OBLIGATED GROUP
FINANCIAL STATEMENT
(UNAUDITED)

3rd QUARTER
JUNE 2014

Obligated Group Financial Statements and Other Financial Information
(Unaudited)

For the Quarter and Nine Months Ended June 30, 2014

Contents

SHARP HEALTHCARE
OBLIGATED GROUP BALANCE SHEET (UNAUDITED)
June 30, 2014
($ in 000's)

ASSETS

	JUNE 2014	JUNE 2013	SEPT. 2013
Current assets:			
Cash and cash equivalents	$ 217,436	$ 167,529	$ 150,936
Short-term investments	50,755	55,771	52,526
Accounts receivable, net	275,423	282,265	279,998
Intercompany receivables, net	16,964	24,642	20,918
Estimated settlements receivable from government programs, net	18,155	13,203	5,605
Inventories	37,898	34,855	38,165
Prepaid expenses and other	52,791	47,824	44,899
Total current assets	669,422	626,089	593,047
Assets limited as to use:			
Designated for property	1,341,492	1,027,987	1,139,242
Under bond indentures	147,993	21,363	16,535
Total assets limited as to use	1,489,485	1,049,350	1,155,777
Net property, plant and equipment	1,012,053	964,660	975,795
Unamortized financing costs	7,657	6,466	6,335
Other assets	35,430	26,440	33,140
Beneficial interest in foundations	72,484	62,727	63,037
Total Assets	$ 3,286,531	$ 2,735,732	$ 2,827,131

LIABILITIES AND NET ASSETS

	JUNE 2014	JUNE 2013	SEPT. 2013
Current liabilities:			
Accounts payable and accrued liabilities	$ 177,257	$ 179,309	$ 167,462
Intercompany payables, net	-	74	73
Accrued compensation and benefits	104,994	112,135	132,597
Current portion of long-term debt	11,082	16,239	19,458
Accrued interest	9,866	7,369	3,296
Total current liabilities	303,199	315,126	322,886
Long-term liabilities	124,655	129,697	109,288
Reserves for professional liability	2,201	3,300	2,201
Long-term debt	724,117	585,397	577,665
Total liabilities	1,154,172	1,033,520	1,012,040
Net Assets:			
Unrestricted	2,067,931	1,644,740	1,757,164
Temporarily restricted	58,250	51,800	51,884
Permanently restricted	6,178	5,672	6,043
Ending net assets	2,132,359	1,702,212	1,815,091
Total Liabilities and Net Assets	$ 3,286,531	$ 2,735,732	$ 2,827,131

SHARP HEALTHCARE
OBLIGATED GROUP STATEMENT OF OPERATIONS (UNAUDITED)
FOR THE QUARTER ENDED JUNE 30, 2014 AND NINE MONTHS ENDED JUNE 30, 2014
($ in 000's)

QUARTER					YEAR - TO - DATE			
Last Year	Actual	Budget	Variance	D E S C R I P T I O N	Last Year	Actual	Budget	Variance
$ 397,762	$ 435,355	$ 412,607	$ 22,748	NET PATIENT SERVICE REVENUE	$ 1,184,787	$ 1,280,053	$ 1,242,527	$ 37,526
71,756	-	12,635	(12,635)	PROVIDER TAX REVENUE	114,287	24,005	36,640	(12,635)
191,946	207,109	199,340	7,769	PREMIUM REVENUE	574,060	604,893	591,432	13,461
24,567	25,701	25,561	140	OTHER OPERATING REVENUE	70,428	76,856	77,120	(264)
686,031	668,165	650,143	18,022	TOTAL OPERATING REVENUE	1,943,562	1,985,807	1,947,719	38,088
				OPERATING EXPENSES:				
301,754	313,815	314,681	866	Staffing	890,937	938,436	938,991	555
80,093	86,399	79,353	(7,046)	Supplies	227,123	248,770	240,576	(8,194)
55,364	66,801	65,729	(1,072)	Medical fees	178,362	190,235	194,239	4,004
66,683	70,659	68,046	(2,613)	Purchased services	188,229	206,963	203,055	(3,908)
53,168	-	8,727	8,727	Provider tax	85,565	17,742	26,469	8,727
27,994	29,044	29,466	422	Maint., utilities & rentals	79,720	84,168	88,552	4,384
2,815	3,372	3,542	170	Business insurance	10,262	7,615	10,579	2,964
6,466	6,736	7,226	490	Other	19,453	23,496	22,562	(934)
594,337	576,826	576,770	(56)	TOTAL OPERATING EXPENSES	1,679,651	1,717,425	1,725,023	7,598
91,694	91,339	73,373	17,966	EBITDA from Operations	263,911	268,382	222,696	45,686
23,574	23,355	26,791	3,436	Depreciation & amortization	72,149	70,652	75,110	4,458
37	40	38	(2)	Taxes	103	119	113	(6)
5,733	7,027	6,841	(186)	Interest	17,088	19,195	20,652	1,457
62,350	60,917	39,703	21,214	INCOME FROM OPERATIONS	174,571	178,416	126,821	51,595
9.1%	9.1%	6.1%	-	% OF OPERATING REVENUE	9.0%	9.0%	6.5%	-
				NON-OPERATING INCOME (LOSS)				
(9,908)	37,919	7,391	30,528	Investment income (loss)	37,057	91,270	26,564	64,706
717	(1,557)	-	(1,557)	Mark to market swaps	2,708	(1,835)	-	(1,835)
(913)	(959)	(1,005)	46	Other expense	(2,673)	(2,927)	(2,998)	71
(10,104)	35,403	6,386	29,017	TOTAL NON-OPERATING INCOME (LOSS)	37,092	86,508	23,566	62,942
52,246	96,320	46,089	50,231	EXCESS OF REVENUE OVER EXPENSES	211,663	264,924	150,387	114,537
7.6%	14.4%	7.1%	-	% OF OPERATING REVENUE	10.9%	13.3%	7.7%	-
$ 81,590	$ 126,742	$ 79,759	$ 46,983	EBITDA	$ 301,003	$ 354,890	$ 246,262	$ 108,628

SHARP HEALTHCARE
OBLIGATED GROUP STATEMENT OF CHANGES IN NET ASSETS (UNAUDITED)
FOR THE QUARTER ENDED JUNE 30, 2014
AND NINE MONTHS ENDED JUNE 30, 2014
($ in 000's)

