



CONSOLIDATED FINANCIAL STATEMENTS  
AND CONSOLIDATING INFORMATION

Indiana University Health Bloomington Hospital and Affiliates  
(formerly known as Bloomington Hospital, Inc. and Affiliates)  
Years Ended December 31, 2010 and 2009  
With Reports of Independent Auditors

Ernst & Young LLP

 **ERNST & YOUNG**

Indiana University Health Bloomington Hospital and Affiliates

Consolidated Financial Statements and  
Consolidating Information

Years Ended December 31, 2010 and 2009

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## Report of Independent Auditors

The Board of Directors  
Indiana University Health Bloomington Hospital and Affiliates

We have audited the accompanying consolidated balance sheets of Indiana University Health Bloomington Hospital and Affiliates (IU Health Bloomington) as of December 31, 2010 and 2009, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of IU Health Bloomington's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of IU Health Bloomington's internal control over financial reporting. Our audits included 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 IU Health Bloomington'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 consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Indiana University Health Bloomington Hospital and Affiliates at December 31, 2010 and 2009, and the consolidated results of their operations and changes in their net assets and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

*Ernst & Young LLP*

April 22, 2011

# Indiana University Health Bloomington Hospital and Affiliates

## Consolidated Balance Sheets

*(Thousands of Dollars)*

|  | December 31 |            |
|--|-------------|------------|
|  | 2010        | 2009       |
| <b>Assets</b>  |             |            |
| Current assets:  |             |            |
| Cash and cash equivalents  | \$ 55,672   | \$ 42,639  |
| Patient accounts receivable, less allowance<br>for uncollectible accounts of \$14,767 and<br>\$13,689 at 2010 and 2009, respectively | 41,903      | 38,275     |
| Prepaid expenses   | 9,888       | 9,149      |
| Inventories  | 5,636       | 5,780      |
| Current portion of trustee-held funds  | 4,428       | 4,501      |
| Total current assets   | 117,527     | 100,344    |
| Assets limited as to use:  |             |            |
| Board-designated investment funds  | 99,701      | 82,512     |
| Property and equipment:  |             |            |
| Cost of property and equipment in service  | 358,860     | 353,489    |
| Less accumulated depreciation  | (229,586)   | (214,309)  |
|  | 129,274     | 139,180    |
| Construction-in-progress   | 2,149       | 761        |
| Total property and equipment, net  | 131,423     | 139,941    |
| Other assets:  |             |            |
| Equity interest in unconsolidated subsidiaries   | 2,318       | 2,137      |
| Interest in net assets of foundations  | 4,314       | 4,109      |
| Unamortized bond issuance costs  | 715         | 790        |
| Other  | 2,889       | 603        |
| Total other assets   | 10,236      | 7,639      |
| Total assets   | \$ 358,887  | \$ 330,436 |

Indiana University Health Bloomington Hospital and Affiliates

Consolidated Balance Sheets

(Thousands of Dollars)

|  | December 31       |                   |
|--|-------------------|-------------------|
|  | 2010              | 2009              |
| <b>Liabilities and net assets</b>                |                   |                   |
| Current liabilities:                             |                   |                   |
| Accounts payable and accrued expenses            | \$ 9,870          | \$ 8,748          |
| Accrued salaries, wages, and related liabilities | 26,092            | 21,046            |
| Estimated third-party payor allowances           | 5,434             | 4,940             |
| Current portion of long-term debt                | 8,123             | 9,370             |
| Total current liabilities                        | <u>49,519</u>     | <u>44,104</u>     |
| Noncurrent liabilities:                          |                   |                   |
| Long-term debt, less current portion             | 50,883            | 59,358            |
| Accrued pension obligations                      | 10,339            | 10,805            |
| Accrued medical malpractice claims               | 1,809             | 1,822             |
| Other  | 216               | 216               |
| Total noncurrent liabilities                     | <u>63,247</u>     | <u>72,201</u>     |
| Total liabilities                                | <u>112,766</u>    | <u>116,305</u>    |
| Net assets:                                      |                   |                   |
| Indiana University Health Bloomington            | 241,648           | 210,023           |
| Noncontrolling interest in affiliates            | 160               | -                 |
| Total unrestricted                               | <u>241,808</u>    | <u>210,023</u>    |
| Temporarily restricted                           | 3,679             | 3,474             |
| Permanently restricted                           | 634               | 634               |
| Total net assets                                 | <u>246,121</u>    | <u>214,131</u>    |
| <br>   |                   |                   |
| Total liabilities and net assets                 | <u>\$ 358,887</u> | <u>\$ 330,436</u> |

See accompanying notes.

Indiana University Health Bloomington Hospital and Affiliates  
Consolidated Statements of Operations and Changes in Net Assets  
*(Thousands of Dollars)*

|  | <b>Year Ended December 31</b> |             |
|--|-------------------------------|-------------|
|  | <b>2010</b>                   | <b>2009</b> |
| Revenues:                                      |                               |             |
| Net patient service revenue                    | \$ 348,921                    | \$ 340,250  |
| Other revenue                                  | 10,437                        | 7,329       |
| Total operating revenues                       | <b>359,358</b>                | 347,579     |
| Expenses:                                      |                               |             |
| Salaries, wages, and benefits                  | 181,308                       | 167,910     |
| Supplies, drugs, purchased services, and other | 110,780                       | 107,208     |
| Depreciation and amortization                  | 18,470                        | 18,598      |
| Provision for uncollected patient accounts     | 27,842                        | 32,670      |
| Interest                                       | 2,916                         | 3,024       |
| Total operating expenses                       | <b>341,316</b>                | 329,410     |
| Operating income                               | <b>18,042</b>                 | 18,169      |
| Nonoperating income (losses):                  |                               |             |
| Investment income, net                         | 12,182                        | 13,222      |
| Total nonoperating income                      | <b>12,182</b>                 | 13,222      |
| Consolidated excess of revenues over expenses  | <b>30,224</b>                 | 31,391      |

*Continued on next page.*

## Indiana University Health Bloomington Hospital and Affiliates

### Consolidated Statements of Operations and Changes in Net Assets (continued) (Thousands of Dollars)

|  | December 31<br>2010      |                          |                      | December 31<br>2009 |                   |                |
|--|--------------------------|--------------------------|----------------------|---------------------|-------------------|----------------|
|  | Total                    | Controlling              | Noncontrolling       | Total               | Controlling       | Noncontrolling |
| Unrestricted net assets:                                   |                          |                          |                      |                     |                   |                |
| Excess of revenues over expenses                           | \$ 30,224                | \$ 30,224                | \$ -                 | \$ 31,391           | \$ 31,391         | \$ -           |
| Change in pension obligations                              | 1,204                    | 1,204                    | -                    | 8,829               | 8,829             | -              |
| Foundation contributions for capital expenditures          | 197                      | 197                      | -                    | -                   | -                 | -              |
| Noncontrolling interest acquired                           | 160                      | -                        | 160                  | -                   | -                 | -              |
| Increase in unrestricted net assets                        | <u>31,785</u>            | <u>31,625</u>            | <u>160</u>           | 40,220              | 40,220            | -              |
| Temporarily restricted net assets:                         |                          |                          |                      |                     |                   |                |
| Change in beneficial interest in net assets of foundations | 205                      | 205                      | -                    | 322                 | 322               | -              |
| Increase in temporarily restricted net assets              | <u>205</u>               | <u>205</u>               | <u>-</u>             | 322                 | 322               | -              |
| Permanently restricted net assets:                         |                          |                          |                      |                     |                   |                |
| Change in beneficial interest in net assets of foundations | -                        | -                        | -                    | 83                  | 83                | -              |
| Increase in permanently restricted net assets              | <u>-</u>                 | <u>-</u>                 | <u>-</u>             | 83                  | 83                | -              |
| Increase in net assets                                     | <b>31,990</b>            | <b>31,830</b>            | <b>160</b>           | 40,625              | 40,625            | -              |
| Net assets at beginning of year                            | <u>214,131</u>           | <u>214,131</u>           | <u>-</u>             | 173,506             | 173,506           | -              |
| Net assets at end of year                                  | <u><b>\$ 246,121</b></u> | <u><b>\$ 245,961</b></u> | <u><b>\$ 160</b></u> | <u>\$ 214,131</u>   | <u>\$ 214,131</u> | <u>\$ -</u>    |

*See accompanying notes.*

# Indiana University Health Bloomington Hospital and Affiliates

## Consolidated Statements of Cash Flows

*(Thousands of Dollars)*

|   | <b>Year Ended December 31</b> |                  |
|---|-------------------------------|------------------|
|   | <b>2010</b>                   | <b>2009</b>      |
| <b>Operating activities</b>   |                               |                  |
| Increase in net assets  | \$ 31,990                     | \$ 40,625        |
| Adjustments to reconcile increase in net assets to net cash provided by operating activities: |                               |                  |
| Change in pension liability   | (1,204)                       | (8,829)          |
| Income in unconsolidated subsidiaries   | (1,437)                       | (712)            |
| Provision for uncollected patient accounts  | 27,842                        | 32,670           |
| Depreciation and amortization   | 18,470                        | 18,598           |
| Gain on sale of equipment   | 24                            | 606              |
| Change in net assets held by foundations and contributions for capital expenditures           | (402)                         | (405)            |
| Trading securities  | (17,116)                      | (17,578)         |
| Other   | (160)                         | -                |
| Net changes in operating assets and liabilities:  |                               |                  |
| Patient accounts receivable   | (31,200)                      | (27,396)         |
| Inventories and other assets  | 313                           | (591)            |
| Accounts payable, accrued and other liabilities   | 1,847                         | (3,858)          |
| Salaries, wages, and related liabilities  | 5,046                         | 664              |
| Estimated third-party payor allowances  | 494                           | 1,982            |
| Net cash provided by operating activities   | <b>34,507</b>                 | <b>35,776</b>    |
| <b>Investing activities</b>   |                               |                  |
| Purchase of property and equipment, net of disposals  | (9,826)                       | (15,505)         |
| Investment in joint venture   | -                             | (250)            |
| Other   | (2,123)                       | 38               |
| Net cash used in investing activities   | <b>(11,949)</b>               | <b>(15,717)</b>  |
| <b>Financing activities</b>   |                               |                  |
| Repayments on long-term debt  | (9,722)                       | (8,471)          |
| Contributions received for capital expenditures   | 197                           | -                |
| Net cash used in financing activities   | <b>(9,525)</b>                | <b>(8,471)</b>   |
| Increase in cash and cash equivalents   | <b>13,033</b>                 | 11,588           |
| Cash and cash equivalents at beginning of year  | <b>42,639</b>                 | 31,051           |
| Cash and cash equivalents at end of year  | <b>\$ 55,672</b>              | <b>\$ 42,639</b> |

*See accompanying notes.*

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (Thousands of Dollars)

December 31, 2010

### 1. Organization and Nature of Operations

#### Name Change

During 2010, Bloomington Hospital, Inc. filed a Certificate of Assumed Business Name with the Secretary of the State of Indiana for itself and certain of its subsidiaries to change the “doing business as” names of the entities to include specific reference to Indiana University Health. No change in the corporate structure, management, or governance was made as a result of this name change.

