HOSPITAL SISTERS SERVICES, INC. –
OBLIGATED GROUP
Springfield, Illinois

Consolidated Financial Statements and Supplementary Information

June 30, 2010 and 2009

(With Independent Auditors’ Report Thereon)

KPMG LLP
303 East Wacker Drive
Chicago, IL 60601-5212

Independent Auditors' Report

The Board of Directors
Hospital Sisters Services, Inc.:

We have audited the accompanying consolidated balance sheets of Hospital Sisters Services, Inc. – Obligated Group (the Obligated Group) as of June 30, 2010 and 2009, 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 Obligated Group'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 of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Obligated Group's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall 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 Hospital Sisters Services, Inc. – Obligated Group as of June 30, 2010 and 2009, and the results of its operations, changes in net assets, and cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

Our 2010 audit was made for the purpose of forming an opinion on the basic 2010 consolidated financial statements taken as a whole. The 2010 consolidating information included in schedules 1 – 3 is presented for purposes of additional analysis of the basic 2010 consolidated financial statements rather than to present the financial position, results of operations, and changes in net assets of the individual entities. The 2010 consolidating information has been subjected to the auditing procedures applied in the audit of the basic 2010 consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic 2010 consolidated financial statements taken as a whole.

KPMG LLP

October 11, 2010

HOSPITAL SISTERS SERVICES, INC. –
OBLIGATED GROUP
Springfield, Illinois

Consolidated Balance Sheets

June 30, 2010 and 2009

(Dollars in thousands)

Assets		**2010**	**2009**
Current assets:			
Cash and cash equivalents	$	45,063	57,812
Receivables:			
Patients' accounts, less allowance for uncollectible accounts of $73,075 in 2010 and $70,263 in 2009		237,884	215,940
Due from third-party reimbursement programs		2,723	9,417
Other		26,350	30,271
Total receivables		266,957	255,628
Current portion of assets whose use is limited or restricted		199,138	210,333
Inventories		40,551	37,371
Prepaid expenses		16,692	19,964
Total current assets		568,401	581,108
Assets whose use is limited or restricted, net of current portion		1,387,269	1,249,312
Property, plant, and equipment, net		835,997	820,768
Other assets		70,137	89,758
Total assets	$	2,861,804	2,740,946
Liabilities and Net Assets			
Current liabilities:			
Current installments of long-term debt	$	15,475	16,900
Long-term debt subject to short-term remarketing agreements		184,771	196,190
Accounts payable		63,240	61,025
Accrued liabilities		98,218	81,416
Estimated payables under third-party reimbursement programs		30,950	32,114
Total current liabilities		392,654	387,645
Long-term debt, excluding current installments		370,088	373,343
Estimated self-insurance liabilities		51,729	56,064
Derivative instruments		36,013	24,289
Accrued benefit liability		347,854	171,628
Other noncurrent liabilities		30,353	30,990
Total liabilities		1,228,691	1,043,959
Net assets:			
Unrestricted		1,545,960	1,619,157
Temporarily restricted		66,172	57,202
Permanently restricted		20,981	20,628
Total net assets		1,633,113	1,696,987
	$	2,861,804	2,740,946

See accompanying notes to consolidated financial statements.

HOSPITAL SISTERS SERVICES, INC. –
OBLIGATED GROUP
Springfield, Illinois

Consolidated Statements of Operations

Years ended June 30, 2010 and 2009

(Dollars in thousands)

		2010	2009
Net patient service revenues	$	1,764,177	1,599,534
Other revenues:			
Investment income (loss)		9,069	(7,392)
Net assets released from restrictions used for operations		3,493	3,800
Other		50,162	51,471
Total revenues		1,826,901	1,647,413
Expenses:			
Sisters’ services		486	402
Salaries and wages		551,725	560,539
Employee benefits		187,738	171,074
Professional fees		104,913	95,557
Supplies		287,398	274,150
Depreciation and amortization		99,848	103,039
Interest		5,242	8,320
Provision for uncollectible accounts		94,904	91,561
Other		461,423	295,618
Total expenses		1,793,677	1,600,260
Income from operations		33,224	47,153
Nonoperating income (loss):			
Investment income (loss)		86,946	(125,238)
Revenues in excess (deficient) of expenses and nonoperating income (loss)		120,170	(78,085)
Other changes in unrestricted net assets:			
Net assets released from restrictions used for the purchase of property, plant, and equipment		2,107	3,064
Transfer to affiliate		(19,248)	(40,100)
Recognition of change in pension funded status		(176,226)	(161,668)
Change in unrestricted net assets	$	(73,197)	(276,789)

See accompanying notes to consolidated financial statements.

HOSPITAL SISTERS SERVICES, INC. –
OBLIGATED GROUP
Springfield, Illinois

Consolidated Statements of Changes in Net Assets

Years ended June 30, 2010 and 2009

(Dollars in thousands)

		2010	2009
Unrestricted net assets:			
Revenues in excess (deficient) of expenses and nonoperating income (loss)	$	120,170	(78,085)
Other changes in unrestricted net assets:			
Net assets released from restrictions used for the purchase of property, plant, and equipment		2,107	3,064
Transfer to affiliate		(19,248)	(40,100)
Recognition of change in pension funded status		(176,226)	(161,668)
Change in unrestricted net assets		(73,197)	(276,789)
Temporarily restricted net assets:			
Investment income (loss)		6,785	(8,342)
Contributions		7,785	7,799
Net reclassification of net assets based on donor intent		—	(831)
Net assets released from restrictions		(5,600)	(6,864)
Change in temporarily restricted net assets		8,970	(8,238)
Permanently restricted net assets:			
Investment income		35	—
Net reclassification of net assets based on donor intent		—	831
Contributions		318	2,427
Change in permanently restricted net assets		353	3,258
Change in net assets		(63,874)	(281,769)
Net assets at beginning of year		1,696,987	1,978,756
Net assets at end of year	$	1,633,113	1,696,987

See accompanying notes to consolidated financial statements.

HOSPITAL SISTERS SERVICES, INC. –
OBLIGATED GROUP
Springfield, Illinois

Consolidated Statements of Cash Flows

Years ended June 30, 2010 and 2009

(Dollars in thousands)

		2010	2009
Cash flows from operating activities:			
Change in net assets	$	(63,874)	(281,769)
Adjustments to reconcile change in net assets to net cash provided by operating activities:			
Transfer to affiliate		19,248	40,100
Recognition of changes in pension funded status		176,226	161,668
Income from equity basis investments		(5,249)	(1,113)
Permanently restricted contributions and investment return		(353)	(2,427)
Amortization of bond issuance costs and premiums, included in interest expense		241	225
Depreciation and amortization		99,848	103,039
Provision for uncollectible accounts		94,904	91,561
Change in net unrealized gain and losses on investments		(70,997)	55,982
Change in the fair value of interest rate swaps		11,724	17,973
Change in net interest in the Foundation		(9,382)	4,923
Changes in assets and liabilities:			
Patients accounts receivable		(116,848)	(69,849)
Other receivables		3,921	(718)
Inventories		(3,180)	(1,000)
Prepaid expenses		3,272	6,820
Net amounts due to third-party reimbursement programs		5,530	162
Accounts payable and accrued liabilities		19,017	4,735
Estimated self-insurance and other noncurrent liabilities		(4,972)	(4,371)
Net cash provided by operating activities		159,076	125,941
Cash flows from investing activities:			
Acquisition of property, plant, and equipment		(115,077)	(121,219)
Cash received from equity basis investments, net		316	4,639
Gross deposits into HSHS pooled investment program		(194,995)	(211,579)
Gross withdrawals from the HSHS pooled investment program		148,612	291,498
Change in other assets		24,046	(9,307)
Net cash used in investing activities		(137,098)	(45,968)
Cash flows from financing activities:			
Repayment of long-term debt		(15,832)	(13,229)
Proceeds from issuance of long-term debt, including premium		—	4,262
Transfer to affiliate		(19,248)	(40,100)
Proceeds from permanently restricted contributions and investment return		353	2,427
Net cash used in financing activities		(34,727)	(46,640)
Change in cash and cash equivalents		(12,749)	33,333
Cash and cash equivalents at beginning of year		57,812	24,479
Cash and cash equivalents at end of year	$	45,063	57,812
Supplemental disclosure of cash flow information:			
Cash paid for interest, net of amounts capitalized	$	6,337	9,252

See accompanying notes to consolidated financial statements.

(1) Organization and Purpose

Hospital Sisters Services, Inc. (HSSI), a not-for-profit holding company, is the sole corporate member of 13 hospitals in Illinois and Wisconsin (collectively referred to as the Obligated Group), Hospital Sisters Healthcare – West, Inc. (HCW), HSHS Medical Group, Inc., and HSHS Wisconsin Medical Group, Inc. (collectively referred to as the Medical Group). HSSI and the 13 hospitals have formed an Obligated Group for debt financing purposes through the use of a Master Trust Indenture (MTI) (note 12). The hospitals are organized for the purpose of providing inpatient and outpatient healthcare services. HCW and the Medical Group are not members of the Obligated Group.

The 13 hospitals who are members of the Obligated Group and whose financial information are included in the accompanying consolidated financial statements are:

Hospital	Location
	Illinois:
St. Elizabeth's Hospital	Belleville
St. Joseph's Hospital	Breese
St. Mary's Hospital	Decatur
St. Anthony's Memorial Hospital	Effingham
St. Joseph's Hospital	Highland
St. Francis Hospital	Litchfield
St. John's Hospital	Springfield
St. Mary's Hospital	Streator
	Wisconsin:
St. Joseph's Hospital	Chippewa Falls
Sacred Heart Hospital	Eau Claire
St. Mary's Hospital Medical Center	Green Bay
St. Vincent Hospital	Green Bay
St. Nicholas Hospital	Sheboygan

Hospital Sisters Health System (HSHS) is the sole corporate member of HSSI. All of the hospitals in the Obligated Group purchase certain administrative and data processing services from HSHS. Additionally, all of the hospitals in the Obligated Group participate in pooled investment funds administered by HSHS.

The Obligated Group is also related to Hospital Sisters of St. Francis Foundation, Inc. (the Foundation), an entity whose purpose is to solicit and administer philanthropic funds. The Foundation is structured into 14 separate divisions to administer restricted and unrestricted gifts and bequests at each of the respective hospital locations and the Foundation's system office. The Obligated Group records its interest in the net assets of the Foundation as a component of assets whose use is limited or restricted, in the accompanying consolidated balance sheets and its interest in contributions and related investment income as components of temporarily and permanently restricted net assets until such time that the Foundation transfers the funds to the Obligated Group.

