

Jefferson Health System, Inc.
Consolidated Financial Statements
For the Years Ended
June 30, 2011 and 2010

Jefferson Health System, Inc.

Contents

June 30, 2011 and 2010

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Report of Independent Auditors

Board of Trustees
Jefferson Health System, Inc.
Radnor, Pennsylvania

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and changes in net assets and cash flows present fairly, in all material respects, the financial position of Jefferson Health System, Inc. and subsidiaries ("JHS") at June 30, 2011 and 2010, and the results of operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of JHS's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

October 13, 2011

Jefferson Health System, Inc.
Consolidated Balance Sheets
Years Ended June 30, 2011 and 2010

(in millions of dollars)

	2011	2010
Assets		
Current assets		
Cash and cash equivalents	\$ 158.1	\$ 139.6
Investments	472.2	359.3
Accounts receivable, less allowance for doubtful accounts of \$62.8 and \$57.7 in 2011 and 2010, respectively	379.7	363.5
Inventory	36.1	35.3
Other current assets	39.1	85.9
Assets whose use is limited	92.5	135.6
Due from affiliated foundations	14.5	11.2
	<u>1,192.2</u>	<u>1,130.4</u>
Total current assets		
Investments	431.1	383.5
Assets whose use is limited	588.5	475.3
Assets held by affiliated foundations	425.1	391.5
Land, buildings and equipment, net	1,339.4	1,273.8
Beneficial interest in perpetual trusts	65.7	55.8
Other non-current assets	41.6	58.6
	<u>\$4,083.6</u>	<u>\$3,768.9</u>
Total assets		
Liabilities and Net Assets		
Current liabilities		
Current portion of long-term obligations	\$ 13.3	\$ 12.5
Accounts payable and accrued expenses	350.9	319.3
Accrued vacation	56.7	52.1
Current portion of accrued professional liability claims	29.9	34.7
Other current liabilities	6.1	6.4
	<u>456.9</u>	<u>425.0</u>
Total current liabilities		
Long-term obligations	517.6	495.6
Accrued pension liability	267.4	364.1
Accrued professional liability claims	330.1	391.9
Other non-current liabilities	83.4	87.0
	<u>1,655.4</u>	<u>1,763.6</u>
Total liabilities		
Net assets		
Unrestricted	2,148.3	1,757.9
Temporarily restricted	149.8	131.0
Permanently restricted	130.1	116.4
	<u>2,428.2</u>	<u>2,005.3</u>
Total net assets		
Total liabilities and net assets	<u>\$4,083.6</u>	<u>\$3,768.9</u>

The accompanying notes are an integral part of the consolidated financial statements.

Jefferson Health System, Inc.
Consolidated Statements of Operations and Changes in Net Assets
Years Ended June 30, 2011 and 2010

(in millions of dollars)

	2011	2010
Unrestricted net assets		
Unrestricted operating revenues, gains and other support		
Net patient service revenue	\$2,781.6	\$ 2,553.2
Investment income	9.7	8.2
Other revenues	138.3	180.0
Net assets released from restrictions used for operations	21.1	14.5
Total unrestricted operating revenues, gains and other support	<u>2,950.7</u>	<u>2,755.9</u>
Operating expenses		
Salaries and employee benefits	1,411.9	1,339.2
Supplies	509.3	485.2
Depreciation and amortization	142.2	132.1
External physician, clinical and professional service fees	342.5	277.8
Interest expense	18.3	23.3
Insurance	39.9	93.3
Provision for bad debts	78.6	76.1
Other	236.4	200.6
Total operating expenses	<u>2,779.1</u>	<u>2,627.6</u>
Operating income before non-recurring charge	171.6	128.3
Loss on extinguishment of debt	(5.9)	-
Operating income	165.7	128.3
Nonoperating revenues (expenses)		
Investment income and net realized gains	76.0	51.2
Other	(12.8)	(16.8)
Excess of revenues over expenses	<u>\$ 228.9</u>	<u>\$ 162.7</u>

The accompanying notes are an integral part of the consolidated financial statements.

Jefferson Health System, Inc.
Consolidated Statements of Operations and Changes in Net Assets
Years Ended June 30, 2011 and 2010

(in millions of dollars)

	2011	2010
Unrestricted net assets		
Excess of revenues over expenses (from previous page)	\$ 228.9	\$ 162.7
Change in net unrealized gain on investments and net assets held by affiliated foundations	73.0	53.6
Decrease (increase) in pension liability	88.9	(86.4)
Net assets released from restrictions - capital purchases	6.2	9.7
Other	1.9	(.5)
Additional capital contribution / (dividend distribution to shareholder)	(8.5)	(1.9)
Increase in unrestricted net assets	<u>390.4</u>	<u>137.2</u>
Temporarily restricted net assets		
Contributions	16.2	13.2
Investment income and realized gains, net	12.4	7.0
Change in net unrealized loss on investments and net assets held by affiliated foundations	20.2	10.2
Net assets released from restrictions - operations	(21.1)	(14.5)
Net assets released from restrictions - capital purchases	(6.2)	(9.7)
Other	(2.7)	(6.6)
Increase (decrease) in temporarily restricted net assets	<u>18.8</u>	<u>(.4)</u>
Permanently restricted net assets		
Contributions	4.1	3.4
Increase in beneficial interest in perpetual trusts	9.4	5.0
Change in net unrealized gain on investments and assets held by affiliated foundations	0.2	0.2
Increase in permanently restricted net assets	<u>13.7</u>	<u>8.6</u>
Increase in net assets	422.9	145.4
Net assets, beginning of year	<u>2,005.3</u>	<u>1,859.9</u>
Net assets, end of year	<u>\$ 2,428.2</u>	<u>\$ 2,005.3</u>

The accompanying notes are an integral part of the consolidated financial statements.

Jefferson Health System, Inc.
Consolidated Statements of Cash Flows
June 30, 2011 and 2010

(in millions of dollars, unless otherwise noted)

	2011	2010
Cash flows from operating activities		
Increase / (decrease) in net assets	\$ 422.9	\$ 145.4
Adjustments to reconcile (decrease) increase in net assets to net cash provided by operating activities		
Net realized and unrealized (gains) on investments and changes in beneficial interest and affiliated foundations	(149.8)	(94.9)
Increase / (decrease) in fair market value on interest rate swaps	9.5	12.3
Depreciation and amortization	142.2	132.1
(Decrease) / increase in pension liability	(88.9)	86.4
Provision for bad debts	78.6	76.1
Contributions and investment income restricted for long-term purposes	(11.8)	(14.7)
Equity in income of joint ventures and affiliates	6.9	(.2)
Loss on early extinguishment of debt	5.9	-
Changes in assets and liabilities:		
Accounts receivable	(94.8)	(117.5)
Inventory	(.8)	(1.9)
Other assets	63.8	(61.0)
Accounts payable and accrued expenses	11.4	3.4
Accrued vacation	4.6	6.1
Accrued pension liability	(7.8)	3.6
Accrued professional liability	(19.4)	35.4
Other liabilities	(13.4)	4.3
Net cash provided by operating activities	<u>359.1</u>	<u>214.9</u>
Cash flows from investing activities		
Purchase of property and equipment	(187.5)	(213.1)
(Purchase) / Sale of investments and assets whose use is limited, net	<u>(173.2)</u>	<u>(109.0)</u>
Net cash used in investing activities	<u>(360.7)</u>	<u>(322.1)</u>
Cash flows from financing activities		
Proceeds from long-term borrowings	347.9	6.0
Repayment of long-term borrowings	(331.1)	(10.1)
Return of capital / dividend to shareholder	(8.5)	(1.9)
Contributions and investment income restricted for long-term purposes	<u>11.8</u>	<u>14.7</u>
Net cash provided by financing activities	<u>20.1</u>	<u>8.7</u>
Net increase / (decrease) in cash and cash equivalents	18.5	(98.5)
Cash and cash equivalents at beginning of year	<u>139.6</u>	<u>238.1</u>
Cash and cash equivalents at end of year	<u>\$ 158.1</u>	<u>\$ 139.6</u>
Supplemental disclosures		
Interest paid (net of amount capitalized)	\$ 27.9	\$ 23.5
Non-cash expenditures for purchase of property and equipment	\$ 10.1	\$ 16.7
Insurance loss portfolio transfer	\$ 47.2	\$ -
Mortgage obligation and a capital lease	\$ 24.1	\$ 25.5

The accompanying notes are an integral part of the consolidated financial statements.

Jefferson Health System, Inc.

Notes to Consolidated Financial Statements

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1. Summary of Significant Accounting Policies

Organization and Nature of Operations

Jefferson Health System, Inc. (“JHS”), a Pennsylvania nonprofit corporation headquartered in Radnor, Pennsylvania, is the parent of a system of health care organizations comprised of three Member health systems. JHS is the sole corporate member of the parent companies of each of the three Member health systems. These three Member systems are: The Magee Memorial Hospital for Convalescents, d/b/a Magee Rehabilitation Hospital (“Magee”), Main Line Health, Inc. (“MLH”) and TJUH System Inc. (“TJUH”). Magee, MLH and TJUH are collectively referred to as “Members”.