These 2010 financial statements reflect the name change for Indiana University Health Bloomington Hospital and the following affiliates:

| Previously Known As                  | Do Business As  |
|--------------------------------------|---|
| Bloomington Hospital, Inc.           | Indiana University Health Bloomington Hospital        |
| Bloomington Hospital Orange County   | Indiana University Health Paoli Hospital              |
| Southern Indiana Medical Group, Inc. | Indiana University Health Southern Indiana Physicians |

#### Organization and Nature of Operations

The consolidated financial statements of Indiana University Health Bloomington Hospital and Affiliates (IU Health Bloomington) include Indiana University Health Bloomington Hospital (BH), a not-for-profit corporation; Indiana University Health Southern Indiana Physicians (SIP), a wholly owned for-profit group of medical practices; Indiana University Health Paoli Hospital (PH), a not-for-profit corporation whose sole member is BH; HealthLINC (HL), a not-for-profit corporation whose sole member is BH; and the Bloomington Endoscopy Center (BEC), a for-profit joint venture between BH and Premier Healthcare in which BH acquired a 51% interest on December 31, 2010.

BH and PH are general acute care facilities providing inpatient and outpatient services to citizens of Bloomington, Indiana; Paoli, Indiana; and the surrounding communities through acute care and specialty care facilities. SIP provides physician services to citizens of Bloomington, Indiana, and the surrounding communities. HL is a health information exchange organized to coordinate and facilitate the sharing of health information among various community-based health care providers. BEC is a licensed ambulatory surgery center providing endoscopic diagnostic and treatment services to citizens of Bloomington, Indiana, and surrounding communities.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### **1. Organization and Nature of Operations (continued)**

On December 31, 2009, and effective as of that date, Bloomington Hospital, Inc. finalized an Integration Agreement with Clarian Health Partners, Inc. whereby Clarian Health Partners, Inc. became the sole corporate member of Bloomington Hospital, Inc. The Integration Agreement was designed to enable both organizations to further their common charitable missions of improving the health of their respective patients and the communities they serve. Clarian Health Partners, Inc., now known as Indiana University Health, is a not-for-profit organization that operates as a statewide delivery system with a central location in Indianapolis. Under the Integration Agreement, Indiana University Health Bloomington Hospital became a part of the Indiana University Health health care delivery system and serves as the regional hub for South Central Indiana.

IU Health Bloomington was previously affiliated with the Local Council of Women of Bloomington, Indiana, Inc. (the Local Council), a not-for-profit corporation, which is related to and affiliated with Bloomington Hospital Foundation, Inc. (the Foundation) and Bloomington Hospital Auxiliary (the Auxiliary).

### **2. Community Benefit and Charity Care**

IU Health Bloomington provides health care services and other financial support through various programs that are designed, among other matters, to enhance the health of the community, improve the health of low-income patients, and foster medical education and research. In addition, IU Health Bloomington provides services intended to benefit the poor and underserved, including those persons who cannot afford health insurance because of inadequate resources or are uninsured or underinsured. Health care services to patients under government programs, such as Medicare and Medicaid, are also considered part of the IU Health Bloomington's benefit provided to the community since a substantial portion of such services are reimbursed at amounts less than cost.

IU Health Bloomington's financial assistance policy is designed to provide care to patients regardless of their ability to pay. Patients who meet certain criteria for charity care (generally based on up to 400% of federal poverty income guidelines) are provided care without charge or at amounts less than established rates. In addition, financial assistance is available to patients under IU Health Bloomington policies in which services are to be provided at discounted rates, generally determined based on federal poverty income guidelines.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

*(Thousands of Dollars)*

### **2. Community Benefit and Charity Care (continued)**

The amount of charity care provided is determined based on the qualifying criteria, as defined in the financial assistance policy, through approved applications completed by patients and their families or beneficiaries, or based on analysis of patients without third-party insurance coverage who did not apply for charity and whose income was equal to or less than 200% of federal poverty income guidelines. No payment for services is anticipated for those patients whose charity care applications have been approved. Charity care, measured by the difference between standard charges for services rendered and the amount, if any, ultimately received, was \$26,223 and \$20,219 in 2010 and 2009, respectively. In addition, IU Health Bloomington provides a significant amount of uncompensated care to other uninsured and underinsured patients, which is included in the provision for uncollected patient accounts.

Enacted March 23, 2010, the Patient Protection and Affordable Care Act (the Affordable Care Act) requires, among other things, that hospital organizations establish a financial assistance policy and a policy relating to emergency medical care. Both hospital organizations of IU Health Bloomington have adopted a written financial assistance policy which conforms with the Affordable Care Act and includes financial assistance eligibility criteria, the basis for calculating amounts charged to patients, and the method for applying financial assistance, billing, and collections policies with regards to actions that may be taken in the case of nonpayment, as well as their measures to widely publicize the policy within the community served by the organization. Additionally, all of IU Health Bloomington's organizations have adopted written policies requiring the organizations to provide, without discrimination, care for emergency medical conditions to individuals regardless of their eligibility under their financial assistance policy. These hospital organizations have also adopted policies to limit the amount charged for emergency or other medically necessary care that is provided to individuals eligible for assistance under the organization's financial assistance policy to not more than the amounts generally billed to individuals who have insurance covering such care. Finally, both hospital organizations have adopted policies to forgo extraordinary collection actions against an individual before the organization has made reasonable efforts to determine whether the individual is eligible for assistance under IU Health Bloomington's financial assistance policy. Conformance with the Affordable Care Act did not have a material impact on the consolidated financial position or results of operations of IU Health Bloomington for the year ended December 31, 2010.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### **2. Community Benefit and Charity Care (continued)**

Reimbursements are received by IU Health Bloomington for Medicare and Medicaid beneficiaries in accordance with reimbursement agreements and related regulatory rules and regulations. Also, IU Health Bloomington receives certain additional Medicaid Disproportionate Share (DSH) payments from the state of Indiana for those patients who qualify as medically indigent. These reimbursements and payments are less than the cost of providing the related services.

### **3. Summary of Significant Accounting Policies**

#### **Principles of Consolidation**

The accompanying consolidated financial statements include the accounts of IU Health Bloomington (parent), BH, SIP, PH, HL, and BEC. All significant inter-entity transactions have been eliminated in consolidation.

#### **Equity Interest in Unconsolidated Organizations**

Investments in entities where BH or its affiliates own more than 20% and less than 51% and do not have significant operational influence are recorded under the equity method (see Note 11). Under the equity method, original investments are recorded at cost and adjusted for IU Health Bloomington and its affiliates' share of undistributed earnings or losses of these entities. Equity in income or loss of these entities is included in other revenue in the accompanying consolidated statements of operations and changes in net assets.

An investment in an entity where IU Health Bloomington and its affiliates own less than 20% and do not have significant operating influence is recorded at cost.

#### **Use of Estimates**

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 3. Summary of Significant Accounting Policies (continued)

#### Fair Values of Financial Instruments

Financial instruments include cash and cash equivalents, patient accounts receivable, assets whose use is limited, accounts payable and accrued expenses, estimated third-party payer allowances, notes payable to banks, long-term debt, and certain other current assets and liabilities. The fair values for cash and cash equivalents, patient accounts receivable, accounts payable and accrued expenses, estimated third-party payer allowances, notes payable to banks, and certain other current assets and liabilities approximate the carrying amounts reported in the consolidated balance sheets and, in the opinion of management, represent highly liquid assets or short-term obligations. The fair values for assets limited as to use and long-term debt are described in Notes 4 and 6.

In September 2009, accounting guidance was issued to define how to measure the fair value of alternative investments held in the pension plan, as defined in the guidance. This guidance also requires additional disclosures for organizations that hold alternative investments. This guidance was effective for interim and annual periods ended after December 15, 2009. The adoption of this guidance did not have a material impact on IU Health Bloomington's consolidated financial condition or results of operations.

In January 2010, accounting guidance was issued to further expand disclosure requirements related to fair value measurements. Additional disclosures under this guidance include disclosing transfers in and out of Level 1 and Level 2 fair value measurements and the reasons for those transfers, valuation techniques and inputs used to measure Level 2 and Level 3 fair value measurements, and disclosure of purchases, sales, issuances, and settlements separately within the Level 3 fair value measurement reconciliation. IU Health Bloomington adopted this guidance effective January 1, 2010.

#### Net Patient Service Revenue

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

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### **3. Summary of Significant Accounting Policies (continued)**

BH and PH have agreements with third-party payers that provide for payments at amounts different from established rates. A summary of the payment arrangements with major third-party payers follows.

#### **Medicare**

BH's inpatient acute care services rendered to Medicare program beneficiaries, including capital costs, are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, Diagnostic-Related Groups (DRG), and other factors. BH's outpatient services are paid under a separate prospective payment methodology. PH has been classified by the Centers for Medicare and Medicaid Services (CMS) as a Critical Access Hospital (CAH). Under the CAH program, both inpatient acute care and outpatient services are paid based on reasonable cost methodologies.

BH and PH are reimbursed for certain services at a tentative rate with final settlement determined after submission of annual cost reports and audits thereof by the Medicare fiscal intermediary.

Medicare cost reports have been audited by the Medicare fiscal intermediary through fiscal year 2006 for BH and through fiscal year 2008 for PH. Medicare patients accounted for approximately 45% of gross patient charges in 2010 and 44% of gross patient charges in 2009.

#### **Medicaid**

BH and PH inpatient and outpatient services rendered to Medicaid program beneficiaries currently are reimbursed based on inpatient DRG rates and prospectively determined outpatient fee schedules based on cost. Medicaid patients accounted for approximately 11% of gross charges in 2010 and 2009.

#### **Other**

BH and PH have also entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to BH and PH under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined rates.

Indiana University Health Bloomington Hospital and Affiliates

Notes to Consolidated Financial Statements (continued)

(Thousands of Dollars)

**3. Summary of Significant Accounting Policies (continued)**

A reconciliation of the amount of services provided to patients at established rates to net patient service revenue as presented in the consolidated statements of operations and changes in net assets is as follows:

|   | <b>December 31</b> |                   |
|---|--------------------|-------------------|
|   | <b>2010</b>        | <b>2009</b>       |
| Inpatient services                              | \$ 339,938         | \$ 302,807        |
| Outpatient services                             | 376,915            | 356,324           |
|   | <b>716,853</b>     | 659,131           |
| Less charity care revenues foregone             | 26,224             | 20,219            |
| Gross patient charges                           | <b>690,629</b>     | 638,912           |
| Less contractual allowances and other discounts | <b>341,708</b>     | 298,662           |
| Net patient service revenue                     | <b>\$ 348,921</b>  | <b>\$ 340,250</b> |

Net patient service revenue is reported at estimated net realizable amounts from patients, third-party payers, and others for services rendered and includes estimated retroactive revenue adjustments due to future audits, reviews, and investigations.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Adjustments to prior year Medicare estimates for these items resulted in an increase in net patient service revenue of \$1,556 and \$818 in 2010 and 2009, respectively.

State DSH payments are recorded when management believes payments are probable and reasonably estimable.

In August 2009, the state of Indiana provided notice to BH and PH of their state DSH program participation eligibility period. During 2010, both hospitals were required to submit new Medicaid DSH eligibility surveys to determine program eligibility status for state fiscal years 2010 and 2011. PH continued to qualify for the state DSH program for state fiscal years 2010 and 2011. However, the state of Indiana notified BH that it failed to qualify for this eligibility period.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 3. Summary of Significant Accounting Policies (continued)

The following summary gives effect to using historical information to report state DSH revenue recognized and the state fiscal year to which the revenues relate:

|   | Year Ended December 31 |                  |
|---|------------------------|------------------|
|   | 2010                   | 2009             |
| Operating income, excluding state DSH revenue | \$ 16,281              | \$ 10,314        |
| 2009  | –                      | 7,084            |
| 2010  | 1,761                  | –                |
| Operating income, as reported                 | <u>\$ 18,042</u>       | <u>\$ 17,398</u> |

There were no state DSH payments receivable at either December 31, 2010 or 2009.