(2) Summary of Significant Accounting Policies

In June 2009, the Financial Accounting Standards Board (FASB) issued an accounting standard, which established the Codification to become the single source of authoritative accounting principles. The standard also provides the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are represented in conformity with generally accepted accounting principles in the United States. All guidance contained in the Codification carries an equal level of authority. The Codification did not change generally accepted accounting principles and simplified accounting research by reorganizing current generally accepted accounting principles into specific accounting topics. The Obligated Group adopted this accounting standard in the first quarter of fiscal year 2010. The adoption of this accounting standard, which was subsequently codified in Accounting Standards Codification (ASC) Topic 105, *Generally Accepted Accounting Principles,* had no impact on the Obligated Group's results of operations, financial position, and liquidity.

The significant accounting policies of the Obligated Group are as follows:

(a) Presentation

For purposes of display, transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are reported as revenues and expenses. Peripheral or incidental transactions are reported as nonoperating losses. Nonoperating income (loss) includes investment income (loss) other than that which is associated with self-insurance programs.

(b) Use of Estimates

The preparation of consolidated 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 consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Significant estimates include: allowances for contractual allowances and bad debts, third-party payor settlements, valuation of investments, land, buildings, and equipment, self-insurance liabilities, derivative instruments, accrued benefit liability, and other liabilities. Actual results could differ from those estimates.

(c) 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 assets whose use is limited or restricted.

(d) Assets Whose Use is Limited or Restricted

Assets whose use is limited or restricted include: assets set aside by the board of trustees for future capital improvements, over which the board of directors retains control and may at its discretion subsequently use for other purposes; assets held by third-party trustees under indenture agreements; assets set aside for self-insurance trust arrangements; funds temporarily or permanently restricted by donors, including the hospitals' interest in the net assets of the Foundation. Management classifies the current portion of assets whose use is limited or restricted based on the approximate amount of the current portion of long-term debt.

Investments in equity securities with readily determinable values and all investments in debt securities are measured at fair value in the accompanying consolidated balance sheets. Investment income on assets deposited in the HSHS self-insurance fund, workers' compensation trust, and funds held by trustee under indenture agreements are reported as other revenues. Investment income from all other investments is reported as nonoperating income (loss) – investment income (loss), unless the income or loss is restricted by donor or law. Changes in net unrealized gains and losses on investments are excluded from revenues in excess (deficient) of expenses and nonoperating income (loss) unless the investments are trading securities. Management considers all investments to be trading securities.

(e) Inventories

Inventories are stated at the lower of cost or market. Cost is determined on a first-in, first-out basis.

(f) Prepaid Expenses

For the years ended June 30, 2010 and 2009, employee benefit costs were reduced by HSHS to the extent revenues exceeded expenses in the HSHS Healthcare Trust Fund. As of June 30, 2010 and 2009, $0 and $6,001, respectively, in prepaid expenses is credited to the Obligated Group from the HSHS Healthcare Trust Fund and will be used to offset the employer portion of future premiums.

(g) Property, Plant, and Equipment

Property, plant, and equipment acquisitions are stated at cost or fair value at the date of acquisition or donation. Depreciation is provided over the estimated useful life of each class of depreciable assets and is computed using the straight-line method. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Capitalized interest is reduced by the amount of investment income earned on remaining project fund investments.

In 2010, the Obligated Group, using a valuation consultant, performed asset useful life studies at five hospitals on the major fixed assets, primarily buildings, in order to more appropriately recognize useful lives reflective of the remaining expected lives of those component assets taking into consideration the longevity and functional use of such long-lived assets. As a result of these studies and the change in estimated useful lives, annual depreciation expense was reduced by $6,968.

(h) Long-Lived Assets

Long-lived assets (including property, plant, and, equipment) are periodically assessed for recoverability based on the occurrence of a significant adverse event or change in the environment in which the Obligated Group operates or if the expected future cash flows (undiscounted and without interest) would become less than the carrying amount of the asset. An impairment loss would be recorded in the period such determination is made based on the fair value of the related entity. No impairments were recorded for the years ended June 30, 2010 and 2009.

(i) Other Assets – Joint Ventures

The Obligated Group invests in various organizations that are not wholly owned or controlled by the Obligated Group. Investments in limited partnerships are recorded at fair value as determined by the partnership. Investments in affiliates in which the Obligated Group has significant influence but does not control are reported on the equity method of accounting, which represents the Obligated Group's equity in the underlying net book value. The equity method of accounting is discontinued when the investment is reduced to zero unless the Obligated Group has guaranteed the obligations of the organization or is committed to provide additional capital support. There were no existing guarantees at June 30, 2010 or 2009.

For investments representing more than 50% voting interest or for which the Obligated Group has control, the investee is consolidated in the accompanying consolidated financial statements with a minority interest recorded for the portion of the investee not owned by the Obligated Group.

(j) Provision for Self-Insured Liabilities

The provision for self-insured professional and general liability and workers' compensation claims includes the ultimate cost for both reported losses and losses incurred but not reported as of the respective consolidated balance sheet dates.

(k) Derivative Instruments

The Obligated Group accounts for derivatives and hedging activities in accordance with ASC Subtopic 815-10, *Accounting for Derivative Instruments and Hedging Activities*, which requires that an entity recognize all derivatives as either assets or liabilities in the consolidated balance sheet and measure those instruments at fair value. The Obligated Group is involved in six interest rate swaps. The fair value of the interest rate swap programs is included as derivative instruments in the accompanying consolidated balance sheets. For the Obligated Group, the derivatives are not designated as hedge instruments, and therefore, the change in fair value of the interest rate swap agreements is recognized in the consolidated statements of operations as a component of nonoperating income (loss) – investment income (loss) in the period of change.

(l) Asbestos Removal Costs

The Obligated Group accounts for asbestos removal costs in accordance with ASC Subtopic 410-20, *Accounting for Conditional Asset Retirement Obligations*. ASC Subtopic 410-20 requires the current recognition of a liability when a legal obligation exists to perform an asset retirement obligation (ARO) in which the timing or method of settlement is conditional on a future event that may or may not be under the control of the entity. ASC Subtopic 410-20 requires an ARO liability be recorded at its net present value with recognition of a related long-lived asset in a corresponding amount. The ARO liability is accreted through periodic charges to depreciation expense. The initially capitalized ARO long-lived asset is depreciated over the corresponding long-lived asset's remaining useful life. The Obligated Group is legally liable to remove asbestos from existing buildings prior to future remodeling or demolishing of the existing hospital buildings. The estimated asbestos removal cost at June 30, 2010 and 2009 is $29,385 and $28,783, respectively, and is included within other noncurrent liabilities in the accompanying consolidated balance sheets. The net book value of the ARO long-lived asset at June 30, 2010 and 2009 is $1,210 and $1,445, respectively, and is included within other assets in the accompanying consolidated balance sheets.

(m) Donor-Restricted Net Assets

Net assets and activities are classified into three classes based on the existence or absence of donor-imposed restrictions: unrestricted, temporarily restricted, and permanently restricted. Temporarily restricted net assets represent those net assets whose use by the Obligated Group has been limited by donors to a specific time period or purpose and the Obligated Group's interest in the net assets of the Foundation. Permanently restricted net assets have been restricted by donors to be maintained by the Obligated Group and Foundation in perpetuity. The Obligated Group's temporarily restricted net assets of $66,172 and $57,202 at June 30, 2010 and 2009, respectively, are restricted for various programs related to the provisions of healthcare and include the hospitals' temporarily restricted interest in the net assets of the Foundation.

In August 2008, the FASB issued ASC Topic 958, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA), and Enhanced Disclosures for All Endowment Funds*. ASC Topic 958 provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization and requires additional disclosure about endowment funds (both donor-restricted and board-designated). The Obligated Group has adopted ASC Topic 958 as of July 1, 2008.

UPMIFA was adopted by the State of Illinois effective June 30, 2009. As of June 30, 2009, the State of Wisconsin follows the Uniform Management of Institutional Funds Act (UMIFA) but legislation has been enacted to adopt UPMIFA as of July 20, 2009. UMIFA indicates that the historical dollar value of permanently restricted endowment funds is not changed by gains or losses unless donors have indicated that gains be accumulated in such funds. UPMIFA eliminates this historical dollar value threshold, an amount below which an organization could not spend from the endowment, and replaces it with guidelines that constitute prudent spending with preservation of the endowment. UPMIFA requires the establishment of a spending policy, which may result in the value of the endowment to drop below the historical dollar value threshold.

The Obligated Group classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment, the original value of subsequent gifts to the permanent endowment, and accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument. Investment returns in excess of spending are classified as increases in temporarily restricted net assets until appropriated for expenditure by the Obligated Group.

The Obligated Group has established a spending policy, which is evaluated and approved by the Foundation board every year. The approved spending rate for fiscal year 2010 and 2009 was 4%. In establishing this policy, the long-term expected return on the endowment is considered. This is consistent with the Obligated Group's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term.

Endowment funds are commingled with the pooled investment fund administered by HSHS. HSHS relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). HSHS targets a diversified asset allocation of 52% fixed income and 48% equities to achieve its long-term return objectives within prudent risk constraints.

(n) Gifts, Bequests, and Grants

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received, which is then treated as cost. 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 as assets released from restrictions.

Gifts of long-lived assets such as land, buildings, and equipment are reported as unrestricted gifts and bequests and are excluded from revenues in excess (deficient) of expenses and nonoperating income (loss), 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 restricted contributions. In the absence of explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

ASC Topic 958, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others*, requires that a specified beneficiary recognize its rights to assets held by a recipient organization as an asset unless the donor has explicitly granted the recipient organization variance power, that is, the unilateral power to redirect the use of the assets. Those rights are an interest in the net assets of the recipient organization, a beneficial interest, or a receivable. Because the Foundation was established and structured to operate exclusively for the benefit of the respective hospitals of the Obligated Group and since variance power from the donors does not exist, the Obligated Group is required to record its interest in the net assets of the Foundation. As of June 30, 2010 and 2009, the Obligated Group has recorded $86,968 and $77,586, respectively, in assets whose use is limited or restricted as its interest in the net assets of the Foundation.

(o) Net Patient Service Revenues

Net patient service revenues are reported at the estimated net realizable amounts due from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. 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.

(p) Charity Care

The Obligated Group provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Amounts determined to qualify as charity care are not reported as net patient service revenues, since the Obligated Group does not pursue collection of such amounts.

(q) Revenues in Excess (Deficient) of Expenses and Nonoperating Income (Loss)

The consolidated statements of operations include revenues in excess (deficient) of expenses and nonoperating income (loss). Changes in unrestricted net assets that are excluded from revenues in excess (deficient) of expenses and nonoperating income (loss), consistent with industry practice, include: contributions of property, plant, and equipment (including assets acquired using contributions that by donor restrictions or grants were to be used for the purpose of acquiring such assets); nonreciprocal transfer to affiliate for other than goods and services; and recognition of change in pension funded status.