	Quarter	YTD	Prior YTD
Unrestricted net assets:			
Excess of revenues over expenses	$ 96,320	$ 264,924	$ 211,663
Net assets released from restrictions used for the purchase of property, plant and equipment	15,522	42,813	28,801
Beneficial Interest in Foundations	1,131	3,030	1,899
Increase in unrestricted net assets	112,973	310,767	242,363
Temporarily restricted net assets:			
Beneficial Interest in Foundations	4,341	6,366	1,618
Increase in temporarily restricted net assets	4,341	6,366	1,618
Permanently restricted net assets:			
Beneficial Interest in Foundations	5	135	109
Increase in permanently restricted net assets	5	135	109
Increase in net assets	117,319	317,268	244,090
Net assets, beginning	2,015,040	1,815,091	1,458,122
Net assets, ending	$ 2,132,359	$ 2,132,359	$ 1,702,212

SHARP HEALTHCARE
OBLIGATED GROUP STATEMENT OF CASH FLOWS (UNAUDITED)
FOR THE QUARTER ENDED JUNE 30, 2014
AND NINE MONTHS ENDED JUNE 30, 2014
($ in 000's)

	Quarter	YTD	Prior YTD
CASH FLOWS FROM OPERATING ACTIVITIES AND OTHER INCOME:			
Increase in net assets	$ 117,319	$ 317,268	$ 244,090
Adjustments to reconcile increase in net assets to net cash provided by operating activities:			
Net assets transferred from related party	(14,391)	(39,452)	(25,744)
Depreciation of operating and nonoperating facilities	23,355	70,652	72,149
Amortization, including deferred financing costs	3	199	140
Other non-operating (gains) losses, net	(12)	(101)	(97)
Provision for doubtful accounts	4,810	19,079	19,261
Change in net unrealized (gains) losses on investments	(26,462)	(55,933)	(9,746)
Change in net unrealized (gains) losses on swap activity	1,557	1,835	(2,708)
Changes in operating assets and liabilities:			
(Increase) decrease in:			
Short-term investments	5,272	1,771	21,487
Accounts receivable, net	(2,596)	(14,504)	(20,656)
Intercompany receivable	(1,404)	3,881	3,055
Est. settlements receivable from govt programs, net	2,350	(12,550)	(496)
Inventories	(1,049)	267	419
Prepaid expenses	4,541	(7,892)	(6,209)
Assets Limited as to use	(78,068)	(277,775)	(162,554)
(Decrease) increase in:			
Accounts payable and accrued liabilities	23,627	9,795	(31,489)
Accrued compensation and benefits	(15,506)	(27,603)	(9,629)
Accrued interest	5,774	6,570	4,118
Other long-term liabilities	(361)	15,367	9,036
Reserve for malpractice	-	-	1,000
Cash provided by operating activites	48,759	10,874	105,427
CASH FLOWS FROM INVESTING ACTIVITIES:			
Acquisition of property, plant and equipment, net of retirements	(26,018)	(61,844)	(79,866)
Change in other assets	(5,463)	(13,162)	(11,276)
Investments in joint ventures	-	(1,078)	-
Distributions from joint ventures	1,705	2,502	2,292
Cash used in investing activities	(29,776)	(73,582)	(88,850)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Current maturities and payments on long-term debt	(7,972)	(8,517)	(1,237)
Current payments under capital lease obligations	(492)	(1,393)	(1,192)
Extinguishment of long-term debt	-	(24,895)	-
Proceeds from the issuance of long-term debt	(47)	164,294	-
Transfers, other changes in long-term debt	(94)	(281)	(23)
Cash provided by (used in) financing activities	(8,605)	129,208	(2,452)
NET INCREASE IN CASH AND CASH EQUIVALENTS	10,378	66,500	14,125
BEGINNING CASH AND CASH EQUIVALENTS BALANCE	207,058	150,936	153,404
ENDING CASH AND CASH EQUIVALENTS BALANCE	$ 217,436	$ 217,436	$ 167,529

SUPPLEMENTAL DISCLOSURE OF NON CASH INVESTING AND FINANCING ACTIVITIES:

Capital lease obligations for building and equipment	**$ 1,239**	**$ 5,512**	**$ 4,096**
Net assets transferred from a related party	**$ 14,391**	**$ 39,452**	**$ 25,744**

Sharp HealthCare
Notes to Obligated Group Financial Statements (Unaudited)
Quarter Ended June 30, 2014

1. Summary of Significant Accounting Policies

Organization

Sharp HealthCare (SHC) is a California nonprofit public benefit corporation with corporate offices in San Diego, California. SHC, together with its affiliated entities (collectively Sharp), constitute a regional integrated health care delivery system which does business as Sharp HealthCare, primarily serving the residents of San Diego County and includes the following:

- Sharp Memorial Hospital (SMH), including Stephen Birch Healthcare Center, Sharp Mary Birch Hospital for Women & Newborns, Sharp Outpatient Pavilion, Sharp Mesa Vista Hospital, and Sharp McDonald Center (formerly Sharp Vista Pacifica)
- Sharp Chula Vista Medical Center (SCVMC)
- Sharp Grossmont Hospital (SGH)
- Sharp Coronado Hospital and HealthCare Center (SCHHC)
- Sharp Health Plan (SHP)
- Continuous Quality Insurance SPC (CQI SPC)
- Sharp HealthCare Foundation (SHF)
- Grossmont Hospital Foundation (GHF)

SHC, SMH, SCVMC and SGH are collectively the “Obligated Group” under certain bond indentures. The obligated group records beneficial interest in SHF and GHF, which are not members of the obligated group.

On January 1, 2012, SHC, together with two of its affiliated medical groups, Sharp Community Medical Group (SCMG) and Sharp Rees-Stealy Medical Group (SRSMG), formed the Sharp HealthCare ACO, a limited liability company (Sharp ACO). Sharp ACO was awarded a contract with the Centers for Medicare & Medicaid Services (CMS) as a Pioneer Accountable Care Organization (Pioneer ACO). SHC holds a one third percentage interest in Sharp ACO. The Pioneer ACO is a shared-savings model in which participating organizations are eligible for shared savings payments from CMS if they achieve medical cost savings while providing high quality, coordinated patient care for an assigned group of beneficiaries. Participating organizations also share risk in the form of increased cost payments with CMS for any increase in medical cost. For 2012 and 2013, Sharp ACO’s performance was under a defined 2% and 1.9% minimum threshold, respectively, so no shared savings payments were earned and no increased cost payments were due. In evaluating participation for the year ended December 31, 2014 (“Performance Year 3”), Sharp ACO determined it was at risk for a significant shared loss, despite meaningful reductions in readmission rates and hospital and skilled nursing utilization. In June 2014, Sharp ACO determined it would not continue in the Pioneer ACO Program for Performance Year 3 and notified CMMI of its decision on June 20, 2014. As such, Sharp has no responsibility for an Increased Cost Payment for Performance Year 3 nor potential for any

1. Summary of Significant Accounting Policies (continued)

Organization (continued)

Shared Savings Payment. Because the Pioneer financial model is based on national financial trend factors that are not adjusted for specific conditions that an ACO is facing in a particular region (e.g., San Diego), the model was financially detrimental to Sharp ACO despite favorable underlying utilization and quality performance.