### Cash and Cash Equivalents

Investments in highly liquid instruments with an original maturity of three months or less when purchased, excluding assets whose use is limited, are considered by management to be cash equivalents. IU Health Bloomington routinely invests in money market funds. These funds generally invest in highly liquid U.S. government and agency obligations. IU Health Bloomington places its cash and cash equivalents with institutions with high credit quality.

### Accounts Receivable and Allowance for Uncollectible Accounts

IU Health Bloomington and its affiliates extend credit to patients, substantially all of whom are residents of the state of Indiana, and do not require collateral or other security for the delivery of health care services. However, assignment of benefit payments payable under patients' health insurance programs and plans (e.g., Medicare, Medicaid, health insurance organizations, and commercial insurance policies) is routinely obtained, consistent with industry practice.

The provision for uncollectible patient accounts is based upon management's assessment of historical and expected net collections considering business and economic conditions, trends in health care coverage, and other collection indicators. Management routinely assesses the adequacy of the allowance for uncollectible accounts based upon accounts receivable payer composition and aging, and historical write-off experience by payer category as adjusted for collection indicators. In addition, IU Health Bloomington follows established guidelines for

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

(Thousands of Dollars)

### 3. Summary of Significant Accounting Policies (continued)

placing certain past due patient balances with collection agencies, which are charged against the allowance for uncollectible accounts in accordance with the collection policies of IU Health Bloomington.

IU Health Bloomington grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payer agreements. The mix of gross receivables from patients and third-party payers for 2010 and 2009 was as follows:

|                           | <b>2010</b> | <b>2009</b> |
|---------------------------|-------------|-------------|
| Medicare                  | <b>39%</b>  | 24%         |
| Medicaid                  | <b>9</b>    | 3           |
| Commercial insurance      | <b>32</b>   | 54          |
| Self-pay and other payers | <b>20</b>   | 19          |
|                           | <b>100%</b> | 100%        |

A managed care payor represented 27% and 26% of net patient accounts receivables at December 31, 2010 and 2009, respectively.

BH has an arrangement with Monroe Bank to finance certain patient accounts receivable, with recourse to BH if the guarantor does not pay such amounts. Such receivables totaled approximately \$2,291 and \$1,861 at December 31, 2010 and 2009, respectively. PH has a similar relationship with Monroe Bank to finance certain of its patient accounts receivable. PH receivables with Monroe Bank totaled approximately \$292 and \$389 at December 31, 2010 and 2009, respectively.

### Inventories

Inventories, consisting of medical, pharmaceutical, dietary, surgical, office, and cleaning supplies, are determined by physical count and are priced and carried at the lower of cost (first-in, first-out method for pharmacy and surgery and weighted-average method for all other inventory) or market.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

*(Thousands of Dollars)*

### **3. Summary of Significant Accounting Policies (continued)**

#### **Assets Whose Use is Limited**

Assets whose use is limited consist of Board-designated funds and funds held by the trustee under the trust indenture and related agreements. Board-designated funds are to be used for retirement of long-term debt and capital replacement, but may be used for other purposes at the discretion of the Board of Directors. Investments in equity and debt securities are measured at fair value. Management considers all investments, excluding investments in Funds of Funds, to be trading and, accordingly, all realized and unrealized gains and losses are recorded as non-operating gains and losses in the accompanying consolidated statements of operations and changes in net assets.

Funds held by the trustee are to be used for payment of principal and interest. These investments consist principally of U.S. government securities.

IU Health Bloomington is a limited partner in funds that focus on absolute return investment strategies. These investments are accounted for using the equity method of accounting, based on the fund's financial information.

#### **Property and Equipment**

Property and equipment are recorded at cost or, if donated, at fair market value at the date of donation. Routine maintenance and repairs are charged to expense as incurred. Gains and losses on the sale of property and equipment are recorded in the period sold. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of acquiring those assets.

Equipment under capital lease obligations is amortized on the straight-line method over the lease term or the estimated useful life of the equipment, whichever period is shorter. Such amortization is included with depreciation in the consolidated statements of operations and changes in net assets.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### **3. Summary of Significant Accounting Policies (continued)**

#### **Unamortized Bond Issuance Costs and Bond Discount or Premium**

Deferred financing costs include costs associated with the issuance of long-term debt, primarily underwriting fees, and are carried at cost, net of accumulated amortization. Depreciation and amortization expense reported in the consolidated statements of operations and changes in net assets includes approximately \$105 and \$112 of amortization expense for the years ended December 31, 2010 and 2009, respectively. Bond issuance costs are amortized using the effective interest method over the terms of the various bond issues.

#### **Noncontrolling Interest in Subsidiaries**

In December 2007, accounting guidance was issued related to noncontrolling (minority) interests in a consolidated subsidiary. This guidance became effective for not-for-profit organizations for fiscal years beginning after December 15, 2009, and, among other matters, requires the recognition of a noncontrolling interest as net assets in the consolidated financial statements and separate from the parent's net assets. The amount of net income attributable to the noncontrolling interest is included in consolidated excess of revenues over expenses in the consolidated statements of operations and changes in net assets. IU Health Bloomington adopted the guidance on January 1, 2010. This accounting guidance also stated that a portion of the excess of revenues over expenses would be allocated (on a prospective basis) to the noncontrolling interest even if the majority interest had not been credited the full amount of losses it had absorbed under prior guidance. The adoption of this guidance did not have a material impact on IU Health Bloomington's consolidated financial condition or results of operations.

#### **Contributions and Temporarily and Permanently Restricted Net Assets**

Unconditional promises to give cash and other assets to IU Health Bloomington and its affiliates are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. Permanently restricted net assets have been restricted by donors to be maintained for the benefit of BH in perpetuity. Temporarily restricted net assets are those whose use by BH has been limited by donors to a specific time period or purpose. When a donor restriction expires, that is, when a stipulated time restriction

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

(Thousands of Dollars)

### 3. Summary of Significant Accounting Policies (continued)

ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions. When the restriction of a temporarily restricted contribution is satisfied in the same reporting period as it is received, it is reported as other operating revenues if it is a program restriction or as unrestricted net assets if it is a capital expenditure restriction.

Temporarily restricted net assets are those whose use by IU Health Bloomington has been limited by donors to a specific time period or purpose.

Temporarily restricted net assets as of December 31, 2010 and 2009, are available for the following purposes:

|                          | <b>December 31</b> |                 |
|--------------------------|--------------------|-----------------|
|                          | <b>2010</b>        | <b>2009</b>     |
| Medical education        | \$ 114             | \$ 109          |
| Clinical/patient support | <b>3,565</b>       | 3,365           |
|                          | <b>\$ 3,679</b>    | <b>\$ 3,474</b> |

Permanently restricted net assets have been restricted by donors to be maintained in perpetuity. Income from permanently restricted net assets is to be used for clinical and patient support.

### Interest in Net Assets of the Foundation

In accordance with accounting guidance, BH recognizes an asset equal to its interest in the Foundation. BH's interest is adjusted for BH's share of the change in temporarily and permanently restricted net assets of the Foundation. The Foundation contributed \$197 and \$0 to BH for capital purchases during 2010 and 2009, respectively.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 3. Summary of Significant Accounting Policies (continued)

#### Operating and Performance Indicators

The activities of IU Health Bloomington and its affiliates are primarily related to providing healthcare services and, accordingly, expense information by functional classification is not used as a basis for measuring performance. Further, since substantially all resources are derived from providing healthcare services, similar to that if provided by a business enterprise, the following indicators are considered important in evaluating how well management has discharged its stewardship responsibilities:

**Operating Indicator (Operating Income)** – Includes all unrestricted revenue, gains and other support, and expenses directly related to the recurring and ongoing health care operations during the reporting period and to equity in the earnings of unconsolidated investments. The operating indicator excludes investment income, including realized and unrealized gains and losses on investments, and gains and losses deemed by management not to be directly related to providing health care services.

**Performance Indicator (Excess of Revenues and Gains Over Expenses)** – The performance indicator excludes changes in pension obligation and contributions for capital expenditures.

#### Income Taxes

BH, PH, and HL are exempt from federal income taxes on related functional income pursuant to Section 501(a) of the Internal Revenue Code (IRC) as an organization described in Section 501(c)(3) of the IRC. Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences of tax and financial statement differences. SIP is a taxable corporation with a net operating loss carry-forward at December 31, 2010, of \$7.8 million, which is available to offset future federal and state taxable income. The net operating loss expires in periods from 2011 through 2030. A valuation allowance has been provided against any deferred tax asset related to these losses, as it is more likely than not that the deferred tax asset will not be realized.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### **3. Summary of Significant Accounting Policies (continued)**

#### **Reclassifications**

Certain amounts in the 2009 consolidated financial statements have been reclassified to conform to the 2010 presentation and to the accounting policies of Indiana University Health. Such reclassifications had no effect on previously reported deficit of revenues and losses over expenses, or net assets.

#### **Subsequent Events**

For the consolidated financial statements as of and for the year ended December 31, 2010, management has evaluated subsequent events through April 22, 2011, the date that these consolidated financial statements were available to be issued.

#### **New Accounting Guidance Not Yet Applicable**

In August 2010, new accounting guidance was issued that requires cost be used as the measurement basis for charity care disclosure purposes and, for those purposes, defines cost as the direct and indirect costs of providing charity care. This guidance also requires disclosure of the method used to identify and determine costs. This guidance is effective for fiscal years beginning after December 15, 2010. Adoption of this guidance will not have an impact on IU Health Bloomington's financial condition or results of operations.

In August 2010, new accounting guidance was issued that clarifies health care entities should not net expected insurance recoveries against a related claim liability. In addition, the claim liability is determined without consideration of insurance recoveries. A cumulative-effect adjustment is to be recognized in the opening net assets in the period of adoption if a difference exists between any liabilities and insurance receivables recorded as a result of applying this new guidance. This guidance is effective for annual or interim periods beginning after December 15, 2010. IU Health Bloomington is currently evaluating the impact of adoption of this guidance on January 1, 2011, on its financial condition and results of operations, but the impact, if any, is not expected to be material.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

*(Thousands of Dollars)*

### **4. Assets Limited as to Use**

Board-designated investment funds are invested in accordance with Board-approved policies, which include, among other matters, targeted investment returns balanced by diversification of the investment portfolio, establishment of credit risk parameters, and limitation in the amount of investment in any single organization.

The estimated fair value of the assets limited as to use is determined using market information and other appropriate valuation methodologies. The methods and assumptions used to estimate the fair value of assets limited as to use are as follows: cash and cash equivalents – the carrying amounts reported in the consolidated balance sheets approximate fair value; marketable securities – the fair value amounts of marketable securities are based on quoted market prices or, if quoted market prices are not available, fair values are based on quoted market prices of comparable instruments; and other investments, including alternative investments (such as hedge funds, absolute return investments, and private equity investments) – these investments are accounted for using the equity method of accounting based upon the net asset values as determined by the administrators of each underlying fund, in consultation with and approval of the fund investment managers.

IU Health Bloomington invests, as a limited partner, in Funds of Funds that focus on absolute return investment strategies. Although execution could be limited, absolute return investment strategies are designed to reduce overall portfolio risk while producing positive investment returns regardless of market direction; however, investment returns are not guaranteed. Redemptions may be made with written notice of 95 days of each quarter-end; however, the Funds have redemption charges of 3% of net asset value for redemptions made on or before the first anniversary date of initial investment. Upon complete redemption, the Funds have “hold-back” provisions of up to 10% that are returned only after the Funds’ audited financial statements for the redemption period are issued.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 4. Assets Limited as to Use (continued)

Alternative investments include certain other risks that may not exist with other investments that are more widely traded. These risks include reliance on the skill of the fund managers, who often employ complex strategies with various financial instruments, including futures contracts, foreign currency contracts, structured notes, and interest rate, total return, and credit default swaps. Additionally, alternative investments may have limited information on a fund's underlying assets and valuation, and limited redemption or redemption-penalty provisions. Management believes that IU Health Bloomington, in consultation with its investment advisor, has the capacity to analyze and interpret the risks associated with alternative investments, and with this understanding, has determined that investing in these investments creates a balanced approach to its portfolio management.

