PRESBYTERIAN

Presbyterian Healthcare Services
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(505) 923-5700
www.phs.org

April 27, 2016

Digital Assurance Certification
390 North Orange Avenue
Suite 1750
Orlando, Florida 32801

ATT'N: Shana Bridge

RE: 1. Continuing Disclosure Agreement(s) dated as of November 25, 2008 between Presbyterian Healthcare Services and Wells Fargo Bank, National Association (the "Continuing Disclosure Agreement")

2. Continuing Disclosure Agreement dated as of September 24, 2009 between Presbyterian Healthcare Services and Wells Fargo Bank, National Association (the "Continuing Disclosure Agreement")

3. Continuing Disclosure Agreement dated as of August 30, 2012 between Presbyterian Healthcare Services and Wells Fargo Bank, National Association (the "Continuing Disclosure Agreement")

4. Continuing Disclosure Agreement dated as of May 19, 2015 between Presbyterian Healthcare Services and Wells Fargo Bank, National Association (the "Continuing Disclosure Agreement")

Dear Ms. Bridge,

Pursuant to Section 3(c) of all of the above referenced Continuing Disclosure Agreements and in my capacity as an Obligate Group Representative, I hereby certify that the enclosed Annual Financial Information and Annual Operating Information as of December 31, 2015 for the Obligated Group, as defined in the above referenced Continuing Disclosure Agreements complies with the applicable requirements of Section 3(c).

As per Section 3.10 of the above referenced Master Trust Indenture attached please find the Officer's Certificate stating compliance with the covenants contained in Article III of the Master Trust Indenture and disclosure of the Debt Service Coverage Ratio.

Please distribute copies of the audited financial statements (Annual Financial Information), Annual Operating Information, Officers Certificate pursuant to Section 3.10 of the Master Trust Indenture and discussion of operating results to the Master Trustee, each NRMSIR, SID (as applicable) and to the Electronic Municipal Market Access system for the Municipal Securities Rulemaking Board, each as defined in the Continuing Disclosure Agreements.

Should you have any questions, please do not hesitate to contact me at dmaxwell@phs.org or 505.923.5353.

Regards,

Dale Maxwell
Executive Vice President & Chief Administrative Officer, Treasurer

Enclosures

OFFICER'S CERTIFICATE
PURSUANT TO
Section 3.10 of the Master Trust Indenture (Amended and Restated)
Dated as of July 28, 2005
among
Presbyterian Healthcare Services, Presbyterian Healthcare Foundation, Bernalillo County Health Care Corporation and Other Members of the Obligated Group, if any
and
Wells Fargo Bank, National Association, as Trustee
(the "Master Indenture")

I, the undersigned, hereby certify that I am the duly chosen, qualified and acting Executive Vice President and Chief Administrative Officer of Presbyterian Healthcare Services and that:

1. To the best knowledge of the undersigned, all Members of the Obligated Group have complied with the covenants contained in Article III of the Master Trust Indenture (Amended and Restated) dated as of July 28, 2005 among Presbyterian Healthcare Services, Presbyterian Healthcare Foundation, and Bernalillo County Healthcare Corporation and Wells Fargo Bank New Mexico, N.A., as Trustee.

2. The Debt Service Coverage Ratio of the Obligated Group for the period ending December 31, 2015 was 5.79.

3. The terms used in this Officer's Certificate shall have the meaning specified in the Master Indenture.

PRESBYTERIAN HEALTHCARE SERVICES

Date: April 27, 2016

By: Dale Maxwell
Dale Maxwell
Executive Vice President and Chief Administrative Officer
Treasurer

Combined Financial Statements and Supplementary Information

Presbyterian Healthcare Services and Affiliates
Years Ended December 31, 2015 and 2014
With Report of Independent Auditors

Ernst & Young LLP

Building a better working world

Presbyterian Healthcare Services and Affiliates

Combined Financial Statements
and Supplementary Information

Years Ended December 31, 2015 and 2014

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1511-1739628

Building a better working world

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Report of Independent Auditors