Any Member institution may voluntarily withdraw from the System effective July 1, 2022 upon not less than two years prior notice provided that such Member refinances all the System debt allocated to it. Voluntary withdrawal of any Member will result in the dissolution of JHS subsequent to the refinancing of all debt obligations of JHS.

Magee includes Magee Rehabilitation Services, Inc. and other related organizations.

MLH includes Main Line Hospitals, Inc. (The Bryn Mawr Hospital; The Lankenau Hospital; Paoli Hospital); Lankenau Institute of Medical Research; Main Line Diversified Services, Inc. (Bryn Mawr Rehabilitation Hospital and other related organizations); Main Line Health Care (formerly Great Valley Health, a physician group practice); and Riddle Health System (Riddle Memorial Hospital, Riddle Enterprises, Inc., Riddle Healthcare Associates, Riddle System Services, Riddle Physician Services, Riddle Healthcare Services, Mirmont Alcohol Rehabilitation Center, and other related organizations) (“RHS”).

TJUH includes Thomas Jefferson University Hospitals, Inc. (Thomas Jefferson University Hospital and its subsidiaries; the Jefferson Hospital for Neuroscience and the Methodist Hospital Division); TJUH Physician Affiliates; Jeffex, Inc. and the Atrium Corporation and other related organizations.

On September 19, 1996, ownership of Whitehall Station Insurance Company Ltd. (“Whitehall”), a captive insurance company domiciled in the Cayman Islands, was transferred from MLH to JHS. Effective December 2002, JHS formed Mountain Laurel Risk Retention Group, Inc. (“RRG”). The RRG is domiciled in Vermont. Effective beginning in fiscal year 2004, the RRG was used by JHS and Members of JHS to insure certain of their professional and general liability exposures. As of July 1, 2007, JHS formed a Delaware captive, Five Pointe Professional Liability Insurance Company (“Five Pointe”). Five Pointe is a Delaware not-for-profit sponsored captive insurance company, which is exempt from federal income taxation under section 501(c)(3) of the Internal Revenue Code. JHS is the sole common member of Five Pointe. Five Pointe is the reinsurer for the RRG and insures JHS and Members of JHS (current and past) for certain of their professional liability exposures. Whitehall, RRG and Five Pointe are all consolidated subsidiaries of JHS.

The Members and their affiliated organizations provide inpatient, outpatient and emergency care services through acute and rehabilitation hospitals, as well as behavioral health, long-term care, ambulatory care, home care, physician and other primary and speciality care services, principally to residents of Southeastern Pennsylvania and Southern New Jersey. JHS maintains a close contractual affiliation with a former Member Aria Health (formerly known as Frankford Health Care System) (“Aria”), which involves clinical affiliations and collaboration in areas such as quality reporting and

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benchmarking among Aria and the Members as well as the provision of certain support services by JHS to Aria.

Basis of Presentation and Use of Estimates

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting. These consolidated financial statements include the accounts of JHS; Magee and its controlled affiliates; MLH and its controlled affiliates; TJUH and its controlled affiliates; Whitehall; Five Pointe; and RRG. Investments in companies in which JHS and Members do not have control, but in which they have a substantial (20-50 percent) ownership interest and can exercise significant influence, are accounted for using the equity method. All significant intercompany accounts and transactions have been eliminated.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period and the accompanying notes. Actual results could differ from these estimates.

Assets Held by Affiliated Foundations

Unconditional promises to give (pledges) are recorded as receivables and revenues or increases in net assets and require the organization to distinguish between contributions received for each net asset category in accordance with donor imposed restrictions. Additionally, The Bryn Mawr Hospital Foundation, The Bryn Mawr Rehabilitation Foundation, The Lankenau Hospital Foundation, The Magee Rehabilitation Hospital Foundation, The Methodist Hospital Foundation, The Paoli Hospital Foundation and The Riddle Healthcare Foundation (collectively, the "Foundations") are each treated, for accounting purposes only, as though acting on behalf of their respective supported hospital affiliate and therefore, the Foundations' net assets and financial results are included in the consolidated results of JHS.

The consolidated financial statements of JHS reflect net assets held by affiliated Foundations relating to net assets held, managed, and controlled by all the aforementioned Foundations. This required accounting treatment does not imply that the Foundations' net assets, or investment income, are those of their respective hospital affiliates. Under the by-laws of each Foundation, its Board of Trustees has sole discretion whether to make any Foundation assets available, except with respect to the terms of certain restricted gifts to the Foundations or net assets held by the Foundations in a special projects fund (which are available to fund hospital requests for contributions by the Foundations for identified purposes other than voluntary or required prepayments or payments of debt).

The consolidated financial statements of JHS do not reflect or establish the legal relationship, agency or otherwise, between a Foundation and its hospital affiliates or any right to any net assets owned by a Foundation. The Foundations are separately incorporated non-membership nonprofit corporations governed by individual self-perpetuating Boards of Trustees. The by-laws of each Foundation provide that all net assets held by it, including net assets in its Special Projects Fund, if any, shall not be subject to attachment, execution or sequestration for any debt, obligation or liability of its hospital affiliate or any other person or entity, and shall not be subject to pledge, assignment, conveyance or anticipation by that hospital or any other person or entity. The Foundations are not parties to or obligated by the Amended and Restated Master Trust Indenture ("Master Indenture") (See Note 6), and assets owned by the Foundations are not subject to the lien of the Master Indenture.

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Net Assets

Resources are classified for accounting and reporting purposes into three net asset categories according to donor imposed restrictions. A description of the three net asset categories follows:

- Unrestricted Net Assets are those net assets that are available for the support of operations and whose use is not externally restricted, although their use may be limited by other factors such as by contract or board designation.
- Temporarily Restricted Net Assets include gifts for which donor-imposed restrictions such as specific time period or purpose have not been met and trust activity and pledges receivable for which the ultimate purpose of the proceeds is not permanently restricted.
- Permanently Restricted Net Assets include gifts, trusts, and pledges which require by donor restriction that the corpus be invested in perpetuity and only the income be made available for operations in accordance with donor restrictions.

Performance Indicator

In the accompanying consolidated statements of operations and changes in net assets, the primary indicator of JHS' results is "Excess of revenues over expenses". As such, it includes all unrestricted revenues, operating investment income (as defined in the Investments and Investment Income policy note), expenses and non operating revenues and non-operating expenses. Transactions such as restricted contributions and contributions for long-lived assets (e.g., capital equipment), certain investment income, realized and unrealized gains and losses related to these transactions and certain adjustments to pension liabilities are not included in "Excess of revenues over expenses".

Cash and Cash Equivalents

Cash and cash equivalents consist of cash and investments in highly liquid debt instruments with an original maturity of three months or less. At June 30, 2011 and 2010 JHS had cash balances in financial institutions which exceed federal depository insurance limits. Management believes that credit risk related to these deposits is minimal.

Investments and Investment Income

JHS segregates investment income between operating and non-operating income to better match operating income with operating expenses. Investment income or loss on unrestricted cash, short-term investments and trustee-held funds associated with debt obligations (including realized gains and losses on investments, interest and dividends) are included in operating income. Long term investment income, realized gains and losses, and the change in unrealized gains or losses on alternative investments are included in non-operating revenues. Unrealized gains and losses on all investments, except alternative investments, are shown below the excess of revenues over expenses. Investment income or loss on investments of donor-restricted funds, including unrealized gains and losses, is added to (deducted from) the appropriate net asset category based on the donor's restrictions or state law. An impairment review of investments is performed annually to determine if declines in fair value below cost are other-than-temporary. This review is subjective and requires a high degree of judgment. JHS and its Members evaluate their investments using both quantitative and qualitative factors, to determine whether any declines in value are other-than-temporary.

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Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date.

The guidance also establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value as follows:

Level 1	Inputs that reflect unadjusted quoted prices in active markets for identical assets or liabilities;
Level 2	Observable inputs other than Level 1 prices, such as quoted prices for similar instruments; quoted prices in markets that are not active; or other inputs that are observable or that can be corroborated by observable market data;
Level 3	Unobservable inputs that are supported by little or no market activity and are significant to the fair value measurement.

The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Assets and liabilities are measured at fair value and are based on one or more of the three valuation techniques as follows:

Market approach: Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities,

Cost approach: Amount that would be required to replace the service capacity of an asset (i.e. replacement cost),

Income approach: Techniques to convert future amounts to a single present amount based on market expectations (including present value techniques and option-pricing models).

Investments that are generally valued based on quoted market prices in active markets obtained from exchange or dealer markets for identical assets, and are accordingly categorized as Level 1 in the fair value hierarchy, with no valuation adjustments applied.