The largest fund allocation to any fund is \$4,468 at December 31, 2010, and there are no investments in any individual fund greater than 1% of the Funds' net assets. As of December 31, 2010, there are no unfunded commitments relating to alternative investments. Changes in fair value of these Funds are included in nonoperating income and losses in the accompanying consolidated statements of operations and changes in net assets.

Assets whose use is limited consist of the following:

|   | <b>December 31</b> |             |
|---|--------------------|-------------|
|   | <b>2010</b>        | <b>2009</b> |
| Cash and cash equivalents                           | \$ 7,037           | \$ 8,032    |
| Obligations of the U.S. government and its agencies | 8,315              | 3,778       |
| Equities  | 67,317             | 50,619      |
| Mortgage-backed securities                          | 128                | 6,319       |
| Corporate bonds                                     | 12,469             | 14,607      |
| Alternative investments                             | 8,863              | 3,658       |
|   | <b>104,129</b>     | 87,013      |
| Less assets whose use is limited – current portion  | (4,428)            | (4,501)     |
| Total Board-designated funds                        | <b>\$ 99,701</b>   | \$ 82,512   |

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 4. Assets Limited as to Use (continued)

Investment income and gains and losses for assets whose use is limited included in nonoperating (losses) gains are comprised of the following:

|  | Year Ended December 31 |                  |
|--|------------------------|------------------|
|  | 2010                   | 2009             |
| <b>Investment income</b>                               |                        |                  |
| Interest and dividend income                           | \$ 64                  | \$ 64            |
| Realized gains and losses on sales of investments      | 6,056                  | (6,432)          |
| Change in net unrealized gains (losses) on investments | 6,062                  | 19,590           |
|  | <u>\$ 12,182</u>       | <u>\$ 13,222</u> |

IU Health Bloomington's investments are exposed to various kinds and levels of risk. Fixed-income securities expose IU Health Bloomington to interest rate risk, credit risk, and liquidity risk. As interest rates change, the value of many fixed-income securities is affected, particularly of those with fixed interest rates. Credit risk is the risk that the obligor of the security will not fulfill its obligation. Liquidity risk is affected by the willingness of market participants to buy and sell given securities.

Equity securities expose IU Health Bloomington to market risk, performance risk, and liquidity risk. Market risk is the risk associated with major movements of the equity markets, both foreign and domestic. Performance risk is the risk associated with a particular company's operating performance. Liquidity risk, as previously defined, tends to be higher for international equities and small capitalization equity companies.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

*(Thousands of Dollars)*

### 5. Property and Equipment

The cost of property and equipment in service is summarized as follows:

|                            | <b>December 31</b> |                   |
|----------------------------|--------------------|-------------------|
|                            | <b>2010</b>        | <b>2009</b>       |
| Land and improvements      | \$ 17,091          | \$ 15,603         |
| Buildings and improvements | 235,545            | 233,772           |
| Equipment                  | 106,224            | 104,114           |
|                            | <u>\$ 358,860</u>  | <u>\$ 353,489</u> |

Useful lives of each category of assets are based on the estimated useful time frame that the particular assets are expected to be in service, generally in accordance with guidelines established by the American Hospital Association. Assets are depreciated on a straight-line basis beginning in the month when placed in service with asset lives ranging as follows: 20–25 years for land improvements, 5–40 years for buildings and improvements, and 3–20 years for equipment.

As of December 31, 2010, material commitments for acquisition of fixed assets totaled \$10,694. Of this total, \$4,409 is committed to the purchase of and a building currently known as the Great West Building at Bloomington's North Park Office Center for the purpose of future development of a second campus for provision of BH's services. The next purchase will be made in January 2011 at a cost of \$1.5 million. The remainder of contractual commitments for purchases of property and equipment is related to various capital purchase orders still open at year-end.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 6. Debt

Long-term debt as of December 31, 2010 and 2009, consists of the following:

|  | 2010             | 2009             |
|--|------------------|------------------|
| <b>Hospital Revenue Refunding Bonds, Series 1997</b>   |                  |                  |
| Serial bonds payable in annual principal installments beginning May 1998 through May 2012 in amounts ranging from \$1,670 to \$1,945. Interest payable semiannually at annual interest rates ranging from 3.9% to 5.2%.  | \$ 3,795         | \$ 5,555         |
| Less unamortized original issue discount   | (1)              | (3)              |
|  | <b>3,794</b>     | <b>5,552</b>     |
| <b>Hospital Revenue Bonds, Series 1999B</b>  |                  |                  |
| Serial bonds, payable in annual principal installments beginning May 2013 through May 2019 in amounts ranging from \$1,275 to \$1,795. Interest payable semiannually at fixed rates of interest ranging from 6.625% to 6%.   | <b>10,630</b>    | 10,630           |
| Term bonds, payable May 2024 and 2029 in amounts of \$10,685 and \$14,250, subject to mandatory redemption through operation of a sinking fund commencing May 2020 and May 2025, respectively. Interest payable semiannually at annual interest rates of 5.875% and 6%, respectively.  | <b>24,935</b>    | 24,935           |
| Less unamortized original issue discount   | (328)            | (356)            |
|  | <b>35,237</b>    | <b>35,209</b>    |
| Tax-exempt equipment loans, payable semiannually through July 2016 in amounts ranging from \$273 to \$1,346. Interest payable semiannually at variable annual interest rates ranging from 1.32% to 1.55% at December 31, 2010.   | <b>9,183</b>     | 11,795           |
| <b>Hospital Revenue Bonds, Series 2008</b>   |                  |                  |
| Indiana Finance Authority Bonds issued for BHOC in November 2008, in amounts from \$100 to \$150, principal and interest payable quarterly beginning January 2010 through January 2019. Interest payable at a variable rate equal to the one-month London Interbank Offered Rate (LIBOR) index plus 0.55%, not to exceed 7.50%; 0.811% at December 31, 2010. | <b>3,612</b>     | 3,941            |
| Commercial note payable, Old National Bank, due May 1, 2011, principal payable annually in amounts ranging from \$3,165 to \$3,800. Interest payable monthly at a variable rate equal to the one-month LIBOR index plus 0.83%; 1.091% at December 31, 2010.  | <b>3,165</b>     | 6,965            |
| Capital leases   | <b>810</b>       | 1,213            |
| Other notes payable  | <b>3,205</b>     | 4,053            |
|  | <b>59,006</b>    | <b>68,728</b>    |
| Less current portion:  |                  |                  |
| Series 1997 bonds  | <b>1,849</b>     | 1,758            |
| BHOC Series 2008 bonds   | <b>438</b>       | 438              |
| Tax-exempt equipment loans   | <b>2,100</b>     | 2,612            |
| Commercial note payable  | <b>3,165</b>     | 3,800            |
| Capital leases   | <b>353</b>       | 414              |
| Other notes payable  | <b>218</b>       | 348              |
| Total current portion of long-term obligations   | <b>8,123</b>     | <b>9,370</b>     |
| Long-term obligations, net of current portion  | <b>\$ 50,883</b> | <b>\$ 59,358</b> |

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

*(Thousands of Dollars)*

### **6. Debt (continued)**

In July 1997, the Hospital Authority of Monroe County (the Authority) issued its Hospital Revenue Refunding Bonds, Series 1997 in the aggregate principal amount of \$17,075. BH used the proceeds of the 1997 issue to refund \$13,285 of the outstanding Hospital Revenue Bonds, Series 1992 maturing on or after May 1, 2003. Additionally, the 1997 issue refinanced the Monroe County, Indiana Economic Development Revenue Bonds, Series 1994 with the Public Health Nursing Association and was used to pay the costs of construction and renovation for certain health care facilities of BH and to pay certain issuance costs in connection therewith.

In January 1999, the Authority issued \$36,700 of Series 1999A Hospital Revenue Refunding Bonds for the benefit of BH, the sole member of the Obligated Group. The Obligated Group used the bond proceeds to refund \$35,255 of the outstanding Series 1989 debt, and the balance was used to finance the construction, renovation, remodeling, and equipping of certain health care facilities. In September 2008, BH early-retired \$300 of variable rate bonds and repaid \$11,100 of these variable rate bonds being held as Bank Bonds by Dexia Credit Local. In conjunction with this refinancing, BH borrowed \$10,565 under a note payable to Old National Bank (ONB), Bloomington, Indiana. The principal on this commercial note payable will be repaid in three annual installments ranging from \$3,165 to \$3,800. Interest is payable monthly at a variable rate equal to the one-month LIBOR index plus 0.83%. This note payable contains provisions that are not objectively determinable and allow ONB, at its sole discretion, to require accelerated payment of the note payable.

On November 17, 1999, the Authority issued \$35,565 of Series 1999B Hospital Revenue Bonds for the benefit of the Obligated Group. The 1999B bonds are collateralized by a security interest in gross revenues. Proceeds of the bonds were used to pay the costs of construction, renovation, remodeling, and equipping of certain health care facilities of BH.

In February 2006, the Authority entered into a tax-exempt equipment financing agreement with Citigroup Global Markets, Inc. for the benefit of BH. Total tax-exempt funds borrowed under this financing arrangement were \$19,962; agreement terms vary from five to ten years, based on the useful lives of the financed equipment. Rates of interest for all funding are variable, based on a fixed spread over the Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Index rate, and can be converted to fixed rates during the term of the arrangement at the discretion of BH. Payments of principal and interest will be made semiannually on January 1 and July 1, commencing with the first interest payment on

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 6. Debt (continued)

July 1, 2006, and the first payment of principal on January 1, 2007. All proceeds from this financing arrangement have been used to finance medical and computer equipment, including software licenses.

During 2007, BH assumed a \$3,743, 19-year mortgage related to the purchase of the Great West building, which is included in other notes payable.

In November 2008, the Indiana Finance Authority issued \$4,050 of Series 2008 Hospital Revenue Bonds for the benefit of PH. Proceeds of the bonds were used to pay the costs of construction, renovation, remodeling, and equipping of certain health care facilities at PH.

IU Health Bloomington's fixed rate revenue bonds had aggregate fair values, based on quoted market values, of approximately \$35,997 and \$36,996 at December 31, 2010 and 2009, respectively. The recorded value of the variable rate ONB note payable, the variable rate revenue bonds, the variable rate tax-exempt equipment loans, and other notes payable approximate fair value.

Required principal payments of IU Health Bloomington's long-term debt, excluding capitalized leases, are as follows:

|            |    |               |
|------------|----|---------------|
| 2011       | \$ | 8,123         |
| 2012       |    | 4,305         |
| 2013       |    | 3,669         |
| 2014       |    | 3,418         |
| 2015       |    | 3,391         |
| Thereafter |    | 36,100        |
|            | \$ | <u>59,006</u> |

Total interest paid on long-term debt for the years ended December 31, 2010 and 2009, aggregated \$2,942 and \$3,024, respectively.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 6. Debt (continued)

Since August 2002, BH has had a line-of-credit agreement with its primary bank, Monroe Bank of Bloomington, Indiana, under which it may borrow sums of cash as needed, to a maximum total of \$4,000. Interest accrues on such borrowings at a variable rate equal to the base rate on corporate loans posted by at least 75% of the nation's 30 largest banks, as published in *The Wall Street Journal*. Loan principal is payable upon the lender's demand or at the borrower's discretion; interest on any outstanding principal is payable monthly. There were no funds borrowed against the line of credit at either December 31, 2010 or 2009.