(r) Income Taxes

The members of the Obligated Group are not-for-profit organizations 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.

On July 1, 2007, the Obligated Group adopted ASC Subtopic 740-10, *Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement No. 109*. ASC Subtopic 740-10 addresses the determination of how tax benefits claimed or expected to be claimed on a tax return should be recorded in the consolidated financial statements. Under ASC Subtopic 740-10, the Obligated Group must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the consolidated financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. ASC Subtopic 740-10 also provides guidance on derecognition, classification, interest and penalties on income taxes, and accounting in interim periods and requires

 (Continued)

increased disclosures. As of June 30, 2010 and 2009, the Obligated Group does not have a liability for unrecognized tax benefits.

(s) Fair Value

On July 1, 2008, the Obligated Group adopted the provisions of ASC Subtopic 820-10, *Fair Value Measurements*, for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the consolidated financial statements on a recurring basis. ASC Subtopic 820-10 defines fair value as 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. ASC Subtopic 820-10 also establishes a framework for measuring fair value and expands disclosures about fair value measurements. ASC Subtopic 820-10, *Effective Date of FASB Statement No. 157*, delayed the effective date of ASC Subtopic 820-10 until fiscal years beginning after November 15, 2008 for all nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis.

Starting July 1, 2009, the Obligated Group is required to apply the provisions of ASC Subtopic 820-10 to fair value measurements of nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the consolidated financial statements on a nonrecurring basis.

In October 2008, the FASB issued ASC Subtopic 820-10, ??? *Determining the Fair Value of a Financial Asset When the Market for That Asset is Not Active*, which was effective upon issuance. ASC Subtopic 820-10 clarifies the application of ASC Subtopic 820-10 in cases where the market for a financial instrument is not active and provides an example to illustrate key considerations in determining fair value in those circumstances. The Obligated Group considered the guidance provided by ASC Subtopic 820-10 in its determination of estimated fair values beginning in 2009.

Effective July 1, 2008, the Obligated Group adopted the provisions of ASC Subtopic 825-10, *The Fair Value Option for Financial Assets and Financial Liabilities*. ASC Subtopic 825-10 gives the Obligated Group the irrevocable option to report most financial assets and financial liabilities at fair value on an instrument-by-instrument basis, with changes in fair value reported in earnings. The Obligated Group's management did not elect to measure any additional eligible financial assets or financial liabilities at fair value, and as a result, adoption of this FASB did not have an effect on the results of operations or financial position of the Obligated Group.

(t) Reclassifications

Certain 2009 amounts have been reclassified to conform to the 2010 consolidated financial statement presentation.

(Dollars in thousands)

(3) Community Benefit

Consistent with its mission, the Obligated Group provides medical care to all patients regardless of their ability to pay. In addition, the Obligated Group provides services intended to benefit the poor and underserved, including those persons who cannot afford health insurance because of inadequate resources and/or are uninsured or underinsured, and to enhance the health status of the communities in which it operates.

The following summary has been prepared in accordance with the Catholic Health Association of the United States' (CHA) policy document, *A Guide for Planning and Reporting Community Benefit*, released in May 2006. The Obligated Group uses a cost-to-charge ratio to calculate the cost of charity care and the unpaid cost of Medicaid.

The amounts in the following table reflect the quantifiable costs of the hospitals' community benefit for the years ended June 30:

		2010	2009
Benefits for the poor:			
Charity care at cost	$	32,308	31,343
Unpaid cost of Medicaid and other public programs		89,191	59,959
Community health services		1,276	1,541
Other		557	299
		123,332	93,142
Benefits for the broader community:			
Community health services		4,438	7,657
Health professions education		10,908	10,443
Other		13,513	12,902
		28,859	31,002
Total community benefit	$	152,191	124,144

Benefits for the poor represent the cost of services provided to persons who cannot afford healthcare because of inadequate resources and who are uninsured or underinsured.

Benefits for the broader community represent the cost of services provided to other needy populations that may not qualify as poor, but that need special services and support. It also includes the cost of services for the general benefit of the communities in which the Obligated Group operates. Many programs are targeted toward populations that may be poor, but also include those areas that may need special health services and support. These programs are not financially self-supporting.

Charity care at cost represents the cost of services provided to patients who cannot afford healthcare services due to inadequate resources. All or a portion of a patient's services may be considered charity care for which no payment is anticipated in accordance with the Obligated Group's established policies.

Unpaid cost of Medicaid and other public programs represents the cost of providing services to beneficiaries of public programs, including state Medicaid and indigent care programs, in excess of payments for those services. (See note 4 for an explanation of changes to the Medicaid reimbursement from the State of Illinois and the State of Wisconsin.)

Community health services are activities and services for which no patient bill exists, although there may be nominal patient fees. These services are not expected to be financially self-supporting, although some may be partially supported by outside grants or funding.

Health professions education includes the unreimbursed cost of training health professionals such as medical residents, nursing students, technicians, and students in allied health professions.

Other benefits include subsidized health services, in-kind donations, and other benefits.

In addition to the amounts reported above, the Obligated Group committed significant resources in serving the Medicare population. The cost (determined using a cost-to-charge ratio) of providing services to primarily elderly beneficiaries of the Medicare program, in excess of governmental and managed care contract payments, was $159,322 and $157,003 for the years ended June 30, 2010 and 2009, respectively.

A related organization, the Foundation, contributed $5,600 and $6,864 for charity care, other operating expenses, or property, plant, and equipment on behalf of the hospital during the years ended June 30, 2010 and 2009, respectively. The community benefits reported above are net of the contributions from the Foundation for such benefits.

The Obligated Group also provides a significant amount of uncompensated care for patients, which is not included above, but is reported in the consolidated statements of operations as a provision for uncollectible accounts. Many of those patients are uninsured or underinsured, but did not apply for, or qualify for, charity care.

(4) Net Patient Service Revenues

The members of the Obligated Group have agreements with third-party payors that provide for payment at amounts different from their established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare – Inpatient acute care services rendered to Medicare program beneficiaries are generally 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 and certain outpatient services related to Medicare beneficiaries are paid based upon a cost reimbursement method, prospectively determined rates, established fee screens, or a combination thereof. The hospitals are reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the hospitals and audits by the Medicare fiscal intermediary. Certain outpatient services performed by the hospitals are reimbursed at a prospectively determined rate per service based upon their ambulatory payment classification. Home health services performed by the hospitals are reimbursed at a prospectively determined rate per episodic treatment.

As of June 30, 2010, Medicare cost reports have been audited and final settled through June 30, 2007 or 2008.

Medicaid – Inpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates per discharge. Outpatient services rendered to Medicaid program beneficiaries are reimbursed based upon per visit rates. Medicaid payment methodologies and rates for services are based on the amount of funding available to state Medicaid programs.

The Obligated Group participates in the State of Illinois (the State) assessment program that assists in the financing of its Medicaid program. The State assessment program has been renewed by the State since its inception in 2004 and was renewed again on December 4, 2008 for the State's fiscal years ended June 30, 2009 through June 30, 2013. Pursuant to this program, hospitals within the State are required to remit payment to the State Medicaid program under an assessment formula approved by the Centers for Medicare and Medicaid Services (CMS). The Obligated Group has included its related prorated assessments of $26,740 in 2010 and 2009 within other expenses in the accompanying consolidated statements of operations. The assessment program also provides hospitals within the State with additional Medicaid reimbursement based on funding formulas also approved by CMS. The Obligated Group has included its additional related prorated reimbursement of $47,108 in 2010 and $46,928 in 2009 within net patient service revenues in the accompanying consolidated statements of operations.

During 2009, the State of Wisconsin enacted an assessment tax on the gross revenues of all Wisconsin hospitals retroactive to July 1, 2008, which is used to increase reimbursements made under its Medicaid program. During 2010, the State of Wisconsin expanded the eligibility of the Medicaid program. During the year ended June 30, 2010 and 2009, the Wisconsin Hospitals of the Obligated Group were assessed $19,209 and $17,209, respectively, related to this tax, which is included as a component of other expenses in the accompanying consolidated statements of operations and received $35,086 and $35,126, respectively, in supplemental Medicaid reimbursement, which is included as a component of net patient service revenue in the accompanying consolidated statements of operations.

Other – The hospitals have also entered into payment agreements with Blue Cross, certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined per diem rates.

(Dollars in thousands)

A summary of gross and net patient service revenues for the years ended June 30, 2010 and 2009 follows:

		2010	2009
Inpatient revenues	$	2,027,186	1,985,352
Outpatient revenues		2,188,268	1,691,343
Less provisions for estimated contractual adjustments under third-party reimbursement programs		2,451,277	2,077,161
Net patient service revenues	$	1,764,177	1,599,534

Net patient service revenues for the years ended June 30, 2010 and 2009 include approximately $1,747 and $3,781, respectively, of favorable retrospectively determined prior year settlements with third-party payors.

A summary of the hospitals' Medicare, Medicaid, and managed care/contracted payor utilization percentages, based upon gross patient service revenues, follows:

	2010	2009
Medicare	45%	46%
Medicaid	14	13
Managed care/contracted payor	32	31
Other	9	10

(5) Concentration of Credit Risk

The members of the Obligated Group provide healthcare services through their inpatient and outpatient facilities located in Illinois and Wisconsin. The hospitals grant credit to patients, substantially all of whom are local residents. The hospitals generally do not require collateral or other security in extending credit to patients; however, they routinely obtain assignment of (or are otherwise entitled to receive) patients' benefits payable under their health insurance programs, plans, or policies (e.g., Medicare, Medicaid, Blue Cross, health maintenance organizations, and commercial insurance policies).

The mix of net receivables from patients and third-party payors as of June 30, 2010 and 2009 follows:

	2010	2009
Medicare	28%	29%
Medicaid	8	10
Managed care/contracted payor	50	44
Other	14	17

(Continued)

(Dollars in thousands)

(6) Assets Whose Use Is Limited or Restricted

The Obligated Group participates in the various HSHS administered pooled investment programs covering all assets whose use is limited or restricted and retains a pro rata share of all investments purchased by HSHS.