Investments that are valued at net asset value (NAV) are categorized as Level 2 or Level 3 in the fair value hierarchy. If JHS and its Members have the ability to redeem at a measurement date or in the near-term at NAV, the investment would be classified as a Level 2 in the fair value hierarchy. Alternatively, if JHS and its Members do not have the ability to redeem from the investment at the measurement date or is restricted from redeeming for an uncertain or extended period of time from the measurement date, the investment would be classified as a Level 3 in the fair value hierarchy.

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Inventories

Inventories are stated at the lower of cost or market with cost determined using the first-in-first-out (FIFO) method.

Assets Whose Use Is Limited

Assets whose use is limited are reported at fair value and principally include amounts set aside by the appropriate related Member Boards of Trustees for future capital improvements, self-insurance arrangements, and amounts held by trustees under bond indenture agreements, amounts in temporarily restricted and permanently restricted by donors. Amounts required to meet current liabilities have been classified as current assets in the accompanying consolidated balance sheets.

Land, Buildings and Equipment

Land, buildings and equipment are recorded at cost, net of accumulated depreciation. Donated equipment is recorded at fair market value at the date of receipt, which is then treated as cost. Depreciation is calculated utilizing the straight-line method based on the estimated useful lives of the underlying assets. Building and building improvements, leasehold improvements and land improvements are depreciated using an average estimated useful life of twenty years. Equipment is depreciated using an average estimated useful life of eight years. No depreciation is taken on land or construction in progress. Gains and losses from retirement or disposition of fixed assets are recognized in the statement of operations and changes in net assets as non-operating gains or losses. Interest costs associated with the construction of certain capital assets are capitalized and amortized over the life of the asset being depreciated. Capitalized interest relating to the construction of certain capital assets was \$14.8 million and \$13.9 million during 2011 and 2010, respectively.

Beneficial Interest in Perpetual Trusts

Beneficial interest in perpetual trusts represents the interests of the Members in perpetual trusts which are administered by independent trustees. Because the trusts are perpetual and the original corpus cannot be withdrawn, they are reported as permanently restricted net assets. The beneficial interest in perpetual trusts is reported at the fair value of the underlying assets in the trust. Annual distributions are included in other non-operating income.

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Derivative Financial Instruments

Derivative financial instruments consist of interest rate swaps which are reported at fair market value on a recurring basis. The fair market value of the interest rate swaps is determined based on financial models that consider current and future interest rates.

Insurance

Accrued professional liability claims and insurance expense in the consolidated financial statements are based on individual case estimates for reported losses and estimates of incurred but not reported losses and decreased by reinsurance and liabilities covered by the Medical Care Availability and Reduction of Error (“MCARE”) Fund.

Unpaid losses and loss adjustment expenses are necessarily based on estimates and the ultimate liabilities may vary significantly from such estimates. Any adjustments to these estimates will be reflected in income in the period in which estimates are changed or payments made. JHS reported reserves for unpaid losses and loss adjustment expenses are determined by an independent outside actuary based on loss and loss adjustment expense experience and other factors, at a 65% confidence level and a 3% discount rate for the years ended June 30, 2011 and 2010 (Note 9).

Professional liability claims are insured under a combination of captive insurer, self-insurance and excess commercial reinsurance programs. All of the healthcare provider entities also participate in the MCARE Fund.

Workers’ compensation exposures are insured through self-insurance and commercial insurance programs. Reserves for workers’ compensation liabilities are recorded on a discounted basis, using a rate of 3 percent.

Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and are adjusted in future periods, as final settlements are determined.

Revenue from Medicare and Medical Assistance programs, directly and from managed care plans serving Medicare beneficiaries and Medical Assistance enrollees, for hospital services, accounted for approximately 29.0 percent and 6.0 percent, respectively, of net patient revenue for the fiscal year ended June 30, 2011 and 28.4 percent and 6.8 percent, respectively, for the fiscal year ended June 30, 2010. Most payments from the Medicare and Medical Assistance programs for inpatient hospital services are made on a prospective basis. Under these programs, payments are made at a pre-determined specific rate for each discharge based on a patient’s diagnosis. Additional payments are made for cases that have an extremely long length of stay or unusually high costs in comparison to national or statewide averages. Laws governing the Medicare and Medical Assistance programs are complex and subject to interpretation. JHS member hospitals participated in the Pennsylvania Medicaid Modernization Program in 2011 and 2010 and received increased Medical Assistance revenues associated with this program. There can be no assurance that this program will continue.

JHS has also entered into agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations, the largest being Independence Blue Cross at 28.0

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percent and 27.9 percent of net patient revenue for hospital operations for the years ended June 30, 2011 and June 30, 2010, respectively. The basis for payment under these agreements for hospital services includes prospectively determined rates per discharge, discounts from established charges, prospectively determined daily rates, and a small amount of capitated rates.

Donor-Restricted Gifts

Unconditional promises to receive cash and other assets are reported at fair value at the date the promise is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is met, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statement of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same fiscal year as received are reflected as unrestricted contributions in the accompanying consolidated financial statements.

Charitable Medical Care Provided

The Members provide services to all patients regardless of ability to pay. Although patients are ultimately financially responsible for those hospital services rendered that are not covered by insurance, some uninsured and underinsured patients qualify for charity care under established guidelines and are therefore not responsible for payment for such services. These guidelines require medical indigency status based on federal poverty guidelines. Charges for services rendered to patients who qualify for charity care are not reflected in the accompanying consolidated financial statements. Some uninsured or underinsured patients, who do not qualify for free charity care, qualify for care at reduced rates.

The Members maintain records to identify and monitor the level of charity care provided. These records include the amount of charges forgone for services and supplies furnished. Such amounts have been excluded from net patient service revenue. Management estimates that the charges converted to the cost associated with these services and supplies for charity care provided by the Members approximated \$13.9 million and \$12.7 million for the years ended June 30, 2011 and 2010, respectively. These amounts do not include the provision for bad debts, which is reflected separately in the accompanying consolidated statements of operations and changes in net assets.

Other Uncompensated Community Services (unaudited)

Services are provided to patients in the community who are insured under the Pennsylvania Medical Assistance Program. Payments from the Medical Assistance Program are substantially below the cost of providing such services. The cost of providing services to eligible individuals who participate in the Pennsylvania Medical Assistance Programs directly and from managed care plans serving medical assistance enrollees exceeded reimbursement by approximately \$76.7 million and \$63.7 million in 2011 and 2010, respectively.

In addition to providing direct patient charity care and in furtherance of its exempt purpose to benefit the community, the Members provide various community benefits such as health professions education, screenings and support groups for patients and their families, health wellness festivals, continuum of independent living and senior health programs, heart disease screenings, maternity care and childbirth programs, and other related community health programs and lectures. The Members of JHS are also involved with school partnerships and help organize educational programs for childhood and adolescent health issues, including underage drinking and smoking. Associated amounts

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expended for the above community services approximated \$69.0 million and \$52.4 million for the years ended June 30, 2011 and 2010, respectively.

Income Taxes

Magee and certain of its controlled affiliates; MLH and certain of its controlled affiliates; and TJUH and certain of its controlled affiliates; Five Pointe; and JHS itself are tax exempt pursuant to Section 501(c)(3) of the Internal Revenue Code. In addition to the Members above, JHS also owns or controls for-profit subsidiaries, such as the RRG, which are taxable corporations. Whitehall is a controlled foreign corporation as defined by the Tax Code of the United States.

Subsequent Events

JHS has performed an evaluation of subsequent events through October 13, 2011, which is the date the financial statements were issued.

2. Fair Value Measurements

Assets measured at fair value are presented in the accompanying consolidated balance sheet under the following classifications:

	<u>2011</u>	<u>2010</u>
Investments, current	\$ 472.2	\$ 359.3
Assets whose use is limited, current	92.5	135.6
Long-term investments	431.1	383.5
Assets whose use is limited, long-term	588.5	475.3
	<u>\$ 1,584.3</u>	<u>\$ 1,353.7</u>

Current and long-term assets whose use is limited for 2011 and 2010 are classified as follows:

	<u>2011</u>	<u>2010</u>
Board designated assets, primarily construction and capital	\$ 405.9	\$ 364.2
Bond indenture agreement assets restricted by trustees	0.1	7.7
Self-insurance assets board designated	275.0	239.0
	<u>\$ 681.0</u>	<u>\$ 610.9</u>

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The following tables present assets and liabilities measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy as of June 30, 2011:

	Assets at Fair Value as of June 30, 2011			
	Level 1	Level 2	Level 3	Total
	(in millions)			
Assets, at fair value:				
Mutual funds - primarily US government obligations	\$ 183.7	\$ -	\$ -	\$ 183.7
Mutual funds - marketable equity securities	74.1	126.9	-	201.0
Mutual funds - fixed income securities	-	178.4	-	178.4
Equity Securities	42.1	-	-	42.1
US Government obligations	162.8	-	-	162.8
Corporate bonds	227.3	9.1	-	236.4
Certificates of deposit and other commercial paper	305.8	23.0	-	328.8
Fixed income securities	25.2	121.5	-	146.7
Hedge funds	-	-	25.2	25.2
Other, including alternative assets	9.7	8.1	52.4	70.2
	<u>\$ 1,030.7</u>	<u>\$ 467.0</u>	<u>\$ 77.6</u>	<u>1,575.3</u>
Investments at cost				9.0
				<u>\$ 1,584.3</u>
Beneficial interest in perpetual trusts	\$ -	\$ 39.6	\$ 26.1	\$ 65.7