Pursuant to the Pioneer Agreement, Sharp ACO is obligated to guarantee its ability to pay CMS for twenty five percent of the total increased cost payments for which it could be potentially liable in a given year. Sharp ACO borrowed $4,439,000 and $9,690,000 from SHC for the quarters ended June 30, 2014, and June 30, 2013, respectively, to fund an escrow account to cover a portion of any potential medical cost increases of Sharp ACO. With the termination of the Sharp ACO agreement, all escrow funds were released in July 2014. SHC recorded the loan in accounts receivable, net on the combined balance sheets.

SHC has certain contractual obligations with its affiliates that govern its operations and the use of certain assets. All significant transactions among Sharp's obligated group entities have been eliminated in the accompanying obligated group financial statements.

Use of Estimates

The preparation of Sharp's obligated group financial statements in conformity with accounting principles generally accepted in the United States (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the obligated group financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with original maturities of three months or less. Sharp routinely invests its surplus operating funds in money market mutual funds. These funds generally invest in highly liquid U.S. government and agency obligations.

1. Summary of Significant Accounting Policies (continued)

Short-Term Investments

Short-term investments are classified as trading and include corporate and government obligation securities, which are included in professionally managed portfolios, and are measured at fair value in the balance sheet. The maturities of these securities do not exceed one year. Investment income or loss (including unrealized and realized gains and losses) is included in the obligated group excess of revenues over expenses.

Inventories

Inventories, consisting principally of supplies, are stated at the lower of average cost or market value.

Derivative and Hedging Instruments

Sharp recognizes all derivatives on its obligated group balance sheets at fair value. Derivatives that are not effective hedges are adjusted to fair value through the obligated group statements of operations. If the derivative is an effective hedge, depending on the nature of the hedge, changes in the fair values of the derivatives are offset against either the change in fair value of assets or liabilities. The ineffective portion of a derivative's change in fair value, if any, is immediately recognized in the obligated group excess of revenues over expenses.

In 2003, Sharp entered into a floating-to-fixed interest rate swap which is designed to hedge the variability of the cash flows for Sharp's variable rate revenue bonds. In 2004, Sharp entered into a fixed-spread basis swap. The fixed-spread basis rate swap is designed to improve Sharp's cash position through the term of the contract. In 2006, Sharp entered into a fixed-spread yield curve swap. The yield curve swap is designed to hedge the variability of cash flows on Sharp's variable rate bonds and variable rate swap agreements in exchange for an improved cash position through the term of the contract. There are no collateral requirements on any of Sharp's swaps.

Assets Limited as to Use

Assets limited as to use invested in debt and equity securities with readily determined fair values are measured at fair value in the balance sheet and are classified as trading. Investment income or loss (including unrealized and realized gains and losses) is included in the combined excess of revenues over expenses unless the income or loss is restricted by donor or law.

1. Summary of Significant Accounting Policies (continued)

Assets Limited as to Use (continued)

Assets limited as to use primarily include assets set aside by Sharp's Board of Directors (the Board) for future capital improvements, over which the Board retains control and may at its discretion subsequently use for other purposes, and amounts held by trustees under indenture agreements. Assets limited as to use consist of the following:

> ***Designated for property*** **–** Cash resources not required for operations have been designated as funded depreciation to be used for future capital improvements. This designation may be changed and such funds used for other purposes – $28.5 million at June 30, 2014, and $28.7 million at June 30, 2013, of such assets are pledged as collateral for notes payable and other liabilities.
>
> ***Under bond indentures*** **–** In accordance with the terms of Sharp's various bond indentures, certain bond proceeds and principal and interest payments have been deposited with a trustee and are limited as to use in accordance with the related indentures.

Property and Equipment

Property and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset from 3 to 40 years and is computed using the straight-line method. Property and equipment under capital lease obligations is amortized on the straight-line method over the shorter of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the obligated group financial statements. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Unamortized Financing Costs

Costs incurred in obtaining long-term financing are amortized over the terms of the related obligations using the effective interest method.

1. Summary of Significant Accounting Policies (continued)

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by Sharp has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by Sharp in perpetuity.

Impairment or Disposal of Long-Lived Assets

Sharp accounts for the impairment or disposal of long-lived assets using a future cash flow model to determine whether assets have been impaired. Sharp regularly reviews long-lived assets for circumstances which could indicate carrying values may not be recoverable. No impairments were recorded in 2014 or 2013.

Income from Operations

Sharp's primary purpose is to provide diversified health care services to the community served by its affiliates. Only those activities directly associated with the furtherance of this purpose are considered operating activities and classified as operating revenues and expenses. Items excluded from income from operations consist of investment income, gains and losses on disposition of property and equipment, changes in the fair value of interest rate swaps, and fundraising expense.

Excess of Revenues over Expenses

The accompanying obligated group statements of operations include excess of revenues over expenses and other changes in unrestricted net assets. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice, include permanent transfers of assets to and from affiliates for other than goods and services, long-lived assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets, pension-related changes other than net periodic pension cost, and beneficial interest in the foundations.

1. Summary of Significant Accounting Policies (continued)

Net Patient Service Revenues

Sharp has agreements with third-party payors that provide for payments to Sharp at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges and per diem payments. Net patient service 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 accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined. In the opinion of management, adequate provision has been made for such adjustments.

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, Sharp analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, Sharp analyzes contractually due amounts and provides an allowance for doubtful accounts, if necessary. For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), Sharp records a provision for doubtful accounts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Premium Revenues

Sharp has agreements with various employers and health maintenance organizations to provide medical services to subscribing participants. Under these agreements, Sharp receives monthly capitation payments based on the number of participants who have selected Sharp, regardless of services actually performed by Sharp.

Other Revenues

Other revenues include unrestricted donations, retail pharmacy gross profits, management services and joint venture income.

1. Summary of Significant Accounting Policies (continued)

Health Care Service Costs

Sharp contracts with certain health care providers for the provision of medical services to eligible members. These services include primary care and specialty physician services, inpatient and outpatient facility services, pharmacy, and other medical services. Providers are paid on capitated, per diem, and structured fee-for-service bases.

Health care service costs (included in medical fees and purchased services in the accompanying obligated group statements of operations) are accrued in the period in which the services are provided to enrollees, based in part on estimates, including estimates of medical services provided but not yet reported to Sharp.

Charity Care

Sharp's policy is to accept all patients regardless of their ability to pay. In assessing a patient's ability to pay, Sharp utilizes financial eligibility requirements or criteria. Sharp provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because Sharp does not pursue collection of amounts determined to qualify as charity care, such amounts are not reported as revenue.