Land and buildings with a book value of \$4,417 and \$4,538 at December 31, 2010 and 2009, respectively, are pledged as collateral under IU Health Bloomington's notes payable.

### 7. Fair Value Measurements

Recent accounting guidance addresses aspects of the expanding application of fair value accounting. The fair value accounting guidance provides, among other matters, for the following: 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 and establishes a framework for measuring fair value; establishes a three-level hierarchy for fair value measurements based upon the observability of inputs to the valuation of an asset or liability as of the measurement date; requires consideration of nonperformance risk when valuing liabilities; and expands disclosures about instruments measured at fair value. The three-level hierarchy is based upon the nature of valuation techniques and whether such techniques are based upon observable or unobservable inputs, as defined.

Observable inputs are intended to reflect market data obtained from independent sources, while unobservable inputs may reflect market assumptions made by management or measurements made by financial specialists generally associated with the financial asset or liability. These two types of inputs create the following fair value hierarchy:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities as of the reporting date. Level 1 primarily consists of financial instruments such as money market securities and listed equities.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 7. Fair Value Measurements (continued)

- Level 2 – Pricing inputs other than quoted prices included in Level 1 that are either directly observable or that can be derived or supported from observable data as of the reporting date. Instruments in this category include certain U.S. government agency and sponsored entity debt securities.
- Level 3 – Pricing inputs include those that are significant to the fair value of the financial asset or financial liability and are not observable from objective sources. In evaluating the significance of inputs, IU Health Bloomington generally classifies assets or liabilities as Level 3 when their fair value is determined using unobservable inputs that individually or when aggregated with other observable inputs, represent more than 10% of the fair value of the assets or liabilities. These inputs may be used with internally developed methodologies that result in management’s best estimate of fair value.

The following tables set forth by level within the fair value hierarchy IU Health Bloomington’s financial assets and liabilities that were accounted for at fair value on a recurring basis as of December 31, 2010 and 2009. The financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The assessment of the significance of a particular input to the fair value measurement requires judgment, could be subject to change or variation, and may affect the valuation of fair value assets and liabilities and their classification within the fair value hierarchy levels.

| <b>December 31, 2010</b>                                    | <b>Level 1</b>    | <b>Level 2</b>   | <b>Level 3</b> | <b>Total</b>      |
|---|-------------------|------------------|----------------|-------------------|
| <b>Assets</b>   |                   |                  |                |                   |
| Cash and cash equivalents                                   | \$ 62,709         | \$ –             | \$ –           | \$ 62,709         |
| Obligations of the U.S. government<br>and its agencies      | 1,731             | 6,584            | –              | 8,315             |
| U.S. equity securities                                      | 23,059            | 2,870            | –              | 25,929            |
| Non-U.S. securities   | 40,949            | 438              | –              | 41,387            |
| Mortgage-backed securities                                  | 128               | –                | –              | 128               |
| Corporate bonds   | 6,087             | 6,382            | –              | 12,469            |
| Total assets measured at fair value<br>on a recurring basis | <u>\$ 134,663</u> | <u>\$ 16,274</u> | <u>\$ –</u>    | <u>\$ 150,937</u> |

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 7. Fair Value Measurements (continued)

| December 31, 2009   | Level 1           | Level 2          | Level 3     | Total             |
|---|-------------------|------------------|-------------|-------------------|
| <b>Assets</b>   |                   |                  |             |                   |
| Cash and cash equivalents                                   | \$ 50,670         | \$ —             | \$ —        | \$ 50,670         |
| Obligations of the U.S. government<br>and its agencies      | 3,778             | —                | —           | 3,778             |
| Equities  | 45,502            | 5,117            | —           | 50,619            |
| Mortgage-backed securities                                  | —                 | 6,319            | —           | 6,319             |
| Corporate bonds   | 5,787             | 8,820            | —           | 14,607            |
| Total assets measured at fair value<br>on a recurring basis | <u>\$ 105,737</u> | <u>\$ 20,256</u> | <u>\$ —</u> | <u>\$ 125,993</u> |

The fair value of cash and cash equivalents, which consist mainly of funds invested in money market funds, is based on quoted market prices and classified as Level 1. The fair value of Level 1 trading securities is based on quoted market prices from an active exchange. The fair value of Level 2 trading securities is based on third-party quotes based on quoted market prices of similar securities and other observable inputs.

IU Health Bloomington's \$8,864 and \$3,659 of alternative investments as of December 31, 2010 and 2009, respectively, are not included in the table because they are accounted for using the equity method of accounting (see Note 4).

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 8. Commitments and Contingencies

#### Leases

IU Health Bloomington leases various equipment and other property for use in operations. Future minimum payments under capital lease agreements with initial or remaining terms of one or more years at December 31, 2010, are as follows:

|      | <b>Future Minimum<br/>Payment Including<br/>Imputed Interest</b> | <b>Principal<br/>Payment</b> |
|------|--|------------------------------|
| 2011 | \$ 429   | \$ 353                       |
| 2012 | 279  | 235                          |
| 2013 | 235  | 222                          |
|      | \$ 943   | \$ 810                       |

IU Health Bloomington leases various medical equipment and other property for use in operations. Future minimum payments under noncancelable operating leases with initial or remaining terms of one or more years at December 31, 2010, are as follows:

|            |          |
|------------|----------|
| 2011       | \$ 1,805 |
| 2012       | 764      |
| 2013       | 703      |
| 2014       | 591      |
| 2015       | 333      |
| Thereafter | 3,209    |
|            | \$ 7,405 |

Total rental expense was \$4,648 in 2010 and \$3,128 in 2009, and is included in purchased services in the consolidated statements of operations and changes in net assets.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### **9. Medical Malpractice**

Various claims for employment matters, medical malpractice, and breach of contract have been asserted against IU Health Bloomington and its affiliates by various claimants, and provision for such claims is made in the consolidated financial statements when management considers the contingency to be probable. The claims are in various stages of processing, and some will ultimately be brought to trial. There are known incidents occurring through December 31, 2010, that may result in the assertion of additional claims, and other claims may be asserted arising from services provided to patients in the past.

Malpractice insurance coverage for BH and PH has been obtained on a claims-made basis through the state of Indiana's Patient Compensation Fund and the Reciprocal Risk Retention Group (RRRG). Should the claims-made insurance coverage not be renewed or replaced with equivalent insurance, claims based on occurrences during its term but reported subsequently will be uninsured.

Effective October 1, 2003, BH, along with other Indiana hospitals, formed an RRRG, originally known as VHA Central and currently operating as Indiana Healthcare Reciprocal Risk Retention Group (IHRRRG), for the purpose of providing hospital professional and general liability insurance. This captive insurance company was fully recognized by the state of Indiana's Patient Compensation Fund as of October 1, 2003. The book value of BH's capital investment in the captive insurance group as of December 31, 2010 and 2009, was \$855 and \$456, respectively, and is included in other noncurrent assets.

Medical malpractice coverage is provided through the aforementioned IHRRRG and considers limitations imposed by the Indiana Medical Malpractice Act (the Act). The Act limits liability for malpractice claims against qualified health care providers such as IU Health Bloomington. The law provides for a mandatory State Patient Compensation Fund (the Compensation Fund) to which qualified health care providers contribute a surcharge. The amount of surcharge is established by the Indiana Department of Insurance on an actuarial basis. The amount contributed by each hospital must be sufficient to cover, but may not exceed, the actuarial risk posed to the Compensation Fund by such hospital and its employed physicians with active Indiana medical licenses. For malpractice incidents occurring after December 31, 1989, and before July 1, 1999, the Act provides for a maximum recovery of \$750 per claim (\$3,000 annual aggregate), and the related health care provider is liable for up to \$100 of the recovery. For malpractice incidents occurring on or after July 1, 1999, the Act provides for a maximum recovery of \$1,250 per occurrence (\$7,500 annual aggregate), \$250 of which would be paid by

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### **9. Medical Malpractice (continued)**

IU Health Bloomington (through its insurance coverage to the extent available) and the remainder by the Compensation Fund.

BH and PH estimate and record liabilities related to malpractice insurance claims incurred but not reported as of the fiscal year-end, as a provision for additional claims beyond the first 12 months of estimated claims already accrued by the captive insurance group. The consolidated total of the additional accruals was \$1,809 and \$1,822 as of December 31, 2010 and 2009, respectively. The accrued liability is carried on the consolidated balance sheets as a noncurrent liability. Loss reserves are discounted using an annual discount rate of 5.5%.

### **10. Retirement Plans**

#### **BH Defined-Contribution Plan**

Since 2006, BH has provided to all qualifying employees basic annual pension plan contributions equal to 3% of their base salaries to the defined-contribution 403(b) plan. In addition, for each 1% that employees contribute to the plan from their own earnings, BH will contribute another 0.5%, to a maximum additional contribution of 1.5%. Thus, employees contributing at least 3% of their own earnings will earn a total contribution of 4.5% from BH. Contributions expensed related to this plan were \$4,835 for 2010, which will be funded in 2011, and \$4,661 for 2009, which was funded in 2010. Employees are vested in the employer portion of contributions to their individual retirement accounts on the basis of their years of service with BH: two years completed service, 20% vested; three years, 40% vested; four years, 60% vested; and five years, 80% vested. Following six years of service with BH, the employee becomes 100% vested in the assets contributed by BH, as they also will do upon attainment of the plan's normal retirement age of 65, permanent disability, or death while actively employed by BH.

#### **PH Defined-Contribution Plan**

PH has a defined-contribution plan covering eligible full-time employees, to which PH makes matching contributions to a specified limit. Employer contribution expense related to this plan was \$213 and \$181 for the years ended December 31, 2010 and 2009, respectively, which were funded in the subsequent fiscal year. PH employees are vested in employer contributions to their individual retirement accounts according to their years of service with PH: two years, 20%; three years, 40%; four years, 60%; five years, 80%, and after six years, 100%.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

*(Thousands of Dollars)*

### **10. Retirement Plans (continued)**

#### **BH Defined-Benefit Pension Plan**

BH historically provided a noncontributory, defined-benefit pension plan covering substantially all BH's employees who completed six months of service. BH agreed to contribute such amounts as are necessary to provide assets sufficient to meet the plan's benefit obligations to members. As of July 1, 2006, BH imposed a "soft freeze" on the benefits provided under its defined-benefit plan, beginning its transition to the defined-contribution 403(b) retirement plan.

For all employees of BH who were under 50 years of age as of December 31, 2006, monthly benefits under the defined-benefit plan were frozen at the amount the benefits would have been based on calculations through December 2005.

Employees who had reached the age of 50 or more years as of December 31, 2006, continue to receive years of service credit for the remainder of their tenure with BH, but earnings upon which pension compensation will be based are not increased beyond June 30, 2006. Both those under and those over the age of 50 will continue to receive vesting credit under the revised defined-benefit plan, but no employee hired after June 30, 2006, will become a covered participant.

Adjustments to pension liabilities to reflect funded status are charged or credited to unrestricted net assets.