	Liabilities at Fair Value as of June 30, 2011			
	Level 1	Level 2	Level 3	Total
	(in millions)			
Liabilities, at fair value:				
Interest rate swaps	\$ -	\$ 39.4	\$ -	\$ 39.4
	<u>\$ -</u>	<u>\$ 39.4</u>	<u>\$ -</u>	<u>\$ 39.4</u>

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A roll forward of those assets and liabilities classified as Level 3 as of June 30, 2011 within the fair value hierarchy by JHS is as follows:

(in millions)	<u>Hedge funds</u>	<u>Other, including alternative assets</u>	<u>Total</u>
Balance, at June 30, 2010	\$ 23.5	\$ 42.5	\$ 66.0
Net purchases and sales	(0.1)	3.8	3.7
Realized and unrealized gains (losses), net	1.8	6.1	7.9
Transfers in, net	-	4.4	4.4
Balance, at June 30, 2011	<u>\$ 25.2</u>	<u>\$ 56.8</u>	<u>\$ 82.0</u>

The following tables present assets and liabilities measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy as of June 30, 2010:

	<u>Assets at Fair Value as of June 30, 2010</u>			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
	(in millions)			
Assets, at fair value:				
Mutual funds - primarily US government obligations	\$ 176.9	\$ -	\$ -	\$ 176.9
Mutual funds - marketable equity securities	57.6	99.1	-	156.7
Mutual funds - fixed income securities	-	153.0	-	153.0
Equity Securities	33.4	-	-	33.4
US Government obligations	224.8	-	-	224.8
Corporate bonds	129.0	7.5	-	136.5
Certificates of deposit and other commercial paper	219.2	29.1	-	248.3
Fixed income securities	2.0	132.6	-	134.6
Hedge funds	-	-	23.5	23.5
Other, including alternative assets	12.1	2.0	42.5	56.6
	<u>\$ 855.0</u>	<u>\$ 423.3</u>	<u>\$ 66.0</u>	1,344.3
Investments at cost				9.4
				<u>\$ 1,353.7</u>
Beneficial interest in perpetual trusts	<u>\$ -</u>	<u>\$ 55.8</u>	<u>\$ -</u>	<u>\$ 55.8</u>

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	Liabilities at Fair Value as of June 30, 2010			
	Level 1	Level 2	Level 3	Total
	(in millions)			
Liabilities, at fair value:				
Interest rate swaps	\$ -	\$ 45.8	\$ -	\$ 45.8
	<u>\$ -</u>	<u>\$ 45.8</u>	<u>\$ -</u>	<u>\$ 45.8</u>

A roll forward of those assets and liabilities classified as Level 3 as of June 30, 2010 within the fair value hierarchy by JHS is as follows:

(in millions)	Hedge funds	Other, including alternative assets	Total
Balance, at June 30, 2009	\$ 13.1	\$ 38.1	\$ 51.2
Net purchases and sales	11.0	3.3	14.3
Realized and unrealized gains (losses), net	(0.6)	1.0	0.4
Transfers in, net	-	0.1	0.1
Balance, at June 30, 2010	<u>\$ 23.5</u>	<u>\$ 42.5</u>	<u>\$ 66.0</u>

As of June 30, 2011 and 2010, JHS recognized an other-than-temporary impairment charge of \$0.5 million and \$1.0 million, respectively, on its investments in marketable securities.

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3. Investment Income

Investment income for 2011 and 2010 is comprised of the following:

	<u>2011</u>	<u>2010</u>
Investment income included in operating income		
Interest and dividends	\$ 7.5	\$ 6.8
Net realized gains (losses) on sales of investments	0.6	(.7)
Equity in earnings in joint venture	1.6	2.1
	<u>9.7</u>	<u>8.2</u>
Investment income included in nonoperating revenues		
Interest and dividends	38.5	28.5
Net realized gains on sales of investments	34.7	24.0
Change in unrealized gains (losses) on alternative and impaired assets	2.8	(1.3)
	<u>76.0</u>	<u>51.2</u>
Total investment income on unrestricted net assets	<u>\$ 85.7</u>	<u>\$ 59.4</u>
	<u>2011</u>	<u>2010</u>
Investment income (temporarily restricted net assets):		
Interest and dividends	\$ 4.0	\$ 3.1
Net realized gains on sales of investments	8.4	3.9
	<u>\$ 12.4</u>	<u>\$ 7.0</u>
Other changes in unrestricted net assets:		
Change in net unrealized gain on investments and net assets held by affiliated foundations	<u>\$ 73.0</u>	<u>\$ 53.6</u>
Other changes in temporarily restricted net assets:		
Change in net unrealized gain on investments and net assets held by affiliated foundations	<u>\$ 20.2</u>	<u>\$ 10.2</u>
Other changes in permanently restricted net assets:		
Change in net unrealized gain on investments and net assets held by affiliated foundations	<u>\$ 0.2</u>	<u>\$ 0.2</u>

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4. Endowment

JHS Members' endowments consist of approximately 125 individual funds established for a variety of purposes. The respective Members' endowments include both donor-restricted endowment funds, if any, and funds designated by the Members' Board of Trustees to function as endowments. Net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

JHS Members have interpreted the Pennsylvania State Prudent Management of Institutional Funds Act (SPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, JHS Members classify as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund, except for beneficial interests in perpetual trusts, that is not classified in permanently restricted net assets is classified in temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by SPMIFA.

At June 30, 2011, the endowment net asset composition by type of fund consisted of the following:

(in millions)	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor - restricted funds	\$ -	\$ 52.9	\$ 130.1	\$ 183.0
Board - restricted funds	75.6	-	-	75.6
	<u>\$ 75.6</u>	<u>\$ 52.9</u>	<u>\$ 130.1</u>	<u>\$ 258.6</u>

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Changes in endowment net assets for the fiscal year ended June 30, 2011 consisted of the following:

(in millions)	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets beginning of year	\$ 64.0	\$ 41.0	\$ 116.4	\$ 221.4
Investment return				
Investment income	0.7	1.6	0.7	3.0
Net appreciation (realized and unrealized)	10.6	9.5	10.1	30.2
Total investment loss	11.3	11.1	10.8	33.2
Contributions	0.1	-	4.1	4.2
Appropriation of endowment assets for expenditure	(3.0)	(1.3)	(1.2)	(5.5)
Other Changes				
Transfers to create board- designated endowment funds	3.2	2.1	-	5.3
Endowment net assets end of year	<u>\$ 75.6</u>	<u>\$ 52.9</u>	<u>\$ 130.1</u>	<u>\$ 258.6</u>

At June 30, 2010, the endowment net asset composition by type of fund consisted of the following:

(in millions)	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor - restricted funds	\$ -	\$ 41.0	\$ 116.4	\$ 157.4
Board - restricted funds	64.0	-	-	64.0
	<u>\$ 64.0</u>	<u>\$ 41.0</u>	<u>\$ 116.4</u>	<u>\$ 221.4</u>

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Changes in endowment net assets for the fiscal year ended June 30, 2010 consisted of the following:

(in millions)	Temporarily Permanently			Total
	Unrestricted	Restricted	Restricted	
Endowment net assets beginning of year	<u>\$ 58.8</u>	<u>\$ 36.4</u>	<u>\$ 107.9</u>	<u>\$ 203.1</u>
Investment return				
Investment income	0.5	1.3	0.5	2.3
Net appreciation (realized and unrealized)	<u>5.2</u>	<u>4.6</u>	<u>5.6</u>	<u>15.4</u>
Total investment loss	<u>5.7</u>	<u>5.9</u>	<u>6.1</u>	<u>17.7</u>
Contributions	0.2	-	3.4	3.6
Appropriation of endowment assets for expenditure	(3.0)	(1.4)	(1.1)	(5.5)
Other Changes				
Transfers to create board- designated endowment funds	<u>2.3</u>	<u>0.1</u>	<u>0.1</u>	<u>2.5</u>
Endowment net assets end of year	<u>\$ 64.0</u>	<u>\$ 41.0</u>	<u>\$ 116.4</u>	<u>\$ 221.4</u>

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5. Land, Buildings and Equipment

A summary of land, buildings and equipment is as follows:

	<u>2011</u>	<u>2010</u>
Land and land improvements	\$ 74.5	\$ 74.6
Buildings	1,593.8	1,485.7
Equipment	1,231.2	1,156.4
Leasehold improvements	30.9	24.8
Construction in progress	<u>135.6</u>	<u>123.7</u>
	3,066.0	2,865.2
Less accumulated depreciation	<u>(1,726.6)</u>	<u>(1,591.4)</u>
	<u>\$1,339.4</u>	<u>\$ 1,273.8</u>

Depreciation expense was \$142.2 million and \$132.1 million for 2011 and 2010, respectively.

