,382
Corporate equities:				
Industrials	17,356	—	—	17,356
Consumer discretionary	17,308	—	—	17,308
Consumer staples	10,768	—	—	10,768
Energy	9,427	—	—	9,427
Financial	20,748	—	—	20,748
Materials	3,982	—	—	3,982
Information technology	16,987	—	—	16,987
Utilities	1,665	—	—	1,665
Health care	14,818	—	—	14,818
Telecommunications	1,737	—	—	1,737
International equities	6,060	—	—	6,060
Mutual funds	51,520	—	—	51,520
Total assets	<u>\$ 218,822</u>	<u>\$ 62,758</u>	<u>\$ —</u>	<u>\$ 281,580</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

13. Pension Plans (continued)

The fair value of plan assets measured at fair value was determined using the following inputs at September 30, 2011:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 8,120	\$ —	\$ —	\$ 8,120
U.S. Treasury obligations	22,358	—	—	22,358
Government obligations	—	32,658	—	32,658
Corporate obligations	—	36,797	—	36,797
Corporate equities:				
Industrials	12,257	—	—	12,257
Consumer discretionary	11,217	—	—	11,217
Consumer staples	8,098	—	—	8,098
Energy	6,843	—	—	6,843
Financial	12,791	—	—	12,791
Materials	2,365	—	—	2,365
Information technology	10,096	—	—	10,096
Utilities	1,674	—	—	1,674
Health care	11,689	—	—	11,689
Telecommunications	1,281	—	—	1,281
Other equities	1,016	—	—	1,016
International equities	3,691	—	—	3,691
Mutual funds	40,528	—	—	40,528
Total assets	\$ 154,024	\$ 69,455	\$ —	\$ 223,479

At September 30, 2013, 2012, and 2011, fair value methodologies for Level 1 and Level 2 assets are consistent with the inputs described in Note 11. There are no Level 3 assets.

Investment managers are employed to invest pension fund assets in a structured portfolio of equity and fixed income. All manager performance is reviewed by management to monitor that market performance has been calculated accurately, to monitor performance among peers and benchmarking, and to evaluate portfolio structure considering current and future needs based on economic forecasts and actuarial projections. MHS believes that a diversified portfolio will limit the degree of risk to the plans and stabilize the long-term results. The plans' diversified blend of marketable securities also takes into consideration the cash flow requirements of the plans to provide for the monthly payout of benefits required.

Projected rates of return for each asset category were selected after analyzing historical experience and future expectations of the returns and volatility for assets of the category.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

13. Pension Plans (continued)

Pension expense by affiliate is as follows:

	Years Ended September 30		
	2013	2012	2011
MMC	\$ 9,572	\$ 9,582	\$ 21,016
MHS	1,421	1,524	1,930
MPS	895	935	2,514
MHSvc	378	426	1,118
MHSCI	110	113	204
Net pension cost	<u>\$ 12,376</u>	<u>\$ 12,580</u>	<u>\$ 26,782</u>

During the year ending September 30, 2014, MHS plans to make contributions to the plans in the amount of \$10,000.

The following benefit payments, which reflect expected future service, are expected to be paid:

<u>Years Ending September 30</u>	
2014	\$ 11,680
2015	12,648
2016	14,013
2017	15,266
2018	17,081
2019–2023	106,678

Defined Contribution Plans

The Defined Contribution Plan is intended to qualify as a profit-sharing plan under Code Section 401(a), and includes a cash or deferred arrangement that is approved to qualify under Code Section 401(k). The plan allows employee contributions and an employer matching contribution of up to 3% of eligible pay, and provides a discretionary service-based employer contribution of between 3% and 7%. MHS is also providing a discretionary transition contribution to long-term employees who are closer to retirement. The amount of the discretionary transition contribution, which may be paid for a maximum of five years, will not exceed a percentage of eligible pay, based on age and service requirements as of January 1, 2012.

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

13. Pension Plans (continued)

MHS contributes the employer match throughout the year, as the employee contributes to the plan through payroll deduction. The total pension expense for the employer matching contribution was \$4,487, \$3,203, and \$0 for the years ended September 30, 2013, 2012, and 2011, respectively. The services based and transition contributions for the Defined Contribution Plan calendar plan year are discretionary and subject to approval by the MHS Board of Directors. As of December 10, 2013, no approval of contribution has been made for plan calendar year 2013. The pension expense for the service contribution and transition contribution related to plan calendar year 2012 was \$9,215 and \$1,220, respectively, for the year ended September 30, 2013. There was no pension expense for the service contribution and transition contribution for the years ended September 30, 2012 or 2011.

MHS also has a Defined Contribution Restoration Plan. This plan is intended to qualify as an eligible deferred compensation plan under code Section 457(b). This plan excludes anyone eligible to receive a benefit under the MHS Pension Restoration Plan. The pension expense for the employer matching contribution was \$341 for the year ended September 30, 2013.

ALMH, TMH and MHCCI have separate defined contribution plans with varying employer matches. The total expense related to these plans was \$1,524, \$1,718, and \$1,540 for the years ended September 30, 2013, 2012, and 2011, respectively. On December 31, 2013, ALMH and TMH defined contribution plans will be frozen and the Defined Contribution Plan will be amended to include ALMH and TMH as participating employers effective January 1, 2014.

14. Post-Employment and Other Benefits

MHS provides an unfunded post-employment benefit plan to certain employees. The cost for this plan was \$705, \$492, and \$303 for the years ended September 30, 2013, 2012, and 2011, respectively. As of September 30, 2013, 2012, and 2011, the accumulated post-employment benefit obligation was \$7,331, \$7,749, and \$5,916, respectively. Discount rates ranged from 4.50% to 5.25%. The MHS plan assumes a medical plan trend rate of 6.5% in 2013, decreasing by 0.5% annually to 5% thereafter. A one-percentage-point increase in the assumed medical plan trend rates would have increased the September 30, 2013, accumulated post-employment benefit obligation by \$1,428. A one-percentage-point decrease in the assumed medical plan trend rates would have decreased the September 30, 2013, accumulated post-employment benefit obligation by \$(1,140).

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

14. Post-Employment and Other Benefits (continued)

Included in unrestricted net assets are the following amounts that have not yet been recognized in net periodic post-employment benefit cost:

	2013	September 30 2012	2011
Unrecognized prior service cost	\$ (130)	\$ (477)	\$ (823)
Unrecognized actuarial losses	2,981	4,373	3,220
Total	<u>\$ 2,851</u>	<u>\$ 3,896</u>	<u>\$ 2,397</u>

Other post-employment and other benefit plans liabilities include continuation of medical benefits to employees on long-term disability, sick time at retirement, and the paid sick time program, which was \$6,140, \$5,485, and \$5,171 at September 30, 2013, 2012, and 2011, respectively.

15. Operating Leases

Revenues

Rental revenues were \$7,115, \$6,655, and \$6,536 for the years ended September 30, 2013, 2012, and 2011, respectively, from unaffiliated entities. MP owns medical office buildings and leases them to MPS under a master lease agreement. There are significant intercompany rental agreements. All intercompany rental activities are eliminated in the consolidated financial statements. As of September 30, 2013, 2012, and 2011, the cost of the buildings held for lease was \$87,143, \$67,587, and \$67,441, respectively, and the related accumulated depreciation was \$24,346, \$21,427, and \$21,729, respectively.

Future minimum rental revenue (excluding intercompany rent) under noncancelable operating leases as of September 30, 2013, which have initial or remaining terms in excess of one year, is as follows:

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

15. Operating Leases (continued)

**Years Ending
September 30**

2014	\$ 6,804
2015	7,628
2016	7,575
2017	7,618
2018	7,640
Thereafter	141,317
Total minimum lease revenue	<u>\$ 178,582</u>

Expense

Rental expense was \$3,760, \$3,684, and \$3,454 for the years ended September 30, 2013, 2012, and 2011, respectively.

Future minimum rental payments under noncancelable operating leases as of September 30, 2013, which have initial or remaining terms in excess of one year, are as follows:

**Years Ending
September 30**

2014	\$ 1,781
2015	1,670
2016	916
2017	624
2018	607
Thereafter	198
Total minimum lease payment	<u>\$ 5,796</u>

Memorial Health System and Subsidiaries

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

16. Commitments and Contingencies

Firm commitments for construction in progress totaled \$115,330 at September 30, 2013.

MMC is committed to pay Southern Illinois University School of Medicine \$14,328 at September 30, 2013, under an academic support agreement.

Regulatory Compliance

The U.S. Department of Justice and other federal and state agencies are increasing resources dedicated to regulatory investigations and compliance audits of health care providers. MHS is not exempt from these regulatory efforts and has received inquiries from federal and state agencies with regard to such initiatives. In consultation with legal counsel, management estimates these matters will be resolved without material adverse effect on MHS's consolidated balance sheets or consolidated statements of operations and changes in net assets. MHS has a formal corporate compliance function, which management believes will help monitor MHS' compliance with applicable laws and regulations.

Litigation

MHS is involved in litigation arising in the normal course of business. After consultation with legal counsel, it is management's opinion that these matters will be resolved without a material adverse effect on MHS's consolidated balance sheets or consolidated statements of operations and changes in net assets.

17. Subsequent Events

MHS evaluated events and transactions occurring subsequent to September 30, 2013 through December 10, 2013, the date the consolidated financial statements were issued.

The Obligated Group plans to go to the bond market in December 2013 for debt financing in an amount not to exceed \$140,000. The proceeds are intended to be utilized for the construction of the MMC Expansion Project, which includes a patient tower, main operating rooms, main entrance and lobby reconfiguration, and the Memorial Center for Learning and Innovation. There also will be updates to the facility infrastructure including the MMC energy plant.

Passavant Area Hospital (PAH) and MHS signed a non-binding letter of intent on October 6, 2013 to enter negotiations for PAH to become an affiliated corporation of MHS. It is anticipated that an affiliation agreement would be signed amongst the parties by December 31, 2013 and the transaction would close by April 1, 2014, subject to due diligence and regulatory approvals. The parties have contemplated MHS would be the sole corporate member through a membership substitution.

Supplementary Information

**MEMORIAL HEALTH SYSTEM
CONSOLIDATING BALANCE SHEET
SEPTEMBER 30, 2013**

(dollars in thousands)

Assets	MHS	MMC	ELIMIN- ATIONS	OBLIGATED GROUP	ALHF	TSH	MHV	MHSve	MHCCI	MP's	MP	MMCF	TSHF	ALHF	ELIMIN- ATIONS	TOTAL
Current assets:																
Cash and cash equivalents	\$ 15,358	75,556	-	90,914	17,784	8,659	1,970	7,819	4,617	5,309	2,992	1,205	329	466	-	\$ 142,064
Short-term investments	34,248	78,207	-	112,455	1,790	1,504	-	227	7,351	-	2,110	-	3,536	23	-	128,996
Assets whose use is limited - current portion	218	2,118	-	2,336	1,138	488	-	-	-	-	1,651	-	-	-	-	5,613
Patient accounts receivable	-	107,390	-	107,390	8,229	7,266	1,198	5,384	468	7,383	-	-	-	-	-	137,218
Allowance for uncollectible accounts	-	(12,382)	-	(12,382)	(1,632)	(1,514)	(459)	(965)	(258)	(1,899)	-	-	-	-	-	(23,725)
Net patient accounts receivable	-	95,008	-	95,008	6,597	5,752	739	4,419	210	5,484	-	-	-	-	-	113,493
Receivables from third-party payors	-	7,644	-	7,644	-	287	-	-	-	-	-	-	-	-	-	7,931
Due from affiliates	46	344	(258)	132	169	8	27	72	-	466	4	3	-	-	(881)	-
Other	1,546	15,884	-	17,430	1,223	927	294	499	2,687	16	4	155	8	79	(514)	22,808
Inventories	-	9,579	-	9,579	514	679	-	356	-	784	-	-	-	-	-	11,912
Prepaid expenses	5,740	6,126	-	11,866	173	349	57	100	201	268	86	81	-	-	-	13,181
Total current assets	57,156	285,466	(258)	342,364	29,388	18,653	3,087	13,492	15,066	13,031	6,847	1,444	3,873	568	(1,395)	446,398
Assets whose use is limited:																
Board-designated funds	-	165,796	-	165,796	15,743	2,826	-	-	447	-	-	10,101	-	18,750	-	213,643
Self-insurance trusts	-	20,383	-	20,383	-	-	-	-	-	-	-	-	-	-	-	20,383
Bond trustee assets	-	1,563	-	1,563	-	-	-	-	-	-	-	-	-	-	-	1,563
Donor restricted assets	-	934	-	934	-	-	-	-	-	-	-	9,000	131	-	-	10,065
Deferred compensation investments	8,748	2,668	-	11,416	-	-	-	-	-	8,607	-	-	-	-	-	20,023
Total assets whose use is limited	8,748	191,344	-	200,092	15,743	2,826	-	-	447	8,607	-	19,101	131	18,750	-	265,677
Property, plant, and equipment	218,429	401,488	-	619,917	62,770	50,814	322	10,276	11,877	3,942	34,412	147	-	342	-	794,819
Less accumulated depreciation	(69,564)	(233,907)	-	(303,471)	(16,903)	(24,625)	(265)	(7,622)	(7,574)	(3,001)	(15,230)	(147)	-	(342)	-	(379,178)
Net property, plant, and equipment	148,865	167,581	-	316,446	45,867	26,189	57	2,654	4,303	941	19,182	-	-	-	-	415,641
Other assets:																
Investments in partnerships	702	19,018	-	19,720	-	-	6,292	661	58	14,469	-	-	-	-	(35,918)	5,282
Unamortized bond insurance costs	599	1,580	-	2,179	737	318	-	-	-	-	-	-	-	-	-	3,234
Beneficial interest in remainder trust	-	35,391	-	35,391	-	-	-	-	-	-	-	-	-	-	-	35,391
Other	5,211	4,362	-	9,573	60	-	-	-	100	-	-	1,067	-	-	(100)	10,700
Total other assets	6,512	60,351	-	66,863	797	318	6,292	661	158	14,469	-	1,067	-	-	(36,018)	54,607
Total assets	\$ 221,281	704,742	(258)	925,765	91,797	47,966	9,436	16,807	19,974	37,048	26,029	21,612	4,004	19,298	(37,413)	\$ 1,182,323
Liabilities and net assets																
Current liabilities:																
Long-term debt - current portion	\$ 3,489	1,638	-	5,127	188	81	-	-	-	-	2,200	-	-	-	-	\$ 7,596
Accounts payable	8,965	35,884	-	44,849	693	632	94	1,555	397	2,716	70	31	-	83	25	51,145
Accrued payroll	2,642	20,320	-	22,962	1,130	1,822	-	1,265	539	1,310	1	-	-	-	-	29,020
Interest payable	433	2,302	-	2,735	1,138	488	-	-	-	-	1	-	-	-	-	4,362
Due to affiliates	846	79	(258)	667	15	38	37	-	7	60	-	12	-	54	(890)	-
Payables to third-party payors	-	25,716	-	25,716	4,494	769	-	-	-	-	-	-	-	-	-	30,979
Other	2,445	12,044	-	14,489	534	422	-	-	552	1,860	418	469	6	-	(630)	18,120
Total current liabilities	18,820	97,983	(258)	116,545	8,192	4,252	131	2,820	1,495	5,946	2,690	512	6	137	(1,495)	141,231
Long-term debt obligations - less current portion	87,670	104,990	-	192,660	42,192	18,081	-	-	-	-	8,870	-	-	-	-	261,803
Other liabilities:																
Deferred compensation and benefits	9,421	2,668	-	12,089	-	-	-	-	-	8,912	-	-	-	-	-	21,001
Self-insurance accrued expenses	320	16,501	-	16,821	-	-	-	246	-	-	-	-	-	-	-	17,067
Accrued employee benefits	2,770	5,721	-	8,491	-	-	-	204	-	4,775	-	-	-	-	-	13,470
Pension obligation	5,269	22,343	-	27,612	-	-	-	-	-	946	-	-	-	-	-	28,558
Other	3,326	6,012	-	9,338	-	446	-	-	-	-	-	80	-	-	-	9,864
Total other liabilities	21,106	53,245	-	74,351	-	446	-	450	-	14,633	-	80	-	-	-	89,960
Net assets:																
Unrestricted	93,685	393,281	-	486,966	41,413	25,187	9,305	13,229	17,077	16,469	14,469	6,711	2,608	-	(17,000)	616,434
Unrestricted - board-designated	-	-	-	-	-	-	-	-	447	-	-	5,309	1,259	19,048	-	26,063
Temporarily restricted	-	55,243	-	55,243	-	-	-	225	955	-	-	3,972	81	113	(18,918)	41,671
Permanently restricted	-	-	-	-	-	-	-	83	-	-	-	5,028	50	-	-	5,161
Total net assets	93,685	448,524	-	542,209	41,413	25,187	9,305	13,537	18,479	16,469	14,469	21,020	3,998	19,161	(35,918)	689,329
TOTAL LIABILITIES AND NET ASSETS	\$ 221,281	704,742	(258)	925,765	91,797	47,966	9,436	16,807	19,974	37,048	26,029	21,612	4,004	19,298	(37,413)	\$ 1,182,323