The Board of Directors
Presbyterian Healthcare Services

We have audited the accompanying combined financial statements of Presbyterian Healthcare Services and Affiliates, which comprise the combined balance sheets as of December 31, 2015 and 2014, and the related combined statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the combined financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Building a better
working world

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the combined financial position of Presbyterian Healthcare Services and Affiliates at December 31, 2015 and 2014, and the combined results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

April 22, 2016

Presbyterian Healthcare Services and Affiliates

Combined Balance Sheets

	December 31 2015	December 31 2014
	(In Thousands)	
Assets		
Current assets:		
Cash and cash equivalents	**$ 285,896**	$ 245,327
Accounts receivable, less allowance for doubtful accounts of $33,702 and $50,460 in 2015 and 2014, respectively	**113,367**	110,736
Other receivables	**119,958**	91,528
Inventories, prepaid expenses, and other current assets	**49,468**	36,905
Total current assets	**568,689**	484,496
Assets limited as to use or restricted:		
Designated for long-term purposes	**1,688,322**	1,564,318
Designated for self-insurance funds	**119,338**	124,328
Restricted by donors	**34,807**	34,477
Held by trustee	**51,838**	7,244
Restricted for statutory requirements	**109,716**	103,685
	2,004,021	1,834,052
Property and equipment, net	**857,048**	815,772
Goodwill	**55,626**	57,589
Other assets	**85,273**	79,391
Total assets	**$ 3,570,657**	$ 3,271,300
Liabilities and net assets		
Current liabilities:		
Accounts payable	**$ 57,782**	$ 55,349
Due under Medicaid contract	**168,296**	45,591
Accrued liabilities	**161,570**	160,069
Medical claims payable	**139,397**	127,919
Estimated third-party payor settlements	**1,826**	2,966
Current portion of long-term debt and capital leases	**14,797**	13,435
Total current liabilities	**543,668**	405,329
Long-term debt and capital leases, net of current portion	**709,972**	596,321
Employee benefit plans	**198,511**	201,850
Self-insurance plans	**145,092**	127,439
Other liabilities	**107,032**	105,151
Total liabilities	**1,704,275**	1,436,090
Net assets:		
Unrestricted	**1,829,534**	1,799,701
Temporarily restricted	**25,997**	27,143
Permanently restricted	**10,851**	8,366
Total net assets	**1,866,382**	1,835,210
Total liabilities and net assets	**$ 3,570,657**	$ 3,271,300

See accompanying notes.

Presbyterian Healthcare Services and Affiliates

Combined Statements of Operations

	Year Ended December 31	
	2015	2014
	(In Thousands)	
Revenues:		
Net premiums	**$ 1,819,856**	$ 1,671,890
Patient service revenue	**1,059,443**	1,001,743
Less provision for doubtful accounts	**(56,481)**	(91,964)
Net patient service revenue	**1,002,962**	909,779
Other operating revenues	**72,437**	70,999
Total operating revenues	**2,895,255**	2,652,668
Expenses:		
Medical claims	**1,044,092**	890,251
Salaries, wages, and employee benefits	**873,637**	810,631
Purchased services and other	**453,876**	412,548
Supplies	**240,788**	211,713
Professional fees	**38,049**	38,112
Depreciation and amortization	**94,612**	92,548
Interest	**24,886**	25,742
Total expenses	**2,769,940**	2,481,545
Operating income	**125,315**	171,123
Other (loss) income:		
Investment income	**71,593**	121,129
Changes in net unrealized gains on investments	**(106,125)**	(39,331)
Loss on bond defeasance	**(24,061)**	–
Change in fair value of interest rate swaps	**(149)**	(7,933)
Total other (loss) income	**(58,742)**	73,865
Excess of revenues over expenses before income taxes	**66,573**	244,988
Provision for income taxes	**35,086**	52,572
Excess of revenues over expenses	**$ 31,487**	$ 192,416

See accompanying notes.