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6. Long-Term Obligations

Long-term obligations consist of the following:

	<u>2011</u>	<u>2010</u>
Jefferson Health System Revenue Bonds, including unamortized premium of \$0.3 for 2011, Series A of 2010 due in varying annual amounts through 2040. Interest rates ranging from 2.00% to 5.25% (a)	\$ 161.6	\$ -
Jefferson Health System Revenue Bonds, including unamortized premium of \$2.3 for 2011, Series B of 2010 due in varying annual amounts through 2040. Interest rates ranging from 2.00% to 5.25% (b)	179.5	-
Jefferson Health System Revenue Bonds Series A of 2005 due in varying annual amounts from 2022 through 2028. Interest rate resets weekly. Average interest rates were 0.28% and 0.23% during fiscal 2011 and 2010, respectively (c)	23.6	24.1
Jefferson Health System Revenue Bonds, net of unamortized discount \$0.2 million for 2010, Series A and B of 2004 due in varying annual amounts from 2010 through 2038. Interest rate resets weekly. Average interest rates were 0.24% during fiscal 2010 (d)	-	66.9
Jefferson Health System Revenue Bonds, net of unamortized discount of \$0.3 million for 2010, Series A of 1997 due in varying annual amounts through 2018. Interest rates ranging from 5.00% to 5.50% (e)	-	68.2
Jefferson Health System Revenue Bonds, net of unamortized discount of \$3.1 million for 2010, Series B of 1997 due in varying annual amounts through 2027. Interest rates ranging from 4.60% to 5.35% (e)	-	173.9
Other bonds and notes payable (f)	166.2	175.0
	<u>530.9</u>	<u>508.1</u>
Less current portion of long term obligations	<u>(13.3)</u>	<u>(12.5)</u>
	<u>\$ 517.6</u>	<u>\$ 495.6</u>

As of July 1, 2010, JHS entered into a sixth supplement to the Master Indenture, which was originally dated November 1, 1997, which provides for, among other things, the issuance from time to time of general unsecured debt obligations of JHS. None of the Members of JHS are directly obligated to pay the principal or interest on any bonds issued pursuant to the Master Indenture.

In addition, JHS entered into an Amended and Restated Contribution Agreement, dated as of July 1, 2010 with certain TJUH entities and certain MLH entities (the "Institutions") whereby the Institutions have agreed to pay, loan or otherwise transfer to JHS such amounts as are necessary to pay the principal of and interest on the Series 2005A, the Series 2010A Bonds and the Series 2010B Bonds.

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- (a) JHS issued the Series A of 2010 Bonds (“2010A Bonds”) with a par amount of approximately \$164.5 million through the Chester County Health and Education Facilities Authority to JHS, dated as of July 1, 2010. JHS used the 2010A Bond proceeds to: (i) refinance a portion of the Chester County Authority’s Health System Revenue Bonds, Series 1997B, originally issued in the principal amount of \$199.1 million, of which \$176.9 million in principal amount was outstanding; (ii) refinance all of the Chester County Authority’s Health System Revenue Bonds, Series 2004A and 2004B, originally issued in the principal amount of \$67.1 million, of which \$67.1 million in principal amount was outstanding; (iii) finance or reimburse certain capital expenditures for Main Line Health; and (iv) pay certain expenses incurred in connection with the issuance of the Series 2010A Bonds. This transaction resulted in a loss on refunding of \$2.1 million, which is included in the Consolidated Statements of Operations and Changes in Net Assets as a non-recurring charge.
- (b) JHS issued the Series B of 2010 Bonds (“2010B Bonds”) with a par amount of approximately \$183.4 million through the Hospitals and Higher Education Facilities Authority of Philadelphia to JHS as of July 1, 2010. JHS used the 2010B Bond proceeds to: (i) refinance all of the currently outstanding Philadelphia Hospital Authority’s Health System Revenue Bonds, Series 1997A, originally issued in the principal amount of \$134.8 million, of which \$68.5 million in principal amount was outstanding; (ii) refinance the portion of the Series 1997B Bonds not being refunded with the proceeds of the Series 2010A Bonds; and (iii) pay certain expenses incurred in connection with the issuance of the Series 2010B Bonds. This transaction resulted in a loss on refunding of \$3.8 million, which is included in the Consolidated Statements of Operations and Changes in Net Assets as a non-recurring charge.
- (c) On April 1, 2005, the Pennsylvania Economic Development Financing Authority (“PEDFA”) issued \$26.7 million of Health System Revenue Bonds, Series A of 2005 (“2005 Bonds”). The proceeds received by PEDFA were loaned to JHS and were used to (i) reimburse TJUH for costs related to the acquisition of the short-term acute care hospital business of St. Agnes Medical Center as well as costs incurred in its related expansion of emergency care facilities, capital improvements, equipment purchases and other capital expenditures at Methodist Hospital and (ii) reimburse TJUH for costs related to the acquisition of a 40% interest in the limited liability partnership established to own and operate a new long-term acute care hospital located in Philadelphia.
- (d) On May 7, 2004 the Chester County Health and Education Facilities Authority (“Chester County Issuer”) issued \$67.1 million of Health System Revenue Bonds, Series 2004A and 2004B (“2004 Bonds”). The proceeds received by the Chester County Issuer were loaned to JHS and were used to refund the 1994 MLH Revenue Bonds Series A and Series B.
- (e) On December 16, 1997, on behalf of JHS, the Philadelphia Issuer and the Chester County Issuer (collectively referred to herein as the “Authorities”) issued \$333.9 million of Health System Revenue Bonds, Series 1997A and 1997B (“1997 Bonds”). The proceeds received by the Authorities were loaned to JHS and were used to: (i) fund certain capital expenditures of MLH and TJUH, including TJUH’s purchase of the land and buildings from TJU for \$130.0 million; (ii) repay an outstanding loan of TJUH and (iii) pay certain expenses incurred in connection with the issuance of the 1997 Bonds.
- (f) Other bonds and notes payable, which are not part of the 1997 Master Indenture, are as follows:

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On December 31, 2009, an agreement was entered into by TJUH in the amount of \$3.6 million. The term of the loan was 25 years, which included rate resets every five years during the term of the loan. The new rate effective January 1, 2009 and for the next five years is 2.55%. The outstanding balance as of June 30, 2011 was \$3.3 million.

On December 10, 2009, an agreement was entered into by TJUH in the amount of \$22.0 million to fund the acquisition of the property located at 925 Chestnut Street, Philadelphia, Pennsylvania. The loan bears interest at a rate equal to LIBOR plus 190 basis points with a mortgage-style amortization of 20 years. The outstanding balance as of June 30, 2011 was \$20.7 million.

On October 9, 2009, a Master Lease Agreement was entered into by TJUH for a term of 60 months commencing July 2010 in the amount of \$5.9 million. The outstanding balance as of June 30, 2011 was \$5.7 million.

On August 16, 2007, The Pennsylvania Economic Development Financing Authority ("PEDFA") issued:

The Series 2007 MLH Revenue Bonds (the "2007 Bonds"), mature on October 1, 2027, in the amount of \$34.6 million. The bondholders have a put option that can be exercised in August 2012, at which point the Bonds would be either remarketed or repurchased by MLH. The purpose of the issuance was to (i) redeem the existing Riddle Hospital Series of 1998 Bonds outstanding at June 30, 2007 in the amount of \$37.0 million; (ii) pay the costs incurred in connection with the issuance of the 2007 Bonds; and (iii) eliminate the 1998 Bond requirement to maintain a Debt Service Reserve Fund, which had an August 16, 2007 market value of \$3.4 million. The outstanding balance as of June 30, 2011 was \$34.6 million.

The Series 2007 TJUH System Revenue Bonds (the "Bonds"), mature on October 1, 2037, in the amount of \$100.0 million. The bondholders have a put option that can be exercised in August 2012, at which point the Bonds would be either remarketed or repurchased by TJUH. Otherwise, the Bonds are subject to annual mandatory sinking fund redemption from 2027 to 2037 in amounts ranging from \$7.4 million to \$11.0 million. The bond proceeds were being used to finance the addition of critical care beds; expansion of the emergency department; upgrade and expansion of oncology infusion services; other infrastructure improvements; and, the costs of issuing the Bonds. The total estimated cost for these projects is \$137.0 million. The bonds traded at a rate of 0.71% at June 30, 2010. Interest rates ranged from 0.55% to 0.83% during 2010. The outstanding balance as of June 30, 2011 was \$100.0 million.

While MLH and TJUH are each solely responsible for payments to be made to PEDFA pursuant to separate loan agreements dated August 1, 2007, the payment obligations under each loan agreement are guaranteed by the other borrower that is not party to the agreement. The guarantees are collateralized by certain real estate and are subordinate to the rights of JHS and its other Members.