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS
YEAR ENDED SEPTEMBER 30, 2013
(dollars in thousands)

	MHS	MMC	ELIMIN- ATIONS	OBLIGATED GROUP	ALMH	TMH	MHV	MHSvc	MHCCT	MPS	MP	MMCF	TMHF	ALHF	ELIMIN- ATIONS	TOTAL
Patient Service Revenues:																
Liquist revenues	\$ -	945,702	(36,125)	909,577	18,876	16,021	-	-	-	-	-	-	-	-	-	\$ 944,474
Outpatient revenues	-	761,372	-	761,372	71,683	70,438	15,170	32,142	14,643	78,622	-	-	-	-	(415)	1,043,655
Total patient service revenues	-	1,707,074	(36,125)	1,670,949	90,559	86,459	15,170	32,142	14,643	78,622	-	-	-	-	(415)	1,988,129
Less charity	-	58,296	-	58,296	4,524	4,339	29	406	65	214	-	-	-	-	-	67,873
Less contractual allowances	-	1,145,740	(36,125)	1,109,615	46,191	48,040	8,251	8,788	1,458	38,717	-	-	-	-	-	1,261,060
Patient service revenues	-	503,038	-	503,038	39,844	34,080	6,890	22,948	13,120	39,691	-	-	-	-	(415)	659,196
Provision for uncollectible accounts	-	8,680	-	8,680	1,622	435	744	697	18	1,171	-	-	-	-	-	13,367
	-	494,358	-	494,358	38,222	33,645	6,146	22,251	13,102	38,520	-	-	-	-	(415)	645,829
Hospital access improvement payments	-	27,394	-	27,394	2,951	2,396	-	-	-	-	-	-	-	-	-	32,741
Capitation revenues	-	53,091	-	53,091	-	-	-	-	-	-	-	-	-	-	-	53,091
Other revenues:																
Management fees	37,040	-	(28,157)	8,883	15	-	-	-	-	-	-	-	-	-	(8,898)	-
Other	12,114	17,448	(2,826)	26,736	1,203	615	1,201	512	388	1,272	5,909	-	-	-	(9,498)	28,338
Total other revenues	49,154	17,448	(30,983)	35,619	1,218	615	1,201	512	388	1,272	5,909	-	-	-	(18,396)	28,338
Total revenues	49,154	592,291	(30,983)	610,462	42,391	36,656	7,347	22,763	13,490	39,792	5,909	-	-	-	(18,811)	759,999
Expenses:																
Salaries and wages	22,870	175,196	-	198,066	13,266	13,585	5,201	11,398	8,016	12,794	413	-	-	-	-	262,739
Employee benefits	7,043	60,874	-	67,917	4,014	4,320	433	4,231	1,938	4,385	143	-	-	-	-	87,381
Physician fees	887	30,157	-	31,044	2,121	2,013	59	105	208	20,399	-	-	-	-	-	55,949
Utilities	1,231	7,435	-	8,666	582	738	17	162	332	206	746	-	-	-	-	11,449
Pharmaceutical supplies	-	18,863	-	18,863	1,125	958	95	349	44	2,323	-	-	-	-	-	23,757
Food	10	4,441	-	4,451	328	369	4	7	95	8	-	-	-	-	-	5,262
Patient service supplies	-	77,195	-	77,195	1,995	1,627	86	416	-	1,113	-	-	-	-	-	82,432
System management fee	-	28,157	(28,157)	-	1,989	1,835	627	944	300	3,074	100	-	-	-	(8,869)	-
Supplies and other	7,637	62,025	(2,826)	66,836	4,075	4,521	1,146	3,778	1,745	8,115	1,258	-	-	-	(9,942)	81,532
Hospital provider assessment	-	17,214	-	17,214	991	809	-	-	-	-	-	-	-	-	-	19,014
Purchased medical services	-	31,785	-	31,785	-	-	-	-	-	-	-	-	-	-	-	31,785
Depreciation and amortization	7,564	29,125	-	36,689	4,497	2,997	15	1,002	379	173	1,177	-	-	-	-	46,929
Amortization of bond issuance expenses	45	277	-	322	134	58	-	-	-	-	-	-	-	-	-	514
Interest expense and other financing costs	1,867	5,431	-	7,298	2,281	977	-	-	-	-	109	-	-	-	-	10,665
Total expenses	49,154	548,175	(30,983)	566,346	37,398	34,807	7,683	22,392	13,057	52,590	3,946	-	-	-	(18,811)	719,408
Income (loss) from operations	-	44,116	-	44,116	4,993	1,849	(336)	371	433	(12,798)	1,963	-	-	-	-	40,591
% of total operating revenue	-	-	-	-	-	-	-	-	-	-	-	NA	NA	NA	-	-
Nonoperating gains (losses):																
Interest and dividends	639	3,227	-	3,866	451	99	12	46	158	283	9	182	53	521	-	5,680
Realized gain (loss) on investments, net	453	4,891	-	5,344	300	25	-	-	8	-	-	1,204	63	2,824	-	9,768
Unrealized gain (loss) on investments, net	2,988	19,292	-	22,270	716	211	-	-	(83)	561	-	(698)	76	(1,694)	-	21,367
Change in fair value of interest rate swap	1,513	1,424	-	2,937	-	-	-	-	-	-	-	-	-	-	-	2,937
Contributions	-	158	-	158	-	617	-	-	-	-	-	921	161	126	-	1,983
Equity in income of affiliate	-	-	-	-	-	-	-	-	-	1,972	-	-	-	-	(1,972)	-
Provision for income taxes	-	-	-	-	-	-	-	(621)	-	-	-	-	-	-	-	(621)
Other revenue (expense), net	(1,447)	538	-	(909)	(1)	-	-	-	1	(845)	-	(911)	(44)	(345)	-	(3,053)
Total nonoperating gains (losses), net	4,146	29,520	-	33,666	1,466	953	12	(565)	82	1,971	9	698	309	1,432	(1,972)	38,061
Excess (deficiency) of revenues over expense	\$ 4,146	73,636	-	77,782	6,459	2,802	(324)	(194)	515	(10,827)	1,972	698	309	1,432	(1,972)	\$ 78,652

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS (CONTINUED)
YEAR ENDED SEPTEMBER 30, 2013
(dollars in thousands)

	MHS	MMC	ELIMIN- ATIONS	OBLIGATED GROUP	ALABH	TMBH	MHV	MHSve	MHCCI	MPS	MP	MMCF	TMBF	ALHF	ELIMIN- ATIONS	TOTAL
Unrestricted net assets:																
Excess (deficiency) of revenues over expenses	\$ 4,146	73,636	-	77,782	6,459	2,802	(324)	(194)	515	(10,827)	1,972	698	309	1,432	(1,972)	\$ 78,652
Change in minimum pension obligation	244	75,999	-	76,243	-	-	-	-	-	845	-	-	-	-	-	77,088
Change in fair value of interest rate swap	9	90	-	99	-	-	-	-	-	-	-	-	-	-	-	90
Net assets released from restrictions for property acquisitions	-	3	-	3	-	-	-	-	-	-	-	-	-	-	-	3
Other	(1)	-	-	(1)	-	-	-	-	(1)	-	-	298	54	-	-	350
Transfers (to) related organizations	(13,346)	(4,888)	4,878	(13,356)	-	-	-	-	-	-	-	-	-	-	-	-
Transfers from related organizations	4,878	-	(4,878)	-	-	-	-	-	-	13,346	-	10	-	-	(13,356)	-
Increase (decrease) in unrestricted assets	(4,070)	144,840	-	140,770	6,459	2,802	(324)	(194)	514	3,364	1,972	1,006	363	1,432	(1,972)	156,192
Temporarily restricted net assets:																
Contributions	-	490	-	490	8	-	-	53	-	-	-	418	56	97	-	1,122
Net realized gains on investments	-	9,925	-	9,925	-	-	-	-	-	-	-	718	-	-	-	10,643
Net assets released from restrictions (non-operating)	-	(995)	-	(995)	(5)	-	-	-	-	-	-	-	-	-	-	(1,000)
Net assets released from restrictions (operating)	-	(433)	-	(433)	(8)	-	-	(62)	(21)	-	-	(474)	(14)	(47)	-	(1,059)
Net assets released from restrictions for property acquisitions	-	(3)	-	(3)	-	-	-	-	-	-	-	-	-	-	-	(3)
Change in value of split-interest agreements	-	-	-	-	-	-	-	-	-	-	-	16	-	-	-	16
Gain (loss) on interest in net assets of foundation	-	1,199	-	1,199	-	-	-	-	-	-	-	-	-	-	-	-
Other	-	1	-	1	-	(192)	-	-	1	-	-	(508)	(100)	-	-	(802)
Increase (decrease) in temporarily restricted assets	-	10,184	-	10,184	(5)	(192)	-	(9)	(20)	-	-	170	(62)	50	(1,199)	8,917
Permanently restricted net assets - contributions	-	-	-	-	-	-	-	-	-	-	-	156	50	-	-	206
Increase (decrease) in net assets	(4,070)	155,024	-	150,954	6,454	2,610	(324)	(203)	494	3,364	1,972	1,332	351	1,482	(3,171)	165,315
Net assets, beginning of period	97,755	293,500	-	391,255	34,999	22,577	9,629	13,740	17,985	13,105	12,497	19,688	3,647	17,679	(32,747)	524,014
Net assets, end of period	\$ 93,685	448,524	-	542,209	41,413	25,187	9,305	13,537	18,479	16,469	14,469	21,020	3,998	19,161	(35,918)	\$ 689,329

MEMORIAL HEALTH SYSTEM
CONSOLIDATING STATEMENT OF CASH FLOWS
YEAR ENDED SEPTEMBER 30, 2013
(dollars in thousands)

	MHS	MMC	OBLIGATED GROUP	ALMH	TMH	MHV	MHSve	MHCCI	MPS	MP	MMCF	TMHF	ALHF	Elimination/ Rounding	TOTAL
Cash flows from operating activities:															
Changes in net assets	\$ (4,070)	155,024	150,954	6,454	2,610	(324)	(203)	494	3,364	1,972	1,332	351	1,482	(3,171)	\$ 165,315
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:															
Non cash contribution	—	—	—	—	—	—	—	—	—	—	(112)	—	—	—	(112)
Change in unrealized (gain) losses on interest rate swap	(1,513)	(1,424)	(2,937)	—	—	—	—	—	—	—	—	—	—	—	(2,937)
Restricted contributions and gains	—	(490)	(490)	(8)	—	—	(53)	—	—	—	(436)	(106)	(97)	—	(1,190)
Increase in beneficial interest in perpetual trust	—	(9,925)	(9,925)	—	—	—	—	—	—	—	—	—	—	—	(9,925)
Depreciation and amortization	7,564	29,125	36,689	4,497	2,997	15	1,002	379	173	1,177	2	—	—	—	46,931
Amortization of bond issuance costs	45	277	322	134	58	—	—	—	—	—	—	—	—	—	514
(Gain) loss on disposal of assets	(19)	270	251	—	—	—	—	—	—	1	—	—	—	—	252
Provision for uncollectible accounts	—	8,680	8,680	1,622	435	744	697	18	1,171	—	—	—	—	—	13,367
Change in pension obligation	(244)	(75,999)	(76,243)	—	—	—	—	—	(845)	—	—	—	—	—	(77,088)
Changes in assets and liabilities:															
Accounts receivable	—	8,958	8,958	(1,173)	5	(748)	(717)	(90)	(2,805)	—	—	—	—	—	3,430
Inventory and other assets	(666)	(12,684)	(13,350)	(899)	(876)	(218)	590	1,603	368	(16)	21	88	457	(19)	(12,251)
Change in unrealized (gain) loss on investments, net	(2,988)	(19,282)	(22,270)	(716)	(211)	—	(10)	85	(561)	—	1,726	(76)	1,694	—	(20,339)
(Deposits) withdrawals in investments, net	(1,476)	(6,169)	(7,645)	(3,970)	—	—	—	(1,969)	—	—	(53)	(43)	(234)	—	(13,916)
Other investment activity, net	1,459	(9,620)	(8,161)	(555)	(93)	—	(2)	—	63	(77)	(3,482)	(261)	(3,771)	—	(15,942)
Estimated third-party payor settlements	—	4,249	4,249	1,271	664	—	—	—	—	—	—	—	—	—	6,184
Accounts payable and other current liabilities	4,646	11,022	15,668	518	345	4	(610)	136	(982)	(100)	(58)	4	40	56	15,021
Self-insurance and other long-term liabilities	447	(10,045)	(9,598)	—	—	—	58	—	1,147	—	(6)	—	—	—	(8,399)
Amount due to (from) affiliates	221	172	393	(251)	1	41	(33)	12	(219)	(10)	6	—	76	(16)	—
Equity in (income) loss of unconsolidated affiliates and foundation	—	(1,199)	(1,199)	—	—	—	—	—	—	—	—	—	—	1,199	—
Transfers to (from) related organizations	8,468	4,888	13,356	—	—	—	—	(13,346)	—	—	(10)	—	—	—	—
Net cash provided by (used in) operating activities	11,874	75,828	87,702	6,924	5,933	(486)	719	668	(12,472)	2,947	(1,071)	(45)	47	(1,951)	88,915
Cash flows from investing activities:															
Acquisition of property and equipment	(47,078)	(46,571)	(93,649)	(818)	(1,773)	(45)	(995)	(260)	(397)	(263)	—	—	—	—	(98,200)
Proceeds on sale of property	200	108	308	—	—	—	—	—	—	221	—	—	—	—	529
Change in investment in partnerships	(702)	—	(702)	—	—	54	72	(27)	(1,972)	—	—	—	—	1,972	(603)
Net change in other assets	346	—	346	—	—	—	—	—	—	—	16	—	—	(21)	341
Net cash provided by (used in) investing activities	(47,234)	(46,463)	(93,697)	(818)	(1,773)	9	(923)	(287)	(2,369)	(42)	16	—	—	1,951	(97,933)
Cash flows from financing activities:															
Restricted contributions and gains	—	490	490	8	—	—	53	—	—	—	436	106	97	—	1,190
Repayment of long-term debt	(1,610)	(4,594)	(6,204)	(201)	(86)	—	—	—	—	(2,100)	—	—	—	—	(8,591)
Issuance of long-term debt	60,000	—	60,000	—	—	—	—	—	—	—	—	—	—	—	60,000
Proceeds from short-term borrowings	60,000	—	60,000	—	—	—	—	—	—	—	—	—	—	—	60,000
Repayment of short-term borrowings	(60,000)	—	(60,000)	—	—	—	—	—	—	—	—	—	—	—	(60,000)
Distributions from beneficial interest in remainder trust	—	995	995	—	—	—	—	—	—	—	—	—	—	—	995
Transfers (to) from related organizations	(8,468)	(4,888)	(13,356)	—	—	—	—	13,346	—	—	10	—	—	—	—
Net cash flows provided by (used in) financing activities	49,922	(7,997)	41,925	(193)	(86)	—	53	—	13,346	(2,100)	446	106	97	—	53,594
Net increase (decrease) in cash and cash equivalents	14,562	21,368	35,930	5,913	4,074	(477)	(151)	381	(1,493)	805	(609)	61	144	—	44,576
Cash and cash equivalents, beginning of period	796	54,188	54,984	11,871	4,385	2,447	7,970	4,236	6,804	2,187	1,814	268	322	—	97,488
Cash and cash equivalents, end of period	\$ 15,358	\$ 75,556	\$ 90,914	\$ 17,784	\$ 8,659	\$ 1,970	\$ 7,819	\$ 4,617	\$ 5,309	\$ 2,992	\$ 1,205	\$ 329	\$ 466	\$ —	\$ 142,064