At June 30, 2010 and 2009, the Obligated Group's pro rata share of the pooled investment program, including the Obligated Group's interest in the net assets of the Foundation and the interest rate swap programs, consisted of the following:

		2010	2009
Cash and cash equivalents	$	100,876	257,030
Common and preferred stocks		434,023	278,473
U.S. government securities		518,891	487,733
Municipal securities		23,701	443
Corporate bonds		140,549	218,250
Foreign securities		175,811	171,240
Commingled funds		111,162	—
Accrued interest receivable		8,250	8,794
Pledges receivable and other		73,144	37,682
	$	1,586,407	1,459,645

A summary of assets whose use is limited or restricted as of June 30, 2010 and 2009 at fair value follows:

		2010	2009
Assets whose use is limited or restricted:			
By the board for capital improvements	$	1,214,068	1,075,082
Funds held by trustee under indenture agreements		183,328	208,822
Funds held by trustee for self-insurance		101,858	97,911
Funds temporarily restricted by donors		185	244
Interest in the net assets of the Foundation		86,968	77,586
Total assets whose use is limited or restricted	$	1,586,407	1,459,645

(Dollars in thousands)

The composition of the Obligated Group's pro rata share of the funds' investment return for the years ended June 30, 2010 and 2009 follows:

		2010	2009
Investment return:			
Interest and dividend income	$	41,420	50,428
Net realized gains (losses) on sale of investments		3,727	(105,827)
Change in net unrealized gains and losses		70,997	(55,982)
Change in fair value of interest rate swaps		(11,724)	(17,973)
Change in net unrealized gains and losses on investments held at the Foundation		4,377	(4,138)
Total investment return	$	108,797	(133,492)

Investment returns are included in the accompanying consolidated statements of operations and changes in net assets for the years ended June 30, 2010 and 2009 as follows:

		2010	2009
Other revenues – investment income (loss)	$	9,069	(7,392)
Nonoperating gains – investment income (loss)		86,946	(125,238)
Temporarily restricted net assets – investment income (loss)		6,785	(8,342)
Permanently restricted net assets – investment income		35	—
Interest income capitalized as part of construction in progress		5,962	7,480
Total investment return	$	108,797	(133,492)

(7) Derivative Instruments

The Obligated Group has interest-rate-related derivative instruments to manage its exposure on its debt instruments. The Obligated Group does not enter into derivative instruments for any purpose other than cash flow hedging purposes and the Obligated Group does not speculate using derivative instruments.

By using derivative financial instruments to hedge exposures to changes in interest rates, the Obligated Group exposes itself to credit risk, tax risk, and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes the Obligated Group, which creates credit risk for the Obligated Group. When the fair value of a derivative contract is negative, the Obligated Group owes the counterparty, and therefore, it does not possess credit risk. The Obligated Group minimizes the credit risk in derivative instruments by entering into transactions with high-quality counterparties whose credit rating is higher than Aa or better.

Tax risk is the adverse effect that the Obligated Group takes on to the extent that tax law changes impact the rates paid to a variable rate bondholder (either positively or negatively) that would affect the variable rate received from the counterparty under a LIBOR-based swap that may not match that bond payment. The Obligated Group minimizes the tax risk in derivative instruments by maintaining sufficient cash reserves to handle potential and known tax law changes.

Market risk is the adverse effect on the value of the derivative instrument that results from a change in interest rates. The market risk associated with interest rate contracts is managed by establishing and monitoring parameters that limit the types and degree of market risk that may be undertaken.

The Obligated Group entered into an interest rate swap agreement in fiscal year 2007, which effectively changes a portion of the interest rate exposure on the Series 1998 Bonds from fixed to variable rates. The Obligate Group receives fixed rate payments of 4.10% and pays the Securities Industry and Financial Markets Association (SIFMA) Index variable rate. The interest rate swap agreement has a notional amount of $60,890 at June 30, 2010 and 2009, which will amortize through June 2018 in accordance with the principal repayments on the Series 1998 Bonds. The Series 1998 Bonds were defeased in June 2008 but the swap is still maintained. The counterparty has the one-time right on August 14, 2011 to terminate the swap at par.

The Obligated Group maintains an interest rate swap agreement, which effectively changes a portion of the fixed interest rate exposure on the Series 2003D Bonds from a fixed to a variable rate. The Obligated Group receives a fixed rate payment of 3.01% and pays the SIFMA Index variable rate. The interest rate swap agreement has a notional amount of $4,965 and $7,285 at June 30, 2010 and 2009, respectively, which will amortize through December of 2011 in accordance with principal repayments on the fixed rate components of the Series 2003D Bonds.

The Obligated Group maintains an interest rate swap agreement, which effectively changes a portion of the interest rate exposure on the Series 2007B-1 Bonds from variable rates to a fixed rate. The Obligated Group receives the SIFMA Index variable rate and pays a fixed rate of 4.02%. The interest rate swap agreement has a notional amount of $76,750 at June 30, 2010 and 2009, which will amortize through March 2036 in accordance with principal repayments on the Series 2007B-1 Bonds.

The Obligated Group entered into two interest rate swap agreements in fiscal year 2008, which effectively changed the interest rate exposure on the Series 2007B-2 and 2007C Bonds from variable to fixed rates. The Obligated Group pays fixed rate payments of 3.47% for both swaps and receives the SIFMA Index variable rate. The interest rate swap agreements have a notional amount of $41,300 and $100,425 for Series 2007B-2 and 2007C Bonds, respectively, at June 30, 2010 and 2009, which will amortize through March 2036 in accordance with principal repayments on the Series 2007B-2 and 2007C Bonds. The Obligated Group also entered into a fixed spread basis swap in fiscal year 2008 that removes the tax risk from the bond holders and transfers the risk to the Obligated Group. The premium that the Obligated Group receives for taking on this risk is 67% of the one-month LIBOR plus a spread of 48 basis points less the SIFMA Index rate. The fixed spread basis swap has a notional amount of $150,000 with a final maturity in May 2033.

(Dollars in thousands)

The Obligated Group is exposed to credit loss in the event of nonperformance by the counterparty to the interest rate swap agreements; however, this is not anticipated. During the years ended June 30, 2010 and 2009, HSHS was not required to post collateral.

Payments equal to the differential to be paid or received under the interest rate swap agreements are recognized quarterly. The Obligated Group has recognized $4,489 and $3,762 in interest expense in the accompanying consolidated statements of operations during 2010 and 2009, respectively, as its portion of the net interest rate differential paid as a result of the interest rate swap agreements. For fiscal years ended June 30, 2010 and 2009, the aggregate change in the fair value of all swap agreements was a decrease of $11,724 and $17,973, respectively, which is recognized within nonoperating income (loss) – investment income (loss) in the accompanying consolidated statements of operations.

The fair value of the swap agreements under ASC Subtopic 820-10 was $(36,013) and $(24,289) and is recorded as derivative instruments in the accompanying consolidated balance sheets at June 30, 2010 and 2009, respectively. The settlement value, if terminated, of the swap agreements at June 30, 2010 and 2009 was $(39,843) and $(27,208), respectively.

The following is a summary of the swaps as of June 30, 2010:

Type of interest swap	Notional amount	Settlement value	Fair value
Fixed receiver	$ 4,965	112	112
Fixed receiver	60,890	2,411	2,254
Fixed payor	76,750	(9,330)	(9,035)
Fixed basis	150,000	(9,068)	(7,266)
Fixed payor	41,300	(6,981)	(6,431)
Fixed payor	100,425	(16,987)	(15,647)
		$ (39,843)	(36,013)

The following is a summary of the swaps as of June 30, 2009:

Type of interest swap	Notional amount	Settlement value	Fair value
Fixed receiver	$ 7,285	192	188
Fixed receiver	60,890	2,351	2,110
Fixed payor	76,750	(4,723)	(4,848)
Fixed basis	150,000	(9,276)	(7,294)
Fixed payor	41,300	(4,588)	(4,208)
Fixed payor	100,425	(11,164)	(10,237)
		$ (27,208)	(24,289)

(Continued)

(8) Fair Value Measurement

(a) Fair Value of Financial Instruments

The following methods and assumptions were used by the Obligated Group in estimating the fair value of its financial instruments:

- The carrying amount reported in the consolidated balance sheets for the following approximates fair value because of the short maturities of these instruments: cash and cash equivalents, accounts payable, accrued expenses, and estimated receivables (payables) under third-party reimbursement programs.
- Fair values of the Obligated Group’s investments held as assets whose use is limited or restricted assets are estimated based on prices provided by its investment managers and its custodian bank except for the carrying value of pledges receivable, which equals fair value. Fair value for cash and cash equivalents, corporate stocks, international stocks, U.S. government bonds, corporate bonds, municipal bonds, and mortgage- and asset-backed securities is measured using quoted market prices at the reporting date multiplied by the quantity held. The carrying value equals fair value.
- Fair value of fixed rate long-term debt is estimated based on the quoted market prices for the same or similar issues or on the current rates offered to the Obligated Group for debt of the same remaining maturities. For variable rate debt, carrying amounts approximate fair value. Fair value was estimated using quoted market prices based upon the Obligated Group’s current borrowing rates for similar types of long-term debt securities.
- Fair value of interest rate swaps is determined using pricing models developed based on the LIBOR swap rate and other observable market data. The value was determined after considering the potential impact of collateralization and netting agreements, adjusted to reflect nonperformance risk of both the counterparty and the Obligated Group. The carrying value equals fair value.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Obligated Group 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.

(Dollars in thousands)

The following table presents the carrying amounts and estimated fair values of the Obligated Group's financial instruments not carried at fair value at June 30, 2010 and 2009.

	2010		2009	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
Long-term debt	$ 570,334	569,002	586,433	581,344

(b) Fair Value Hierarchy

The Obligated Group adopted ASC Subtopic 820-10 on July 1, 2008 for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the consolidated financial statements on a recurring basis. ASC Subtopic 820-10 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques 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 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the corporations have the ability to access at the measurement date.
- Level 2 are observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 inputs are unobservable inputs for the asset or liability.

(Dollars in thousands)

The following table presents the Obligated Group's fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of June 30, 2010.

	Fair value June 30, 2010	Fair value measurements at June 30 using		
		Level 1	Level 2	Level 3
Financial assets:				
Cash and cash equivalents	$ 45,063	45,063	—	—
Assets whose use is limited or restricted, excluding pledges receivable and other of $73,144 and accrued interest receivable of $8,250:				
Cash and cash equivalents	100,876	48,621	52,255	—
Common and preferred stocks	434,023	434,023	—	—
U.S. government securities	518,891	—	518,891	—
Municipal bonds	23,701	—	23,701	—
Corporate bonds	140,549	—	140,549	—
Foreign securities	175,811	131,331	44,480	—
Commingled funds	111,162	—	111,162	—
Total financial assets	$ 1,550,076	659,038	891,038	—
Liabilities:				
Derivative instruments	$ 36,013	—	36,013	—

(Dollars in thousands)

The following table sets forth a summary of changes in the fair value of the plan's level 3 assets for the year ended June 30, 2010.

		Level 3 assets year ended June 30, 2010 guaranteed investment contract
Balance, beginning of year	$	154,391
Interest income		5,663
Distributions		(160,054)
Balance, end of year	$	—

The following table presents the Obligated Group's fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of June 30, 2009.