Charity care costs are calculated using a ratio of cost to gross charge methodology by department. Direct revenues and costs of each department were included in the calculation, in addition to a step down of overhead costs.

Donor-Restricted Gifts

Unconditional promises to give cash and other assets to Sharp are reported at fair value at the date the promise is received. Conditional promises to give and indications or intentions to give are reported at fair value at the date the gift becomes unconditional. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the obligated group statements of operations as other operating revenues. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the obligated group financial statements.

1. Summary of Significant Accounting Policies (continued)

Income Taxes

The principal operations of Sharp are exempt from taxation pursuant to Section 501(c)(3) of the Internal Revenue Code and related California provisions.

Sharp recognizes tax benefits from any uncertain tax positions only if it is more likely than not the tax position will be sustained, based solely on its technical merits, with the taxing authority having full knowledge of all relevant information. Sharp records a liability for unrecognized tax benefits from uncertain tax positions as discrete tax adjustments in the first interim period that the more likely than not threshold is not met. Sharp recognizes deferred tax assets and liabilities for temporary differences between the financial reporting basis and the tax basis of its assets and liabilities along with net operating loss and tax credit carryovers only for tax positions that meet the more likely than not recognition criteria. At June 30, 2014 and 2013, no such assets or liabilities were recorded.

Adoption of New Accounting Pronouncements

In May 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-04, Fair Value Measurement (Topic 820), which clarifies the intent of existing fair value measurement and disclosure requirements under Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures. Adoption of ASU 2011-04 did not have any significant impact on Sharp's obligated group financial statements.

In December 2011, the FASB issued ASU 2011-11, Balance Sheet (Topic 210), which requires additional disclosures relating to the offsetting of financial instruments. Adoption of ASU 2011-11 did not have a material impact on Sharp's obligated group financial statements.

Recent Accounting Pronouncements

In April 2013, the FASB issued ASU 2013-06, Not-for-Profit Entities (Topic 958), which requires a recipient not-for-profit entity to recognize all contributed services received from personnel of an affiliate that directly benefit the recipient not-for-profit entity. The adoption of ASU 2013-06 is required for Sharp on October 1, 2014, and is not expected to have a material impact on Sharp's obligated group financial statements.

In July 2013, the FASB issued ASU 2013-11, Income Taxes (Topic 740), which require unrecognized tax benefits to be offset against a deferred tax asset for a net operating loss carryforward, similar tax loss or tax credit carryforward in certain situations. The adoption of ASU 2013-11 is required for Sharp on October 1, 2015, and is not expected to have a material impact on Sharp's obligated group financial statements.

1. Summary of Significant Accounting Policies (continued)

Recent Accounting Pronouncements (continued)

In April 2014, the FASB issued ASU 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360), which requires that a disposal of a component of an entity or a group of components of an entity be reported in discontinued operations if the disposal represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results when it meets the criteria to be classified as held for sale, or is disposed of by sale or other than by sale. It also requires an entity to present, for each comparative period, the assets and liabilities of a disposal group that includes a discontinued operation separately in the asset and liability sections, respectively, of the statement of financial position. The adoption of ASU 2014-08 is required for Sharp on October 1, 2015; Sharp's management is evaluating the potential impact on Sharp's obligated group financial statements.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), which requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The adoption of ASU 2014-09 is required for Sharp on October 1, 2017; Sharp's management is evaluating the potential impact on Sharp's obligated group financial statements.

In June 2014, the FASB issued ASU 2014-11, Transfers and Servicing (Topic 860), which requires a repurchase to maturity transactions to be accounted for as secured borrowing and certain repurchase agreements to follow secured borrowing accounting. The adoption of ASU 2014-011 is required for Sharp on October 1, 2015; Sharp's management is evaluating the potential impact on Sharp's obligated group financial statements.

2. Fair Value Measurements

FASB ASC 820 clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, FASB ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

- Level 1: Pricing is based on observable inputs such as quoted prices in active markets. Financial assets and liabilities in Level 1 include U.S. Treasury securities and listed equities.

2. Fair Value Measurements (continued)

- Level 2: Pricing inputs are based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Financial assets and liabilities in this category generally include corporate bonds, U.S. government agency securities, commercial paper, fixed income funds, mortgage-backed securities, interest rate swaps, and commingled plan trust funds.

- Level 3: Pricing inputs are generally unobservable and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require management's judgment or estimation of assumptions that market participants would use in pricing the assets or liabilities. The fair values are therefore determined using factors that involve considerable judgment and interpretations, including not but limited to private and public comparables, third party appraisals, discounted cash flow models, and fund manager estimates. The obligated group does not hold any financial assets that would be included in this category.

Assets and liabilities measured at fair value are based on one or more of three valuation techniques noted in FASB ASC 820 as identified below. The valuation techniques are as follows:

(a) Market approach. Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. This technique was utilized for all Level 1 investments.

(b) Cost approach. Amount that would be required to replace the service capacity of an asset (replacement cost). This technique was utilized for all Level 2 investments except for the interest rate swaps.

(c) Income approach. Techniques to convert future amounts to a single present amount based on market expectations (including present value techniques, option-pricing and excess earnings model). This technique was utilized for the interest rate swaps.

The obligated group's investments in partnerships, limited liability companies, and similarly structured entities amounting to approximately $9,534,000 and $11,034,000 as of June 30, 2014 and June 30, 2013, respectively, are accounted for using the equity method of accounting, which is not a fair value measurement.

2. Fair Value Measurements (continued)

The following table provides the composition of certain investment assets as of June 30, 2014. Only assets and liabilities measured at fair value on a recurring basis are shown in the three-tier fair value hierarchy.

	June 30, 2014	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(In Thousands)			
Short-term investments:				
U.S. Treasury obligations	$ 9,161	$ 9,161	$ -	$ -
Corporate bonds	22,687	-	22,687	-
U.S. government agencies	4,472	-	4,472	-
Commercial paper	14,233	-	14,233	-
Interest receivable	202	-	202	-
	$ 50,755	$ 9,161	$ 41,594	$ -
Assets limited as to use:				
Designated for property:				
Cash and short-term investments	$ 9,572	$ 9,572	$ -	$ -
Equities	601,336	601,336	-	-
U.S. Treasury obligations	266,614	266,614	-	-
Corporate bonds	250,873	-	250,873	-
U.S. government agencies	119,117	-	119,117	-
Commercial paper	20,880	-	20,880	-
Mortgaged backed securities and collateralized mortgage obligations	44,098	-	44,098	-
Asset-back securities	25,217	-	25,217	-
Interest receivable	3,785	-	3,785	-
	$ 1,341,492	$ 877,522	$ 463,970	$ -

2. Fair Value Measurements (continued)

	June 30, 2014	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(In Thousands)		
Under bond indentures:				
Cash and short-term investments	**$ 11,715**	**$ 11,715**	**$ -**	**$ -**
U.S. Treasury obligations	**51,807**	**51,807**	**-**	**-**
Corporate bonds	**24,259**	**-**	**24,259**	**-**
U.S. government agencies	**44,915**	**-**	**44,915**	**-**
Commercial paper	**14,984**		**14,984**	
Interest receivable	**313**	**-**	**313**	**-**
	$ 147,993	**$ 63,522**	**$ 84,471**	**$ -**
Long-term debt:				
Interest rate swap liability	**$ 1,967**	**$ -**	**$ 1,967**	**$ -**
	$ 1,967	**$ -**	**$ 1,967**	**$ -**

The following table provides the composition of certain investment assets as of June 30, 2013. Only assets and liabilities measured at fair value on a recurring basis are shown in the three-tier fair value hierarchy.