Presbyterian Healthcare Services and Affiliates

Combined Statements of Changes in Net Assets

	Year Ended December 31	
	2015	**2014**
	(In Thousands)	
Unrestricted net assets		
Excess of revenues over expenses	**$ 31,487**	$ 192,416
Change in pension obligation	**(2,015)**	(112,520)
Other changes in net assets	**361**	1,806
Increase in unrestricted net assets	**29,833**	81,702
Temporarily restricted net assets		
Donor-restricted contributions and earnings	**2,951**	4,041
Net assets released from restrictions	**(2,466)**	(3,308)
Net unrealized gains on investments	**(1,687)**	(748)
Other changes in net assets	**56**	2,890
(Decrease) increase in temporarily restricted net assets	**(1,146)**	2,875
Permanently restricted net assets		
Donor-restricted contributions	**(10)**	121
Other changes in net assets	**2,495**	(2,890)
Increase (decrease) in permanently restricted net assets	**2,485**	(2,769)
Increase in net assets	**31,172**	81,808
Net assets, beginning of year	**1,835,210**	1,753,402
Net assets, end of year	**$ 1,866,382**	$ 1,835,210

See accompanying notes.

Presbyterian Healthcare Services and Affiliates

Combined Statements of Cash Flows

	Year Ended December 31	
	2015	**2014**
	(In Thousands)	
Operating activities		
Increase in net assets	**$ 31,172**	$ 81,808
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Change in unrealized gains on investments	**106,125**	39,331
Change in fair value of interest rate swaps	**149**	7,933
Loss on bond defeasance	**24,061**	–
Depreciation and amortization	**94,612**	92,548
Provision for doubtful accounts	**56,481**	91,964
Changes in operating assets and liabilities:		
Accounts receivable	**(59,112)**	(70,211)
Other receivables	**(28,430)**	(23,713)
Inventories, prepaid expenses, and other current assets	**(12,563)**	(2,051)
Trading securities, net	**(225,470)**	(220,800)
Other assets	**(5,882)**	(12,255)
Accounts payable	**2,433**	2,889
Due under Medicaid contract	**122,705**	45,591
Accrued liabilities	**1,501**	50,939
Medical claims payable	**11,478**	31,287
Estimated third-party payor settlements	**(1,140)**	(6,851)
Other liabilities	**16,046**	103,583
Net cash provided by operating activities	**134,166**	211,992
Investing activities		
Sales of assets held by trustee and statutory deposits	**90,453**	32,264
Purchases of assets held by trustee and statutory deposits	**(141,078)**	(11,797)
Purchases of property and equipment	**(133,924)**	(116,843)
Net cash used in investing activities	**(184,549)**	(96,376)
Financing activities		
Proceeds from issuance of long-term debt	**262,140**	12,638
Payments on long-term debt and capital leases	**(171,188)**	(12,897)
Net cash provided by (used in) financing activities	**90,952**	(259)
Net increase (decrease) in cash and cash equivalents	**40,569**	115,357
Cash and cash equivalents, beginning of year	**245,327**	129,970
Cash and cash equivalents, end of year	**$ 285,896**	$ 245,327
Supplemental disclosures		
Cash paid for interest	**$ 26,662**	$ 27,010
Cash paid for income taxes	**$ 51,130**	$ 50,005

See accompanying notes.

1. Organization

Presbyterian Healthcare Services (PHS) is a New Mexico nonprofit corporation exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. PHS is a diversified health care organization that owns, leases, controls, operates, or manages a variety of health care-related organizations, including six hospitals in New Mexico, a for-profit managed care organization (MCO), and several other affiliated organizations. PHS provides a broad range of health care services, including inpatient, outpatient, subacute, home health care, and physician services.

PHS consists of the following divisions and affiliates:

Presbyterian Healthcare Services Divisions

Presbyterian Hospital,* including the following, which are designated as remote locations of Presbyterian Hospital:
- Presbyterian Kaseman Hospital*
- Presbyterian Northside*
- Presbyterian Rust Medical Center*

Plains Regional Medical Center*
Presbyterian Española Hospital*
Socorro General Hospital*
Lincoln County Medical Center (leased facility)
Dr. Dan C. Trigg Memorial Hospital (leased facility)

Presbyterian Healthcare Services Affiliates

Southwest Health Foundation
Presbyterian Network, Inc. (PNI):
- Presbyterian Insurance Company, Inc.
- Presbyterian Health Plan, Inc.
- Albuquerque Imaging Associates
- Southwest Magnetic Imaging Associates

Presbyterian Properties, Inc.
Presbyterian Healthcare Foundation*
Bernalillo County Health Care Corporation d.b.a. Albuquerque Ambulance Service*

* Denotes Obligated Group members.