		Fair value June 30, 2009	Fair value measurements at June 30 using		
			Level 1	Level 2	Level 3
Financial assets:					
Cash and cash equivalents	$	57,812	57,812	—	—
Assets whose use is limited or restricted, excluding pledges receivable and other of $73,144 and accrued interest receivable of $8,250:					
Cash and cash equivalents		102,639	11,988	90,651	—
Guaranteed investment contract		154,391	—	—	154,391
Common and preferred stocks		278,473	278,473	—	—
U.S. government securities		487,733	—	487,733	—
Municipal bonds		443	—	443	—
Corporate bonds		218,250	—	218,250	—
Foreign securities		171,240	92,470	78,770	—
Total financial assets	$	1,470,981	440,743	875,847	154,391
Liabilities:					
Derivative instruments	$	24,289	—	24,289	—

(Dollars in thousands)

The following table sets forth a summary of changes in the fair value of the plan's level 3 assets for the year ended June 30, 2009.

	Level 3 assets year ended June 30, 2009 guaranteed investment contract
Balance, beginning of year	$ 157,266
Interest income	8,414
Distributions	(11,289)
Balance, end of year	$ 154,391

(9) Property, Plant, and Equipment

A summary of property, plant, and equipment at June 30, 2010 and 2009 is as follows:

	2010	2009
Land	$ 39,952	35,374
Land improvements	34,188	32,808
Buildings and permanent fixtures	1,106,218	1,039,420
Equipment and furnishings	783,910	742,607
	1,964,268	1,850,209
Less accumulated depreciation	1,172,258	1,097,565
	792,010	752,644
Construction in progress	43,987	68,124
	$ 835,997	820,768

As of June 30, 2010, construction in progress represents various building and remodeling projects. These projects, which have remaining contracted costs at June 30, 2010 of approximately $60,991, will be financed with board-designated assets or from operations.

(Dollars in thousands)

A reconciliation of total interest cost, as reported in the accompanying consolidated statements of operations for 2010 and 2009, is as follows:

		2010	2009
Interest cost capitalized	$	6,574	8,968
Interest charged to expense		5,242	8,320
Total interest costs incurred	$	11,816	17,288
Interest income capitalized	$	5,962	7,480

(10) Self-Insurance

(a) Professional and General Liability

The eight Illinois hospitals participate in the HSHS self-insurance fund for the purpose of providing professional and general liability insurance. An independent actuary has been retained to assist management in determining funding requirements. The amounts funded have been placed in a trust account that is administered by a bank. The trust account assets are reported as assets whose use is limited or restricted in the accompanying consolidated balance sheets.

The hospitals are involved in litigation arising in the ordinary course of business. Reported claims are in various stages of litigation. Additional claims may be asserted against the hospitals arising from services through June 30, 2010. It is the opinion of management that the estimated malpractice liabilities accrued at June 30, 2010 are adequate to provide for potential losses resulting from pending or threatened litigation.

At June 30, 2010 and 2009, funds held by the trustee for professional and general liability self-insurance are $82,208 and $80,648, respectively, and related estimated self-insurance liabilities are $38,386 and $42,786, respectively. The discount rate at June 30, 2010 and 2009 used to compute the estimated self-insurance liability for all future claims payments was 5% and 4.25%, respectively. The amount included in expenses for professional and general liability insurance for 2010 and 2009 was $8,670 and $(573), respectively, and is included in other expense in the consolidated statements of operations.

The five Wisconsin hospitals had primary professional and general liability insurance with limits for claims incurred during a policy year regardless of when the claim is reported (occurrence coverage) through December 31, 2003. During calendar year 2004, the hospitals' primary professional liability coverage changed from occurrence coverage to claims-made coverage. As of June 30, 2010 and 2009, a liability of $80 and $82, respectively, was recognized as an estimate for tail exposures. As of January 1, 2005, the hospitals changed back to occurrence coverage. Losses in excess of primary professional liability limits are fully covered through the hospitals' mandatory participation in the State of Wisconsin Injured Patients and Families Compensation Fund.

On April 23**,** 2010, HSHS received approval to form and operate its captive insurance company, Renaissance Quality Insurance, Ltd. (RQIL) through the Cayman Islands' Monetary Authority. RQIL will provide general and professional liability (GPL) insurance to all 13 hospitals, employed physicians of the hospitals, and those physicians employed by the Medical Group.

Beginning on July 1, 2010, the trust, which covered retrospective insurance obligations for the 8 Illinois hospitals, transferred assets and estimated self-insurance obligations of $42,694 to RQIL. Beginning July 1, 2010, primary GPL premiums and all future liabilities from that date for HSHS' critical access hospitals (St. Joseph's Hospital, Highland and St. Francis Hospital, Litchfield) will remain with the trust. Also, beginning on July 1, 2010, GPL obligations for the 5 Wisconsin hospitals are being fully reinsured through RQIL. Prior to July 1, 2010, the 5 Wisconsin hospitals purchased primary GPL coverage through the Wisconsin Health Care Liability Insurance Plan on an occurrence basis and excess coverage through the State of Wisconsin Injured Patients and Families Compensation Fund.

The operations of RQIL began July 1, 2010 and will be consolidated as a wholly owned subsidiary of HSSI.

(b) Workers' Compensation

The members of the Obligated Group also participate in the HSHS self-insurance program, providing workers' compensation insurance and health insurance for employees. An independent actuary has been retained to assist management in determining funding requirements. The amounts funded for each program have been placed in separate accounts that are administered by the bank.

At June 30, 2010 and 2009, funds held by the bank for workers' compensation liability self-insurance are $19,650 and $17,263, respectively, and related estimated self-insurance liabilities are $13,263 and $13,196, respectively. The discount rate used to compute the estimated self-insurance liability at June 30, 2010 and 2009 was 5.00% and 4.25%, respectively, for all future claim payments. The amount included in employee benefits for workers' compensation insurance for 2010 and 2009 was $8,034 and $7,383, respectively, and is included in other expense in the consolidated statements of operations.

(11) Pension

The hospitals participate in The Hospital Sisters Health System Employees Pension Plan (the Plan). This noncontributory defined benefit pension plan covers substantially all employees of the hospitals who have completed 1,000 hours of employment during any calendar year subsequent to the commencement of employment. The Plan recognizes and funds the costs related to employee service using the projected unit credit actuarial cost method. The information below represents the aggregation of the Obligated Group's pension financial status, which is determined by the consulting actuaries on a member-specific basis.

(Dollars in thousands)

The following table sets forth the Plan's funded status, amounts recognized in the Obligated Group's consolidated financial statements, and assumptions at June 30, 2010 and 2009:

		2010	2009
Change in benefit obligation:			
Benefit obligation at beginning of year	$	719,493	639,885
Service cost		28,001	28,095
Interest cost		49,439	46,316
Adjustment for transfer		(54)	(393)
Actuarial loss		195,488	17,553
Expected expenses		(4,109)	(4,721)
Benefits paid		(9,967)	(7,242)
Benefit obligation at end of year	$	978,291	719,493
Change in plan assets:			
Fair value of plan assets at beginning of year	$	547,865	629,922
Actual gain (loss) on plan assets		70,184	(89,055)
Employer contributions		22,409	14,633
Adjustments for transfers		(54)	(393)
Benefits paid		(9,967)	(7,242)
Fair value of plan assets at end of year	$	630,437	547,865
Reconciliation of funded status:			
Funded status	$	(347,854)	(171,628)
Amounts recognized in the accompanying consolidated balance sheets:			
Accrued benefit liability	$	(347,854)	(171,628)
Amounts not yet reflected in net periodic benefit cost and included as an accumulated charge to unrestricted net assets:			
Prior service credit	$	21	752
Actuarial loss		(347,875)	(172,380)
	$	(347,854)	(171,628)

(Dollars in thousands)

		2010	2009
Changes recognized in unrestricted net assets:			
Net loss arising during the period	$	175,493	160,935
Amortization of prior service credit		733	733
Total recognized in unrestricted net assets	$	176,226	161,668
Total recognized in net periodic pension cost and unrestricted net assets	$	198,634	176,297
Estimated amounts that will be amortized from unrestricted net assets over the next fiscal year:			
Prior service credit	$	733	733
Net loss		(14,323)	—
Total	$	(13,590)	733
Accumulated benefit obligation	$	832,478	609,604
Components of net periodic benefit cost:			
Service cost	$	28,001	28,095
Interest cost		49,439	46,315
Expected return on plan assets		(54,299)	(59,048)
Amortization of prior service credit		(733)	(733)
Net periodic benefit cost	$	22,408	14,629
Weighted average assumptions used to determine benefit obligations at June 30:			
Discount rate		5.60%	6.96%
Average rate of compensation increase		3.50	3.50
Measurement date		6/30/2010	6/30/2009
Weighted average assumptions used to determine net periodic benefit cost for the year ended June 30:			
Discount rate		6.96%	7.18%
Expected long-term return on plan assets		8.25	8.50
Average rate of compensation increase		3.50	4.00
Measurement date		6/30/2009	6/30/2008

The expected long-term rate of return is based on the portfolio as a whole and not on the sum of the returns on individual assets categories. The return is based exclusively on historical returns, without adjustments.

As of July 1, 2006, the Plan began using the Mercer Pension Discount Yield Curve to select the discount rate used to measure the liabilities of the Plan. The Mercer Pension Discount Yield Curve discounts the

(Dollars in thousands)

Plan's cash flow and calculates the Plan's appropriate equivalent single discount rate for the given cash flow.

The Obligated Group expects to contribute to its pension plan for the 2011 fiscal year the following amount	$	43,279
The following benefit payments that reflect expected future service, as appropriate, are expected to be paid:		
2011	$	16,102
2012		20,187
2013		24,706
2014		29,547
2015		34,789
2016 – 2018		266,374

The expected benefits are based on the same assumptions used to measure the Obligated Group's benefit obligation at June 30, 2010 and include estimated future employee service.

The Plan has developed a Pension Plan Investment Policy and Guidelines (the policy), which is reviewed and approved by the HSHS board of directors. The policy established goals and objectives of the fund, asset allocations, allowable and prohibited investments, socially responsible guidelines, and asset classifications, as well as specific investment manager guidelines. The policy dictates that assets should be rebalanced back to target allocation on a quarterly basis. Investments are managed by independent advisors. Management monitors the performance of these managers on a monthly basis.

The table below lists the target asset allocation and acceptable ranges and actual asset allocations as of June 30, 2010 and 2009:

Asset	Target allocation	Acceptable range	Actual allocation at June 30 2010	Actual allocation at June 30 2009
Equities	60%	24% – 75%	52%	48%
Debt securities	40	32% – 70%	44	46
Cash and cash equivalents	—	0% – 6%	4	6

(a) Fair Value of Financial Instruments

The following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at June 30, 2010 and 2009.

- Cash and cash equivalents: Valued at the carrying amount that approximates fair value because of the short-term maturity of these investments.