	June 30, 2013	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(In Thousands)		
Short-term investments:				
Cash and cash equivalents	$ 475	$ 475	$ -	$ -
U.S. Treasury obligations	9,233	9,233	-	-
Corporate bonds	25,585	-	25,585	-
U.S. government agencies	7,173	-	7,173	-
Commercial paper	12,988	-	12,988	-
Interest receivable	317	-	317	-
	$ 55,771	$ 9,708	$ 46,063	$ -

2. Fair Value Measurements (continued)

	June 30, 2013	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets limited as to use:				
Designated for property:				
Cash and short-term investments	$ 5,111	$ 5,111	$ -	$ -
Equities	460,697	460,697	-	-
U.S. Treasury obligations	186,443	186,443	-	-
Corporate bonds	190,349	-	190,349	-
U.S. government agencies	115,323	-	115,323	-
Commercial paper	18,899	-	18,899	-
Mortgaged backed securities and collateralized mortgage obligations	47,797	-	47,797	-
Interest receivable	3,368	-	3,368	-
	$ 1,027,987	$ 652,251	$ 375,736	$ -
Under bond indentures:				
Cash and short-term investments	$ 1,745	$ 1,745	$ -	$ -
U.S. Treasury obligations	4,152	4,152	-	-
Corporate bonds	3,594	-	3,594	-
U.S. government agencies	11,784	-	11,784	-
Interest receivable	88	-	88	-
	$ 21,363	$ 5,897	$ 15,466	$ -
Long-term debt:				
Interest rate swap liability	$ 506	$ -	$ 506	$ -
	$ 506	$ -	$ 506	$ -

3. Investment Income

Investment income for assets limited as to use, short-term investments and cash equivalents are comprised of the following:

	Nine Months Ended June 30	
	2014	**2013**
	(In Thousands)	
Interest income	**$ 19,875**	$ 17,624
Unrealized gains (losses), net	**55,933**	9,746
Realized gains, net	**15,462**	9,687
Investment income	**$ 91,270**	$ 37,057

4. Endowments

Two of Sharp's affiliated entities excluded from the obligated group, SHF and GHF, are foundations which operate for the benefit of Sharp entities. As such the obligated group maintains a beneficial interest in these two foundations. Sharp's endowments consist of 48 separate endowment funds included in assets limited as to use established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Directors of the foundations to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

On September 30, 2008, California Senate Bill No. 1329 was signed into law which enacted the Uniform Prudent Management of Institutional Funds Act ("UPMIFA") for California. California also adopted one of the "optional" provisions of the act, creating a rebuttable presumption of imprudence for spending more than 7% of the value of an endowment fund in one year (based on a three-year rolling average). The Board has interpreted UPMIFA 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, Sharp classifies 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 that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Sharp in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, Sharp considers the following factors in making a

4. Endowments (continued)

determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the fund, (2) the purposes of Sharp and the donor-restricted endowment fund, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments, (6) other resources of Sharp, and (7) the investment policies of Sharp.

The endowment net asset composition as of June 30, 2014 by fund type was as follows:

	Temporarily Restricted	Permanently Restricted	Total
		(In Thousands)	
Board-designated endowment funds	$ 2,472	$ –	$ 2,472
Donor-restricted endowment funds	5,969	6,178	12,147
Total funds	$ 8,441	$ 6,178	$ 14,619

Sharp has adopted investment and spending policies for endowment assets that attempt to provide a stream of funding to programs supported by its endowment while balancing the risk of investment loss with long-term preservation of purchasing power. Endowment assets include those assets of donor-restricted funds that Sharp must hold in perpetuity or for a donor-specified period as well as board-designated funds.

Sharp targets a diversified asset allocation that places greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints. Sharp's spending policy is to annually appropriate for distribution no more than 4% per year of each endowment fund's average fair value (based on a two-year rolling average).

	Temporarily Restricted	Permanently Restricted	Total
		(In Thousands)	
Endowment net assets, October 1, 2012	$ 6,237	$ 5,562	$ 11,799
Investment return:			
Investment income	824	–	824
Net depreciation (realized and unrealized)	283	–	283
Total investment return	1,107	–	1,107
Contributions	8	481	489
Appropriation of endowment asset for expenditure	(110)	–	(110)
Endowment net assets, September 30, 2013	7,242	6,043	13,285

Investment return:			
Investment income	**566**	**–**	**566**
Net depreciation (realized and unrealized)	**627**	**–**	**627**
Total investment return	**1,193**	**–**	**1,193**
Contributions	**102**	**135**	**237**
Appropriation of endowment asset for expenditure	**(96)**	**–**	**(96)**
Endowment net assets, December 31, 2013	**$ 8,441**	**$ 6,178**	**$ 14,619**

5. Subsequent Events

In preparing these obligated group financial statements, management has evaluated and disclosed all material subsequent events up to August 22, 2014 which is the date that the obligated group financial statements were available to be issued.

Other Financial Information

SIGNIFICANT FINANCIAL TRANSACTIONS

On January 7, 2014, Sharp transferred $31.9 million into an escrow account with the intent of defeasing $30.0 million of the 2009B bonds. The funds transferred to escrow will be sufficient to provide for (i) the payment of unpaid accrued interest on the 2009B bonds to August 1, 2014 ("Redemption Date"), when the 2009B bonds are subject to optional redemption and (ii) the redemption of the 2009B bonds on the Redemption Date. The 2009B bond defeasance escrow fund is included in "under bond indentures" on the balance sheet.

In February 2014, Sharp HealthCare issued the Series 2014A fixed rate bonds ("2014A bonds") in the amount of $166.1 million to be used for future capital projects and to refund the 2003C bonds in March 2014. Prior capital expenditures totaling $27.7 million were reimbursed with bond funds in February. Costs of issuance associated with the 2014A bonds totaled $1.8 million as of June 30, 2014, and will be amortized over the life of the bonds.