MEMORIAL HEALTH SYSTEM AND SUBSIDIARIES
CONSOLIDATING BALANCE SHEET
SEPTEMBER 30, 2012
(dollars in thousands)

Assets	MHS	MMC	ELIMIN- ATIONS	OBLIGATED GROUP	ALMH	TMH	MHV	MHSve	MHCCI	MPS	MP	MMCF	TMHF	ALHF	ELIMIN- ATIONS	TOTAL
Current assets:																
Cash and cash equivalents	\$ 796	54,188	—	54,084	11,871	4,585	2,447	7,970	4,236	6,804	2,187	1,814	268	322	—	\$ 97,488
Short-term investments	29,648	65,999	—	95,647	2,810	1,494	—	215	5,501	—	2,109	—	3,142	33	—	116,951
Assets whose use is limited – current portion	219	2,133	—	2,352	1,142	489	—	—	—	—	1,576	—	—	—	—	5,559
Patients accounts receivable	—	126,539	—	126,539	8,447	7,332	1,063	5,265	299	5,436	—	—	—	—	—	154,381
Allowance for uncollectible accounts	—	(18,893)	—	(18,893)	(1,401)	(1,160)	(328)	(867)	(161)	(882)	—	—	—	—	—	(23,692)
Net patient accounts receivable	—	107,646	—	107,646	7,046	6,172	735	4,398	138	4,554	—	—	—	—	—	130,689
Receivables from third-party payors	—	16,347	—	16,347	—	488	—	—	—	—	—	—	—	—	—	16,835
Due from affiliates	95	601	(576)	120	—	11	41	39	7	187	—	—	—	—	(405)	—
Other	1,582	6,266	—	7,848	348	113	112	988	4,307	302	20	161	96	536	(533)	14,298
Investments	—	8,386	—	8,386	462	668	—	417	—	781	—	—	—	—	—	10,714
Prepaid expenses	5,038	4,263	—	9,301	181	298	21	100	162	353	54	96	—	—	—	10,566
Total current assets	37,378	265,829	(576)	302,631	23,860	14,318	3,356	14,167	14,351	12,981	5,946	2,071	3,506	891	(938)	397,140
Assets whose use is limited:																
Board-designated funds	—	143,310	—	143,310	9,478	2,529	—	—	413	—	—	8,617	—	16,809	—	181,156
Self-insurance trusts	—	20,351	—	20,351	—	—	—	—	—	—	—	—	—	—	—	20,351
Bond trustee assets	—	1,555	—	1,555	—	—	—	—	—	—	—	—	—	—	—	1,555
Other restricted assets	1,200	—	—	1,200	—	—	—	—	—	—	—	—	—	—	—	1,200
Donor-restricted assets	—	880	—	880	—	—	—	—	—	—	—	8,674	143	—	—	9,697
Deferred compensation investments	9,290	2,370	—	11,660	—	—	—	—	—	8,109	—	—	—	—	—	19,769
Total assets whose use is limited	10,490	168,466	—	178,956	9,478	2,529	—	—	413	8,109	—	17,291	143	16,809	—	233,728
Property, plant, and equipment	173,368	363,908	—	537,276	61,988	49,046	277	9,717	11,646	3,926	35,095	147	—	342	—	709,460
Less accumulated depreciation	(67,836)	(213,395)	—	(277,231)	(12,440)	(21,633)	(250)	(7,056)	(7,224)	(3,209)	(14,777)	(145)	—	(342)	—	(244,307)
Net property, plant, and equipment	109,532	150,513	—	260,045	49,548	27,413	27	2,661	4,422	717	20,318	2	—	—	—	365,153
Other assets:																
Investments in partnerships	—	17,819	—	17,819	—	—	6,346	733	31	12,497	—	—	—	—	(32,747)	4,679
Unamortized bond issuance costs	644	1,858	—	2,502	871	376	—	—	—	—	—	—	—	—	—	3,749
Beneficial interest in remainder trust	—	26,460	—	26,460	—	—	—	—	—	—	—	—	—	—	—	26,460
Other	5,408	4,351	—	9,759	80	—	—	—	122	—	—	971	—	—	(122)	10,810
Total other assets	6,052	50,488	—	56,540	951	376	6,346	733	153	12,497	—	971	—	—	(32,869)	45,698
Total assets	163,452	635,296	(576)	798,172	83,837	44,636	9,729	17,561	19,339	34,304	26,264	20,335	3,649	17,700	(33,807)	1,041,719
Liabilities and net assets																
Current liabilities:																
Long-term debt – current portion	1,609	1,594	—	3,203	201	86	—	—	—	—	2,100	—	—	—	—	5,590
Accounts payable	4,776	21,482	—	36,258	767	783	90	2,286	361	2,680	89	102	—	43	10	43,469
Accrued payroll	2,555	19,906	—	22,461	1,068	1,746	—	1,141	501	1,438	—	—	—	—	—	28,355
Interest payable	314	2,318	—	2,632	1,142	490	—	—	—	—	2	—	—	—	—	4,266
Due to affiliates	674	164	(576)	262	97	40	10	1	2	—	6	3	—	(22)	(399)	—
Payables to third-party payors	—	30,170	—	30,170	3,223	306	—	—	—	—	—	—	—	—	—	33,699
Other	2,193	5,821	—	8,014	—	—	—	—	490	2,750	500	456	2	—	(671)	11,541
Total current liabilities	12,121	91,455	(576)	103,000	6,498	3,451	100	3,428	1,354	6,868	2,697	561	2	21	(1,060)	126,920
Long-term debt – less current portion	31,160	109,628	—	140,788	42,380	18,162	—	—	—	—	11,070	—	—	—	—	212,400
Other liabilities:																
Deferred compensation and benefits	9,869	2,370	—	12,239	—	—	—	—	—	8,415	—	—	—	—	—	20,654
Self-insurance accrued expenses	325	18,849	—	19,174	—	—	—	224	—	—	—	—	—	—	—	19,398
Accrued employee benefits	2,828	5,166	—	7,994	—	—	—	—	169	5,071	—	—	—	—	—	13,234
Pension obligation	4,555	106,708	—	111,263	—	—	—	—	—	845	—	—	—	—	—	112,108
Other	4,859	7,620	—	12,459	—	446	—	—	—	—	86	—	—	—	—	12,991
Total other liabilities	22,416	140,713	—	163,129	—	446	—	393	—	14,331	—	86	—	—	—	178,385
Net assets:																
Unrestricted	97,755	248,441	—	346,196	34,954	22,385	9,629	13,423	17,010	13,105	12,497	11,014	3,504	17,616	(15,028)	486,305
Temporarily restricted	—	45,059	—	45,059	5	192	—	234	975	—	—	3,802	143	63	(17,719)	32,754
Permanently restricted	—	—	—	—	—	—	—	83	—	—	—	4,872	—	—	—	4,955
Total net assets	97,755	293,500	—	391,255	34,959	22,577	9,629	13,740	17,985	13,105	12,497	19,688	3,647	17,679	(32,747)	524,014
Total liabilities and net assets	\$ 163,452	635,296	(576)	798,172	83,837	44,636	9,729	17,561	19,339	34,304	26,264	20,335	3,649	17,700	(33,807)	\$ 1,041,719

MEMORIAL HEALTH SYSTEM AND SUBSIDIARIES
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS
YEAR ENDED SEPTEMBER 30, 2012
(dollars in thousands)

	MHS	MMC	ELIMIN- ATIONS	OBLIGATED GROUP	ALMH	TMH	MHV	MHSve	MHCCI	MPS	MP	MMCF	TMHF	ALHF	ELIMIN- ATIONS	TOTAL
Patient service revenues:																
Inpatient revenues	\$ -	946,303	(30,894)	915,409	16,126	15,237	-	-	-	-	-	-	-	-	-	\$ 946,772
Outpatient revenues	-	718,302	-	718,302	65,129	61,989	14,323	30,936	14,015	74,865	-	-	-	-	(259)	979,500
Total patient revenues	-	1,664,605	(30,894)	1,633,711	81,255	77,226	14,323	30,936	14,015	74,865	-	-	-	-	(259)	1,926,072
Less charity	-	56,523	-	56,523	4,525	2,487	40	333	39	149	-	-	-	-	-	64,096
Less contractual allowances	-	1,085,765	(30,894)	1,054,871	40,782	40,435	8,190	7,789	1,297	37,355	-	-	-	-	-	1,190,719
Net patient service revenues	-	522,317	-	522,317	35,948	34,304	6,093	22,814	12,679	37,361	-	-	-	-	(259)	671,257
Provision for uncollectible accounts	-	12,673	-	12,673	782	2,236	743	674	9	954	-	-	-	-	-	18,071
	-	509,644	-	509,644	35,166	32,068	5,350	22,140	12,670	36,407	-	-	-	-	(259)	653,186
Hospital access improvement revenue	-	19,794	-	19,794	1,855	1,592	-	-	-	-	-	-	-	-	-	23,241
Capitation revenues	-	49,341	-	49,341	-	-	-	-	-	-	-	-	-	-	-	49,341
Other revenues:																
Management fees	34,618	-	(26,351)	8,267	14	-	-	-	-	-	-	-	-	-	(8,381)	-
Other	11,007	18,285	(2,695)	26,597	1,306	902	1,012	483	481	1,102	5,884	-	-	-	(8,721)	29,046
Total other revenues	45,625	18,285	(29,046)	34,864	1,320	902	1,012	483	481	1,102	5,884	-	-	-	(17,002)	29,046
Total revenues	45,625	597,064	(29,046)	613,643	38,341	34,562	6,362	22,623	13,151	37,509	5,884	-	-	-	(17,261)	754,814
Expenses:																
Salaries and wages	21,468	173,492	-	194,960	13,193	12,847	4,922	10,724	7,719	11,679	377	-	-	-	-	256,421
Employee benefits	5,658	49,983	-	55,641	4,009	4,480	432	3,549	1,969	3,735	131	-	-	-	-	73,946
Physician fees	748	24,373	-	25,321	1,848	2,020	36	108	215	20,742	-	-	-	-	-	50,290
Utilities	825	7,963	-	8,788	671	857	18	164	318	242	710	-	-	-	-	11,768
Pharmaceutical supplies	-	18,616	-	18,616	993	966	97	336	40	1,893	-	-	-	-	-	22,941
Patient service supplies	-	84,601	-	84,601	1,877	1,453	75	213	-	1,090	-	-	-	-	-	89,309
System management fee	-	26,351	(26,351)	-	1,781	1,652	557	864	266	3,050	100	-	-	-	(8,270)	-
Supplies and other	7,486	74,085	(2,695)	78,876	4,311	4,359	1,173	3,691	1,723	7,670	1,364	-	-	-	(8,991)	94,176
Hospital provider assessment	-	11,329	-	11,329	453	410	-	-	-	-	-	-	-	-	-	12,192
Purchased medical services	-	31,655	-	31,655	-	-	-	-	-	-	-	-	-	-	-	31,655
Depreciation and amortization	7,844	29,548	-	37,392	4,425	2,921	16	1,042	396	160	1,387	-	-	-	-	47,739
Amortization of bond issuance expenses	44	277	-	321	134	58	-	-	-	-	-	-	-	-	-	513
Interest expense and other financing costs	1,552	5,728	-	7,280	2,290	981	-	-	-	-	125	-	-	-	-	10,676
Total expenses	45,625	538,201	(29,046)	554,780	35,985	33,004	7,326	20,691	12,646	50,261	4,194	-	-	-	(17,261)	701,626
Income (loss) from operations	-	58,863	-	58,863	2,356	1,558	(964)	1,932	505	(12,752)	1,690	-	-	-	-	53,188
Nonoperating gains (losses):																
Interest and dividends	729	3,506	-	4,235	226	74	28	64	150	217	9	153	4	434	-	5,594
Realized gain (loss) on investments, net	1,265	8,623	-	9,888	18	(198)	-	-	11	-	-	(17)	38	7	-	9,747
Unrealized gain (loss) on investments, net	2,687	19,183	-	21,870	407	367	-	20	10	1,051	-	1,295	165	1,689	-	26,874
Change in fair value of interest rate swap	(383)	(128)	-	(511)	-	-	-	-	-	-	-	-	-	-	-	(511)
Contributions	-	100	-	100	433	-	-	-	-	-	-	1,354	31	174	-	2,092
Equity in income of affiliate	-	-	-	-	-	-	-	-	-	1,874	-	-	-	-	(1,874)	-
Provision for income taxes	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(503)
Other revenue (expense)	(1,855)	240	-	(1,615)	168	-	-	-	-	(1,067)	1	(505)	(60)	(350)	-	(3,428)
Total nonoperating gains (losses) - net	2,443	31,524	-	33,967	1,252	243	28	(419)	171	2,075	10	2,280	178	1,954	(1,874)	39,865
Excess (deficiency) of revenues over expenses	2,443	90,387	-	92,830	3,608	1,801	(936)	1,513	676	(10,677)	1,700	2,280	178	1,954	(1,874)	93,053

MEMORIAL HEALTH SYSTEM AND SUBSIDIARIES
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (CONTINUED)
YEAR ENDED SEPTEMBER 30, 2012
(dollars in thousands)

	MHS	MMC	ELIMIN- ATIONS	OBLIGATED GROUP	ALMH	TMH	MHV	MHSve	MHCCI	MPS	MP	MMCF	TMBF	ALHF	ELIMIN- ATIONS	TOTAL
Unrestricted net assets:																
Excess of revenues over expenses	\$ 2,443	90,387	-	92,830	3,608	1,891	(936)	1,513	676	(10,677)	1,700	2,280	178	1,954	(1,874)	\$ 93,053
Change in minimum pension obligation	(1,299)	(51,594)	-	(52,893)	-	-	-	-	-	(128)	-	-	-	-	-	(53,021)
Change in fair value of interest rate swap	9	90	-	99	-	-	-	-	-	-	-	-	-	-	-	99
Net assets released from restrictions for property acquisitions	-	820	-	820	-	-	-	-	-	-	-	-	-	-	-	820
Other	-	1	-	1	-	(1)	-	(1)	-	1	-	161	-	(1)	-	160
Transfers to related organizations	(12,130)	(32,886)	32,681	(12,455)	-	-	-	-	-	-	-	-	-	-	-	12,455
Transfers from related organizations	32,681	-	(32,681)	-	-	-	-	-	-	12,250	174	31	-	-	-	(12,455)
Increase (decrease) in unrestricted assets	21,584	6,818	-	28,402	3,608	1,890	(936)	1,512	676	1,446	1,874	2,472	178	1,953	(1,874)	41,111
Temporarily restricted net assets:																
Contributions	-	1,252	-	1,252	-	-	-	56	-	-	-	422	(1)	50	-	1,779
Net realized gain on investments	-	6,375	-	6,375	-	-	-	-	-	-	-	1,144	-	-	-	7,519
Net assets released from restrictions (nonoperating)	-	(997)	-	(997)	-	-	-	-	-	-	-	-	-	-	-	(997)
Net assets released from restrictions (operating)	-	(403)	-	(403)	-	-	-	(51)	(9)	-	-	(409)	-	-	-	(872)
Net assets released from restrictions for property acquisitions	-	(820)	-	(820)	-	-	-	-	-	-	-	-	-	-	-	(820)
Change in value of split-interest agreements	-	-	-	-	-	-	-	-	-	-	-	21	-	-	-	21
Gain (loss) on interest in net assets of foundation	-	3,095	-	3,095	-	-	-	-	-	-	-	-	-	-	-	(3,095)
Other	-	1	-	1	5	192	-	-	-	-	-	(227)	8	-	-	(21)
Increase (decrease) in temporarily restricted assets	-	8,503	-	8,503	5	192	-	5	(9)	-	-	951	7	50	(3,095)	6,609
Permanently restricted net assets - contributions	-	-	-	-	-	-	-	-	-	-	-	16	-	-	-	16
Increase (decrease) in net assets	21,584	15,321	-	36,905	3,613	1,992	(936)	1,517	667	1,446	1,874	3,439	185	2,003	(4,969)	47,736
Net assets, beginning of year	76,171	278,179	-	354,350	31,346	20,585	10,565	12,223	17,318	11,659	10,623	16,249	3,462	15,676	(27,776)	476,278
Net assets, end of year	\$ 97,755	293,500	-	391,255	34,959	22,577	9,629	13,740	17,985	13,105	12,497	19,688	3,647	17,679	(32,747)	\$ 524,014