Indiana University Health Bloomington Hospital and Affiliates

Notes to Consolidated Financial Statements (continued)

(Thousands of Dollars)

**10. Retirement Plans (continued)**

The following table sets forth the funded status of the defined-benefit pension plan and amounts recognized in the consolidated financial statements as of and for the years ended December 31, 2010 and 2009. Date of data collection was January 1, 2010 and 2009 (rolled forward to measurement dates of December 31, 2010 and 2009, and adjusted for changes in employment status).

|   | <u>2010</u>        | <u>2009</u>        |
|---|--------------------|--------------------|
| Changes in benefit obligation of the plan:                            |                    |                    |
| Benefit obligation at beginning of the year                           | \$ 78,289          | \$ 73,211          |
| Service cost  | 2,094              | 2,248              |
| Interest cost   | 4,680              | 4,437              |
| Actuarial loss  | 3,842              | 640                |
| Benefits paid   | (3,133)            | (2,247)            |
| Benefit obligation at end of year                                     | <u>85,772</u>      | <u>78,289</u>      |
| Changes in assets of the plan:  |                    |                    |
| Fair value of assets at beginning of year                             | 67,484             | 51,178             |
| Actual return on assets   | 8,980              | 11,104             |
| Employer contributions  | 2,102              | 7,449              |
| Benefits paid   | (3,133)            | (2,247)            |
| Fair value of assets at end of year                                   | <u>75,433</u>      | <u>67,484</u>      |
| Funded deficiency at December 31                                      | <u>\$ (10,339)</u> | <u>\$ (10,805)</u> |
| Items not yet recognized as a component of net periodic pension cost: |                    |                    |
| Net actuarial loss  | \$ 17,207          | \$ 18,405          |
| Prior service cost  | 16                 | 22                 |
| Net transition obligation   | -                  | -                  |
|   | <u>\$ 17,223</u>   | <u>\$ 18,427</u>   |

Indiana University Health Bloomington Hospital and Affiliates

Notes to Consolidated Financial Statements (continued)  
(Thousands of Dollars)

**10. Retirement Plans (continued)**

|   | <b>2010</b>     | <b>2009</b>     |
|---|-----------------|-----------------|
| Components of net pension benefit cost:         |                 |                 |
| Service cost                                    | \$ 2,094        | \$ 2,248        |
| Interest cost                                   | 4,680           | 4,437           |
| Expected return on assets                       | (5,479)         | (4,284)         |
| Amortization of unrecognized prior service cost | 6               | 6               |
| Amortization of unrecognized net loss           | 1,540           | 2,643           |
| Net periodic pension cost                       | <u>\$ 2,841</u> | <u>\$ 5,050</u> |

|  | <b>2010</b>                            | <b>2009</b>                            |
|--|--|--|
| Weighted-average actuarial assumptions to determine benefit cost:  |  |  |
| Discount rate for net periodic pension cost                        | 6.00%                                  | 6.08%                                  |
| Discount rate for benefit obligations                              | 5.70                                   | 6.00                                   |
| Expected rate of return on plan assets                             | 8.00                                   | 8.00                                   |
| Rate of compensation increase                                      | No salary increase after June 30, 2006 | No salary increase after June 30, 2006 |
| Accumulated benefit obligation                                     | \$ 85,602                              | \$ 78,144                              |
| Fair value of assets at end of year                                | <u>75,433</u>                          | <u>67,484</u>                          |
| Accumulated benefit obligation exceeding fair value of plan assets | <u>\$ 10,169</u>                       | <u>\$ 10,660</u>                       |

Expected future benefit payments:

|           |          |
|-----------|----------|
| 2011      | \$ 1,366 |
| 2012      | 1,734    |
| 2013      | 2,102    |
| 2014      | 2,569    |
| 2015      | 3,186    |
| 2016–2020 | 27,755   |

BH expects to contribute approximately \$2.2 million to the defined-benefit pension plan in 2011.

Indiana University Health Bloomington Hospital and Affiliates

Notes to Consolidated Financial Statements (continued)  
(Thousands of Dollars)

**10. Retirement Plans (continued)**

BH's weighted-average asset allocations by asset category at December 31, 2010 and 2009, are as follows:

|                         | Target<br>Allocation | Percentage of Plan Assets at<br>Measurement Date |             |
|-------------------------|----------------------|--|-------------|
|                         |                      | 2010   | 2009        |
| Equity securities       | 60–80%               | 79%  | 74%         |
| Fixed-income securities | 20–30%               | 12   | 17          |
| Other                   | 0–17.5%              | 9  | 9           |
|                         |                      | <b>100%</b>                                      | <b>100%</b> |

The following table presents the plan's financial instruments as of December 31, 2010 and 2009, measured at fair value on a recurring basis within the fair value hierarchy as disclosed in Note 7:

| December 31, 2010  | Level 1          | Level 2          | Level 3     | Total            |
|--|------------------|------------------|-------------|------------------|
| Assets   |                  |                  |             |                  |
| Cash equivalents   | \$ 2,123         | \$ –             | \$ –        | \$ 2,123         |
| Equity securities  | 54,552           | 2,877            | –           | 57,429           |
| Fixed-income securities                                  | 7,307            | 1,839            | –           | 9,146            |
| Absolute return strategy (Fund of Funds)                 | –                | 6,735            | –           | 6,735            |
| Total assets measured at fair value on a recurring basis | <b>\$ 63,982</b> | <b>\$ 11,451</b> | <b>\$ –</b> | <b>\$ 75,433</b> |
| December 31, 2009  | Level 1          | Level 2          | Level 3     | Total            |
| Assets   |                  |                  |             |                  |
| Cash equivalents   | \$ 3,387         | \$ –             | \$ –        | \$ 3,387         |
| Equity securities  | 41,736           | 7,907            | –           | 49,643           |
| Fixed-income securities                                  | 11,382           | –                | –           | 11,382           |
| Absolute return strategy (Fund of Funds)                 | –                | 3,072            | –           | 3,072            |
| Total assets measured at fair value on a recurring basis | <b>\$ 56,505</b> | <b>\$ 10,979</b> | <b>\$ –</b> | <b>\$ 67,484</b> |

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

*(Thousands of Dollars)*

### **10. Retirement Plans (continued)**

The fair value of cash equivalents, which consist mainly of funds invested in money market funds, is based on quoted market prices and classified as Level 1. The fair value of Level 1 investments is based on quoted market prices from an active exchange. The fair value of Level 2 investments is based on third-party quotes based on quoted market prices of similar securities and other observable inputs.

The investment policy reflects the long-term nature of the pension plan's funding obligations. Assets are invested to achieve a rate of return consistent with policy allocation targets, which significantly contributes to meeting the current and future obligations of the plan and strives to help ensure solvency of the plan over time. This objective is to be achieved through a well-diversified asset portfolio and emphasis on long-term capital appreciation as a primary source of return. The plan utilizes a multimanager structure of complimentary investment styles and classes. Manager qualitative performance is continually evaluated, while a manager's investment performance is judged over an investment market cycle of at least three years.

Plan assets are exposed to risk and fluctuations in market value from year to year. To minimize risk, each manager maintains a diversification of their portfolio to insulate the portfolio from substantial losses in any single security or sector of the market. The asset allocation is reviewed for deviations in the allowable range for each asset class, and rebalancing is implemented as necessary.

The long-term rate of return of the plan investment allocation is designed to be commensurate with a conservatively managed balance allocation. The Funds' fixed-income securities are to consist of investment grade bonds rated A or better, with a weighted-average maturity not to exceed 10 years. Equity securities are allocated among small-cap growth and value companies, large-cap growth and value companies, and international companies.

Each investment type is managed by an asset manager specializing in these various security types. Performance of each of these accounts is benchmarked against the corresponding Russell benchmark.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

### 11. Employee Medical and Dental Benefits

As part of investment policies and strategies, the plan's investment committee meets quarterly to review performance. At least annually, the investment committee reviews and formulates the specific investment and allocation plan. Any adjustments that are deemed necessary are based on specific criteria, i.e., necessary plan funding, plan obligations, plan expenses, and plan liquidity needs.

BH and PH have elected to self-insure certain costs related to employee medical and dental benefit programs. Costs resulting from such incidents are expensed when incurred. BH and PH maintain stop-loss insurance for annual claims in excess of \$225 per employee. At December 31, 2010 and 2009, the consolidated self-insurance liability recorded totaled \$2,967 and \$2,092, respectively, and is included in salaries, wages, and related liabilities in the accompanying consolidated balance sheets.

### 12. Related-Party Transactions

The following is a summary of BH's equity method investments in joint ventures for the years ended December 31, 2010 and 2009:

|                              | <b>Southern<br/>Indiana Surgery<br/>Center</b> | <b>Brown County<br/>Medical</b> | <b>Total</b>    |
|------------------------------|--|---------------------------------|-----------------|
| Balance at January 1, 2009   | \$ 1,253                                       | \$ 777                          | \$ 2,030        |
| Distributions                | (1,270)  | -                               | (1,270)         |
| Equity in net earnings       | 714  | (42)                            | 672             |
| Balance at December 31, 2009 | 697  | 735                             | 1,432           |
| Distributions                | <b>(1,256)</b>                                 | -                               | <b>(1,256)</b>  |
| Equity in net earnings       | <b>1,479</b>                                   | <b>(42)</b>                     | <b>1,437</b>    |
| Balance at December 31, 2010 | <b>\$ 920</b>                                  | <b>\$ 693</b>                   | <b>\$ 1,613</b> |

## Indiana University Health Bloomington Hospital and Affiliates

### Notes to Consolidated Financial Statements (continued) (Thousands of Dollars)

#### 12. Related Party Transactions (continued)

Summarized and aggregated financial information for Southern Indiana Surgery Center and Brown County Medical as of and for the years ended December 31, 2010 and 2009, is as follows:

|   | 2010                                  |                         | 2009                                  |                         |
|---|---------------------------------------|-------------------------|---------------------------------------|-------------------------|
|   | Southern<br>Indiana Surgery<br>Center | Brown County<br>Medical | Southern<br>Indiana Surgery<br>Center | Brown County<br>Medical |
| Current assets  | \$ 2,029                              | \$ 141                  | \$ 1,514                              | \$ 167                  |
| Noncurrent assets   | 1,912                                 | 1,423                   | 1,889                                 | 1,469                   |
| Total assets  | <u>\$ 3,941</u>                       | <u>\$ 1,564</u>         | <u>\$ 3,403</u>                       | <u>\$ 1,636</u>         |
| Current liabilities   | \$ 578                                | \$ 179                  | \$ 469                                | \$ 169                  |
| Noncurrent liabilities  | 288                                   | -                       | 392                                   | -                       |
| Total liabilities   | <u>866</u>                            | <u>179</u>              | <u>861</u>                            | <u>169</u>              |
| Net assets  | <u>3,075</u>                          | <u>1,385</u>            | <u>2,542</u>                          | <u>1,467</u>            |
| Total liabilities and net assets  | <u>\$ 3,941</u>                       | <u>\$ 1,564</u>         | <u>\$ 3,403</u>                       | <u>\$ 1,636</u>         |
| Revenues  | \$ 7,754                              | \$ 189                  | \$ 6,351                              | \$ 191                  |
| Operating expenses  | 4,306                                 | 270                     | 4,257                                 | 278                     |
| Operating income (loss)   | <u>3,448</u>                          | <u>(81)</u>             | <u>2,094</u>                          | <u>(87)</u>             |
| Nonoperating income   | (32)                                  | -                       | (53)                                  | -                       |
| Net income (loss)   | <u>\$ 3,416</u>                       | <u>\$ (81)</u>          | <u>\$ 2,041</u>                       | <u>\$ (87)</u>          |
| IU Health Bloomington's equity<br>in net earnings of<br>unconsolidated affiliates | <u>\$ 1,479</u>                       | <u>\$ (42)</u>          | <u>\$ 714</u>                         | <u>\$ (42)</u>          |

BH also owns one investment in which its ownership is less than 20% and is reported using the cost method. The carrying value of this investment is included in investment in joint ventures at \$705 at both December 31, 2010 and 2009.