- Common and preferred stocks, U.S. government securities, and foreign securities: Valued at the closing price reported on the active market on which the individual securities are traded.
- Municipal bonds, corporate bonds, notes, and debentures: Certain corporate bonds are valued at the closing price reported in the active market in which the bond is traded. Other corporate bonds are valued based on yields currently available on comparable securities of issuers with similar credit ratings. When quoted prices are not available for identical or similar bonds, the bond is valued under a discounted cash flows approach that maximizes observable inputs, such as current yields of similar instruments, but includes adjustments for certain risks that may not be observable, such as credit and liquidity.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Plan 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.

(b) Fair Value Hierarchy

The Plan adopted ASC Subtopic 715-20-50 on July 1, 2009 for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the consolidated financial statements on a recurring basis. ASC Subtopic 715-20-50 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value.

(Continued)

(Dollars in thousands)

The following table presents the Plan's fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of June 30, 2010.

		Fair value	Level 1	Level 2	Level 3
Investments, excluding accrued interest and dividends of $1,994:					
Cash and cash equivalents	$	26,537	—	26,537	—
Common and preferred stocks		218,730	218,730	—	—
U.S. government securities		116,252	—	116,252	—
Mutual Funds		132,217	—	132,217	—
Municipal bonds		944	—	944	—
Corporate bonds, notes, and debentures		19,757	—	19,757	—
Foreign securities		114,006	108,994	5,012	—
Total assets at fair value	$	628,443	327,724	300,719	—

(12) Long-Term Debt

Under the terms of the Obligated Group MTI, each member of the Obligated Group is jointly and severally liable for all obligations issued thereunder. Bonds issued are unsecured general obligations, but carry covenants regarding withdrawals from the Obligated Group, issuance of additional debt, and creations of liens on property. Obligations outstanding under the Obligated Group MTI are issued through state health facility authorities and comprise both serial and term bonds with varying maturities. Financial Security Assurance, Inc. is used as the bond insurer for all outstanding bonds, except for Series 2007A, 2008A, and 2008B, which were issued as fixed rate and variable rate debt based on HSSI's Aa rating.

(Dollars in thousands)

As of June 30, 2010 and 2009, long-term debt consisted of the following:

Series	Interest rates	Final maturity dates		2010	2009
Fixed interest rate issues:					
2003D	4.00% to 5.00%	December 1, 2011	$	4,965	7,285
2007A	5.00%	March 15, 2028		72,035	72,035
Variable interest rate issues:					
2003A	Variable 0.32% and 0.31% at June 30, 2010 and 2009, respectively	December 1, 2023		65,550	65,550
2003B	Variable 0.45% to 0.65% and 0.60% at June 30, 2010 and 2009, respectively	December 1, 2023		69,850	69,850
2007B-1	Variable 0.30% and 0.31% at June 30, 2010 and 2009, respectively	March 15, 2036		76,750	76,750
2007B-2	Variable 0.32% and 0.31% at June 30, 2010 and 2009, respectively	March 15, 2036		41,300	41,300
2007C	Variable 0.32% and 0.31% at June 30, 2010 and 2009, respectively	March 15, 2036		100,425	100,425
2008A	Variable 0.40% to 0.65% and 1.75% at June 30, 2009 and 2008, respectively	June 1, 2029		108,940	118,380
2008B	Variable 0.40% to 0.65% and 1.75% at June 30, 2009 and 2008, respectively	June 1, 2029		17,400	18,980
				557,215	570,555
Other long-term debt				10,071	12,563
				567,286	583,118
Plus unamortized bond issue premiums				3,048	3,315
Total debt				570,334	586,433
Less current installments				15,475	16,900
Less long-term debt subject to short-term remarketing agreements				184,771	196,190
Total long-term debt, excluding current installments			$	370,088	373,343

(Continued)

(Dollars in thousands)

The Obligated Group's effective interest rates for variable debt for the years ended June 30, 2010 and 2009 are as follows:

	2010	**2009**
Variable interest rate issues:		
2003A	0.27%	1.61%
2003B	0.54	1.80
2007B-1	0.26	1.53
2007B-2	0.27	1.61
2007C	0.27	1.61
2008A	0.33	1.16
2008B	0.34	1.17

Bond issue premiums and costs are amortized over the term of the related bonds using the bonds outstanding method. Bond issuance costs, net of amortization, are reported as other assets in the accompanying consolidated balance sheets.

The Obligated Group has variable rate demand notes that have a put option available to the creditor. If the put option is exercised, the bonds are presented to the bank, which in turn draws on the underlying letter of credit, if available. The bond series and the underlying credit facility terms are described as follows:

Series	**Terms**
Series 2003A	Equal quarterly installments on the first business day of each January, April, July, or October whichever occurs first on or following the 367th day after the purchase date and paid in full no later than the fifth anniversary of the purchase date
Series 2003B	Self-liquidity
Series 2007B-1	Equal quarterly installments on the first business day of each January, April, July, or October whichever occurs first on or following the 367th day after the purchase date and paid in full no later than the fifth anniversary of the purchase date
Series 2007B-2	Equal quarterly installments on the first business day of each January, April, July, or October whichever occurs first on or following the 367th day after the purchase date and paid in full no later than the fifth anniversary of the purchase date

(Dollars in thousands)

Series	Terms
Series 2007C	Equal quarterly installments on the first business day of each January, April, July, or October whichever occurs first on or following the 367th day after the purchase date and paid in full no later than the fifth anniversary of the purchase date
Series 2008A	Self-liquidity
Series 2008B	Self-liquidity

Scheduled principal repayments on long-term debt based on the variable rate demand notes being put back to the Obligated Group and a corresponding draw being made on the underlying credit facility, if available, are as follows:

Year ending June 30:		
2011	$	200,246
2012		56,136
2013		71,365
2014		71,383
2015		71,331
Thereafter		96,825
	$	567,286

Scheduled principal repayments on the long-term debt based on the scheduled redemptions according to the Obligated Group MTI are as follows:

Year ending June 30:		
2011	$	15,475
2012		14,706
2013		15,259
2014		15,797
2015		16,265
Thereafter		489,784
	$	567,286

(Dollars in thousands)

(13) Functional Expenses

The Obligated Group provides general healthcare services to residents within its respective geographic regions. Expenses related to providing these services for the years ended June 30, 2010 and 2009 are as follows:

		2010	2009
Healthcare services	$	1,517,388	1,358,357
General and administrative services		276,289	241,903
	$	1,793,677	1,600,260

(14) Prevea

St. Vincent Hospital (St. Vincent) and St. Mary's Hospital Medical Center (St. Mary's) (collectively referred to as the Green Bay Hospitals), two members of the Obligated Group located in Green Bay, Wisconsin, each have a 25% interest in Prevea Health Systems, Inc. (Prevea). The Green Bay Hospitals held $22,180 (22,180 shares) at June 30, 2010, and $48,000 (48,000 shares) at June 30, 2009 of Prevea preferred stock. Prevea has 9,000 shares of authorized common stock of which 645 shares are outstanding at June 30, 2010 and 2009. The Green Bay Hospitals held 100 shares of the common stock at June 30, 2010 and 2009. The preferred stockholders of Prevea have liquidation preferences to common stockholders, as defined in the Articles of Incorporation of Prevea. The preferred stock entitles the Green Bay Hospitals to receive dividends equal to 7% of the face value of the preferred stock and the preferred stock dividends are cumulative. The Green Bay Hospitals' policy is to recognize preferred stock dividends when the dividends are declared. No dividends were declared or paid by Prevea in 2010 and 2009. The investment in Prevea is accounted for on the equity method, and the carrying value of the Green Bay Hospitals' investment in Prevea, inclusive of preferred stock holdings, is reported as other assets in the accompanying consolidated balance sheets.

Prevea formed a wholly owned subsidiary, Prevea Clinic, Inc. (the Clinic). The Clinic consists of several medical clinic locations throughout the Green Bay area with approximately 230 physicians and midlevel providers.

Prevea formed Prevea Regional Services, Inc. (Prevea Regional) in 1997 to develop a regional clinic system throughout the outlying areas of Green Bay. Prevea held all of the voting common stock of Prevea Regional on June 30, 2009. The Green Bay Hospitals held $5,550, (1,110 shares) at June 30, 2009 of nonvoting preferred stock in Prevea Regional. In August 2009, Prevea Regional was merged into the Clinic by Prevea. Also in August 2009, the Green Bay Hospitals' preferred stock shares of $5,550, (5,550 shares) in Prevea Regional were exchanged for shares of equal value in Prevea.

(Dollars in thousands)

In September 2009, the Clinic entered into several transactions with St. Vincent. They are summarized as follows:

- The sale, transfer, and assignment of certain assets of $31,370 in exchange for the redemption of the appropriate number of shares of preferred stock owned by St. Vincent having the same value.
- Lease arrangements – St. Vincent leased all real property, equipment, furnishings, and other personal property and intellectual property from the Clinic for use in the operations of the Clinic.
- Physician services agreement – St. Vincent entered into physician services agreement with the Clinic whereby the Clinic provides certain professional medical services in connection with the operations of the Clinic.
- Managed and staff services agreement – St. Vincent entered into a management and nonphysician staff services agreement with the Clinic in connection with the operations of the clinics whereby the Clinic provides certain management and nonphysician staff services in connection with the operations of the Clinic.

Since September 2009, St. Vincent, with the completion of these transactions, has assumed ownership of the Clinic's medical clinic locations, and it is now operating these sites as St. Vincent doing business as Prevea Health receiving all of the Clinic's patient revenues and responsible for all of the operating expenses. The expenses directly related to Prevea Health, mainly for the leasing of all employees and doctors, for the year ended June 30, 2010 are $107,796 and are included in other expenses in the consolidated statement of operations.

During the years ended June 30, 2010 and 2009, the Green Bay Hospitals have $973 and $994 respectively, of notes receivable for cash advances to Prevea.

The following are Prevea's condensed unaudited financial statement data as of and for the years ended June 30, 2010 and 2009:

		2010	2009
Total assets	$	82,499	111,923
Total liabilities		54,181	56,372
Total equity		28,318	55,551
Total net revenue		160,680	157,437
Net income		5,196	54

The Green Bay Hospitals' equity portion in Prevea increased (decreased) by $2,598 and $(177), respectively, which is included in other operating income in the June 30, 2010 and 2009 consolidated statements of operations. The Green Bay Hospitals' equity portion of the net loss of the Clinic is contractually limited to budgeted operating income plus other income and expenses.