MEMORIAL HEALTH SYSTEM AND SUBSIDIARIES
CONSOLIDATING STATEMENT OF CASH FLOWS
YEAR ENDED SEPTEMBER 30, 2012
(dollars in thousands)

	MHS	MMC	OBLIGATED GROUP	ALMHI	TMH	MHV	MHSve	MHCCI	MPS	MP	MMCF	TMHF	ALHF	ELIMI-NATION/ROUNDING	TOTAL
Cash flows from operating activities:															
Changes in net assets	\$ 21,384	15,321	36,905	3,613	1,992	(936)	1,517	667	1,446	1,874	3,439	185	2,003	(4,969)	\$ 47,736
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:															
Change in unrealized loss on interest rate swaps	383	128	511	-	-	-	-	-	-	-	-	-	-	-	511
Restricted contributions and other	-	(1,252)	(1,252)	-	-	-	(56)	-	-	-	(438)	1	(50)	-	(1,795)
Increase in beneficial interest in perpetual trust	-	(6,375)	(6,375)	-	-	-	-	-	-	-	-	-	-	-	(6,375)
Depreciation and amortization	7,844	29,548	37,392	4,425	2,921	16	1,042	396	160	1,387	3	-	-	-	47,742
Amortization of bond issuance costs	44	277	321	134	58	-	-	-	-	-	-	-	-	-	513
(Gain) loss on disposal of assets	24	123	147	-	-	-	-	(9)	-	-	-	-	-	-	138
Provision for uncollectible accounts	-	12,673	12,673	782	2,236	743	674	9	954	-	-	-	-	-	18,071
Change in pension obligation	1,299	51,594	52,893	-	-	-	-	-	128	-	-	-	-	-	53,021
Changes in assets and liabilities:															
Accounts receivable	-	(34,061)	(34,061)	(2,675)	(3,386)	(656)	(1,270)	(4)	(370)	-	-	-	-	-	(42,622)
Inventory and other assets	(2,201)	9,697	7,496	(43)	50	(44)	(473)	(280)	(223)	44	(10)	203	245	55	7,020
Change in unrealized (gains) losses on investments	(2,687)	(19,183)	(21,870)	(407)	(367)	-	(20)	(10)	(1,051)	-	(2,290)	(165)	(1,689)	-	(27,869)
(Deposits) withdrawals in investments, net	-	8,562	8,562	3,294	98	-	-	(2,283)	-	-	(6)	(650)	459	-	9,474
Other investment activity, net	(2,175)	(12,200)	(14,375)	(119)	211	-	(2)	(26)	11	(153)	(769)	(24)	(827)	-	(16,073)
Receivable from/payable to third-party payors	-	(3,828)	(3,828)	4,203	(384)	-	-	-	-	-	-	-	-	-	(7)
Accounts payable and other current liabilities	1,563	2,342	3,905	(581)	(14)	(36)	1,041	(154)	2,699	(7)	165	(73)	(7)	(216)	6,722
Self-insurance and other long-term liabilities	712	(14,941)	(14,229)	-	-	(58)	-	1,309	-	(4)	-	-	-	-	(12,982)
Amount due to (from) affiliates	1,051	(432)	619	104	41	6	(89)	(183)	(617)	14	(22)	-	(58)	185	-
Equity in (income) loss of unconsolidated affiliates and foundation	-	(3,095)	(3,095)	-	-	-	-	-	-	-	-	-	-	3,095	-
Transfers to (from) related organizations	(20,431)	32,886	12,455	-	-	-	-	-	(12,250)	(174)	(31)	-	-	-	-
Net cash provided by (used in) operating activities	7,010	67,784	74,794	12,732	3,436	(907)	2,306	(1,877)	(8,004)	2,985	37	(523)	76	(1,850)	83,225
Cash flows from investing activities:															
Acquisition of property and equipment	(25,015)	(22,341)	(47,356)	(757)	(1,696)	(1)	(816)	(100)	(256)	(514)	-	-	-	-	(51,496)
Proceeds on sale of property	197	415	612	-	-	26	-	15	-	-	-	-	-	-	653
Change in investment in partnerships	-	-	-	-	-	(65)	(91)	16	(1,494)	-	-	-	-	1,874	240
Net change in other assets	(395)	-	(395)	-	-	-	-	-	-	-	(64)	-	-	(24)	(483)
Net cash provided by (used in) investing activities	(25,213)	(21,926)	(47,139)	(757)	(1,696)	(40)	(907)	(69)	(1,730)	(514)	(64)	-	-	1,850	(51,086)
Cash flows from financing activities:															
Restricted contributions and other	-	1,252	1,252	-	-	-	56	-	-	-	438	(1)	50	-	1,795
Repayment of long-term debt	(1,537)	(4,623)	(6,160)	(252)	(108)	-	-	-	-	(1,900)	-	-	-	-	(8,420)
Payment of bond issuance cost and discount	(263)	-	(263)	-	-	-	-	-	-	-	-	-	-	-	(263)
Distributions from beneficial interest in remainder trust	-	997	997	-	-	-	-	-	-	-	-	-	-	-	997
Transfers (to) from related organizations	20,431	(32,886)	(12,455)	-	-	-	-	-	12,250	174	31	-	-	-	-
Net cash provided by (used in) financing activities	18,631	(35,260)	(16,629)	(252)	(108)	-	56	-	12,250	(1,726)	469	(1)	50	-	(5,891)
Net increase (decrease) in cash and cash equivalents	418	10,598	11,026	11,723	1,652	(947)	1,455	(1,946)	2,496	745	442	(524)	126	-	26,248
Cash and cash equivalents, beginning of year	368	43,590	43,958	148	2,933	3,394	6,315	6,182	4,308	1,442	1,372	792	196	-	71,240
Cash and cash equivalents, end of year	\$ 786	\$ 54,188	\$ 54,984	\$ 11,871	\$ 4,585	\$ 2,447	\$ 7,770	\$ 4,236	\$ 6,804	\$ 2,187	\$ 1,814	\$ 268	\$ 322	\$ -	\$ 97,488

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MEMORIAL HEALTH SYSTEM AND SUBSIDIARIES
CONSOLIDATING BALANCE SHEET
SEPTEMBER 30, 2011
(dollars in thousands)

Assets	MHS	MMC	ELIMIN- ATIONS	OBLIGATED GROUP	ALMBI	TMH	MHV	MHSw	MHCCI	MPS	MP	MMCf	TMHF	ALHF	ELIMIN- ATIONS	TOTAL
Current assets:																
Cash and cash equivalents	\$ 368	43,590	—	43,958	148	2,933	3,394	6,515	6,182	4,308	1,442	1,372	792	196	—	\$ 71,240
Short-term investments	25,876	55,803	—	81,679	6,051	3,962	—	193	3,208	—	2,106	—	2,303	23	—	99,525
Assets whose use is limited – current portion	220	13,176	—	13,396	1,147	492	—	—	—	—	1,428	—	—	—	—	16,461
Patient accounts receivable	—	103,811	—	103,811	6,366	6,276	1,126	4,301	409	5,746	—	—	—	—	—	128,235
Allowance for uncollectible accounts	—	(17,553)	—	(17,553)	(1,213)	(1,254)	(304)	(698)	(266)	(808)	—	—	—	—	—	(22,096)
Net patient accounts receivable	—	86,258	—	86,258	5,153	5,022	822	3,803	143	4,938	—	—	—	—	—	106,139
Receivables from third-party payors	—	9,680	—	9,680	1,747	211	—	—	—	—	—	—	—	—	—	11,638
Due from affiliates	536	569	(533)	572	36	15	38	18	4	46	9	—	—	—	(738)	—
Other	1,521	15,916	—	17,437	295	301	61	361	4,011	221	26	178	306	781	(478)	23,700
Investment	—	8,970	—	8,970	439	643	—	424	—	612	—	—	—	—	—	11,088
Prepaid expenses	2,898	3,827	—	6,725	190	185	28	87	157	380	92	69	—	—	—	7,913
Total current assets	31,419	237,789	(533)	268,675	15,206	13,764	4,243	11,601	13,705	10,505	5,101	1,619	3,401	1,000	(1,216)	347,704
Assets whose use is limited:																
Board-designated funds	—	121,923	—	121,923	9,000	—	—	—	387	—	—	6,519	—	14,762	—	152,591
Self-insurance trusts	—	17,857	—	17,857	—	—	—	—	—	—	—	—	—	—	—	17,857
Bond trustee assets	—	1,614	—	1,614	—	—	—	—	—	—	—	—	—	—	—	1,614
Donor-restricted assets	—	851	—	851	—	—	—	—	—	—	7,707	136	—	—	—	8,694
Deferred compensation investments	9,442	2,553	—	11,995	—	—	—	—	—	7,069	—	—	—	—	—	19,064
Total assets whose use is limited	9,442	144,798	—	154,240	9,000	—	—	—	387	7,069	—	14,226	136	14,762	—	199,820
Property, plant, and equipment	152,522	355,787	—	508,309	61,311	47,350	561	9,832	11,679	3,691	34,581	147	—	342	—	677,803
Less accumulated depreciation	(59,940)	(197,529)	—	(257,469)	(8,095)	(18,712)	(491)	(6,946)	(6,955)	(3,070)	(13,391)	(142)	—	(342)	—	(315,613)
Net property, plant, and equipment	92,582	158,258	—	250,840	53,216	28,638	70	2,886	4,724	621	21,190	5	—	—	—	362,190
Other assets:																
Investments in partnerships	—	14,724	—	14,724	—	—	6,281	642	47	11,003	—	—	—	—	(27,778)	4,919
Unamortized bond issuance costs	424	2,135	—	2,559	1,006	434	—	—	—	—	—	—	—	—	—	3,999
Beneficial interest in remainder trust	—	21,082	—	21,082	—	—	—	—	—	—	—	—	—	—	—	21,082
Other	4,970	4,251	—	9,221	103	—	—	—	143	—	—	907	—	—	(145)	10,229
Total other assets	5,394	42,192	—	47,586	1,109	434	6,281	642	190	11,003	—	907	—	—	(27,923)	40,229
Total assets	138,837	583,037	(533)	721,341	78,531	42,836	10,694	15,129	19,006	29,198	26,291	16,757	3,537	15,762	(29,139)	949,943
Liabilities and net assets																
Current liabilities:																
Long-term debt – current portion	1,538	1,623	—	3,161	251	108	—	—	—	—	1,900	—	—	—	—	5,420
Accounts payable	3,814	26,179	—	29,993	915	483	128	1,339	397	1,970	74	17	1	30	192	33,561
Accrued payroll	2,224	18,396	—	20,620	1,032	1,658	—	1,047	771	1,191	5	—	—	—	—	26,324
Interest payable	320	2,350	—	2,650	1,147	492	—	—	—	—	3	—	—	—	—	4,292
Due to affiliates	64	564	(533)	95	29	3	1	69	182	476	—	25	—	36	(916)	—
Payables to third-party payors	—	27,331	—	27,331	765	413	—	—	—	—	—	—	—	—	—	28,509
Other	1,916	10,281	—	12,197	464	398	—	—	338	1,008	516	376	74	—	(637)	34,734
Total current liabilities	9,876	86,704	(533)	96,047	4,603	3,557	129	2,455	1,688	4,645	2,498	418	75	86	(1,361)	114,840
Long-term debt – less current portion	32,768	114,222	—	146,990	42,582	18,248	—	—	—	—	13,170	—	—	—	—	220,990
Other liabilities:																
Deferred compensation and benefits	9,870	2,553	—	12,423	—	—	—	—	—	7,375	—	—	—	—	—	19,798
Self-insurance accrued expenses	369	18,195	—	18,564	—	—	—	294	—	—	—	—	—	—	—	18,858
Accrued employee benefits	2,219	4,875	—	7,094	—	—	—	157	—	3,836	—	—	—	—	—	11,087
Pension obligation	3,108	70,860	—	73,968	—	—	—	—	—	1,683	—	—	—	—	—	75,651
Other	4,456	7,449	—	11,905	—	446	—	—	—	—	90	—	—	—	—	12,441
Total other liabilities	20,022	103,932	—	123,954	—	446	—	451	—	12,894	—	90	—	—	—	137,835
Net assets:																
Unrestricted	76,171	241,623	—	317,794	31,346	20,585	10,565	11,911	16,334	11,659	10,623	8,342	3,326	15,663	(13,154)	445,194
Temporarily restricted	—	36,556	—	36,556	—	—	—	229	984	—	—	2,851	136	13	(14,624)	26,145
Permanently restricted	—	—	—	—	—	—	—	83	—	—	—	4,856	—	—	—	4,939
Total net assets	76,171	278,179	—	354,950	31,346	20,585	10,565	12,223	17,318	11,659	10,623	16,249	3,462	15,676	(27,778)	476,278
Total liabilities and net assets	\$ 138,837	\$ 583,037	(533)	721,341	78,531	42,836	10,694	15,129	19,006	29,198	26,291	16,757	3,537	15,762	(29,139)	\$ 949,943

MEMORIAL HEALTH SYSTEM AND SUBSIDIARIES
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS
YEAR ENDED SEPTEMBER 30, 2011
(dollars in thousands)

	MHS	MMC	ELIMIN- ATIONS	OBLIGATED GROUP	ALMH	TMH	MHV	MHSe	MHCCI	MPS	MP	MMCF	TMHF	ALHF	ELIMIN- ATIONS	TOTAL
Patient service revenues:																
Inpatient revenues	\$ -	\$ 864,827	(38,385)	\$ 826,442	\$ 14,109	\$ 15,216	-	-	-	-	-	-	-	-	-	\$ 855,767
Outpatient revenues	-	650,894	-	650,894	60,236	54,727	14,850	27,458	14,813	64,033	-	-	-	-	-	887,011
Total patient revenues	-	1,515,721	(38,385)	1,477,336	74,345	69,943	14,850	27,458	14,813	64,033	-	-	-	-	-	1,742,778
Less charity	-	51,248	-	51,248	3,052	2,659	29	442	33	92	-	-	-	-	-	57,555
Less contractual allowances	-	984,945	(38,385)	946,560	35,347	34,517	8,428	5,862	1,838	30,532	-	-	-	-	-	1,065,084
Net patient service revenues	-	479,528	-	479,528	35,946	32,767	6,393	21,154	12,942	33,409	-	-	-	-	-	622,139
Provision for uncollectible accounts	-	13,379	-	13,379	1,547	2,165	-	503	9	743	-	-	-	-	-	19,030
	-	466,149	-	466,149	34,399	30,602	5,709	20,551	12,933	32,666	-	-	-	-	-	603,109
Hospital rooms improvement revenue	-	20,802	-	20,802	2,643	2,278	-	-	-	-	-	-	-	-	-	25,723
Capitation revenues	-	64,688	-	64,688	-	-	-	-	-	-	-	-	-	-	-	64,688
Other revenues:																
Management fees	37,674	-	(29,225)	8,449	14	-	-	-	-	-	-	-	-	-	(8,463)	-
Other	9,962	14,006	(2,737)	21,231	449	267	2,622	388	406	752	5,782	-	-	-	(8,382)	23,515
Total other revenues	47,636	14,006	(31,962)	29,680	463	267	2,622	388	406	752	5,782	-	-	-	(16,845)	23,515
Total revenues	47,636	565,645	(31,962)	581,319	37,505	33,147	8,731	21,039	13,339	33,418	5,782	-	-	-	(16,845)	717,035
Expenses:																
Salaries and wages	20,785	174,877	-	195,662	13,239	11,985	4,977	10,421	7,718	11,013	373	-	-	-	-	255,288
Employee benefits	6,120	61,468	-	67,588	3,967	3,913	567	4,163	1,920	4,014	132	-	-	-	-	86,264
Physician fees	766	21,074	-	21,840	1,559	2,550	36	91	196	15,424	-	-	-	-	-	41,696
Utilities	1,206	7,751	-	8,957	771	906	27	179	343	172	661	-	-	-	-	11,996
Pharmaceutical supplies	-	17,399	-	17,399	1,047	925	82	315	79	1,811	-	-	-	-	-	21,708
Patient service supplies	-	83,355	-	83,355	1,782	1,415	89	179	-	1,072	-	-	-	-	-	87,892
System management fee	-	29,225	(29,225)	-	1,535	1,509	499	845	283	3,687	100	-	-	-	(8,458)	-
Supplies and other	8,942	69,913	(2,737)	76,118	6,495	4,893	1,255	3,579	1,855	6,835	1,508	-	-	-	(8,387)	94,151
Hospital provider assessment	-	11,366	-	11,366	463	392	-	-	-	-	-	-	-	-	-	12,221
Purchased medical services	-	35,516	-	35,516	-	-	-	-	-	-	-	-	-	-	-	35,516
Depreciation and amortization	8,024	24,030	-	32,054	3,366	2,275	54	1,011	438	142	1,404	-	-	-	-	40,744
Amortization of bond insurance expenses	44	277	-	321	58	-	-	-	2	-	-	-	-	-	-	515
Interest expense and other financing costs	1,749	5,722	-	7,471	1,531	758	-	-	9	145	-	-	-	-	-	9,894
Total expenses	47,636	541,953	(31,962)	557,627	35,889	31,609	7,586	20,783	12,843	44,170	4,523	-	-	-	(16,845)	697,985
Income (loss) from operations	-	23,692	-	23,692	1,616	1,538	745	256	496	(10,752)	1,459	-	-	-	-	19,050
Nonoperating gains (losses):																
Interest and dividends	830	4,065	-	4,895	197	68	27	130	133	211	9	109	35	323	-	6,137
Realized gain (loss) on investments, net	242	2,357	-	2,599	-	128	-	-	3	-	-	104	62	(184)	-	2,712
Unrealized gain (loss) on investments, net	(1,905)	(12,702)	-	(14,607)	(18)	(193)	-	-	70	(363)	-	(293)	(76)	(560)	-	(16,040)
Change in fair value of interest rate swap	(128)	18	-	(110)	-	-	-	-	-	-	-	-	-	-	-	(110)
Contributions	-	164	-	164	(171)	40	-	(5)	-	-	-	1,253	32	783	-	2,996
Equity in income of affiliate	-	-	-	-	-	-	-	-	-	1,468	-	-	-	-	(1,468)	-
Provision for income taxes	-	-	-	-	-	-	-	(388)	-	-	-	-	-	-	-	(388)
Other revenue (expense)	(187)	649	-	462	(1,516)	-	-	(1)	1	191	-	(983)	(126)	(648)	-	(2,660)
Total nonoperating gains (losses) - net	(1,148)	(5,449)	-	(6,597)	(1,308)	43	27	(284)	207	1,557	9	190	(73)	(526)	(1,468)	(8,253)
Excess (deficiency) of revenues over expenses	(1,148)	18,243	-	17,095	108	1,581	772	(8)	703	(9,245)	1,468	190	(73)	(326)	(1,468)	10,797