# Indiana University Health Bloomington Hospital and Affiliates

## Notes to Consolidated Financial Statements (continued)

*(Thousands of Dollars)*

### **13. Health Care Legislation and Regulation**

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, participation requirements, reimbursement for patient services, Medicare and Medicaid fraud and abuse, and security, privacy, and standards of health information. Government activity has continued with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and noncompliance with regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, significant repayments for patient services previously billed, and disruptions or delays in processing administrative transactions, including the adjudication of claims and payment.

In the opinion of management, there are no known regulatory inquiries that are expected to have a material adverse effect on the consolidated financial statements of IU Health Bloomington; however, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

In March 2010, Congress adopted comprehensive health care insurance legislation, the Patient Care Protection and Affordable Care Act and Health Care and Education Reconciliation Act. The legislation, among other matters, is designed to expand access to coverage to substantively all citizens by 2019 through a combination of public program expansion and private industry health insurance. Changes to existing Medicare and Medicaid coverage and payments are also expected to occur as a result of this legislation. Implementing regulations are generally required for these legislative acts, which are to be adopted over a period of years and, accordingly, the specific impact of any future regulations is not determinable.

# Consolidating Information

## Report of Independent Auditors on Consolidating Information

The Board of Directors  
Indiana University Health Bloomington Hospital and Affiliates

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The consolidating information presented hereinafter is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position and results of operations of the individual entities and is not a required part of the consolidated financial statements. Such information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

*Ernst & Young LLP*

April 22, 2011

Indiana University Health Bloomington Hospital and Affiliates

Consolidating Balance Sheet

December 31, 2010

(Thousands of Dollars)

|  | Total      | Eliminations | Indiana University Health Bloomington Endoscopy | Indiana University Health Healthline Corp | Indiana University Health Paoli Hospital | Indiana University Health Southern Indiana Physicians | Indiana University Health Bloomington Hospital |
|--|------------|--------------|---|---|--|---|--|
| <b>Assets</b>                                  |            |              |   |   |  |   |  |
| Current assets:                                |            |              |   |   |  |   |  |
| Cash and cash equivalents                      | \$ 55,672  | \$ -         | \$ 1  | \$ 247                                    | \$ 13,723                                | \$ 322  | \$ 41,379                                      |
| Patient accounts receivable, net               | 41,903     | -            | 270   | -   | 2,161                                    | 355   | 39,117   |
| Prepaid expenses                               | 9,888      | (1,037)      | -   | 69  | 277                                      | (9)   | 10,588   |
| Inventories                                    | 5,636      | -            | 46  | -   | 648                                      | -   | 4,942  |
| Current portion of trustee-held funds          | 4,428      | -            | -   | -   | 117                                      | -   | 4,311  |
| Total current assets                           | 117,527    | (1,037)      | 317   | 316                                       | 16,926                                   | 668   | 100,337  |
| Assets limited as to use:                      |            |              |   |   |  |   |  |
| Board-designated investment funds              | 99,701     | -            | -   | -   | 2,228                                    | -   | 97,473   |
| Property and equipment:                        |            |              |   |   |  |   |  |
| Cost of property and equipment in service      | 358,860    | -            | 10  | -   | 13,130                                   | 557   | 345,163  |
| Less accumulated depreciation                  | (229,586)  | -            | -   | -   | (5,589)                                  | (344)   | (223,653)                                      |
|  | 129,274    | -            | 10  | -   | 7,541                                    | 213   | 121,510  |
| Construction-in-progress                       | 2,149      | -            | -   | -   | 123                                      | -   | 2,026  |
| Total property and equipment, net              | 131,423    | -            | 10  | -   | 7,664                                    | 213   | 123,536  |
| Other assets:                                  |            |              |   |   |  |   |  |
| Equity interest in unconsolidated subsidiaries | 2,318      | (167)        | -   | -   | -  | -   | 2,485  |
| Interest in net assets of foundations          | 4,314      | -            | -   | -   | -  | -   | 4,314  |
| Unamortized bond issuance costs                | 715        | -            | -   | -   | -  | -   | 715  |
| Other  | 2,889      | -            | -   | -   | -  | -   | 2,889  |
| Total other assets                             | 10,236     | (167)        | -   | -   | -  | -   | 10,403   |
| Total assets                                   | \$ 358,887 | \$ (1,204)   | \$ 327  | \$ 316                                    | \$ 26,818                                | \$ 881  | \$ 331,749                                     |

Indiana University Health Bloomington Hospital and Affiliates

Consolidating Balance Sheet (continued)

|  | Total      | Eliminations | Indiana University Health Bloomington Endoscopy | Indiana University Health Healthline Corp | Indiana University Health Paoli Hospital | Indiana University Health Southern Indiana Physicians | Indiana University Health Bloomington Hospital |
|--|------------|--------------|---|---|--|---|--|
| <b>Liabilities and net assets</b>                |            |              |   |   |  |   |  |
| Current liabilities:                             |            |              |   |   |  |   |  |
| Accounts payable and accrued expenses            | \$ 9,870   | \$ -         | \$ -  | \$ 217                                    | \$ 303                                   | \$ 55   | \$ 9,295                                       |
| Accrued salaries, wages, and related liabilities | 26,092     | -            | -   | -   | 1,210                                    | 669   | 24,213   |
| Estimated third-party payor allowances           | 5,434      | -            | -   | -   | 1,603                                    | -   | 3,831  |
| Current portion of long-term debt                | 8,123      | -            | -   | -   | 539                                      | -   | 7,584  |
| Due to affiliated entities                       | -          | (1,036)      | -   | -   | 910                                      | 126   | -  |
| Total current liabilities                        | 49,519     | (1,036)      | -   | 217                                       | 4,565                                    | 850   | 44,923   |
| Noncurrent liabilities:                          |            |              |   |   |  |   |  |
| Long-term debt, less current portion             | 50,883     | -            | -   | -   | 3,174                                    | -   | 47,709   |
| Accrued pension obligations                      | 10,339     | -            | -   | -   | -  | -   | 10,339   |
| Accrued medical malpractice claims               | 1,809      | -            | -   | -   | 264                                      | -   | 1,545  |
| Other  | 216        | -            | -   | -   | -  | -   | 216  |
| Total noncurrent liabilities                     | 63,247     | -            | -   | -   | 3,438                                    | -   | 59,809   |
| Total liabilities                                | 112,766    | (1,036)      | -   | 217                                       | 8,003                                    | 850   | 104,732  |
| Net assets:                                      |            |              |   |   |  |   |  |
| Unrestricted                                     | 241,808    | (168)        | 327   | 99  | 18,815                                   | 31  | 222,704  |
| Temporarily restricted                           | 3,679      | -            | -   | -   | -  | -   | 3,679  |
| Permanently restricted                           | 634        | -            | -   | -   | -  | -   | 634  |
| Total net assets                                 | 246,121    | (168)        | 327   | 99  | 18,815                                   | 31  | 227,017  |
| Total liabilities and net assets                 | \$ 358,887 | \$ (1,204)   | \$ 327  | \$ 316                                    | \$ 26,818                                | \$ 881  | \$ 331,749                                     |

# Indiana University Health Bloomington Hospital and Affiliates

## Consolidating Balance Sheet

December 31, 2009

*(Thousands of Dollars)*

|  | Total             | Eliminations    | Indiana<br>University<br>Health<br>Paoli<br>Hospital | Indiana<br>University<br>Health<br>Southern Indiana<br>Physicians | Indiana<br>University<br>Health<br>Bloomington<br>Hospital |
|--|-------------------|-----------------|--|---|--|
| <b>Assets</b>                                  |                   |                 |  |   |  |
| Current assets:                                |                   |                 |  |   |  |
| Cash and cash equivalents                      | \$ 42,639         | \$ -            | \$ 9,898   | \$ 878  | \$ 31,863  |
| Patient accounts receivable, net               | 38,275            | -               | 2,093  | 290   | 35,892   |
| Prepaid expenses                               | 9,149             | (828)           | 403  | 24  | 9,550  |
| Inventories                                    | 5,780             | -               | 640  | -   | 5,140  |
| Current portion of trustee-held funds          | 4,501             | -               | 235  | -   | 4,266  |
| Total current assets                           | <u>100,344</u>    | <u>(828)</u>    | <u>13,269</u>  | <u>1,192</u>  | <u>86,711</u>  |
| Assets limited as to use:                      |                   |                 |  |   |  |
| Board-designated investment funds              | 82,512            | -               | 1,956  | -   | 80,556   |
| Property and equipment:                        |                   |                 |  |   |  |
| Cost of property and equipment in service      | 353,489           | -               | 12,244   | 548   | 340,697  |
| Less accumulated depreciation                  | (214,309)         | -               | (4,659)  | (455)   | (209,195)  |
|  | <u>139,180</u>    | <u>-</u>        | <u>7,585</u>   | <u>93</u>   | <u>131,502</u>   |
| Construction-in-progress                       | 761               | -               | 147  | -   | 614  |
| Total property and equipment, net              | <u>139,941</u>    | <u>-</u>        | <u>7,732</u>   | <u>93</u>   | <u>132,116</u>   |
| Other assets:                                  |                   |                 |  |   |  |
| Equity interest in unconsolidated subsidiaries | 2,137             | -               | -  | -   | 2,137  |
| Interest in net assets of foundations          | 4,109             | -               | -  | -   | 4,109  |
| Unamortized bond issuance costs                | 790               | -               | -  | -   | 790  |
| Other  | 603               | -               | -  | -   | 603  |
| Total other assets                             | <u>7,639</u>      | <u>-</u>        | <u>-</u>   | <u>-</u>  | <u>7,639</u>   |
| Total assets                                   | <u>\$ 330,436</u> | <u>\$ (828)</u> | <u>\$ 22,957</u>                                     | <u>\$ 1,285</u>   | <u>\$ 307,022</u>  |

## Indiana University Health Bloomington Hospital and Affiliates

### Consolidating Balance Sheet (continued)

|  | <b>Total</b>      | <b>Eliminations</b> | <b>Indiana<br/>University<br/>Health<br/>Paoli<br/>Hospital</b> | <b>Indiana<br/>University<br/>Health<br/>Southern Indiana<br/>Physicians</b> | <b>Indiana<br/>University<br/>Health<br/>Bloomington<br/>Hospital</b> |
|--|-------------------|---------------------|---|--|---|
| <b>Liabilities and net assets</b>                |                   |                     |   |  |   |
| Current liabilities:                             |                   |                     |   |  |   |
| Accounts payable and accrued expenses            | \$ 8,748          | \$ —                | \$ 442  | \$ 99  | \$ 8,207  |
| Accrued salaries, wages, and related liabilities | 21,046            | —                   | 1,151   | 492  | 19,403  |
| Estimated third-party payor allowances           | 4,940             | —                   | 779   | —  | 4,161   |
| Current portion of long-term debt                | 9,370             | —                   | 734   | —  | 8,636   |
| Due to affiliated entities                       | —                 | (827)               | 827   | —  | —   |
| <b>Total current liabilities</b>                 | <b>44,104</b>     | <b>(827)</b>        | <b>3,933</b>  | <b>591</b>   | <b>40,407</b>   |
| Noncurrent liabilities:                          |                   |                     |   |  |   |
| Long-term debt, less current portion             | 59,358            | —                   | 3,604   | —  | 55,754  |
| Accrued pension obligations                      | 10,805            | —                   | —   | —  | 10,805  |
| Accrued medical malpractice claims               | 1,822             | —                   | 291   | —  | 1,531   |
| Other  | 216               | —                   | —   | —  | 216   |
| <b>Total noncurrent liabilities</b>              | <b>72,201</b>     | <b>—</b>            | <b>3,895</b>  | <b>—</b>   | <b>68,306</b>   |
| <b>Total liabilities</b>                         | <b>116,305</b>    | <b>(827)</b>        | <b>7,828</b>  | <b>591</b>   | <b>108,713</b>  |
| Net assets:                                      |                   |                     |   |  |   |
| Unrestricted                                     | 210,023           | (1)                 | 15,129  | 694  | 194,201   |
| Temporarily restricted                           | 3,474             | —                   | —   | —  | 3,474   |
| Permanently restricted                           | 634               | —                   | —   | —  | 634   |
| <b>Total net assets</b>                          | <b>214,131</b>    | <b>(1)</b>          | <b>15,129</b>   | <b>694</b>   | <b>198,309</b>  |
| <b>Total liabilities and net assets</b>          | <b>\$ 330,436</b> | <b>\$ (828)</b>     | <b>\$ 22,957</b>  | <b>\$ 1,285</b>  | <b>\$ 307,022</b>   |