PHS accesses the capital markets through an Obligated Group. Obligated Group members include PHS and certain divisions and affiliates as noted above, which are jointly and severally liable for the long-term debt outstanding under a Master Trust Indenture. None of the other PHS affiliates have any obligation related to requirements of the Master Trust Indenture. The Obligated Group's net assets represent approximately 75% and 76% of PHS and affiliates' combined net assets at December 31, 2015 and 2014, respectively.

1. Organization (continued)

Presbyterian Network, Inc. (PNI) is a wholly owned subsidiary of Southwest Health Foundation. PNI is the parent organization of two wholly owned subsidiaries: Presbyterian Health Plan, Inc. (PHP) and Presbyterian Insurance Company, Inc. (PIC). PHP is a state-licensed Health Maintenance Organization (HMO) in New Mexico and is also a federally qualified HMO under Title XIII of the Public Health Service Act. PHP provides comprehensive health care services in New Mexico to individuals primarily through health maintenance contracts with employer groups and individuals, both on and off the New Mexico Health Insurance Exchange. PHP also offers an HMO product to Medicare-eligible individuals (Medicare Advantage). The Medicare Advantage product provides managed care services that include all Medicare benefits and, in some cases, additional managed care services. PIC offers preferred provider and indemnity products to individuals through contracts with employer groups.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying combined financial statements include the accounts of PHS and its affiliates as described in Note 1 (collectively, Presbyterian Healthcare Services). All significant intercompany balances and transactions have been eliminated in combination.

New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date,* which further clarifies the accounting for revenue and related revenue transactions, including the timing and amount of revenue to be recorded, as well as the determination as to when revenue adjustments should be classified as reductions to net patient service revenue or provision for doubtful accounts. The standard was recently delayed and will be effective beginning in 2018. Management is currently evaluating the effect of adopting the new standard on its financial statements.

2. Summary of Significant Accounting Policies (continued)

In May 2015, the FASB issued Accounting Standards Update (ASU) No. 2015-07, *Fair Value Measurement (Topic 820)*: *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*. Topic 820, *Fair Value Measurement*, permits a reporting entity, as a practical expedient, to measure the fair value of certain investments using the net asset value per share of the investment. ASU 2015-07 removes the requirement to categorize investments within the fair value hierarchy for which fair values are measured using the net asset value per share practical expedient. It also limits disclosures to investments for which the entity has elected to measure the fair value using the practical expedient. The provisions of ASU 2015-07 are effective for PHS January 1, 2016, which will primarily impact the pension asset disclosures.

In April 2015, the FASB issued ASU No. 2015-03, *Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*, ASU 2015-03 requires that debt issuance costs be presented in the balance sheet as a direct deduction from the carrying amount of debt liability, consistent with debt discounts or premiums. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in ASU 2015-03. The provisions of ASU 2015-03 are effective for PHS January 1, 2016. The adoption of ASU 2015-03 will result in a reclassification of approximately $6,436 from other assets to long-term debt.

Cash and Cash Equivalents

Cash and cash equivalents include bank deposits and highly liquid investments with original maturities at the time of purchase of three months or less. The carrying value of cash and cash equivalents approximates fair value.

Net Patient Accounts Receivable

Net patient accounts receivable have been adjusted to the estimated amounts expected to be collected. Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, PHS analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for doubtful accounts.