In December 2013, Sharp entered into an asset purchase agreement to acquire the assets and medical records of Adamson & Dembitsky Medical Corporation. Sharp entered into a professional services agreement with Adamson & Dembitsky Medical Corporation to provide continuous physician and mid-level provider coverage in the Sharp Cardiovascular & Thoracic Center ("SCTC") for a five year period beginning March 1, 2014.

On March 1, 2014, Sharp HealthCare refunded the 2003C bonds in the amount of $24.9 million. As a result of the refunding, a $136,000 unfavorable adjustment was recorded to interest expense to write-off the remaining unamortized cost of issuance and bond discount of the 2003C bonds.

In March 2014, Sharp Grossmont Hospital executed an amendment to the $15.5 million Reverse Repurchase Agreement, effective April 1, 2014, to extend the final repurchase date to April 1, 2017.

The American Recovery and Reinvestment Act of 2009 included provisions for implementing health information technology under the Health Information Technology for Economic and Clinical Health Act ("HITECH"). The provisions were designed to increase the use of electronic health record ("EHR") technology and establish the requirements for a Medicare and Medi-Cal incentive payment program beginning in 2011 for eligible providers and professionals that adopt and meaningfully use certified EHR technology. Eligibility for annual Medicare incentive payments is dependent on providers and professionals demonstrating meaningful use of EHR technology in each period over a four-year period. Medi-Cal incentive payments are available to providers and professionals that adopt, implement or upgrade certified EHR technology. Providers and professionals must demonstrate meaningful use of such technology in subsequent years to qualify for additional Medi-Cal incentive payments. Providers are able to receive payments from both programs while professionals are only allowed to participate in one of the programs and must choose in which program they want to participate. Income from incentive payments is subject to retrospective adjustment as the incentive payments are calculated using Medicare cost report data

SIGNIFICANT FINANCIAL TRANSACTIONS (continued)

that is subject to audit. Additionally, the Company's compliance with the meaningful use criteria is subject to audit by the federal government.

In March 2014 and April 2014, Sharp recognized revenue from Medicare for professional incentives after the eligible physicians demonstrated compliance with the meaningful use criteria. Year to date, professional incentive payments totaling $722,000 are included in total operating revenue in the accompanying statement of operations and changes in net assets. The professional's compliance with the meaningful use criteria is subject to audit by the federal government.

In June 2014, Sharp converted the Series 2010 Bank Qualified DeMinimis Bonds ("2010A Bonds") to change the applicable spread to 0.55% (from 0.75%) and extend the Bank Mode Tender Date to June 10, 2019.

In June 2014, Sharp extended its' Basis Swap with Citibank to a 20-year maturity. Under the extension ("Basis Swap Extension"), Sharp will pay SIFMA and receive 67% of one-month LIBOR plus 73.3 basis points, providing an annual benefit of $146,400 through the current Basis Swap's maturity and approximately $576,000 annually for years 11-20. Sharp will continue to have no collateral posting requirements on the Basis Swap Extension. Transaction costs are built into the basis swap spread.

On June 3, 2014, voters in the Grossmont Healthcare District ("District") approved Proposition H, a ballot initiative authorizing the District to enter into an extended lease agreement with Sharp for the operation of Grossmont Hospital. With the passage of Proposition H the District may renegotiate or extend the original 1991 lease for up to an additional 30 year term. As of June 30, 2014, no lease extension had been agreed to by the District and Sharp.

In 2011, Sharp Community Medical Group ("SCMG"), Sharp Rees-Stealy Medical Group ("SRSMG"), and Sharp formed the Sharp HealthCare ACO, a limited liability company ("Sharp ACO"), and applied to be a Pioneer Accountable Care Organization ("ACO"). Sharp ACO was selected by the Center for Medicare and Medicaid Innovation ("CMMI") as one of an initial 32 Pioneer ACO's. Sharp ACO entered into an agreement to participate in the Pioneer ACO Model ("Pioneer Agreement") effective January 1, 2012. The Pioneer Agreement provides Sharp ACO with the right to terminate at any time and if the termination is made during the first six months of any annual period Sharp ACO will not have financial responsibility for that period. In evaluating participation for the year ended December 31, 2014 ("Performance Year 3"), Sharp ACO determined it was at risk for a significant shared loss, despite meaningful reductions in readmission rates and hospital and skilled nursing utilization. In June 2014, Sharp ACO determined it would not continue in the Pioneer ACO Program for Performance Year 3 and notified CMMI of its decision on June 20, 2014. As such, Sharp has no responsibility for an Increased Cost Payment for Performance Year 3 nor potential for any Shared Savings Payment. Because the Pioneer financial

SIGNIFICANT FINANCIAL TRANSACTIONS (continued)

model is based on national financial trend factors that are not adjusted for specific conditions that an ACO is facing in a particular region (e.g., San Diego), the model was financially detrimental to Sharp ACO despite favorable underlying utilization and quality performance.

Sharp HealthCare
Management's Discussion and Analysis
Obligated Group
Quarter Ended June 30, 2014

PATIENT ACTIVITY - The obligated group average daily census for the quarter ended June 30, 2014 was 1,151 compared to a budget of 1,130. Acute average daily census was favorable to budget by 21 days and skilled nursing facility average daily census was the same as budget. Other patient statistics for the quarter are as follows:

Quarter Ended June 30, 2014	Last Year	Current Quarter Actual	Budget	Var.	%	YTD Var %
Combined Hospitals:						
Adj. discharges	30,917	31,348	30,657	691	2.3%	1.3%
Acute discharges	19,946	19,766	19,754	12	0.1%	0.1%
SNF discharges	161	219	185	34	18.4%	-0.9%
Outpatient visits	189,605	205,359	194,712	10,647	5.5%	0.1%
Sharp Rees-Stealy:						
Capitation rev as % of net patient rev	72.0%	70.1%	70.9%	-0.8%	-1.1%	-0.1%
Physician visits	299,879	313,191	322,033	(8,842)	-2.7%	-2.3%

RESULTS OF OPERATIONS - A summary of the obligated group results of operations for the quarter is as follows (in thousands):

Quarter Ended June 30, 2014	Last Year Actual	Current Quarter Actual	Budget	Var.	%	YTD Var %
Operating Revenue	$ 686,031	$ 668,165	$ 650,143	$ 18,022	2.8%	2.0%
Operating Expenses	594,337	576,826	576,770	(56)	0.0%	0.4%
EBITDA from Operations	**91,694**	**91,339**	**73,373**	**17,966**	**24.5%**	**20.5%**
Deprec, Amort, Taxes & Interest	29,344	30,422	33,670	3,248	9.6%	6.2%
Income from Operations	**62,350**	**60,917**	**39,703**	**21,214**	**53.4%**	**40.7%**
Investment Income (Loss)	(9,908)	37,919	7,391	30,528	413.0%	243.6%
Mark to Market Swaps	717	(1,557)	-	(1,557)	-100.0%	-100.0%
Other Income (Loss)	(913)	(959)	(1,005)	46	4.6%	2.4%
Non-Operating Income (Loss)	**(10,104)**	**35,403**	**6,386**	**29,017**	**454.4%**	**267.1%**
Excess Revenue over Expense	**$ 52,246**	**$ 96,320**	**$ 46,089**	**$50,231**	**109.0%**	**76.2%**

RESULTS OF OPERATIONS (continued)

For the quarter, total operating revenue ran favorable to budget 2.8%, primarily due to net patient service revenue. Net patient service revenue was favorable to budget by 5.5% and premium revenue was favorable to budget by 3.9%. Operating expenses for the quarter were unfavorable to budget by $56,000 primarily in supplies, medical fees, and purchased services, partially offset by provider tax.