MEMORIAL HEALTH SYSTEM AND SUBSIDIARIES
CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS (CONTINUED)
YEAR ENDED SEPTEMBER 30, 2011
(dollars in thousands)

	MHS	MMC	ELIMIN- ATIONS	OBLIGATED GROUP	ALNH	TMH	MHV	MHSre	MHCCI	MPS	MP	MMCF	TMBF	ALHF	ELIMIN- ATIONS	TOTAL
Unrestricted net assets:																
Excess of revenues over expenses	\$ (1,148)	18,243	-	17,095	108	1,581	772	(8)	703	(9,245)	1,468	190	(73)	(326)	(1,468)	\$ 10,797
Change in minimum pension obligation	379	28,376	-	28,755	-	-	-	-	-	(81)	-	-	-	-	-	28,674
Change in fair value of interest rate swap	9	90	-	99	-	-	-	-	-	-	-	-	-	-	-	99
Net assets released from restrictions for property acquisitions	-	-	-	-	-	-	-	-	-	-	-	-	44	-	-	44
Other	-	1	-	1	-	1	-	-	-	-	-	(10)	1	-	-	(7)
Transfers to related organizations	(11,100)	(7,490)	7,552	(11,038)	-	-	-	-	-	(80)	-	-	-	-	-	11,118
Transfers from related organizations	7,552	-	(7,552)	-	-	-	-	450	-	10,650	-	18	-	-	-	(11,118)
Increase (decrease) in unrestricted assets	(4,308)	39,220	-	34,912	108	1,582	772	442	703	1,244	1,468	198	(28)	(326)	(1,468)	39,607
Temporarily restricted net assets:																
Contributions	-	748	-	748	-	-	-	63	34	-	-	415	48	42	-	1,350
Net realized gain on investments	-	770	-	770	-	-	-	-	-	-	-	(32)	-	-	-	718
Net assets released from restrictions (nonoperating)	-	(802)	-	(802)	-	-	-	-	-	-	-	-	-	(19)	-	(821)
Net assets released from restrictions (operating)	-	(658)	-	(658)	-	-	-	(53)	(5)	-	-	(260)	-	(45)	-	(1,021)
Net assets released from restrictions for property acquisitions	-	-	-	-	-	-	-	-	-	-	-	-	(44)	-	-	(44)
Change in value of split-interest agreements	-	-	-	-	-	-	-	-	-	-	-	(10)	-	-	-	(10)
Gain (loss) on interest in net assets of foundation	-	223	-	223	-	-	-	-	-	-	-	-	-	-	(223)	-
Other	-	1	-	1	-	-	-	-	-	-	-	(85)	-	-	-	(84)
Increase (decrease) in temporarily restricted assets	-	282	-	282	-	-	-	10	29	-	-	8	4	(22)	(223)	88
Permanently restricted net assets - contributions	-	-	-	-	-	-	-	-	-	-	-	42	-	-	-	42
Increase (decrease) in net assets	(4,308)	39,502	-	35,194	108	1,582	772	452	732	1,244	1,468	248	(24)	(348)	(1,691)	39,737
Net assets, beginning of year	80,479	238,677	-	319,156	31,238	19,003	9,793	11,771	16,586	10,415	9,155	16,001	3,486	16,024	(26,087)	436,541
Net assets, end of year	\$ 76,171	278,179	-	354,350	31,346	20,585	10,565	12,223	17,318	11,659	10,623	16,249	3,462	15,676	(27,778)	\$ 476,278

MEMORIAL HEALTH SYSTEM AND SUBSIDIARIES
CONSOLIDATING STATEMENT OF CASH FLOWS
YEAR ENDED SEPTEMBER 30, 2011
(dollar in thousands)

	MHS	MMC	OBLIGATED GROUP	ALMH	TMH	MHV	MHSve	MICCI	MPS	MP	MMCF	TMHF	ALHF	ELIMI- NATION/ ROUNDING	TOTAL
Cash flows from operating activities:															
Changes in net assets	\$ (4,308)	39,502	35,194	108	1,582	772	452	732	1,244	1,468	248	(24)	(348)	(1,691)	\$ 39,737
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:															
Change in unrealized loss on interest rate swaps	128	(18)	110	—	—	—	—	—	—	—	—	—	—	—	110
Restricted contributions and other	—	(748)	(748)	—	—	—	(63)	(34)	—	—	(457)	(48)	(42)	—	(1,392)
Increase in beneficial interest in perpetual trust	—	(770)	(770)	—	—	—	—	—	—	—	—	—	—	—	(770)
Depreciation and amortization	8,024	24,030	32,054	3,366	2,275	54	1,011	438	142	1,404	2	—	—	—	40,746
Amortization of bond issuance costs	44	277	321	134	58	—	—	2	—	—	—	—	—	—	515
(Gain) loss on disposal of assets	377	635	1,012	74	14	—	—	(35)	—	2	—	—	—	—	1,067
Provision for uncollectible accounts	—	13,379	13,379	1,547	2,165	684	503	9	743	—	—	—	—	—	19,030
Change in pension obligation	(379)	(28,376)	(28,755)	—	—	—	—	—	81	—	—	—	—	—	(28,674)
Changes in assets and liabilities:															
Accounts receivable	—	(25,839)	(25,839)	(2,770)	(3,226)	(875)	(1,361)	15	(2,125)	—	—	—	—	—	(36,181)
Inventory and other assets	(1,125)	(1,976)	(3,101)	(14)	149	33	(5)	(288)	232	(10)	(70)	348	196	25	(2,505)
Change in unrealized losses (gains) on investments	1,905	12,702	14,607	18	193	—	—	(70)	363	—	581	76	560	—	16,328
(Deposits) withdrawals in investments, net	(453)	9,030	8,577	5,320	5,901	—	—	—	—	—	195	—	1,522	—	21,515
Other investment activity, net	(1,014)	(7,367)	(8,381)	(99)	(134)	—	4	71	(411)	(78)	(363)	(110)	(2,346)	—	(12,047)
Receivable from/payable to third-party payors	—	(5,186)	(5,186)	(1,832)	(83)	—	—	—	—	—	—	—	—	—	(7,101)
Accounts payable and other current liabilities	566	(10,612)	(10,046)	(4,186)	(1,245)	23	450	613	(245)	(57)	54	74	—	153	(14,412)
Self-insurance and other long-term liabilities	36	2,964	3,000	—	—	—	21	—	685	—	(4)	—	—	—	3,702
Amount due to (from) affiliates	632	(1,087)	(455)	1	(7)	(77)	85	143	384	43	19	—	21	(157)	—
Equity in (income) loss of unconsolidated affiliates and foundation	—	(223)	(223)	—	—	—	—	—	—	—	—	—	—	223	—
Transfers to (from) related organizations	3,548	7,490	11,038	—	—	—	(450)	—	(10,570)	—	(18)	—	—	—	—
Net cash provided by (used in) operating activities	7,981	27,807	35,788	1,667	7,642	614	647	1,596	(9,477)	2,772	(13)	316	(437)	(1,447)	39,668
Cash flows from investing activities:															
Acquisition of property and equipment	(6,489)	(42,547)	(49,036)	(20,089)	(11,323)	—	(1,095)	(207)	(66)	(515)	—	—	—	—	(82,331)
Proceeds on sale of property	7	31	38	—	25	—	—	59	—	—	—	—	—	—	122
Change in investment in partnerships	—	—	—	—	1,872	(77)	(23)	(1,376)	—	—	—	—	—	1,467	1,863
Net change in other assets	1,755	—	1,755	—	—	—	22	—	—	—	67	—	—	(20)	1,824
Net cash provided by (used in) investing activities	(4,727)	(42,516)	(47,243)	(20,089)	(11,298)	1,872	(1,172)	(149)	(1,443)	(515)	67	—	—	1,447	(78,522)
Cash flows from financing activities:															
Restricted contributions and other	—	748	748	—	—	—	63	34	—	—	457	48	42	—	1,392
Repayment of long-term debt	(1,465)	(1,603)	(3,068)	(267)	(114)	—	—	(315)	—	(1,800)	—	—	—	—	(5,564)
Distributions from beneficial interest in remainder trust	—	802	802	—	—	—	—	—	—	—	—	—	—	—	802
Transfers (to) from related organizations	(3,548)	(7,490)	(11,038)	—	—	—	450	—	10,570	—	18	—	—	—	—
Net cash provided by (used in) financing activities	(5,013)	(7,543)	(12,556)	(267)	(114)	—	513	(281)	10,570	(1,800)	475	48	42	—	(3,370)
Net increase (decrease) in cash and cash equivalents	(1,759)	(22,252)	(24,011)	(18,689)	(3,770)	2,486	(12)	1,166	(349)	457	529	364	(395)	—	(42,224)
Cash and cash equivalents, beginning of year	2,127	65,842	67,969	18,837	6,703	908	6,527	5,016	4,657	985	843	428	591	—	113,464
Cash and cash equivalents, end of year	\$ 368	43,590	43,958	148	2,933	3,394	6,515	6,182	4,308	1,442	1,372	792	196	—	\$ 71,240

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Passavant Area Hospital Association and Affiliates

Jacksonville, Illinois

Consolidated Financial Statements and Supplementary Information

Years Ended September 30, 2012 and 2011

Passavant Area Hospital Association and Affiliates

Consolidated Financial Statements and Supplementary Information

Years Ended September 30, 2012 and 2011

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Independent Auditor's Report

Board of Directors
Passavant Area Hospital Association
Jacksonville, Illinois

We have audited the accompanying consolidated balance sheets of Passavant Area Hospital Association and Affiliates (the "Association") as of September 30, 2012 and 2011, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Passavant Area Hospital Association and Affiliates as of September 30, 2012 and 2011, and the results of their operations, changes in their net assets, and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.

Wipfli LLP

Wipfli LLP

January 16, 2013
Milwaukee, Wisconsin

Passavant Area Hospital Association and Affiliates

Consolidated Balance Sheets

September 30, 2012 and 2011

<i>Assets</i>	2012	2011
Current assets:		
Cash	\$ 7,864,770	\$ 7,565,094
Short-term investments	6,181,503	3,051,841
Assets limited as to use	965,000	935,000
Patient accounts receivable - Net	16,065,034	13,979,239
Inventory	746,200	687,856
Prepaid expenses	1,608,436	1,816,047
Total current assets	33,430,943	28,035,077
Assets limited as to use	50,491,440	44,055,029
Property and equipment - Net	49,007,211	50,711,759
Other assets:		
Beneficial interest in perpetual trusts	16,991,019	13,909,435
Other	1,670,577	1,903,080
Total other assets	18,661,596	15,812,515
TOTAL ASSETS	\$151,591,190	\$138,614,380

<i>Liabilities and Net Assets</i>	2012	2011
Current liabilities:		
Current maturities of long-term debt	\$ 1,475,400	\$ 1,332,534
Accounts payable	2,002,745	1,673,747
Accrued liabilities	6,585,337	7,729,428
Estimated amounts due to third-party payers	3,981,317	4,360,767
Total current liabilities	14,044,799	15,096,476
Long-term liabilities:		
Long-term debt, less current maturities	29,903,787	29,704,125
Interest rate swap agreements	3,267,404	3,160,290
Total long-term liabilities	33,171,191	32,864,415
Total liabilities	47,215,990	47,960,891
Net assets:		
Unrestricted	83,894,261	73,233,579
Temporarily restricted	723,036	743,592
Permanently restricted	19,757,903	16,676,318
Total net assets	104,375,200	90,653,489
TOTAL LIABILITIES AND NET ASSETS	\$151,591,190	\$138,614,380

See accompanying notes to consolidated financial statements.

Passavant Area Hospital Association and Affiliates

Consolidated Statements of Operations

Years Ended September 30, 2012 and 2011

	2012	2011
Revenue:		
Patient service revenue (net of contractual allowances and discounts)	\$ 86,613,997	\$ 88,478,051
Provision for bad debts	(29,039)	(4,332,978)
Net patient service revenue	86,584,958	84,145,073
Contributions	1,437,107	208,666
Other operating revenue	1,932,855	1,620,490
Total revenue	89,954,920	85,974,229
Expenses:		
Salaries and wages	38,288,507	37,452,732
Employee benefits	13,148,842	13,068,643
Purchased services and professional fees	6,683,437	6,062,635
Supplies and other	20,293,676	19,538,928
Depreciation and amortization	6,179,020	6,195,009
Interest	1,564,480	1,560,999
Total expenses	86,157,962	83,878,946
Income from operations	3,796,958	2,095,283
Other income (expense):		
Investment income	7,002,455	536,828
Grants	(16,617)	(28,770)
Other	(15,000)	-
Total other income - Net	6,970,838	508,058
Revenue in excess of expenses	10,767,796	2,603,341
Change in fair value of interest rate swap agreements	(107,114)	(295,933)
Increase in unrestricted net assets	\$ 10,660,682	\$ 2,307,408

See accompanying notes to consolidated financial statements.