(Continued)

During fiscal year 2004, St. Vincent entered into a contract to guarantee the Clinic's repayment of long-term debt related to a building project. Under this guarantee contract, St. Vincent was guaranteeing the repayment of 39.92% of the Clinic's $26,300 taxable variable rate demand notes. Through December 2009, St. Vincent was paid 1.25% on one half of the outstanding notes under the terms of the contract. During fiscal year 2010, the Obligated Group replaced the St. Vincent guarantee whereby the Obligated Group agrees to guarantee the lesser of $10,500 or 39.92% of the outstanding notes. The Obligated Group will be paid 1.25% on one half of the outstanding notes. Included in the guarantee executed in December 2009 are $2,920 taxable variable rate demand notes of PHP Insurance Plan, Inc. (PHP). PHP, a former health maintenance organization, sold its insurance license, changed its corporate structure, and became Prevea Ventures, LLC. Prevea is the sole corporate member of Prevea Ventures, LLC. At June 30, 2010 and 2009, the Clinic has notes outstanding with a balance approximating $23,945 and $24,585, respectively. At June 30, 2010, PHP has notes outstanding of $2,660.

(15) Joint Ventures

Joint ventures are accounted for using the equity method of accounting and represent $16,508 and $14,173 of other long-term assets in the accompanying consolidated balance sheets at June 30, 2010 and 2009, respectively. The most significant of these investments, excluding Prevea (note 14), include:

- Memorial and St. Elizabeth's Healthcare Services, LLP (held by St. Elizabeth's Hospital) – 50% ownership interest;
- Unity Limited Partnership (held by St. Vincent and St. Mary's, Green Bay) – 45% ownership interest and 10% ownership interest, respectively;
- Northeast Wisconsin Radiation Therapy Services, LLC (held by St. Vincent and St. Mary's, Green Bay) – each hospital has a 25% ownership interest;
- Pain Center of Wisconsin, LLC (held by St. Vincent) – 50% ownership interest;
- Surgery Center of Sheboygan, LLC (held by St. Nicholas Hospital) – 50% ownership interest;
- Orange Cross Ambulance, Inc. (held by St. Nicholas Hospital) – 50% ownership interest;
- Wisconsin Upper Peninsula Oncology Management Services, Inc. (held by St. Vincent) – 50% ownership interest. At June 30, 2008, this entity was consolidated as part of St. Vincent's financial statements. St. Vincent's equity interest at July 1, 2008 was $2,369.
- Prairie Heart Institute – Carbondale, LLC (held by St. John's Hospital) – 50% ownership interest until June 11, 2008 when the joint venture agreement expired. Included in other receivables at June 30, 2008 is $4,718, which represents the St. John's Hospital's share of the equity that was to be distributed in 2009 due to the expiration of the joint venture agreement. During the year ended June 30, 2009, St. John's Hospital received $4,961 of which $243 is recognized as a component of other revenue in the accompanying consolidated statements of operations.

(Dollars in thousands)

For the years ended June 30, 2010 and 2009, the Obligated Group recognized income of $2,651 and $1,290, respectively, in investments in affiliated companies. This activity is included as a component of other revenue in the accompanying consolidated statements of operations. During 2010 and 2009, the Obligated Group received cash distributions of $1,350 and $429, respectively, from the joint ventures. During 2010 and 2009, the Obligated Group also contributed cash of $1,034 and $751, respectively, to the joint ventures.

The following table summarizes the unaudited aggregated financial information of unconsolidated affiliated companies of the Obligated Group as of June 30, 2010 and 2009:

		2010	2009
Total assets	$	35,606	31,454
Total liabilities		9,288	8,158
Total equity		26,318	23,296
Total net revenue		38,087	30,157
Net income		5,205	2,535

(16) Pledges Receivable

Pledges, net of a present value discount rate, determined in the year the pledge is made, and an allowance for uncollectible pledges, are recorded as a component of assets whose used is limited or restricted in the accompanying consolidated financial statements based on their expected collection date.

Included in assets whose use is limited or restricted at June 30, 2010 and 2009 are the following unconditional promises to give:

		2010	2009
Unconditional promises to give	$	8,411	7,662
Less unamortized discount		628	521
		7,783	7,141
Less allowance for uncollectible pledges		264	152
Net pledges receivable	$	7,519	6,989
Amounts due in:			
Less than one year	$	2,714	2,581
One to five years		5,393	4,637
More than five years		304	444
Total	$	8,411	7,662

(Dollars in thousands)

(17) Temporarily and Permanently Restricted Assets

Temporarily restricted assets are available for the following purposes or periods at June 30, 2010 and 2009:

		2010	2009
Healthcare services	$	51,955	47,364
Capital expenditures		14,030	9,734
Colleges of nursing		187	104
	$	66,172	57,202

As of June 30, 2010 and 2009, the Obligated Group has permanently restricted endowments as follows:

		2010	2009
Assets to be held in perpetuity, the income from which is expendable to support nursing schools	$	2,119	1,201
Assets to be held in perpetuity, the income from which is expendable to support operations of HSHS facilities		18,862	19,427
	$	20,981	20,628

As of June 30, 2010 and 2009, the Obligated Group has temporarily restricted funds that represent the unspent accumulation of earnings for endowment funds as follows:

		2010	2009
Unspent income (loss) from which is expendable to support nursing schools	$	63	(20)
Unspent income from which is expendable to support specific operations of HSHS facilities		4,773	4,619
	$	4,836	4,599

(18) Related-Party Transactions

HSHS and HSSI are sponsored by a religious congregation, The Hospital Sisters of the Third Order of St. Francis. During the years ended June 30, 2010 and 2009, the 13 hospitals had administrative and information systems expenses incurred with HSHS of $72,303 and $52,317, respectively.

(Dollars in thousands)

(19) Commitments and Contingencies

(a) Operating Leases

The Obligated Group occupies space in certain facilities and leases various pieces of equipment under long-term noncancelable operating lease arrangements. Total equipment rental, asset lease, and facility rental expense in 2010 and 2009 was $17,967 and $7,289, respectively.

The following is a schedule by year of future minimum lease payments to be made under operating leases as of June 30, 2010 that have initial or remaining lease terms in excess of one year:

	Amount
Year ending June 30:	
2011	$ 16,233
2012	13,515
2013	10,527
2014	9,170
2015	2,742
Thereafter	9,163

(b) Regulatory Investigations

The U.S. Department of Justice and other federal agencies routinely conduct regulatory investigations and compliance audits of healthcare providers. The Obligated Group is subject to these regulatory efforts. Management is currently unaware of any regulatory matters that may have a material adverse effect on the Obligated Group's consolidated financial position or results of operations.

(c) Litigation

The Obligated Group is involved in litigation arising in the ordinary course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the Obligated Group's future consolidated financial position or results of operations.

(d) Unemployment

The Wisconsin hospitals of the Obligated Group pledged a U.S. Treasury note as collateral for any unpaid unemployment compensation claims with a face value of $3,000 to the Wisconsin Unemployment Reserve Fund. The pledged U.S. Treasury note remained unused at June 30, 2010 and 2009.

(Continued)

(e) Investment Risk and Uncertainties

HSHS invests in various investment securities. Investment securities are exposed to various risks such as interest rate, credit, and overall market volatility risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the accompanying consolidated balance sheet.

(20) Subsequent Events

The Obligated Group evaluated events and transactions through October 11, 2010, the date the consolidated financial statements were issued, noting no subsequent events requiring recording or disclosure, except as noted in note 10, in the consolidated financial statements or related notes to the consolidated financial statements.

HOSPITAL SISTERS SERVICES, INC. –
OBLIGATED GROUP
Springfield, Illinois

Consolidating Balance Sheet Information

June 30, 2010

(Dollars in thousands)

Assets	**St. Elizabeth's Belleville, Illinois**	**St. Joseph's Breese, Illinois**	**St. Mary's Decatur, Illinois**	**St. Anthony's Effingham, Illinois**	**St. Joseph's Highland, Illinois**	**St. Francis Litchfield, Illinois**	**St. John's Springfield, Illinois**	**St. Mary's Streator, Illinois**
Current assets:								
Cash and cash equivalents	$ (1,785)	3,411	5,721	5,159	616	3,042	(9,185)	2,487
Receivables:								
Patients' accounts, less allowance for uncollectible accounts of $73,075	23,550	5,088	19,712	16,547	3,455	2,807	54,151	7,712
Due from third-party reimbursement program	825	—	198	39	—	—	—	—
Other	3,019	514	1,329	453	732	1,539	5,536	861
Total receivables	27,394	5,602	21,239	17,039	4,187	4,346	59,687	8,573
Current portion of assets whose use is limited or restricted	16,765	3,350	7,450	13,520	1,180	1,065	62,765	3,170
Inventories	2,700	511	2,867	5,228	364	459	10,891	1,496
Prepaid expenses	1,684	378	935	192	215	479	6,601	409
Total current assets	46,758	13,252	38,212	41,138	6,562	9,391	130,759	16,135
Assets whose use is limited or restricted, net of current portion	54,038	58,527	52,586	170,163	6,732	28,216	449,103	29,273
Property, plant, and equipment, net	61,642	23,732	56,397	53,433	8,423	7,117	226,837	44,045
Other assets	5,601	404	1,988	298	117	122	6,380	667
	$ 168,039	95,915	149,183	265,032	21,834	44,846	813,079	90,120
Liabilities and Net Assets								
Current liabilities:								
Current installments of long-term debt	$ 1,505	300	670	1,510	105	95	5,640	290
Long-term debt subject to short-term remarketing agreement	15,260	3,050	6,780	12,010	1,075	970	57,125	2,880
Accounts payable	5,498	1,343	9,053	2,021	1,300	769	15,995	1,707
Accrued liabilities	8,122	2,093	5,490	3,972	1,167	1,807	19,171	2,558
Estimated payables under third-party reimbursement program	2,323	674	4,612	7,270	56	521	10,671	2,017
Total current liabilities	32,708	7,460	26,605	26,783	3,703	4,162	108,602	9,452
Long-term debt, excluding current installments	33,124	8,200	22,184	19,200	7,324	11,537	137,831	10,037
Estimated self-insurance liabilities	8,627	956	6,006	2,644	764	1,751	28,047	1,474
Derivative instruments	3,238	750	1,911	1,865	264	784	12,921	854
Accrued benefit liability	35,860	6,729	25,200	15,707	5,885	8,646	84,006	14,950
Other noncurrent liabilities	8,067	2,289	1,574	657	1,727	842	11,027	1,737
Total liabilities	121,624	26,384	83,480	66,856	19,667	27,722	382,434	38,504
Net assets:								
Unrestricted	40,981	68,128	53,104	195,251	396	15,309	408,352	49,713
Temporarily restricted	5,423	1,403	11,368	2,813	1,771	1,192	19,917	1,883
Permanently restricted	11	—	1,231	112	—	623	2,376	20
Total net assets	46,415	69,531	65,703	198,176	2,167	17,124	430,645	51,616
	$ 168,039	95,915	149,183	265,032	21,834	44,846	813,079	90,120

See accompanying independent auditors' report.