The EBITDA margin for the quarter was 19.0% compared to budget of 12.3%. The EBITDA from operations margin for the quarter was 13.7% compared to budget of 11.3%.

KEY FINANCIAL RATIOS - A summary of the obligated group key financial ratios is as follows:

Quarter Ended June 30, 2014	FY 2013 Actual*	Qtr End 6/30/14	YTD Actual	YTD Budget
Key Ratios				
EBITDA From Operations Margin	13.0%	13.7%	13.5%	11.4%
EBITDA Margin	15.9%	19.0%	17.9%	12.6%
Current Ratio	5.4	6.6	6.6	-
Account Receivable (Days)	43.0	50.7	50.7	-
Debt to Capitalization	25.4%	26.2%	26.2%	-
Days Cash on Hand**	204.6		240.9 ***	210.4 ***

* FY 2013 amounts represent final year-end ratios.

** Days Cash on Hand is calculated based on total consolidated system information.

*** YTD Days Cash on Hand amounts are calculated based on year-end forecast and budget.

FY 2013 and FY 2014 actuals include the effects of the Medi-Cal Hospital Fee Program.

Sharp HealthCare
Management's Discussion and Analysis
Obligated Group
Quarter Ended June 30, 2014

YEAR TO DATE PATIENT STATISTICS

Year to Date June 30, 2014	Last Year	Actual	Budget	YTD Budget Var.	%
Combined Hospitals:					
Admissions	60,104	60,684	60,524	160	0.3%
Discharges	60,274	60,644	60,571	73	0.1%
Outpatient Visits	557,804	576,090	575,314	776	0.1%
Outpatient Surgeries	18,116	18,109	18,505	(396)	-2.1%
Total Surgeries	31,313	30,748	32,627	(1,879)	-5.8%
Emergency Room Visits	172,459	181,777	174,774	7,003	4.0%
Newborn Admissions	10,779	11,065	10,442	623	6.0%

FINANCIAL POSITION - During the quarter ended June 30, 2014, operations provided cash of $48.8 million. Cash used in investing activities totaled $29.8 million and included $26.0 million used to acquire property, plant and equipment. Cash used in financing activities totaled $8.6 million for various debt related activities.

Sharp HealthCare
Analysis of Obligated Group Financial Statements
Quarter Ended June 30, 2014

COMBINED STATEMENT OF OPERATIONS:

1. Net Patient Service Revenue for the quarter ended June 2014 totaled $435.4 million compared to $397.8 million at quarter end June 2013. Compared to budget a favorable variance of $22.7 million was realized primarily due to current and prior year settlement activity and greater than anticipated exchange volumes.

   On a year to date basis, net patient service revenue was $1.3 billion, compared to fiscal 2013 of $1.2 billion. Compared to budget a favorable variance of $37.5 million, or 3.0%, was realized.

   For the quarter ended June 2014, deductions from revenue as a percentage of gross patient service revenue equaled 80.7% compared to a budget of 81.0%.

2. Provider Tax Revenue was not recorded in the quarter ended June 2014 as the 30-month program ended December 31, 2013, while there was provider tax revenue of $21.3 million in the prior year. In June 2012, the Centers for Medicare and Medicaid Services ("CMS") preliminarily approved a 30-month hospital fee program that covers July 1, 2011, through December 31, 2013 ("the 30-month program"). Final approval was granted on the fee-for-service portion in June 2012 while the first 24 months of the managed care portion was approved in May 2013. The final six months (covering July through December 2013) of the managed care portion has not yet been approved. Compared to budget, an unfavorable variance of $12.6 million was realized due to the June budget, which reflected the anticipated approval of the final six months of the managed care portion.

   On a year to date basis, provider tax revenue totaled $24.0 million compared to fiscal 2013 of $114.3 million. The year to date activity represents the portion of the fee for service component of the 30-month program attributable to the current fiscal year to date.

3. Premium Revenue for the quarter ended June 2014 totaled $207.1 million compared to $191.9 million at quarter end June 2013. Compared to budget, a favorable variance of $7.8 million, or 3.9%, was realized primarily due to favorable membership.

   On a year to date basis, premium revenue was $604.9 million, compared to fiscal 2013 of $574.1 million. Compared to budget a favorable variance of $13.5 million was realized.

4. Other Operating Revenue includes unrestricted donations, Sharp Rees-Stealy pharmacy gross profits, management services income and joint venture income. For the quarter ended June 2014, other operating revenue totaled $25.7 million compared to $24.6 million at quarter end June 2013. Compared to budget, a favorable variance of $140,000 was realized primarily due to the contract pharmacy program.

COMBINED STATEMENT OF OPERATIONS (continued):

On a year to date basis, other operating revenue was $76.9 million, compared to fiscal 2013 of $70.4 million. Compared to budget an unfavorable variance of $264,000, or 0.3%, was realized.

5. Operating Expenses - For the quarter ended June 2014, operating expenses (excluding depreciation, amortization, taxes and interest) totaled $576.8 million compared to $594.3 million at quarter end June 2013. Compared to budget an unfavorable variance of $56,000 was realized. Significant quarterly fluctuations were the result of the following as compared to budget:

   a. An increase in supplies of $7.0 million, or 8.9%, primarily due to increased surgery volumes, acuity and pharmaceutical expenses.

   b. An increase in medical fees of $1.1 million, or 1.6%, primarily due to SCTC activity, which was not budgeted.

   c. An increase in purchased services of $2.6 million, or 3.8%, primarily due to a true-up of cost per test lab services with Accumen. Sharp has a joint venture equity relationship and management services agreement with Accretive Labs, LLC ("Accumen") for the management of hospital laboratory operations. Under this agreement, Sharp maintains ownership and ultimate clinical authority of laboratory operations. Sharp funds an estimate of the operating expenses of the lab to Accumen in advance on a quarterly basis.

   d. A decrease in provider tax of $8.7 million, representing the budget for the final six months of the managed care portion of the 30-month program. The final six months (covering July through December 2013) of the managed care portion has not yet been approved, but is reflected in the June budget as approval was anticipated.