Passavant Area Hospital Association and Affiliates

Consolidated Statements of Changes in Net Assets

Years Ended September 30, 2012 and 2011

	2012	2011
Unrestricted net assets:		
Revenue in excess of expenses	\$ 10,767,796	\$ 2,603,341
Change in fair value of interest rate swap agreements	(107,114)	(295,933)
Increase in unrestricted net assets	10,660,682	2,307,408
Temporarily restricted net assets:		
Contributions	70,376	1,236
Investment loss	(33,469)	(23,155)
Net assets released from restrictions	(57,463)	(4,594)
Decrease in temporarily restricted net assets	(20,556)	(26,513)
Increase in permanently restricted net assets - Change in beneficial interest in perpetual trusts	3,081,585	1,289,675
Change in net assets	13,721,711	3,570,570
Net assets at beginning	90,653,489	87,082,919
Net assets at end	\$ 104,375,200	\$ 90,653,489

Passavant Area Hospital Association and Affiliates

Consolidated Statements of Cash Flows

Years Ended September 30, 2012 and 2011

	2012	2011
Increase (decrease) in cash and cash equivalents:		
Cash flows from operating activities:		
Increase (decrease) in net assets	\$ 13,721,711	\$ 3,570,570
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:		
Depreciation and amortization	6,179,020	6,195,009
Provision for bad debts	29,039	4,332,978
Net change in unrealized (gains) losses on investments	(4,331,132)	1,480,215
Net realized (gains) losses on investments	40,958	(66,867)
Change in fair value of interest rate swap agreements	107,114	295,933
Change in beneficial interest in perpetual trusts	(3,081,585)	(1,289,675)
Loss on disposal of equipment	24,227	15,166
Equity in earnings of unconsolidated affiliate	(90,756)	(77,083)
Forgiveness of loans to physicians	283,297	844,049
Restricted investment loss	33,469	23,155
Changes in operating assets and liabilities:		
Patient accounts receivable	(2,114,834)	(6,127,802)
Inventory	(58,344)	(29,059)
Prepaid expenses	207,611	146,092
Other assets	98,620	43,394
Accounts payable	360,460	599,674
Accrued liabilities	(1,144,091)	(509,599)
Estimated amounts due to third-party payers	(379,450)	1,290,767
Net cash provided by operating activities	9,885,334	10,736,917

Passavant Area Hospital Association and Affiliates

Consolidated Statements of Cash Flows (Continued)

Years Ended September 30, 2012 and 2011

	2012	2011
Cash flows from investing activities:		
Purchases of property and equipment	\$ (4,492,779)	\$ (4,528,358)
Proceeds from sale of equipment	800	2,501
Purchases of investments	(23,623,785)	(3,284,716)
Proceeds from sales and maturities of investments	18,317,886	-
Loans made to physicians	(96,839)	(376,326)
Net cash used in investing activities	(9,894,717)	(8,186,899)
Cash flows from financing activities:		
Proceeds from issuance of long-term debt	1,674,620	-
Principal payments on long-term debt	(1,332,092)	(1,275,488)
Restricted investment loss	(33,469)	(23,155)
Net cash provided by (used in) financing activities	309,059	(1,298,643)
Net increase in cash and cash equivalents	299,676	1,251,375
Cash and cash equivalents at beginning	7,565,094	6,313,719
Cash and cash equivalents at end	\$ 7,864,770	\$ 7,565,094

Supplemental cash flow information:

Cash paid during the year for interest, net of amount capitalized of \$36,838 and \$391,738 in 2012 and 2011, respectively	\$ 1,527,642	\$ 1,254,212
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Noncash investing and financing activities:

Property and equipment purchases in accounts payable	\$ -	\$ 31,462
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Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies**

The Entity

Passavant Memorial Area Hospital Association (the "Hospital") primarily earns revenues by providing inpatient, outpatient, and emergency care services to patients in Jacksonville, Illinois, and the surrounding area. It also provides physician services in the same geographic area through its separate wholly-owned subsidiary corporation, Passavant Physician Association. Effective November 1, 2010, the Hospital formed a new nonprofit corporation, Jacksonville CRNA's Inc. ("CRNA"). The Hospital employs certain nurse anesthetists and sells their services to CRNA. The Hospital is the sole corporate member of CRNA.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Hospital, Passavant Physician Association, and CRNA (collectively the "Association"). All material intercompany accounts and transactions have been eliminated in consolidation.

Financial Statement Presentation

The Association follows accounting standards contained in the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC). The ASC is the single source of authoritative accounting principles generally accepted in the United States (GAAP) for nongovernmental entities in the preparation of financial statements in conformity with GAAP.

Use of Estimates in Preparation of Financial Statements

The preparation of the accompanying consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that directly affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results may differ from these estimates.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Cash Equivalents

The Association considers all highly liquid debt instruments with an original maturity of three months or less to be cash equivalents, excluding amounts whose use is limited or restricted and amounts held as short-term investments.

Patient Accounts Receivable and Credit Policy

Patient accounts receivable are uncollateralized patient obligations that are stated at the amount management expects to collect from outstanding balances. These obligations are primarily from local residents, most of whom are insured under third-party payer agreements. The Association bills third-party payers on the patients' behalf, or if a patient is uninsured, the patient is billed directly. Once claims are settled with the primary payer, any secondary insurance is billed, and patients are billed for copay and deductible amounts that are the patients' responsibility. Payments on patient accounts receivable are applied to the specific claim identified on the remittance advice or statement. The Association does not have a policy to charge interest on past due accounts.

The carrying amounts of patient accounts receivable are reduced by allowances that reflect management's best estimate of the amounts that will not be collected. Management provides for contractual adjustments under terms of third-party reimbursement agreements through a reduction of gross revenue and a credit to patient accounts receivable. In addition, management provides for probable uncollectible amounts, primarily from uninsured patients and amounts patients are personally responsible for, through a charge to operations and a credit to a valuation allowance based on its assessment of historical collection likelihood and the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to patient accounts receivable.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Patient Accounts Receivable and Credit Policy (Continued)

In evaluating the collectability of patient accounts receivable, the Association analyzes past results and identifies trends for each major payer source of revenue for the purpose of estimating the appropriate amounts of the allowance for doubtful accounts and the provision for bad debts. Data in each major payer source are regularly reviewed to evaluate the adequacy of the allowance for doubtful accounts. Specifically, for receivables relating to services provided to patients having third-party coverage, an allowance for doubtful accounts and a corresponding provision for bad debts are established based on historical write-off percentages; for receivables relating to self-pay patients, a provision for bad debt is made in the period services are rendered based on experience indicating the inability or unwillingness of patients to pay amounts for which they are financially responsible.

Patient accounts receivable are recorded in the accompanying consolidated balance sheets net of contractual adjustments and allowances for doubtful accounts.

Inventory

Inventory is valued at the lower of weighted average cost or market.

Investments and Investment Income

Investments, including short-term investments and assets limited as to use, are recorded at fair value in the accompanying consolidated balance sheets. Investment income or loss includes unrealized and realized gains and losses on investments, interest, and dividends. The Association includes investment income from the bond funds and self-insurance trust in other operating revenue. Other investment income is reflected in the consolidated statements of operations and changes in net assets as other income (expense) or as changes in temporarily restricted net assets if the terms of gifts impose restrictions on the use of the income.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Assets Limited as to Use

Assets limited as to use include (1) assets set aside by the Board of Directors for future capital improvements over which the board retains control and may subsequently be used for other purposes at its discretion, (2) assets accumulated from unrestricted donations and bequests, including earnings thereon, which the Board of Directors has set aside for future specific purposes, (3) assets restricted by donors, and (4) assets held by trustees under bond indenture agreements.

Assets limited as to use that are required for obligations classified as current liabilities are reported as current assets.

Fair Value Measurements

The Association measures fair value of its financial instruments using a three-tier hierarchy which prioritizes the inputs used in measuring fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of fair value hierarchy are described below:

Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Association has the ability to access.

Level 2 Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets.
- Quoted prices for identical or similar assets or liabilities in inactive markets.
- Inputs other than quoted prices that are observable for the asset or liability.
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurements.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs.

Property, Equipment, and Depreciation

Property and equipment acquisitions are recorded at cost or, if donated, at fair value at the date of donation. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Equipment under capital leases is amortized using the straight-line method over the shorter of the estimated useful life of the equipment or the lease term. Amortization of equipment under capital leases is included in depreciation and amortization in the accompanying consolidated statements of operations. Estimated useful lives range from 2 to 20 years for land improvements, 10 to 40 years for buildings and improvements, and 5 to 20 years for equipment.

Interest costs incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support and are excluded from revenue in excess of expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as contributions in temporarily restricted net assets. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported as net assets released from restrictions when the donated or acquired long-lived assets are placed in service.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 Summary of Significant Accounting Policies (Continued)

Asset Retirement Obligations

ASC Topic 410-20, *Asset Retirement Obligations*, clarifies when an entity is required to recognize a liability for a conditional asset retirement obligation. The Association has considered ASC Topic 410-20 specifically as it relates to its legal obligation to perform asset retirement activities, such as asbestos removal, on its existing properties. The Association believes there is an indeterminate settlement date for the asset retirement obligations because the range of time over which the Association may settle the obligation is unknown and cannot be estimated. As a result, the Association cannot reasonably estimate the liability related to these asset retirement activities as of September 30, 2012 and 2011.

Deferred Financing Costs

Costs related to the issuance of long-term debt, included in other assets in the accompanying consolidated balance sheets, are amortized over the life of the related debt using the effective interest method. Amortization is included in depreciation and amortization in the accompanying consolidated statements of operations.

Beneficial Interests in Perpetual Trusts

The Association is the income beneficiary along with other beneficiaries of several trusts controlled by unrelated third parties. The beneficial interests in the assets of these trusts are included in the Association's accompanying consolidated financial statements as permanently restricted net assets. Income is distributed in accordance with the individual trust documents and is included in investment income. Trust income distributed to the Association for the years ended September 30, 2012 and 2011, was \$75,687 and \$45,217, respectively.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Interest Rate Swap Agreements

The Association uses derivative instruments to manage its risk related to interest rate movements. The interest rate risk management strategy is to stabilize cash flow requirements by maintaining the interest rate swaps to convert the variable rate debt to fixed rate. At the inception of the interest rate swap agreements, the risk management strategy and the hedges' effectiveness were documented. Management has determined the swaps to be highly effective. The interest rate swap agreements are reported at fair value in the accompanying consolidated balance sheets, with subsequent changes in fair value included as other changes in unrestricted net assets for the effective portion and other income (expense) for the ineffective portion. If the ineffectiveness exceeds certain prescribed levels, the interest rate swap agreements would no longer be eligible for hedge accounting, all future changes in the fair value would be reported in other income (expense) in the consolidated statements of operations, and the change that was recorded through net assets from the beginning of the interest rate swap would be amortized into earnings over the remaining life of the swap. In the event the interest rate swap is terminated, the total amount that was recorded in net assets from the beginning of the interest rate swap would be reclassified into earnings.

Net Assets

Unrestricted net assets consist of investments and otherwise unrestricted amounts that are available for use in carrying out the mission of the Association and include those expendable resources which have been designated for special use by the Association's Board of Directors. Temporarily restricted net assets are those whose use by the Association has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Association in perpetuity.

The Board of Directors of the Association treats any appreciation in endowment funds as unrestricted unless specified otherwise by the donor. Interest and dividends from permanently restricted investments are credited to unrestricted net assets unless donor stipulations restrict such earnings.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Patient Service Revenue

Patient service revenue includes amounts from patients and third-party payers for services provided. The Association recognizes patient service revenue associated with services provided to patients who have third-party payer coverage primarily on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, the Association recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates based on the Association's uninsured patients policy). Based on historical experience of the Association, a significant portion of uninsured patients will be unwilling or unable to pay for the services provided. Thus, the Association records a significant provision for bad debts related to uninsured patients in the period the services are provided. Patient service revenue also includes estimated retroactive adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Charity Care

The Association provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. The Association maintains records to identify the amount of charges foregone for services and supplies furnished under the charity care policy. Because the Association does not pursue collection of amounts determined to qualify as charity care, they are not reported as net patient service revenue.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Donor-Restricted Gifts

Contributions are considered available for unrestricted use unless specifically restricted by the donor. Unconditional promises to give cash and other assets to the Association are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions.

Revenue in Excess of Expenses

The accompanying consolidated statements of operations and changes in net assets include the classification revenue in excess of expenses, which is considered the operating indicator. Changes in unrestricted net assets, which are excluded from the operating indicator, include the effective portion of the change in fair value of interest rate swap agreements and contributions of long-lived assets, including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets.

Advertising Costs

Advertising costs are expensed as incurred.

Income Taxes

The Hospital and CRNA are tax-exempt corporations as described in Section 501(c)(3) of the Internal Revenue Code (the "Code") and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. The Hospital and CRNA are also exempt from state income taxes on related income. Passavant Physician Association is a for-profit entity and subject to federal and state income taxes.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Income Taxes (Continued)

In order to account for any uncertain tax positions, the Association determines whether it is more likely than not that a tax position will be sustained upon examination on the technical merits of the position assuming the taxing authority has full knowledge of all information. If the tax position does not meet the more-likely-than-not recognition threshold, the benefit of that position is not recognized in the financial statements. The Association recorded no assets or liabilities for uncertain tax positions in 2012 or 2011 as management believes the Association has no material unrecognized income tax positions. Federal tax returns for tax years 2008 and beyond remain subject to examination by the Internal Revenue Service.

Deferred income taxes are provided under the liability method. Deferred tax assets and liabilities are determined based upon the difference between the consolidated financial statement and tax bases of assets and liabilities, as measured by the enacted tax rates which will be in effect when these differences are expected to reverse. The provision for deferred taxes is the result of changes in the deferred tax assets and liabilities.

Subsequent Events

Subsequent events have been evaluated through January 16, 2013, which is the date the consolidated financial statements were available to be issued.

Note 2 **Reimbursement Arrangements With Third-Party Payers**

The Association has agreements with third-party payers that provide for reimbursement at amounts which vary from its established rates. A summary of the basis of reimbursement with major third-party payers follows:

Medicare - Inpatient acute care services are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient nonacute services related to Medicare beneficiaries are paid based on a cost-reimbursement methodology. Outpatient services are paid primarily on prospectively determined rates, also based on a patient classification system, or fixed fee schedules.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 2 Reimbursement Arrangements With Third-Party Payers (Continued)

Medicaid - Inpatient services rendered to Medicaid program beneficiaries are paid primarily at prospectively determined rates per discharge. These rates vary according to a patient classification system based on clinical, diagnostic, and other factors similar to the Medicare system. Outpatient services are paid on a prospectively determined rate per occasion of service.

Physician services - Reimbursement for physician services rendered is based on charges, discounted charges, or in the case of government programs, prospectively determined reimbursement rates.

Blue Cross - The majority of Blue Cross subscribers are paid under a Preferred Provider Organization (PPO) plan. The Blue Cross PPO plan reimburses the Association for inpatient services based on the lesser of net covered charges or the established per diem rate. Outpatient services are reimbursed based on a specified discount from charges. Blue Cross processes claims under a uniform payment plan or an interim basis subject to monthly reconciliation between actual payments received and the agreed-upon contractual amounts. The monthly reconciliation process results in the recognition of a liability that will be liquidated within 60 days.

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

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 2 Reimbursement Arrangements With Third-Party Payers (Continued)

Accounting for Contractual Arrangements

The Hospital is reimbursed by Medicare for certain cost reimbursable items at an interim rate, and final settlements are determined after audit of the Hospital's related annual cost report. Estimated provisions to approximate the final expected settlements after review by the fiscal intermediary are included in the accompanying consolidated financial statements. The Hospital's cost reports have been audited by the Medicare fiscal intermediary through September 30, 2007.

During 2012 and 2011, approximately 39% and 43%, respectively, of patient service revenue (net of contractual allowances and discounts) related to patients participating in the Medicare and Medicaid programs.

On November 21, 2006, the Centers for Medicare & Medicaid Services (CMS) approved state of Illinois (the "State") legislation for a Medicaid Hospital Assessment Program (the "Program") relating to the period June 30, 2006 through June 30, 2008. On August 19, 2008, CMS approved the State's legislation for an extension of the Program to June 30, 2013. Under the Program, the Hospital pays the state an assessment based on the Hospital's adjusted gross hospital revenue and receives additional Medicaid reimbursement from the State. Total reimbursement revenue recognized by the Hospital relating to the Program for 2012 and 2011 amounted to \$3,799,540 in each year and is included in net patient service revenue in the accompanying consolidated statements of operations. The Hospital incurred assessment expenses for 2012 and 2011 of \$1,099,545 in each year, included in supplies and other expense in the accompanying consolidated statements of operations.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 2 Reimbursement Arrangements With Third-Party Payers (Continued)

Compliance

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations, particularly those relating to the Medicare and Medicaid programs, can be subject to government review and interpretation, as well as regulatory actions unknown and unasserted at this time. Violation of these laws and regulations could result in the imposition of fines and penalties, as well as repayments of previously billed and collected revenue from patient services. Management believes that the Association is in substantial compliance with current laws and regulations.