2. Summary of Significant Accounting Policies (continued)

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, PHS analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for doubtful accounts, if necessary (for example, for expected uncollectible deductibles and co-payments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely). PHS has a policy of providing discounts to self-pay patients without insurance. For receivables associated with self-pay patients (which include both patients without insurance and patients with deductible and co-payment balances due for which third-party coverage exists for part of the bill), PHS records a significant 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 applicable) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

PHS's allowance for doubtful accounts as a percentage of self-pay patient receivables was 77% and 80% at December 31, 2015 and 2014, respectively. PHS's provision for doubtful accounts decreased to $56,481 for fiscal year 2015 from $91,964 for fiscal year 2014. The majority of this decrease is the result of a greater number of patients qualifying for Medicaid, which has decreased self-pay revenue and receivables in 2015. PHS's uninsured discount policies during fiscal years 2015 and 2014 provided for a discount of 30% from standard rates for most services. These uninsured discounts are recorded with contractual adjustments as a deduction of patient service revenue.

PHS does not maintain a material allowance for doubtful accounts for accounts receivable from third-party payors, nor have there been significant write-offs from third-party payors.

Assets Limited as to Use or Restricted

Assets limited as to use or restricted include assets set aside by PHS for future long-term purposes, including capital improvements and self-insurance over which PHS retains control and may at its discretion subsequently use for other purposes, and investments held by PNI that are used to meet specified capital requirements for regulatory purposes. In addition, assets limited as to use or

2. Summary of Significant Accounting Policies (continued)

restricted include assets held by trustees under bond indenture agreements, contributions by donors with stipulated restrictions, and amounts on deposit to satisfy statutory requirements of the New Mexico Office of Superintendent of Insurance.

As a condition of its Medicaid Centennial Care contract with the State of New Mexico Human Services Department (HSD), PHP is required to maintain an account with 90% of the average of the past three months, capitation payments made to PHP from HSD. As of December 31, 2015 and 2014, respectively, $92,084 and $85,910 was held in bonds in a restricted managed asset account to satisfy this requirement. HSD also requires a reserve of 1.5% of monthly premium payments to be held in a segregated account related to performance guarantees under PHP’s Centennial Care contract. At December 31, 2015 and 2014, $16,768 and $17,191, respectively, was held in a depository cash account to satisfy these requirements.

These assets consist primarily of cash, cash equivalents, government securities, other fixed-income securities, equity securities, and alternative investments. The carrying amounts of investments in marketable debt and equity securities are reported on the combined balance sheets at fair value. Alternative investments are reported at net asset value using the equity method of accounting, except for alternative investments held by Presbyterian Healthcare Foundation, which are reported at fair value.

Income or loss related to the investment portfolio (including realized and unrealized gains and losses on investments, interest, and dividends) is included in the excess of revenues over expenses unless the income or loss is restricted by donor or law.

Income or loss restricted by donor or by law is classified as a change in temporarily or permanently restricted net assets consistent with the applicable restrictions.

Fair Value Measurements

Accounting Standards Codification (ASC) 820, *Fair Value Measurement*, requires the categorization of financial assets and liabilities into a three-level hierarchy based on pricing inputs to the valuation technique. The fair value hierarchy gives the highest priority to the quoted prices in active markets for identical assets and liabilities and the lowest priority to unobservable inputs. The various levels of the fair value hierarchy are described as follows:

Level 1 – Pricing is based on observable inputs, such as quoted prices in active markets.

2. Summary of Significant Accounting Policies (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.

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 but not limited to private and public comparables, third-party appraisals, discounted cash flow models, and fund manager estimates.

Assets and liabilities measured at fair value are based on one or more of three valuation techniques noted in ASC 820. Where more than one technique is noted, individual assets or liabilities were valued using one or more of the noted techniques. 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

(b) *Cost Approach* – Amount that would be required to replace the service capacity of an asset (replacement cost)

(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 models)

When observable market data is available, it is required to be used in determining the fair value measurement. When inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level of input that is significant to the fair value measurement.

2. Summary of Significant Accounting Policies (continued)

The majority of PHS's marketable debt and equity securities are measured based on observable market prices. PHS's swap instruments and systematic hedge overlay strategy are measured using models based upon observable pricing inputs. Note 7 further describes the methods applied to determine fair value of PHS's financial assets and liabilities.

The carrying values of financial instruments classified as current assets and current liabilities approximate fair value due to their liquidity and short-term natures.