Indiana University Health Bloomington Hospital and Affiliates

Consolidating Statement of Operations and Changes in Net Assets

December 31, 2010

(Thousands of Dollars)

|  | <b>Total</b>   | <b>Eliminations</b> | <b>Indiana<br/>University<br/>Health<br/>Healthline<br/>Corp</b> | <b>Indiana<br/>University<br/>Health<br/>Paoli<br/>Hospital</b> | <b>Indiana<br/>University<br/>Health<br/>Southern Indiana<br/>Physicians</b> | <b>Indiana<br/>University<br/>Health<br/>Bloomington<br/>Hospital</b> |
|--|----------------|---------------------|--|---|--|---|
| <b>Revenues:</b>   |                |                     |  |   |  |   |
| Net patient service revenue                                    | \$ 348,921     | \$ –                | \$ –   | \$ 27,720   | \$ 3,768   | \$ 317,433  |
| Other operating revenue  | 10,437         | (221)               | 298  | 388   | 195  | 9,777   |
| <b>Total operating revenues</b>                                | <b>359,358</b> | <b>(221)</b>        | <b>298</b>   | <b>28,108</b>   | <b>3,963</b>   | <b>327,210</b>  |
| <b>Operating expenses:</b>                                     |                |                     |  |   |  |   |
| Salaries, wages, and benefits                                  | 181,308        | (65)                | 190  | 13,407  | 3,044  | 164,732   |
| Supplies, drugs, purchased services, and other                 | 110,780        | (156)               | 386  | 6,187   | 3,724  | 100,639   |
| Depreciation and amortization                                  | 18,470         | –                   | –  | 1,102   | 43   | 17,325  |
| Provision for uncollected patient accounts                     | 27,842         | –                   | –  | 3,974   | 281  | 23,587  |
| Interest   | 2,916          | –                   | –  | 46  | 3  | 2,867   |
| <b>Total operating expenses</b>                                | <b>341,316</b> | <b>(221)</b>        | <b>576</b>   | <b>24,716</b>   | <b>7,095</b>   | <b>309,150</b>  |
| <b>Operating income (loss)</b>                                 | <b>18,042</b>  | <b>–</b>            | <b>(278)</b>   | <b>3,392</b>  | <b>(3,132)</b>   | <b>18,060</b>   |
| <b>Nonoperating gains:</b>                                     |                |                     |  |   |  |   |
| Investment income  | 12,182         | –                   | –  | 294   | –  | 11,888  |
| <b>Total nonoperating income</b>                               | <b>12,182</b>  | <b>–</b>            | <b>–</b>   | <b>294</b>  | <b>–</b>   | <b>11,888</b>   |
| <b>Excess (deficiency) of revenues and gains over expenses</b> | <b>30,224</b>  | <b>–</b>            | <b>(278)</b>   | <b>3,686</b>  | <b>(3,132)</b>   | <b>29,948</b>   |

Indiana University Health Bloomington Hospital and Affiliates

Consolidating Statement of Operations and Changes in Net Assets (continued)

December 31, 2010  
(Thousands of Dollars)

|  | <b>Total</b> | <b>Eliminations</b> | <b>Indiana<br/>University<br/>Health<br/>Bloomington<br/>Endoscopy</b> | <b>Indiana<br/>University<br/>Health<br/>Healthline<br/>Corp</b> | <b>Indiana<br/>University<br/>Health<br/>Paoli<br/>Hospital</b> | <b>Indiana<br/>University<br/>Health<br/>Southern Indiana<br/>Physicians</b> | <b>Indiana<br/>University<br/>Health<br/>Bloomington<br/>Hospital</b> |
|--|--------------|---------------------|--|--|---|--|---|
| Unrestricted net assets:   |              |                     |  |  |   |  |   |
| Excess (deficiency) of revenues and gains over expenses            | \$ 30,224    | \$ -                | \$ -   | \$ (278)   | \$ 3,686  | \$ (3,132)   | \$ 29,948   |
| Change in pension obligations                                      | 1,204        | -                   | -  | -  | -   | -  | 1,204   |
| Foundation contributions for capital expenditures                  | 197          | -                   | -  | -  | -   | -  | 197   |
| Net assets acquired  | 160          | (167)               | 327  | -  | -   | -  | -   |
| Net assets transferred to affiliates                               | -            | -                   | -  | 377  | -   | -  | (377)   |
| Additional paid-in capital   | -            | -                   | -  | -  | -   | 2,469  | (2,469)   |
| Increase in unrestricted net assets, controlling                   | 31,785       | (167)               | 327  | 99   | 3,686   | (663)  | 28,503  |
| Temporarily restricted net assets:                                 |              |                     |  |  |   |  |   |
| Change in beneficial interest in net assets of foundations         | 205          | -                   | -  | -  | -   | -  | 205   |
| Increase in temporarily restricted net assets                      | 205          | -                   | -  | -  | -   | -  | 205   |
| Permanently restricted net assets:                                 |              |                     |  |  |   |  |   |
| Change in permanently restricted net assets held by the Foundation | -            | -                   | -  | -  | -   | -  | -   |
| Increase in permanently restricted net assets                      | -            | -                   | -  | -  | -   | -  | -   |
| Increase in net assets   | 31,990       | (167)               | 327  | 99   | 3,686   | (663)  | 28,708  |
| Net assets at beginning of year                                    | 214,131      | -                   | -  | -  | 15,129  | 694  | 198,308   |
| Net assets at end of year  | \$ 246,121   | \$ (167)            | \$ 327   | \$ 99  | \$ 18,815   | \$ 31  | \$ 227,016  |

Indiana University Health Bloomington Hospital and Affiliates  
 Consolidating Statement of Operations and Changes in Net Assets

December 31, 2009  
 (Thousands of Dollars)

|   | <b>Total</b>   | <b>Eliminations</b> | <b>Indiana<br/>University<br/>Health<br/>Paoli<br/>Hospital</b> | <b>Indiana<br/>University<br/>Health<br/>Southern Indiana<br/>Physicians</b> | <b>Indiana<br/>University<br/>Health<br/>Bloomington<br/>Hospital</b> |
|---|----------------|---------------------|---|--|---|
| <b>Revenues:</b>                                      |                |                     |   |  |   |
| Net patient service revenue                           | \$ 340,250     | \$ –                | \$ 27,515   | \$ 4,056   | \$ 308,679  |
| Other revenue   | 7,329          | (47)                | 693   | 296  | 6,387   |
| <b>Total operating revenues</b>                       | <b>347,579</b> | <b>(47)</b>         | <b>28,208</b>   | <b>4,352</b>   | <b>315,066</b>  |
| <b>Expenses:</b>                                      |                |                     |   |  |   |
| Salaries, wages, and benefits                         | 167,910        | –                   | 13,512  | 2,698  | 151,700   |
| Supplies, drugs, purchased services, and other        | 107,208        | (47)                | 6,523   | 2,940  | 97,792  |
| Depreciation and amortization                         | 18,598         | –                   | 994   | 46   | 17,558  |
| Provision for uncollected patient accounts            | 32,670         | –                   | 5,130   | 299  | 27,241  |
| Interest  | 3,024          | –                   | 28  | 1  | 2,995   |
| <b>Total operating expenses</b>                       | <b>329,410</b> | <b>(47)</b>         | <b>26,187</b>   | <b>5,984</b>   | <b>297,286</b>  |
| <b>Operating income (loss)</b>                        | <b>18,169</b>  | <b>–</b>            | <b>2,021</b>  | <b>(1,632)</b>   | <b>17,780</b>   |
| <b>Nonoperating gains:</b>                            |                |                     |   |  |   |
| Investment income, net                                | 13,222         | –                   | 114   | –  | 13,108  |
| <b>Total nonoperating income</b>                      | <b>13,222</b>  | <b>–</b>            | <b>114</b>  | <b>–</b>   | <b>13,108</b>   |
| <b>Excess of revenues and<br/>gains over expenses</b> | <b>31,391</b>  | <b>–</b>            | <b>2,135</b>  | <b>(1,632)</b>   | <b>30,888</b>   |

## Indiana University Health Bloomington Hospital and Affiliates

### Consolidating Statement of Operations and Changes in Net Assets (continued)

December 31, 2009

*(Thousands of Dollars)*

|  | <b>Total</b>      | <b>Eliminations</b> | <b>Indiana<br/>University<br/>Health<br/>Paoli<br/>Hospital</b> | <b>Indiana<br/>University<br/>Health<br/>Southern Indiana<br/>Physicians</b> | <b>Indiana<br/>University<br/>Health<br/>Bloomington<br/>Hospital</b> |
|--|-------------------|---------------------|---|--|---|
| Unrestricted net assets:   |                   |                     |   |  |   |
| Excess of revenues and gains over expenses                         | \$ 31,391         | \$ —                | \$ 2,135  | \$ (1,632)   | \$ 30,888   |
| Change in pension obligations                                      | 8,829             | —                   | —   | —  | 8,829   |
| Foundation contributions for capital expenditures                  | —                 | —                   | —   | —  | —   |
| Noncontrolling interest acquired                                   | —                 | —                   | —   | —  | —   |
| Additional paid-in capital   | —                 | —                   | —   | 5,045  | (5,045)   |
| Increase in unrestricted net assets                                | <u>40,220</u>     | <u>—</u>            | <u>2,135</u>  | <u>3,413</u>   | <u>34,672</u>   |
| Temporarily restricted net assets:                                 |                   |                     |   |  |   |
| Change in beneficial interest in net assets of foundations         | 322               | —                   | —   | —  | 322   |
| Increase in temporarily restricted net assets                      | <u>322</u>        | <u>—</u>            | <u>—</u>  | <u>—</u>   | <u>322</u>  |
| Permanently restricted net assets:                                 |                   |                     |   |  |   |
| Change in permanently restricted net assets held by the Foundation | 83                | —                   | —   | —  | 83  |
| Increase in permanently restricted net assets                      | <u>83</u>         | <u>—</u>            | <u>—</u>  | <u>—</u>   | <u>83</u>   |
| Increase in net assets   | 40,625            | —                   | 2,135   | 3,413  | 35,077  |
| Net assets (deficit) at beginning of year                          | 173,506           | (1)                 | 12,994  | (2,719)  | 163,232   |
| Net assets at end of year  | <u>\$ 214,131</u> | <u>\$ (1)</u>       | <u>\$ 15,129</u>  | <u>\$ 694</u>  | <u>\$ 198,309</u>   |

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