CMS uses recovery audit contractors (RACs) as part of CMS's further efforts to ensure accurate payments. RACs search for potentially inaccurate Medicare payments which may have been made to health care providers and not detected through existing CMS program integrity efforts. Once a RAC identifies a claim it believes is inaccurate, it makes a deduction from or addition to the provider's Medicare reimbursement in an amount estimated to equal the overpayment or underpayment. The outcome of any potential reviews is unknown and cannot be reasonably estimated as of September 30, 2012.

Note 3 Patient Accounts Receivable

Patient accounts receivable consisted of the following at September 30:

	2012	2011
Patient accounts receivable	\$ 48,572,927	\$ 36,868,609
Less:		
Contractual adjustments	25,401,918	14,547,322
Allowance for doubtful accounts	7,105,975	8,342,048
Patient accounts receivable - Net	\$ 16,065,034	\$ 13,979,239

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 3 Patient Accounts Receivable (Continued)

The Association decreased its allowance for doubtful accounts from 20.5% to 12.7% of gross accounts receivable at September 30, 2012. A majority of the decrease resulted from the inflation of gross accounts receivable related to significantly delayed Medicaid payments due from the State. Amounts written off during 2012 for self-pay patients and third-party payers were approximately \$5,400,000 and \$3,000,000, respectively. The Association increased its allowance for doubtful accounts from 17.3% to 20.5% of gross accounts receivable at September 30, 2011. This increase resulted from trends experienced in the collection of amounts from self-pay patients and third-party payers. Amounts written off during 2011 for self-pay patients and third-party payers were approximately \$5,500,000 and \$3,000,000, respectively.

Note 4 Short-Term Investments and Assets Limited as to Use

Short-Term Investments

Short-term investments consisted of the following at September 30:

	2012	2011
Cash equivalents	\$ 24,734	\$ 31,740
Mutual funds	6,156,769	3,020,101
Total short-term investments	\$ 6,181,503	\$ 3,051,841

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 4 Short-Term Investments and Assets Limited as to Use (Continued)

Assets limited as to use consisted of the following at September 30:

	2012	2011
Board designated for future specific purposes	\$ 44,828,044	\$ 38,432,137
Restricted by donors	4,072,317	4,025,130
Funds held by trustees under bond indenture agreements	2,556,079	2,532,762
Total assets limited as to use	51,456,440	44,990,029
Less - Current portion	965,000	935,000
Assets limited as to use - Less current portion	\$ 50,491,440	\$ 44,055,029

Assets limited as to use are invested as follows at September 30:

	2012	2011
Cash and cash equivalents	\$ 4,524,286	\$ 4,900,845
Certificates of deposit	669,599	445,402
U.S. government and agency obligations	2,092,918	4,572,316
Corporate obligations	8,781,480	7,743,102
Mutual funds	25,106,643	17,368,903
Real estate investment trusts	77,854	37,902
Equity securities	6,973,888	6,687,797
Farmland	3,098,609	3,104,610
Accrued income	131,163	129,152
Total assets limited as to use	\$ 51,456,440	\$ 44,990,029

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 4 Short-Term Investments and Assets Limited as to Use (Continued)

Investment Income

Investment income, including gains and losses on cash equivalents, investments, and assets limited as to use, consisted of the following for the years ended September 30:

	2012	2011
Unrestricted net assets:		
Other operating revenue	\$ 1,527	\$ 4,167
Other income (expense):		
Interest and dividends	2,712,281	1,950,176
Net realized gains (losses)	(40,958)	66,867
Net unrealized gains (losses)	4,331,132	(1,480,215)
Total other income (expense)	7,002,455	536,828
Temporarily restricted net assets	(33,469)	(23,155)
Total investment income	\$ 6,970,513	\$ 517,840

Investments, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investments, it is reasonably possible that changes in the values of certain investments will occur in the near term and that such changes could materially affect the amounts reported in the consolidated financial statements.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 5 Fair Value Measurements

Following is a description of the valuation methodology used for assets and liabilities measured at fair value:

Money market funds, classified as cash equivalents, are valued using \$1 as the net asset value ("NAV"). Mutual funds and real estate investment trusts are valued at quoted market prices which represents the NAV of shares held by the Association at year-end. U.S. government and agency obligations and domestic corporate and foreign obligations are valued using quotes from pricing vendors based on recent trading activity and other observable market data. Domestic and foreign equity securities are valued at quoted market prices in active markets. The interest rate swap agreements are valued based on estimates by a third-party valuation service, which uses a discounted cash flow analysis using observable market-based inputs, including forward interest rate curves.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Association believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 5 Fair Value Measurements (Continued)

The following table sets forth by level, within the fair value hierarchy, the Association's assets and liabilities at fair value as of September 30:

	2012			Total
	Level 1	Level 2	Level 3	Assets/Liabilities at Fair Value
Assets:				
Money market funds	\$ -	\$ 4,424,946	\$ -	\$ 4,424,946
U.S. Government and agency obligations	-	2,092,918	-	2,092,918
Domestic corporate obligations	-	8,522,280	-	8,522,280
Foreign obligations	-	259,200	-	259,200
Fixed income mutual funds	13,721,432	-	-	13,721,432
Balanced mutual funds	1,683,439	-	-	1,683,439
Equity mutual funds	15,395,774	-	-	15,395,774
International mutual funds	462,767	-	-	462,767
Real estate investment trusts	77,854	-	-	77,854
Domestic equity securities	6,547,255	-	-	6,547,255
Foreign equity securities	426,633	-	-	426,633
Total assets	\$ 38,315,154	\$ 15,299,344	\$ -	\$ 53,614,498
Liabilities - Interest rate swap agreements				
	\$ -	\$ 3,267,404	\$ -	\$ 3,267,404

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 5 Fair Value Measurements (Continued)

	2011			Total Assets/Liabilities at Fair Value
	Level 1	Level 2	Level 3	
Money market funds	\$ -	\$ 4,753,796	\$ -	\$ 4,753,796
U.S. Government and agency obligations	-	4,572,316	-	4,572,316
Domestic corporate obligations	-	7,482,387	-	7,482,387
Foreign obligations	-	260,715	-	260,715
Fixed income mutual funds	6,559,651	-	-	6,559,651
Balanced mutual funds	1,462,833	-	-	1,462,833
Equity mutual funds	12,115,476	-	-	12,115,476
International mutual funds	251,044	-	-	251,044
Real estate investment trusts	37,902	-	-	37,902
Domestic equity securities	6,237,118	-	-	6,237,118
Foreign equity securities	450,679	-	-	450,679
Total assets	\$ 27,114,703	\$ 17,069,214	\$ -	\$ 44,183,917
Liabilities - Interest rate swap agreements	\$ -	\$ 3,160,290	\$ -	\$ 3,160,290

Note 6 Property and Equipment

Property and equipment consisted of the following at September 30:

	2012	2011
Land and land improvements	\$ 3,469,929	\$ 3,583,991
Buildings and improvements	84,423,734	83,001,898
Equipment	40,712,685	38,037,230
Total property and equipment	128,606,348	124,623,119
Less - Accumulated depreciation	82,070,781	75,986,485
Net depreciated value	46,535,567	48,636,634
Construction in progress	2,471,644	2,075,125
Property and equipment - Net	\$ 49,007,211	\$ 50,711,759

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 6 Property and Equipment (Continued)

Equipment under capital lease had an original cost of \$2,708,831, and accumulated amortization of \$386,616 and \$242,830 at September 30, 2012 and 2011, respectively.

Depreciation expense on property and equipment totaled \$6,140,838 and \$6,191,538 for the years ended September 30, 2012 and 2011, respectively.

Construction in progress at September 30, 2012 and 2011, relates to various renovation projects.

Note 7 Long-Term Debt

Long-term debt consisted of the following at September 30:

	2012	2011
Revenue Bonds (Series 2006A), variable interest rate of 2.24% at September 30, 2012, maturing December 2031	\$ 17,375,000	\$ 17,925,000
Revenue Bonds (Series 2006B), variable interest rate of 2.24% at September 30, 2012, maturing December 2031	10,670,000	11,055,000
Capital lease obligations, due through November 2016, collateralized by property and equipment	1,659,567	2,056,659
Jacksonville Savings Bank equipment note, variable interest rate of 3.25% at September 30, 2012, maturing September 2025	1,674,620	-
Totals	31,379,187	31,036,659
Less - Current maturities	1,475,400	1,332,534
Long-term portion	\$ 29,903,787	\$ 29,704,125

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 7 Long-Term Debt (Continued)

The Series 2006A and 2006B Bonds consist of adjustable rate demand industrial revenue bonds (the "Bonds") in the original amounts of \$19,905,000 and \$12,485,000, respectively, both issued December 14, 2006. The variable rate interest on the Bonds is adjusted daily and is payable monthly. Principal is payable in annual installments through 2031.

The city of Jacksonville, Illinois (the "City") issued the Bonds on behalf of the Association. The proceeds of the Bonds were loaned to the Association under a trust indenture and loan agreement dated December 1, 2006. The proceeds of the Series 2006A Bonds were to provide funds for the advance refunding and defeasance of previous borrowings. The proceeds of the Series 2006B Bonds were to provide funds for the construction and development of budgeted capital expenditures and campus-wide refurbishments. The trust indenture requires that certain funds be established with the trustee. These funds are included in assets limited as to use in the accompanying consolidated balance sheets.

Prior to December 2010, the Bonds were secured by an irrevocable direct pay letter of credit with Comerica Bank. In December 2010, the outstanding bonds were purchased by Comerica Bank and the bond documents were amended. Under the amended agreement, the Bonds are paid under the original scheduled revenue bond maturities until the fifth year, at which time the bonds are subject to tender for mandatory purchase by Comerica Bank. However, Comerica Bank may elect to continue to hold the bonds. In the event Comerica Bank does not elect to hold the bonds, the bonds would be remarketed. Management believes if Comerica Bank does not continue to hold the bonds, then the Association will be able to successfully remarket the bonds. Accordingly, the schedule principal payments following reflect the original scheduled maturities.

The bank qualified bond agreements require the Association to comply with certain restrictive covenants, including minimum insurance coverage, restrictions on the incurrence of additional indebtedness, and maintenance of certain leverage, liquidity, and debt service coverage ratios. Management believes the Association is in compliance with restrictive covenants at September 30, 2012.

The Bonds are collateralized by substantially all of the property of the Association.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 7 Long-Term Debt (Continued)

The Association may borrow up to \$2,100,000 on the Jacksonville Savings Bank equipment note. The funds are being drawn down by the Association as equipment is purchased. Principal and interest is due quarterly beginning December 2012. The note bears interest at the prime rate minus 2.0% with a maximum rate of 6.5% and a minimum rate of 3.25%. The note is collateralized by a security interest in the Association's patient accounts receivable.

Scheduled principal payments on the Revenue Bonds and the equipment note at September 30, 2012 are summarized as follows:

2013	\$ 1,057,126
2014	1,114,413
2015	1,153,063
2016	1,196,713
2017	1,240,729
Thereafter	23,957,576
Total	<u>\$ 29,719,620</u>

Minimum future payments under the capital lease obligations at September 30, 2011, are as follows:

2013	\$ 489,578
2014	489,578
2015	379,459
2016	370,584
2017	95,452
Total minimum lease payments	1,824,651
Less - Amount representing interest	<u>165,084</u>
Capital lease obligations	<u>\$ 1,659,567</u>

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 8 Interest Rate Swap Agreements

As a strategy to maintain acceptable levels of exposure to the risk of changes in the future cash flows due to interest rate fluctuations, the Association entered into two interest rate swap agreements on its floating rate Series 2006A and 2006B Bonds. The agreements provide for the Association to receive interest from the counterparties at 67% of LIBOR and to pay interest to the counterparties at a fixed rate of 2.95% and 3.45% on notional amounts of \$17,375,000 and \$10,670,000, respectively.

Management has designated the interest rate swap agreements as cash flow hedging instruments and has determined that the agreements are highly effective. The fair value of the interest rate swap agreements at September 30, 2012 and 2011, was a liability of \$3,267,404 and \$3,160,290, respectively. The change in fair value of the interest rate swap agreements was \$107,114 and \$295,933 for the years ended September 30, 2012 and 2011, respectively, representing decreases in unrestricted net assets in the accompanying consolidated financial statements.

Note 9 Charity Care and Community Benefit

In support of its mission, the Association voluntarily provides free care, or care at substantially reduced fees, to patients who lack financial resources and are deemed to be medically indigent. Because the Association does not pursue collection of amounts determined to qualify as charity care, they are not reported in net patient service revenue.

During 2011, the Association changed its policy for recording charity care to include accounts that have been returned from a collection agency after collection efforts have been exhausted.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 9 Charity Care and Community Benefit (Continued)

The amount of charges foregone for services and supplies furnished under the Association's charity care policy were as follows:

	2012	2011
Charity care allowances	\$ 11,090,715	\$ 10,697,100
Volunteer free clinic allowances	915,602	1,288,776
Charity care and partially reimbursed care based on charges foregone	\$ 12,006,317	\$ 11,985,876

In addition, the Association provides services to other medically indigent patients under certain government-reimbursed public aid programs. Such programs pay providers amounts which are less than established charges for the services provided the recipients, and many times, the payments are less than the cost of rendering the services provided.

The Association's total cost of uncompensated care relating to these and other services are approximated as follows:

	2012	2011
State Medicaid and other public aid programs	\$ 8,004,000	\$ 7,840,000
Less - State critical hospital adjustment payments	564,000	590,000
Uncompensated cost of public aid programs - Net	7,440,000	7,250,000
Charity care, at cost	4,080,000	4,220,000
Total cost of uncompensated care	\$ 11,520,000	\$ 11,470,000

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 9 Charity Care and Community Benefit (Continued)

The estimated net uncompensated cost of state Medicaid and other public aid programs is determined by computing the cost of providing the care less amounts paid by the programs. State Medicaid and other public aid programs above exclude the activity of the Illinois Hospital Medical Assessment Program (see Note 2). The estimated cost of providing care to patients under public aid programs and the Association's charity care policy is calculated by multiplying the ratio of cost to gross charges by the gross uncompensated care charges.

In addition to the above cost of uncompensated care, the Association also commits significant time and resources to endeavors and services which meet otherwise unfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. Such programs include health screening and assessments, childbirth education programs, support to the local hospice program, "Doorbell Dinners" for elder shut-ins, free community education programs, and a variety of support groups.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 10 Patient Service Revenue (Net of Contractual Allowances and Discounts)

The following table sets for the detail of patient service revenue (net of contractual allowances and discounts) prior to the provision for bad debts for the years ended September 30:

	2012	2011
Gross patient service revenue:		
Hospital inpatient	\$ 74,617,769	\$ 71,477,018
Hospital outpatient	158,591,242	146,523,321
Physician services	8,129,175	8,142,276
Total gross patient service revenue	241,338,186	226,142,615
Deductions - Primarily contractual adjustments and third-party reimbursement agreements	154,724,189	137,664,564
Patient service revenue (net of contractual allowances and discounts)	\$ 86,613,997	\$ 88,478,051

Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the years ended September 30, from these major payer sources, is as follows:

	2012	2011
Medicare, Medicaid, Health Maintenance Organization (HMO) Plans, and other third-party payers	\$ 73,217,282	\$ 75,772,257
Uninsured patients	13,396,715	12,705,794
Patient service revenue (net of contractual allowances and discounts)	\$ 86,613,997	\$ 88,478,051

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 11 Self-Insured Health Benefits

Substantially all of the Association's employees are eligible to participate in the Association's health insurance plan. The Association is self-insured for health claims of participating employees and dependents up to limits provided for in an agreement with its insurance plan administrator. A provision is accrued for self-insured employee health claims, including both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims, and other economic and social factors. The Association is insured for paid claims for a covered person during the year in excess of \$225,000. The Association recorded approximately \$7,739,000 and \$7,069,000 of expense related to the self-insured plan for the years ended September 30, 2012 and 2011, respectively. The amount accrued for self-insured employee health claims was \$422,000 and \$611,000 at September 30, 2012 and 2011, respectively, and is included in accrued liabilities in the accompanying consolidated balance sheets.