   On a year to date basis, operating expenses were $1.7 billion, the same as fiscal 2013. Compared to budget, a favorable variance of $7.6 million, or 0.4%, was realized.

6. Earnings before Interest, Taxes, Depreciation and Amortization (EBITDA) from Operations for the quarter ended June 2014 was $91.3 million compared to $91.7 million at quarter end June 2013. Compared to budget a favorable variance of $18.0 million, or 24.5%, was realized.

   On a year to date basis, EBITDA from operations was $268.4 million compared to $263.9 million in the prior year. Compared to budget a favorable variance of $45.7 million, or 20.5%, was realized.

7. Income from Operations for the quarter ended June 2014 resulted in income of $60.9 million compared to $62.4 million at quarter end June 2013. Compared to budget a favorable variance of $21.2 million, or 53.4%, was realized.

COMBINED STATEMENT OF OPERATIONS (continued):

On a year to date basis, operations resulted in income of $178.4 million compared to $174.6 million in the prior year. Compared to budget a favorable variance of $51.6 million, or 40.7%, was realized.

8. Non-Operating Income includes fundraising expenses, gains/losses on disposal of fixed assets, investment income (including realized and unrealized gains and losses), mark to market adjustments on swap investments, and unrealized gains/losses on investments. For the quarter ended June 2014, non-operating income was $35.4 million compared to a loss of $10.1 million at quarter end June 2013. Compared to budget a favorable variance of $29.0 million was realized due primarily to favorable investment income. Investment income was comprised of $11.4 million of realized investment income and $26.5 million of unrealized gains.

   On a year to date basis, non-operating income was $86.5 million compared to $37.1 million in the prior year. Compared to budget a favorable variance of $62.9 million was realized. Year to date investment income was comprised of $35.4 million of realized investment income and $55.9 million of unrealized gains.

9. Excess Revenues over Expenses – Excess revenues over expenses for the quarter ended June 2014 resulted in income of $96.3 million compared to $52.2 million at quarter end June 2013. Compared to budget a favorable variance of $50.2 million, or 109.0%, was realized.

   On a year to date basis, excess revenues over expenses totaled $264.9 million compared to $211.7 million in the prior year. Compared to budget a favorable variance of $114.5 million, or 76.2%, was realized.

10. EBITDA – EBITDA, including the non-operating items, totaled a gain of $126.7 million for the quarter ended June 2014, compared to $81.6 million at quarter end June 2013. Compared to budget a favorable variance of $47.0 million, or 58.9%, was realized.

    On a year to date basis, EBITDA totaled $354.9 million compared to $301.0 million in the prior year. Compared to budget a favorable variance of $108.6 million, or 44.1%, was realized.

BALANCE SHEET:

Assets:

1. Cash and cash equivalents increased $66.5 million year to date due primarily to operations and the timing of payments as they relate to the current and prior quarters, partially offset by the transfer of $32.9 million to the 2009B bond defeasance fund.

BALANCE SHEET (continued):

Assets (continued):

2. Short-term investments decreased $1.8 million year to date due primarily to the reclassification of short-term investments to long-term investments due to scheduled maturities within the next twelve months.

3. Accounts receivable, net decreased $4.6 million year to date due primarily to the 30-month program activity, partially offset by an increase in net patient receivables. Days in accounts receivable were 50.7 as of June 30, 2014 and 48.8 June 30, 2013 without the 30-month program impact.

4. Estimated settlements receivable from government programs, net increased $12.6 million year to date due to prior year Medicare settlement activity and the timing of Medicare PIP payments.

5. Prepaid expenses increased $7.9 million year to date due primarily to the 30-month program activity, prepaid service contracts, and prepaid rent.

6. Assets limited as to use increased $333.7 million year to date due primarily to the issuance of the 2014A Bonds, unrealized gains and investment income year to date, the purchase of long-term investments, and a $29.5 million transfer from cash for the 2009B bond defeasance fund.

7. Net property, plant and equipment increased $36.3 million year to date due primarily to standard asset purchases offset by depreciation.

8. Other assets increased $2.3 million year to date due primarily to CQI activity.

9. Beneficial interest in foundations increased $9.5 million year to date due to favorable foundation performance.

Liabilities:

1. Accounts payable and accrued liabilities increased $9.8 million year to date due primarily to the timing of check runs and accruals as they relate to current quarter and prior year ends and the 30-month program activity.

2. Accrued compensation and benefits decreased $27.6 million year to date due primarily to the timing of pay periods as they relate to current quarter and prior year ends and the payment of the fiscal 2013 management incentives, partially offset by the accrual of three quarters of the fiscal 2014 management incentives.

3. Accrued interest increased $6.6 million year to date due primarily to normal interest accruals.

BALANCE SHEET (continued):

Liabilities (continued):

4. Long-term liabilities increased $15.4 million year to date due primarily to standard pension, workers' compensation and professional liability accruals, partially offset by reduced professional liability reserves resulting from decreased claims activity year to date and an actuarial adjustment to the workers' compensation liability.

5. Long-term debt (including current portion of long-term debt) increased $138.1 million year to date due primarily to issuance of the 2014A Bonds and additions to the Co-Generation notes payable, partially offset by the final payment on the SCVMC MOB, LLC mortgage. Grossmont Hospital Corporation ("GHC") has entered into a Co-Generation Purchase Agreement with the Grossmont Healthcare District ("District") for construction of a new Central Energy Plant. GHC will make lease payments in the form of the District's loan payments directly to an escrow account. The District bears risk of loss related to the Co-Generation Unit. Once the asset is placed into service, GHC will have exclusive use of the equipment, and with this record a nine-year lease liability and a corresponding capital lease asset. Until such time as the asset is placed into service, payments will be recorded as prepaid rent. At the termination of the lease the District will transfer the Co-Generation unit to GHC. In total, $11.5 million has been added to the Co-Generation notes payable.

STATEMENT OF CASH FLOWS:

Cash Flows for the Quarter - During the quarter ended June 30, 2014, operations provided cash of $48.8 million. Cash used in investing activities totaled $29.8 million and included $26.0 million used to acquire property, plant and equipment. Cash used in financing activities totaled $8.6 million for various debt related activities.

Cash Flows for the Year – On a year to date basis, operations provided cash of $10.9 million. Cash used in investing activities totaled $73.6 million and included $61.8 million used to acquire property, plant and equipment. Cash provided by financing activities totaled $129.2 million and included $164.3 million of proceeds from the issuance of the 2014A Bonds, partially offset by $24.9 million used for the refunding of the 2003C bonds and $10.2 million of other debt related activities.