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The 2007 Bonds bear interest at Indexed Put Rates and may be converted to bonds that bear interest at a Daily Interest Rate, Weekly Interest Rate, Long-Term Interest Rate, Bond Interest Term Rate, or an Auction Rate.

During fiscal year 2003, the Philadelphia Issuer issued the Series of 2003 Hospital Revenue Bonds, maturing on January 1, 2017, in the amount of \$6.5 million for the “Thomas Jefferson University Hospital Project”. The proceeds of the bonds were used to provide funding for the construction and equipping of improvements to the existing facilities of TJUH and its affiliates. The bonds were initially issued at a short-term rate of 1.03% and remarketed weekly. The bonds traded at a rate of 0.26% at June 30, 2010. Interest rates ranged from 0.19% to 0.39% during 2010. A reimbursement agreement was entered into by TJUH to provide for the issuance of a long-term letter of credit, which provides amounts sufficient to pay the purchase price of any bonds tendered for purchase and not remarketed. The outstanding balance as of June 30, 2011 is \$1.2 million.

On July 1, 2003, Riddle Memorial Hospital Health Care Center III Associates (“HCC III Associates”), a Pennsylvania limited partnership issued and sold \$8.6 million of its Taxable Variable Rate Demand Bonds, Series 2003 (the “2003 Bonds”). The 2003 Bonds constitute general obligations of HCC III Associates, the payment of which is supported by the assets and credit of HCC III Associates and secured in the trust indenture. The 2003 Bonds will mature on July 1, 2013 and initially bear interest at a weekly rate, and may thereafter be converted to a medium term rate or to a fixed rate. Payment of the principal, interest, and purchase price is collateralized by an irrevocable direct pay letter of credit issued by a local bank. HCC III Associates has entered into an agreement with Bank of New York or its successor (the “2003 Bonds Trustee”) as Trustee for the holders of the 2003 Bonds. Proceeds of the Series 2003 Bonds were used to: (a) refinance existing outstanding indebtedness of \$6.0 million; (b) acquire a leasehold interest in two floors of a medical office building owned by the Hospital for a twenty-five year term after a lump sum rental payment of \$2.5 million pursuant to a lease agreement with the Hospital; (c) pay expenses related to the issuance of the 2003 Bonds. There was no outstanding balance as of June 30, 2011.

The remainder primarily consists of small Member notes and mortgages (\$0.7 million).

JHS generated the required “Income Available for Debt Service,” as defined in the 1997 Master Indenture of at least 110 percent of “Annual Debt Service.”

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Consolidated annual maturities for long-term obligations for each of the next five years, and thereafter, are as follows:

2012	\$ 13.3
2013	143.5
2014	10.9
2015	11.2
2016	11.1
Thereafter	<u>340.9</u>
	<u>\$ 530.9</u>

The unamortized deferred financing fees associated with all the bond issues is \$3.7 million and \$3.5 million as of June 30, 2011 and June 30, 2010, respectively.

The fair value of long-term debt is based on quoted market prices or estimated using discounted cash flow analyses based on the borrower's incremental borrowing rates for similar types of borrowing arrangements.

The carrying amounts and fair values of long-term debt at June 30, 2011 are as follows:

	Carrying Amount	Fair Value
Balance sheet liabilities		
Debt obligations	\$ 530.9	\$ 533.1

The carrying amounts and fair values of long-term debt at June 30, 2010 are as follows:

	Carrying Amount	Fair Value
Balance sheet liabilities		
Debt obligations	\$ 508.1	\$ 512.1

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7. Derivative Financial Instruments

In order to lock in the then current debt interest rates JHS entered into various interest rate swap agreements with notional amounts of \$408.7 million and \$443.6 million at June 30, 2011 and June 30, 2010, respectively. The London InterBank Offered Rate (“LIBOR”) British Bankers' Association (“BBA”) rates for the one month ranged from 0.19 percent to 0.35 percent (average rate of 0.25 percent) in 2011. The LIBOR BBA rates for the five year ranged from 1.31 percent to 2.58 percent (average rate of 1.97 percent) in 2011.

Included in other non-current liabilities on the consolidated balance sheets are unrealized losses of \$39.4 million and \$45.8 million as of June 30, 2011 and 2010, respectively, related to these swap agreements.

Expiration Date (\$ in millions)	JHS Receives	JHS Pays	Notional Amount at June 30, 2011	Notional Amount at June 30, 2010	Balance Sheet Location	Fair Value at June 30, 2011	Fair Value at June 30, 2010
November 1, 2037	68% of United States Dollar Libor BBA (One Month)	3.6319%	\$47.3	\$50.0	Other non-current liabilities	\$6.3	\$7.9
November 1, 2037	68% of United States Dollar Libor BBA (One Month)	3.6460%	\$47.3	\$50.0	Other non-current liabilities	\$6.3	\$7.9
May 1, 2027	68% of United States Dollar Libor BBA (OneMonth)	3.9410%	\$59.6	\$67.0	Other non-current liabilities	\$8.5	\$10.0
May 1, 2018	68% of United States Dollar Libor BBA (One Month)	3.8570%	\$19.9	\$20.2	Other non-current liabilities	\$2.7	\$2.9
May 1, 2027	68% of United States Dollar Libor BBA (One Month)	3.9190%	\$74.5	\$75.0	Other non-current liabilities	\$12.0	\$14.0
May 1, 2027	68% of United States Dollar Libor BBA (One Month)	3.9800%	\$42.8	\$43.1	Other non-current liabilities	\$7.2	\$8.3

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Expiration Date (\$ in millions)	JHS Receives	JHS Pays	Notional Amount at June 30, 2011	Notional Amount at June 30, 2010	Balance Sheet Location	Fair Value at June 30, 2011	Fair Value at June 30, 2010
May 1, 2018	63.73% of United States Dollar LIBOR BBA (Five Year)	68% of United States Dollar Libor BBA (One Month)	\$ -	\$20.2	Other non- current liabilities	-	(\$0.9)
May 1, 2027	68% of United States Dollar LIBOR BBA (Five Year minus 0.2930%)	68% of United States Dollar Libor BBA (One Month)	\$74.5	\$75.0	Other non- current liabilities	(\$3.6)	(\$2.8)
May 1, 2027	68% of United States Dollar LIBOR BBA (Five Year minus 0.325%)	68% of United States Dollar Libor BBA (One Month)	\$42.8	(a) \$43.1	Other non- current liabilities	-	(\$1.5)

(a) In January 2011 the agreement was restructured to a forward start date of July 1, 2016.

All of these swaps are marked to market and recorded as nonoperating revenues investment income and realized gains. Included in other nonoperating revenues (expenses) on the Statements of Operations and Changes in Net Assets is a gain (loss) of \$1.3 million and (\$6.4) million for the years ended June 30, 2011 and 2010, respectively, related to these swap agreements.

All of the JHS derivative instruments contain credit-risk-related provisions that require JHS to post collateral in varying amounts based on respective credit ratings. The counterparties to the derivative instruments would require JHS to post collateral only if the position of the individual derivative instrument is negative by in excess of \$40.0 million. Based on JHS' current credit rating and the position of the derivative instruments, JHS was not required to post collateral as of June 30, 2011 and June 30, 2010.

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8. Pension Plans

Each of the Members has a separate non-contributory defined benefit plan covering substantially all full-time employees (the "Plans"). Generally, benefits under the Plans are based on the employee's compensation and years of service. Contributions to the Plans are designed to meet the minimum funding requirements of the Employee Retirement Income Security Act of 1974.

Items included in unrestricted net assets represent amounts that have not been recognized in net periodic pension expense. The components recognized in unrestricted net assets, as of June 30, 2011 include:

	<u>2011</u>	<u>2010</u>
Amounts recognized in unrestricted net assets		
Unamortized net actuarial loss	\$ 241.9	\$ 317.2
Unamortized prior service (credit)	(17.8)	(4.2)
	<u>\$ 224.1</u>	<u>\$ 313.0</u>

At June 30, 2011 and 2010 amounts in unrestricted net assets that are expected to be recognized as components of net periodic pension expense during fiscal year 2012 and 2011, respectively, are as follows:

Amounts recognized in unrestricted net assets to be amortized		
	<u>2011</u>	<u>2010</u>
Unamortized net actuarial loss	\$.4	\$.9
Unamortized prior service (credit)	\$ (2.0)	\$ (2.0)