In addition, during 2009 the Association offered, as an incentive for early retirement, health insurance coverage to retirees and their spouses until the employee or their spouse, whichever is younger, reaches age 65. The amount accrued for the retiree health insurance was \$862,265 and \$894,882 at September 30, 2012 and 2011, respectively, and is included in accrued liabilities in the accompanying consolidated balance sheets.

Note 12 Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets include assets set aside in accordance with donor restrictions as to time or use. Temporarily restricted net assets were available for the following purposes at September 30:

	2012	2011
Health education	\$ 345,563	\$ 366,119
To purchase equipment	10,000	10,000
To support health care services	367,473	367,473
Total temporarily restricted net assets	\$ 723,036	\$ 743,592

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 12 Temporarily and Permanently Restricted Net Assets (Continued)

Permanently restricted net assets have been restricted by donors to be maintained in perpetuity, the income of which is expendable to support the following at September 30:

	2012	2011
To support health care services	\$ 19,709,309	\$ 16,627,724
To purchase equipment	46,594	46,594
To provide indigent care	2,000	2,000
Total permanently restricted net assets	\$ 19,757,903	\$ 16,676,318

Note 13 Pension Plan

The Association sponsors a defined contribution pension plan, which is available to substantially all Association employees. The Association contributes an amount equal to 6.0% of each participant's annual compensation. Pension expense was approximately \$1,711,000 and \$1,652,000 in 2012 and 2011, respectively.

Note 14 Malpractice Insurance

The Association has joined together with other providers of health care services to form the Illinois Provider Trust and the Illinois Compensation Trust, two risk pools (the "Pools") currently operating as common risk management and insurance programs for its members. The Association pays annual premiums to the Pools for its general liability torts, medical malpractice, and employee injuries insurance coverage. The Pools' governing agreements specify that the Pools will be self-sustaining through member premiums and will reinsure through commercial carriers for claims in excess of specified stop-loss amounts.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 14 Malpractice Insurance (Continued)

The Association purchases medical malpractice insurance described above under a claims-made policy on a fixed premium basis. The policy is maintained for claim losses of \$7,000,000 for each occurrence. Under a claims-made policy, the risk for claims and incidents not asserted within the policy period remains with the Association. The Association does not believe potential claims are significant; however, the Association has recorded a liability of \$300,000 related to the insurance deductible amounts for three potential claims from services provided to patients through September 30, 2012.

At September 30, 2012, the Association had letters of credit for employee injuries insurance coverage of approximately \$1,032,000.

Note 15 Functional Expenses

The Association provides general health care services to residents within its geographic location. Expenses related to providing these services consisted of the following:

	2012	2011
Health care services	\$ 68,665,601	\$ 67,120,181
General and administrative	17,492,361	16,758,765
Total expenses	\$ 86,157,962	\$ 83,878,946

Note 16 Commitments and Contingencies

The Association is subject to legal proceedings and claims that arise in the ordinary course of business. Any such proceedings or litigation have an element of uncertainty. Management of the Association is not able to estimate the amount of any settlements related to pending or threatened actions at this time.

Passavant Area Hospital Association and Affiliates

Notes to Consolidated Financial Statements

Note 17 Concentration of Credit Risk

Financial instruments that potentially subject the Association to possible credit risk consist principally of accounts receivable, cash deposits in excess of insured limits, and investments.

Accounts receivable consist of amounts due from patients, their insurers, or governmental agencies (primarily Medicare and Medicaid) for health care provided to the patients. The majority of the Association's patients are from Jacksonville, Illinois, and the surrounding area.

The mix of receivables from patients and third-party payers was as follows at September 30:

	2012	2011
Medicare	19 %	23 %
Medicaid	38 %	21 %
Other third-party payers	30 %	39 %
Patients	13 %	17 %
Totals	100 %	100 %

The Company maintains depository relationships with area financial institutions that are Federal Depository Insurance Corporation (FDIC) insured institutions. On November 9, 2010, the FDIC issued a final rule implementing section 343 of the Dodd-Frank Wall Street Reform and Consumer Protection Act that provides for unlimited insurance coverage of non-interest-bearing transaction accounts through December 31, 2012. In addition, the Hospital maintains cash in interest-bearing accounts at these institutions which are insured by the FDIC up to \$250,000. At September 30, 2012, the Association exceeded the insured limits by \$7,388,000. In addition, other investments held by financial institutions are uninsured.

Note 18 Reclassifications

Certain reclassifications have been made to the 2011 financial statements to conform to the 2012 classifications.

Supplementary Information



Independent Auditor's Report on Supplementary Information

Board of Directors
Passavant Area Hospital Association
Jacksonville, Illinois

We have audited the basic consolidated financial statements of Passavant Area Hospital Association and Affiliates for the years ended September 30, 2012 and 2011, and our report thereon dated January 16, 2013 which expressed an unqualified opinion on those consolidated financial statements, appears on page 1. Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The supplementary information appearing on pages 39 through 45 is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the basic consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly presented in all material respects in relation to the basic consolidated financial statements taken as a whole.

Wipfli LLP

Wipfli LLP

January 16, 2013
Milwaukee, Wisconsin

Passavant Area Hospital Association and Affiliates

Net Patient Service Revenue

Years Ended September 30, 2012 and 2011

	2012			2011		
	Inpatient	Outpatient	Total	Inpatient	Outpatient	Total
Daily patient services:						
Medical and surgical	\$ 16,647,403	\$ 887,324	\$ 17,534,727	\$ 15,895,438	\$ 911,243	\$ 16,806,681
Pediatrics	275,820	77,670	353,490	407,292	94,618	501,910
Critical care	3,971,092	13,920	3,985,012	3,648,673	23,419	3,672,092
Obstetrics	1,432,190	570,868	2,003,058	1,213,064	345,200	1,558,264
Newborn nurseries	943,924	-	943,924	805,432	-	805,432
Skilled nursing	3,389,455	-	3,389,455	2,942,803	-	2,942,803
Total daily patient services	26,659,884	1,549,782	28,209,666	24,912,702	1,374,480	26,287,182
Other nursing services:						
Operating and recovery	17,586,400	37,316,751	54,903,151	16,213,729	32,918,705	49,132,434
Delivery	694,960	-	694,960	596,872	-	596,872
Anesthesiology	1,292,287	3,165,347	4,457,634	1,245,466	2,812,989	4,058,455
Certified registered nurse anesthetist	-	4,799,277	4,799,277	173,670	4,058,121	4,231,791
Central services and supply	3,029,095	1,497,325	4,526,420	2,823,676	1,544,506	4,368,182
Emergency	2,037,904	11,475,150	13,513,054	2,094,336	10,622,616	12,716,952
Emergency physician	527,655	3,513,397	4,041,052	1,317,654	8,290,419	9,608,073
Cardiac rehabilitation	-	319,033	319,033	156	293,833	293,989
Total other nursing services	25,168,301	62,086,280	87,254,581	24,465,559	60,541,189	85,006,748

Passavant Area Hospital Association and Affiliates

Net Patient Service Revenue (Continued)

Years Ended September 30, 2012 and 2011

	2012			2011		
	Inpatient	Outpatient	Total	Inpatient	Outpatient	Total
Other professional services:						
Laboratories	\$ 9,515,931	\$ 20,511,647	\$ 30,027,578	\$ 9,015,735	\$ 19,098,643	\$ 28,114,378
Radiology	1,787,485	13,318,044	15,105,529	1,719,675	13,081,732	14,801,407
CT scan	3,150,890	22,987,183	26,138,073	3,144,504	19,341,109	22,485,613
MRI scan	365,460	8,108,527	8,473,987	279,504	7,650,261	7,929,765
Nuclear medicine	276,694	3,165,556	3,442,250	291,325	2,631,854	2,923,179
Sonography	354,919	4,078,824	4,433,743	405,335	3,833,921	4,239,256
Pharmacy and intravenous therapy	10,112,820	7,796,337	17,909,157	9,842,399	7,348,469	17,190,868
Chemotherapy	1,031	2,341	3,372	4,182	1,803	5,985
Inhalation therapy	4,301,745	991,722	5,293,467	4,281,911	954,834	5,236,745
Electrocardiology	534,074	2,924,707	3,458,781	507,425	2,584,029	3,091,454
Physical therapy	1,890,890	4,948,021	6,838,911	1,766,367	4,091,966	5,858,333
Occupational therapy	1,430,070	729,496	2,159,566	1,399,438	599,276	1,998,714
Speech therapy	66,119	311,441	377,560	83,791	260,209	344,000
Other therapy	(55)	1,827,731	1,827,676	7,520	1,578,512	1,586,032
WOC clinic	48,757	1,759,889	1,808,646	38,388	1,377,066	1,415,454
Electroencephalography	10,959	89,665	100,624	6,579	129,703	136,282
Aquatic therapy	-	968,586	968,586	-	529,689	529,689
Hyperbarics	32,510	1,348,854	1,381,364	1,779	803,352	805,131
CHF clinic	-	2,211	2,211	-	-	-
Clinic	-	8,129,175	8,129,175	-	8,142,276	8,142,276
Total other professional services	33,880,299	103,999,957	137,880,256	32,795,857	94,038,704	126,834,561
Gross patient service revenue before charity care	85,708,484	167,636,019	253,344,503	82,174,118	155,954,373	238,128,491
Less - Charity care	11,090,715	915,602	12,006,317	10,697,100	1,288,776	11,985,876
Gross patient service revenue	\$ 74,617,769	\$ 166,720,417	\$ 241,338,186	\$ 71,477,018	\$ 154,665,597	\$ 226,142,615

Passavant Area Hospital Association and Affiliates

Net Patient Service Revenue (Continued)

Years Ended September 30, 2012 and 2011

	2012	2011
Gross patient service revenue (carried forward)	\$ 241,338,186	\$ 226,142,615
Deductions:		
Medicare	84,100,036	73,280,781
Medicaid	29,060,208	25,074,065
Other contractual adjustments	38,120,221	36,648,373
Other allowances	3,443,724	2,661,345
Total deductions	154,724,189	137,664,564
Patient service revenue (net of contractual allowances and discounts)	86,613,997	88,478,051
Less - Provision for bad debts	29,039	4,332,978
Net patient service revenue	\$ 86,584,958	\$ 84,145,073

Passavant Area Hospital Association and Affiliates

Other Revenue

Years Ended September 30, 2012 and 2011

	2012	2011
Space rental	\$ 557,051	\$ 563,131
Cafeteria	580,125	547,875
Life line	179,606	190,396
Investment return - Bond funds	1,527	4,167
Miscellaneous	559,705	306,795
Health education	21,605	18,698
Net assets released from restrictions	57,463	4,594
Gain (loss) on disposal of equipment	(24,227)	(15,166)
Total other revenue	\$ 1,932,855	\$ 1,620,490

Passavant Area Hospital Association and Affiliates

Expenses

Years Ended September 30, 2012 and 2011

	2012			2011		
	Salaries and Wages	Supplies and Expense	Total	Salaries and Wages	Supplies and Expense	Total
Nursing services:						
Nursing administration	\$ 704,286	\$ 56,807	\$ 761,093	\$ 805,871	\$ 44,344	\$ 850,215
Medical and surgical	3,412,539	231,579	3,644,118	3,277,711	256,417	3,534,128
Pediatrics	237,366	21,131	258,497	267,581	29,993	297,574
Critical care	928,424	85,325	1,013,749	888,470	85,083	973,553
Obstetrics	413,396	50,074	463,470	405,430	43,174	448,604
Newborn nurseries	283,206	33,383	316,589	251,936	28,812	280,748
Skilled nursing	734,631	63,007	797,638	711,185	39,221	750,406
Operating and recovery	3,545,927	5,546,740	9,092,667	3,316,317	5,078,539	8,394,856
Delivery	70,801	-	70,801	62,984	-	62,984
Anesthesiology	-	345,507	345,507	-	276,985	276,985
Certified registered nurse anesthetist	2,677,520	-	2,677,520	2,459,680	-	2,459,680
Central services and supply	102,889	437,483	540,372	103,694	461,222	564,916
Emergency and outpatient	3,172,195	487,478	3,659,673	2,986,925	457,341	3,444,266
Emergency physician	1,215,594	759,045	1,974,639	2,714,544	438,397	3,152,941
Cardiac rehabilitation	125,179	16,466	141,645	120,388	14,304	134,692
Total nursing services	17,623,953	8,134,025	25,757,978	18,372,716	7,253,832	25,626,548
Other professional services:						
Laboratories	1,848,539	1,882,341	3,730,880	1,770,024	2,001,232	3,771,256
Radiology	1,198,446	481,884	1,680,330	1,157,943	438,703	1,596,646
CT scan	352,714	234,753	587,467	345,813	234,819	580,632
MRI scan	206,753	133,200	339,953	202,162	140,306	342,468
Nuclear medicine	150,099	266,093	416,192	147,517	215,881	363,398
Sonography	231,674	36,689	268,363	251,467	41,752	293,219
Pharmacy	700,991	2,447,621	3,148,612	684,602	2,525,528	3,210,130
Inhalation therapy	446,789	212,262	659,051	455,923	124,640	580,563
Electrocardiology	49,280	49,983	99,263	49,359	38,222	87,581
Physical therapy	1,252,057	323,102	1,575,159	1,140,491	139,326	1,279,817

Passavant Area Hospital Association and Affiliates

Expenses (Continued)

Years Ended September 30, 2012 and 2011

	2012			2011		
	Salaries and Wages	Supplies and Expense	Total	Salaries and Wages	Supplies and Expense	Total
Other professional services (continued):						
Speech therapy	\$ 167,000	\$ 7,478	\$ 174,478	\$ 163,153	\$ 6,352	\$ 169,505
Occupational therapy	337,696	16,136	353,832	307,832	6,728	314,560
Other therapies	76,287	144,156	220,443	71,319	124,813	196,132
Electroencephalography	7,733	2,717	10,450	6,631	2,532	9,163
Medical records	600,850	73,121	673,971	586,712	54,131	640,843
Social service	-	-	-	-	11	11
Utilization review	377,251	198,195	575,446	322,381	69,187	391,568
Quality assurance and risk management	322,768	338,576	661,344	391,330	295,636	686,966
Health education and library	244,588	78,404	322,992	221,967	56,858	278,825
Infection control	76,646	8,153	84,799	74,928	4,581	79,509
Clinics	3,634,049	2,049,143	5,683,192	3,443,154	1,974,449	5,417,603
Aquatic therapy	152,092	87,413	239,505	93,447	85,661	179,108
Hyperbarics	81,549	56,906	138,455	32,010	209,589	241,599
WOC clinic	385,977	390,981	776,958	359,252	249,076	608,328
CHF clinic	3,509	1,848	5,357	-	-	-
Total other professional services	12,905,337	9,521,155	22,426,492	12,279,417	9,040,013	21,319,430
General services:						
Dietary and cafeteria	1,096,180	1,094,372	2,190,552	1,070,058	1,070,485	2,140,543
Operation of plant	907,732	1,823,075	2,730,807	899,829	2,010,005	2,909,834
Housekeeping	844,945	100,815	945,760	824,547	90,422	914,969
Laundry and linen	196,768	99,390	296,158	190,920	135,835	326,755
Communications	-	88,243	88,243	615	76,911	77,526
Total general services	3,045,625	3,205,895	6,251,520	2,985,969	3,383,658	6,369,627

Passavant Area Hospital Association and Affiliates

Expenses (Continued)

Years Ended September 30, 2012 and 2011

	2012			2011		
	Salaries and Wages	Supplies and Expense	Total	Salaries and Wages	Supplies and Expense	Total
Administrative services:						
Administrative	\$ 4,713,592	\$ 6,116,038	\$ 10,829,630	\$ 3,814,630	\$ 5,924,060	\$ 9,738,690
Employee benefits	-	13,148,842	13,148,842	-	13,068,643	13,068,643
Total administrative services	4,713,592	19,264,880	23,978,472	3,814,630	18,992,703	22,807,333
Depreciation and amortization	-	6,179,020	6,179,020	-	6,195,009	6,195,009
Interest	-	1,564,480	1,564,480	-	1,560,999	1,560,999
Total expenses	\$ 38,288,507	\$ 47,869,455	\$ 86,157,962	\$ 37,452,732	\$ 46,426,214	\$ 83,878,946

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**MEMORIAL HEALTH SYSTEM
THE PASSAVANT MEMORIAL AREA HOSPITAL ASSOCIATION
Certificate of Exemption Index**

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