Schedule 1

St. Joseph's Chippewa Falls, Wisconsin	Sacred Heart Eau Claire, Wisconsin	St. Mary's Green Bay, Wisconsin	St. Vincent Green Bay, Wisconsin	St. Nicholas Sheboygan, Wisconsin	Hospital Sisters Services, Inc.	Eliminations	Total
2,794	3,738	5,945	20,978	2,141	1	—	45,063
5,940	22,971	14,627	51,643	9,681	—	—	237,884
195	300	774	392	—	—	—	2,723
322	513	1,340	14,067	1,824	1,312	(7,011)	26,350
6,457	23,784	16,741	66,102	11,505	1,312	(7,011)	266,957
8,092	30,511	8,558	30,427	11,946	339	—	199,138
680	6,266	2,442	4,881	1,766	—	—	40,551
283	817	607	3,120	972	—	—	16,692
18,306	65,116	34,293	125,508	28,330	1,652	(7,011)	568,401
61,066	184,517	28,566	230,441	34,041	—	—	1,387,269
18,544	100,170	79,286	111,905	44,466	—	—	835,997
830	11,852	8,035	32,291	1,432	120	—	70,137
98,746	361,655	150,180	500,145	108,269	1,772	(7,011)	2,861,804
255	1,133	625	1,630	412	1,305	—	15,475
7,837	29,378	7,933	28,939	11,534	—	—	184,771
2,778	7,156	9,368	10,894	2,247	122	(7,011)	63,240
3,801	7,819	4,811	31,396	2,604	3,407	—	98,218
384	2,074	348	—	—	—	—	30,950
15,055	47,560	23,085	72,859	16,797	4,834	(7,011)	392,654
8,175	31,348	25,704	50,202	5,222	—	—	370,088
119	379	55	547	360	—	—	51,729
1,047	3,952	2,204	5,116	1,107	—	—	36,013
17,633	31,418	24,022	65,245	12,553	—	—	347,854
—	360	231	1,468	374	—	—	30,353
42,029	115,017	75,301	195,437	36,413	4,834	(7,011)	1,228,691
45,077	240,732	67,699	299,488	64,792	(3,062)	—	1,545,960
5,912	1,579	4,884	2,593	5,434	—	—	66,172
5,728	4,327	2,296	2,627	1,630	—	—	20,981
56,717	246,638	74,879	304,708	71,856	(3,062)	—	1,633,113
98,746	361,655	150,180	500,145	108,269	1,772	(7,011)	2,861,804

HOSPITAL SISTERS SERVICES, INC. –
OBLIGATED GROUP
Springfield, Illinois

Consolidating Statement of Operations Information

Year ended June 30, 2010

(Dollars in thousands)

	St. Elizabeth's Belleville, Illinois	St. Joseph's Breese, Illinois	St. Mary's Decatur, Illinois	St. Anthony's Effingham, Illinois	St. Joseph's Highland, Illinois	St. Francis Litchfield, Illinois	St. John's Springfield, Illinois
Net patient service revenues	$ 183,293	45,651	126,707	111,909	23,731	35,153	398,004
Other revenues:							
Investment income	1,970	169	1,508	457	221	246	3,806
Net assets released from restrictions used for operations	271	10	64	5	71	17	1,417
Other	5,698	987	4,134	903	551	591	14,779
Total revenues	191,232	46,817	132,413	113,274	24,574	36,007	418,006
Expenses:							
Sisters' services	—	—	2	—	25	—	310
Salaries and wages	64,907	16,796	42,643	31,442	8,565	11,517	131,938
Employee benefits	19,193	6,366	15,203	13,306	3,492	4,362	41,173
Professional fees	18,745	2,947	5,152	4,003	3,087	2,561	35,593
Supplies	26,137	4,328	17,627	18,686	2,314	3,600	86,092
Depreciation and amortization	10,819	3,363	6,968	5,964	1,364	1,570	23,020
Interest	194	158	(59)	430	137	26	2,310
Provision for uncollectible accounts	18,476	2,504	16,927	4,724	1,052	3,204	24,764
Other	46,525	7,637	34,116	19,070	5,447	6,608	83,760
Total expenses	204,996	44,099	138,579	97,625	25,483	33,448	428,960
Income (loss) from operations	(13,764)	2,718	(6,166)	15,649	(909)	2,559	(10,954)
Nonoperating income (loss):							
Investment income (loss)	2,049	3,895	740	12,161	74	486	32,296
Revenues in excess (deficient) of expenses and nonoperating income (loss)	(11,715)	6,613	(5,426)	27,810	(835)	3,045	21,342
Other changes in unrestricted net assets:							
Net assets released from restrictions used for the purchase of property, plant, and equipment	202	470	405	380	—	47	—
Transfer from (to) affiliates	(1,134)	588	(1,593)	441	(136)	(187)	(17,800)
Recognition of change in pension funded status	(16,478)	(3,484)	(13,434)	(8,917)	(2,816)	(4,414)	(46,944)
Change in unrestricted net assets	$ (29,125)	4,187	(20,048)	19,714	(3,787)	(1,509)	(43,402)

See accompanying independent auditors' report.

Schedule 2

St. Mary's Streator, Illinois	St. Joseph's Chippewa Falls, Wisconsin	Sacred Heart Eau Claire, Wisconsin	St. Mary's Green Bay, Wisconsin	St. Vincent Green Bay, Wisconsin	St. Nicholas Sheboygan, Wisconsin	Hospital Sisters Services, Inc.	Eliminations	Total
59,661	61,512	187,884	108,390	359,857	64,238	—	(1,813)	1,764,177
257	13	87	33	123	14	165	—	9,069
27	112	704	38	329	428	—		3,493
751	1,913	3,305	5,414	7,546	3,821	4	(235)	50,162
60,696	63,550	191,980	113,875	367,855	68,501	169	(2,048)	1,826,901
—	—	—	—	149	—	—	—	486
20,645	24,228	59,627	33,189	85,150	21,078	—	—	551,725
7,044	8,747	19,553	12,032	29,267	8,000	—	—	187,738
5,561	2,018	7,086	2,791	11,430	5,752	—	(1,813)	104,913
7,260	5,312	34,301	16,876	54,251	10,614	—	—	287,398
4,330	2,429	12,464	5,898	16,453	5,206	—	—	99,848
205	24	515	441	669	27	165	—	5,242
3,028	2,386	1,933	4,260	9,721	1,925	—	—	94,904
12,346	11,327	32,668	30,304	149,334	19,113	3,403	(235)	461,423
60,419	56,471	168,147	105,791	356,424	71,715	3,568	(2,048)	1,793,677
277	7,079	23,833	8,084	11,431	(3,214)	(3,399)	—	33,224
2,200	2,701	11,960	1,265	14,901	2,330	(112)	—	86,946
2,477	9,780	35,793	9,349	26,332	(884)	(3,511)	—	120,170
39	—	280	43	241	—	—	—	2,107
(322)	(127)	(348)	(226)	1,742	(144)	(2)	—	(19,248)
(7,075)	(7,310)	(16,042)	(9,725)	(33,151)	(6,436)	—	—	(176,226)
(4,881)	2,343	19,683	(559)	(4,836)	(7,464)	(3,513)	—	(73,197)

HOSPITAL SISTERS SERVICES, INC. –
OBLIGATED GROUP
Springfield, Illinois

Consolidating Statement of Changes in Net Assets Information

Year ended June 30, 2010

(Dollars in thousands)

	St. Elizabeth's Belleville, Illinois	**St. Joseph's Breese, Illinois**	**St. Mary's Decatur, Illinois**	**St. Anthony's Effingham, Illinois**	**St. Joseph's Highland, Illinois**	**St. Francis Litchfield, Illinois**	**St. John's Springfield, Illinois**
Unrestricted net assets:							
Revenues in excess (deficient) of expenses and nonoperating income (loss)	$ (11,715)	6,613	(5,426)	27,810	(835)	3,045	21,342
Other changes in unrestricted net assets:							
Net assets released from restrictions used for the purchase of property, plant, and equipment	202	470	405	380	—	47	—
Transfer from (to) affiliate	(1,134)	588	(1,593)	441	(136)	(187)	(17,800)
Recognition of change in pension funded status	(16,478)	(3,484)	(13,434)	(8,917)	(2,816)	(4,414)	(46,944)
Change in unrestricted net assets	(29,125)	4,187	(20,048)	19,714	(3,787)	(1,509)	(43,402)
Temporarily restricted net assets:							
Investment income	408	125	798	145	148	167	1,815
Contributions	442	112	2,799	291	117	(23)	2,002
Net assets released from restrictions	(473)	(480)	(469)	(385)	(71)	(64)	(1,417)
Change in temporarily restricted net assets	377	(243)	3,128	51	194	80	2,400
Investment income	—	—	—	—	—	—	—
Contributions	6	—	—	—	—	—	60
Change in permanently restricted net assets	6	—	—	—	—	—	60
Change in net assets	(28,742)	3,944	(16,920)	19,765	(3,593)	(1,429)	(40,942)
Net assets at beginning of year	75,157	65,587	82,623	178,411	5,760	18,553	471,587
Net assets at end of year	$ 46,415	69,531	65,703	198,176	2,167	17,124	430,645

See accompanying independent auditors' report.

Schedule 3

St. Mary's Streator, Illinois	St. Joseph's Chippewa Falls, Wisconsin	Sacred Heart Eau Claire, Wisconsin	St. Mary's Green Bay, Wisconsin	St. Vincent Green Bay, Wisconsin	St. Nicholas Sheboygan, Wisconsin	Hospital Sisters Services, Inc.	Eliminations	Total
2,477	9,780	35,793	9,349	26,332	(884)	(3,511)	—	120,170
39	—	280	43	241	—	—	—	2,107
(322)	(127)	(348)	(226)	1,742	(144)	(2)	—	(19,248)
(7,075)	(7,310)	(16,042)	(9,725)	(33,151)	(6,436)	—	—	(176,226)
(4,881)	2,343	19,683	(559)	(4,836)	(7,464)	(3,513)	—	(73,197)
166	809	609	499	459	637	—	—	6,785
44	509	162	1,111	121	98	—	—	7,785
(66)	(112)	(984)	(81)	(570)	(428)	—	—	(5,600)
144	1,206	(213)	1,529	10	307	—	—	8,970
—	—	35	—	—	—	—	—	35
20	100	93	—	29	10	—	—	318
20	100	128	—	29	10	—	—	353
(4,717)	3,649	19,598	970	(4,797)	(7,147)	(3,513)	—	(63,874)
56,333	53,068	227,040	73,909	309,505	79,003	451	—	1,696,987
51,616	56,717	246,638	74,879	304,708	71,856	(3,062)	—	1,633,113