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The following table presents the change in the benefit obligation and the change in the fair value of the Plans' assets based on the measurement date, as well as the amounts recognized in the accompanying consolidated financial statements as of June 30, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Change in benefit obligation:		
Benefit obligation at beginning of year -	\$1,030.9	\$854.7
Service cost	35.6	31.9
Interest cost	57.2	53.3
Plan amendment	(16.4)	-
Actuarial loss	4.7	116.7
Benefits paid	(30.1)	(25.7)
	<u>1,081.9</u>	<u>1,030.9</u>
Benefit obligation at end of year		
Change in plan assets:		
Fair value of plan assets at beginning of year -	666.5	580.7
Actual return on plan assets (net of expenses)	120.0	65.0
Employer contributions	58.1	46.8
Benefits paid	(30.1)	(25.7)
	<u>814.5</u>	<u>666.8</u>
Fair value of plan assets at end of year		
Funded status at end of year	<u>(\$267.4)</u>	<u>(\$364.1)</u>
Amounts recognized in the statement of financial position consist of:		
Non-current portion of accrued pension liability	(\$267.4)	(\$364.1)
Net amount recognized	<u>(\$267.4)</u>	<u>(\$364.1)</u>

The following table presents the average assumptions for the Members utilized to estimate year-end pension obligations:

	<u>2011</u>	<u>2010</u>
Assumptions used to estimate June 30, 2011 and 2010 year end pension obligations		
Discount rate	5.53% to 5.75%	5.26% to 5.75%
Rate of compensation increase	4.08%	4.08%

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The following table presents the periodic benefit cost activity of the applicable Plans at June 30, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Periodic Benefit Cost		
Service cost	\$ 35.6	\$ 31.9
Interest cost	57.2	53.3
Expected return on plan assets	(57.8)	(47.4)
Amortization of prior service cost	(2.8)	(2.0)
Amortization of net actuarial gain	<u>17.8</u>	<u>13.6</u>
Net periodic benefit cost	<u>\$ 50.0</u>	<u>\$ 49.4</u>
Weighted-average assumptions used in the measurement of periodic pension costs were:		
Discount rate	5.50%	6.32%
Expected return on plan assets	7.92%	7.92%
Rate of compensation increase	4.17%	4.25%

The consolidated Accumulated Benefit Obligation is \$1,029.0 million and \$959.2 million as of June 30, 2011 and June 30, 2010, respectively.

In aggregate, JHS' Members will make contributions of approximately \$60.3 million to the Plans in fiscal year 2012.

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Asset Allocation

The aggregate asset allocation for the various Plans' investments is as follows:

	Target Allocation	Percentage of Plan Assets June 30	
		<u>2011</u>	<u>2010</u>
		Equity Securities	62%
Fixed Income	33%	32%	34%
Alternative Investments	5%	4%	4%
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>

The following table presents the Plans' assets as of June 30, 2011, measured at fair value on a recurring basis using the fair value hierarchy described in Note 2:

	<u>Assets at Fair Value as of June 30, 2011</u>			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
	<i>(in millions)</i>			
Assets, at fair value:				
Mutual funds - primarily US government obligations	\$ 61.9	\$ -	\$ -	\$ 61.9
Mutual funds - marketable equity securities	102.2	-	-	102.2
Mutual funds - fixed income securities	101.5	-	-	101.5
Equity Securities	125.5	77.0	109.5	312.0
US Government obligations	1.4	-	-	1.4
Corporate bonds	-	5.6	-	5.6
Certificates of deposit and other commercial paper	2.5	12.3	-	14.8
Fixed income securities	3.9	54.2	0.6	58.7
Hedge funds	-	-	21.2	21.2
Other, including alternative assets	(0.4)	5.5	130.1	135.2
	<u>\$ 398.5</u>	<u>\$ 154.6</u>	<u>\$ 261.4</u>	<u>\$ 814.5</u>

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(in millions)	<u>Hedge funds</u>	<u>Other, including alternative assets</u>	<u>Total</u>
Balance, at June 30, 2010	\$ 20.1	\$ 178.6	\$ 198.7
Net purchases and sales	(0.1)	5.2	5.1
Realized and unrealized gains (losses), net	1.2	38.0	39.2
Transfers in, net	-	18.4	18.4
Balance, at June 30, 2011	<u>\$ 21.2</u>	<u>\$ 240.2</u>	<u>\$ 261.4</u>

The following table presents the Plan's assets as of June 30, 2010, measured at fair value on a recurring basis using the fair value hierarchy described in Note 2:

	<u>Assets at Fair Value as of June 30, 2010</u>			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
	<i>(in millions)</i>			
Assets, at fair value:				
Mutual funds - primarily US government obligations	\$ 58.3	\$ -	\$ -	\$ 58.3
Mutual funds - marketable equity securities	75.1	-	-	75.1
Mutual funds - fixed income securities	93.8	-	-	93.8
Equity Securities	112.6	55.7	62.3	230.6
US Government obligations	0.9	-	-	0.9
Corporate bonds	-	4.6	-	4.6
Certificates of deposit and other commercial paper	7.2	12.7	-	19.9
Fixed income securities	6.3	39.1	-	45.4
Hedge funds	-	-	20.1	20.1
Other, including alternative assets	1.8	-	116.3	118.1
	<u>\$ 356.0</u>	<u>\$ 112.1</u>	<u>\$ 198.7</u>	<u>\$ 666.8</u>

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(in millions)	<u>Hedge funds</u>	<u>Other, including alternative assets</u>	<u>Total</u>
Balance, at June 30, 2009	\$ 8.5	\$ 157.6	\$ 166.1
Net purchases and sales	10.9	11.0	21.9
Realized and unrealized gains (losses), net	0.7	10.0	10.7
Transfers in, net	-	-	-
Balance, at June 30, 2010	<u>\$ 20.1</u>	<u>\$ 178.6</u>	<u>\$ 198.7</u>

In selecting the expected long-term rate of return on the Plans' assets assumption, the Members of JHS consider average rate of earnings on the funds invested and to be invested, the Plan's asset allocation and the expected returns likely to be earned over the life of the Plans.

Projected Pension Benefit Payments

Pension benefit payments for the next ten years are currently projected by the Members of JHS to be:

<u>Year</u>	<u>Amount</u>
2012	\$36.1
2013	39.2
2014	42.8
2015	46.3
2016	51.4
2016 - 2020	336.8

9. Professional and General Liability Claims

JHS, the Members, Albert Einstein Healthcare Network (AEHN) until June 30, 2010, Aria, Thomas Jefferson University (TJU), Jefferson University Physicians (JUP) and their affiliated organizations ("Policyholders") have several layers of coverage for professional liability exposures.

As of June 30, 2011 and 2010 for the healthcare provider (hospital, physician / resident), Member organizations, AEHN (until June 30, 2010), Aria and JUP, the first ("primary") layer of coverage is claims made coverage with limits of \$500 thousand per medical incident / \$2.5 million annual aggregate per hospital and \$500 thousand per medical incident and \$1.5 million annual aggregate per physician / residents. The limits for this primary coverage layer are statutorily prescribed in Pennsylvania. In addition, a \$1.0 million per medical incident / \$3.0 million annual aggregate limit is provided per scheduled dentists as well as for scheduled physicians / residents practicing in Delaware and New Jersey.

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As of June 30, 2011 JHS, the Members' non-healthcare provider entities, TJU and Aria's non-healthcare provider entities are each provided with a \$1.0 million / \$3.0 million annual aggregate limit of liability. JUP non-healthcare provider entities continue to be provided with a \$1.0 million/\$2.0 million annual aggregate limit of liability. As of June 30, 2010 JHS, the Members' non-healthcare provider entities, AEHN's non-healthcare provider entities and Aria's non-healthcare provider entities are each provided with a shared \$1.0 million / \$1.0 million annual aggregate limit of liability. As of June 30, 2010 TJU and JUP non-healthcare provider entities are each provided with a \$1.0 million/\$2.0 million annual aggregate limit of liability.

In addition, as of June 30, 2011 and 2010 a \$2.0 million per occurrence / \$5.0 million aggregate general liability coverage limit shared by JHS and the Members is provided. As of June 30, 2011 separate general liability policy limits of \$1.0 million per occurrence / \$3.0 million aggregate are provided to Aria and \$1.0 million per occurrence / \$2.0 million aggregate limits are provided to TJU. As of June 30, 2010 separate general liability policy limits of \$1.0 million per occurrence / \$3.0 million aggregate were also provided to AEHN and Aria. TJU was provided a \$1.0 million per occurrence / \$2.0 million aggregate.

Policyholders obtain their primary hospital and physician professional liability, miscellaneous professional liability and general liability coverages from the RRG. For the professional liability coverages the RRG is 100% reinsured by Five Pointe. The RRG retains 100% of the general liability coverage exposure. AEHN terminated its participation in the RRG and Five Pointe programs as of July 1, 2010.

The premiums charged to policyholders for the primary professional and general liability layers of coverage are determined by an independent outside actuary based on loss and loss adjustment expense experience

The second layer of professional liability coverage for the healthcare provider (hospital, physician / resident) Member organizations is obtained through the MCARE Fund. This second layer, required by statute, consists of coverage limits of \$0.5 million per medical incident and \$1.5 million annual aggregate per hospital and per employed physician at June 30, 2011 and June 30, 2010. The annual assessments for MCARE Fund coverage are based on the schedule of occurrence rates approved by the Insurance Commissioner of Pennsylvania for the Pennsylvania Professional Liability Joint Underwriting Association multiplied by an annual assessment percentage. This assessment is recognized as an expense in the period incurred.

Liabilities for JHS and the Members of JHS and their affiliated organizations for potential losses in excess of the primary and MCARE layers (if applicable) up to \$5.0 million each medical incident / \$5.0 million aggregate per Member retention excess of a \$7.0 million each and every medical incident retention for JHS and the Members of JHS and their affiliated organizations (with the exception of Bryn Mawr Rehabilitation and Magee) and up to \$2.0 million each and every medical incident for Bryn Mawr Rehabilitation Hospital and Magee are based on actuarially determined estimates, which reflect a discount rate of 3 percent and a 65 percent confidence level for fiscal year 2011 and 2010. These estimates are based on historical loss and loss adjustment expense information along with certain assumptions about future events. Changes in assumptions for such considerations as medical costs and actual experience could cause these estimates to change.

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During fiscal year 2011 and 2010, JHS and the Members of JHS and their affiliated organizations maintained claims made excess / umbrella liability insurance coverage through Five Pointe in the amount of \$90.0 million per medical incident / \$90.0 million annual aggregate after a \$5.0 million / \$5.0 million per Member retention excess of a \$7.0 million each and every medical incident retention by JHS and Members of JHS and their affiliated organizations (with the exception of Bryn Mawr Rehabilitation Hospital and Magee). The excess catastrophic professional liability insurance coverage through Five Pointe attaches after a \$2.0 million each and every medical incident retention for Bryn Mawr Rehabilitation Hospital and Magee. During fiscal year 2011 and 2010, Five Pointe reinsured 100 percent of this risk to six currently A-rated insurers (ACE, Zurich, Allied World, Berkley, Endurance, Swiss Re). A separate limit of \$90.0 million per occurrence / \$90.0 million aggregate is also maintained to provide liability insurance coverage excess of the primary general, auto, employers and aviation liability coverages.

For fiscal years 2011 and 2010 Five Pointe continued to provide claims made excess insurance coverage for Aria and its affiliated organizations with limits of \$15.0 million per medical incident / \$15.0 million annual aggregate. Five Pointe reinsured 100 percent of this risk with currently at least A- rated reinsurance carriers. During fiscal year 2010, Five Pointe also provided claims made excess insurance coverage for AEHN and its affiliated organizations with limits of \$40.0 million per medical incident / \$40.0 million annual aggregate. Five Pointe reinsured 100 percent of this risk with currently at least A- rated reinsurance carriers.

10. Commitments and Contingencies

Operating Leases

JHS Members have various lease obligations for equipment, ambulatory facilities and office space. At June 30, 2011, the minimum future rental commitment is as follows:

2012	\$ 33.0
2013	29.5
2014	25.1
2015	23.4
2016	19.5
Thereafter	<u>68.2</u>
	<u>\$ 198.7</u>

Total rental expense was \$43.0 million in 2011 and \$39.8 million in 2010.

Lines of Credit

At June 30, 2011 and 2010, JHS had available unsecured lines of credit of \$15.8 million and \$20.8 million, respectively. There was zero outstanding as of June 30, 2011 and 2010.

Letters of Credit

At June 30, 2011 and 2010, JHS had available open letters of credit aggregating \$58.8 million and \$60.0 million, respectively.

Litigation

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JHS and the Members of JHS are involved in litigation arising in the ordinary course of business. In the opinion of management, all such matters are adequately covered by insurance or by accruals, and if not so covered, are without substantial merit or are of such kind, or involve such amounts, as would not have a material adverse effect on the financial position or results of operations of JHS.

On November 20, 2009, a class action lawsuit was filed against JHS and the Members by certain hourly employees alleging restitution for unfair business practices, injunctive relief for unfair business practices, failure to pay overtime wages, and penalties associated therewith. On September 8, 2011, the Court granted the defendants' Motions to Dismiss all asserted claims but provided the plaintiffs with thirty days to file a second amended complaint. JHS is unable to determine the cost of defending this lawsuit or the impact, if any, this action may have on its results of operations.

FICA Medical Resident Refund

In March 2010, the Internal Revenue Service (IRS) announced that for periods ending before April 1, 2005, medical residents would be eligible for the student exception of Federal Insurance Contributions Act (FICA) taxes. As a result, institutions that had filed timely FICA refund claims covering periods up through that date are eligible for refunds of both the employer and employee portions of FICA taxes paid, plus statutory interest. As a result of the decision by the IRS, TJUH recorded in 2010 revenues of \$14.5 million, a receivable of \$21.8 million and an accrued liability of \$7.3 million. Accounts receivable include both the employer and resident amounts and accrued statutory interest. Accrued liabilities include the portion of the refund which will be collected on behalf of the medical residents. This estimate reflects the initial valuation of the refund which may be subject to changes in future periods.

Other

The health care industry in general and the services that the Members of JHS provide are subject to extensive federal and state laws and regulations. Additionally, a portion of net revenue is from payments by government-sponsored health care programs, principally Medicare and Medical Assistance and is subject to audit and adjustments by applicable governmental agencies. Failure to comply with any of these laws or regulations, the result of regulatory audits and adjustments, or reductions in the amounts payable for services under these programs, could have a material, adverse effect on JHS' financial position and results of operations.

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11. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are primarily comprised of unspent capital appreciation (net realized and unrealized gains) that can be spent in the future subject to certain spending limitations under Pennsylvania Statute:

	<u>2011</u>	<u>2010</u>
Healthcare services	\$ 117.6	\$ 105.1
Fellowship and research	19.5	14.9
Indigent care	12.7	11.0
	<u>\$ 149.8</u>	<u>\$ 131.0</u>

Investment income generated from investment of the following permanently restricted net assets is available to support the following purposes:

	<u>2011</u>	<u>2010</u>
Endowments to be held in perpetuity, the income of which is expendable to support:		
Healthcare services	\$ 67.7	\$ 62.1
Fellowship and research	24.8	21.5
Indigent care	37.6	32.8
	<u>\$ 130.1</u>	<u>\$ 116.4</u>

The above amounts include \$65.7 million and \$55.8 million at June 30, 2011 and 2010, respectively, of beneficial interest in perpetual trusts.

12. Relationship with Thomas Jefferson University

JHS and Thomas Jefferson University (TJU) are parties to a Master Academic Affiliation Agreement, which establishes TJU as the primary academic affiliate for JHS and the Members of JHS. The Academic Affiliation Agreement is intended to strengthen academic programs, enhance patient care and further basic and clinical research activities.

Transactions with TJU

Subsequent to March 1996, TJU agreed to provide to TJUH the following services: physician and non-physician personnel and other support necessary to preserve and maintain the tertiary care capacity of TJUH. TJU also provides clinical space as well as administrative and finance, human resource, information technology, maintenance and security, temporary staffing and other ancillary services to TJUH. Expenses charged by TJU were \$175.9 million and \$134.2 million for the years ended June 30, 2011 and 2010, respectively. The increase in support to TJU in 2011 was largely due to funding of clinically related medical malpractice expenses and for growing and sustaining clinical programs.

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TJUH provides TJU with certain office and clinical space, information systems services, telecommunications services and ancillary services. Expenses charged to TJU for these services aggregated to \$37.0 million and \$27.6 million in 2011 and 2010, respectively.

Approximately \$174.8 million and \$147.8 million of JHS' investments represent participation by TJUH in TJU's pooled investment funds at June 30, 2011 and 2010, respectively.

13. Recent Accounting Pronouncements

Mergers and Acquisitions

In April 2009, the Financial Accounting Standards Board (FASB) issued a standard which provides guidance on improving the quality of information in financial reports provided by a not-for-profit organization regarding business combinations with one or more other not-for-profit entities, businesses or nonprofit activities. The guidance will distinguish mergers (carryover method) from acquisitions (acquisition method) as well as provide updated accounting for goodwill and intangibles. Additional disclosures will be required in order to enable users of financial statements to evaluate the nature and financial effects of the merger or acquisition. This standard is effective for fiscal years beginning after December 15, 2009. Disclosures pertaining to any future mergers or acquisitions occurring after July 1, 2010 will be expanded in accordance with this standard for the consolidated financial statements beginning in fiscal year 2011.

Presentation of Insurance Claims and Related Insurance Recoveries

In August 2010, new guidance was issued for the presentation of insurance claims and associated insurance recoveries for healthcare organizations. Under the new guidance, health care entities are required to reflect their "gross" exposure to claims liabilities with a corresponding receivable for insurance recoveries in order to be consistent with other industries. This guidance will become effective for JHS on July 1, 2011.

Charity Care Disclosure

In August 2010, the FASB issued new guidance regarding the measurement basis used in the disclosure of charity care. The guidance requires that the disclosures related to the level of charity care provided should be based on a healthcare organization's estimated direct and indirect costs of providing the services and that a healthcare organization should separately disclose the amount of charity care reimbursed by third parties. In addition, disclosure of the method used to identify or determine such costs is required. This guidance will become effective for JHS on July 1, 2011.