Inventories

Inventories, consisting of drugs and supplies, are stated at the lower of cost (first-in, first-out method) or market.

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 and is computed using the straight-line method. For property and equipment under capital lease, amortization is determined over the shorter period of the lease term or the estimated useful life of the property and equipment. Such amortization is included in depreciation and amortization expense. The following useful lives are being used by PHS:

Land improvements	2–25 years
Buildings and improvements	5–40 years
Equipment and capitalized software	3–20 years

Interest cost incurred on borrowed funds, net of interest earned on assets held by trustee during the period of construction of qualified capital projects, is capitalized as a component of the cost of acquiring those assets.

Goodwill

PHS follows the provisions of ASC 350, *Intangibles – Goodwill and Other*. Goodwill is not amortized, but rather is tested annually for impairment. Management determined there was a goodwill impairment of $1,963 in 2015 which has been recorded in depreciation and amortization expenses.

2. Summary of Significant Accounting Policies (continued)

Impairment of Long-Lived Assets

PHS evaluates whether events and circumstances have occurred that indicate the remaining estimated useful lives of long-lived assets, other than goodwill, may not be recoverable. The assessment of possible impairment is based on the ability to recover the carrying amount of the asset based on undiscounted cash flows. Impairments are calculated as the total by which the carrying amount of the asset exceeds its estimated fair value. For the year ended December 31, 2015, management determined that there was no impairment of its long-lived assets.

Investments in Unconsolidated Entities

Investments in unconsolidated entities are accounted for under the cost or equity method of accounting, as appropriate. PHS utilizes the equity method of accounting for its investment in entities over which it exercises significant influence. PHS's equity income or loss on these investments is recorded as other operating revenue.

Temporarily and Permanently Restricted Net Assets

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

Unconditional pledges to give cash and other assets are reported at fair value at the date the pledge is received. The gifts are reported as temporarily restricted net assets 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 recognized as a component of other operating revenue. Donor-restricted contributions whose restrictions are met within the same year as received are reflected as unrestricted contributions in other operating revenue.

Premium Revenues, Medical Claims Payable, and Health Care Expenses

Premium revenues are recognized in the month in which members are entitled to health care services. Premiums collected in advance are recorded as unearned premiums and are included in accrued liabilities on the accompanying combined balance sheets. During 2015 and 2014,

2. Summary of Significant Accounting Policies (continued)

premium revenue from the Medicare Advantage product line represented approximately 21% and 21% respectively, of total premium revenue. In addition, during 2015 and 2014, premium revenue from the Medicaid product line represented approximately 59% and 56%, respectively, of total premium revenue. Coordination of benefits and subrogation are recognized in the period such amounts are determined to be recoverable from other insurers.

In 2014, PHP contracted with the state of New Mexico to serve the Medicaid population under the New Mexico Centennial Care program. All Medicaid services, including physical health, behavioral health, and long-term care, are provided as part of this program. PHP was one of four MCOs awarded five-year contracts by the state to administer the New Mexico Centennial Care program.

Under this contract, PHP receives a fixed premium from the state to provide comprehensive health care services for enrollees, including those enrollees receiving services from PHS. PHS facilities and physicians will be paid capitated or discounted fee-for-service rates from each of the MCOs. The medical claims costs of PHP on the combined statements of operations are net of intercompany eliminations for services rendered by PHS facilities totaling approximately $672,092 and $639,503 for the years ended December 31, 2015 and 2014, respectively.

Under the Medicaid Centennial Care contract, PHP is permitted to retain 100% of the underwriting gain generated up to 3% annually. Underwriting gains above 3% are shared 50/50 between PHP and HSD. Additionally, for a Medicaid expansion product and Hepatitis C drugs, PHP is subject to risk corridor adjustments. PHP and HSD share in excess gains or losses generated under the contract based on a tiered structure. Liabilities for the underwriting gain limitation and risk corridor of approximately $105,906 and $45,591, as of December 2015 and 2014 respectively, are recorded on the accompanying balance sheets in due under Medicaid contract.

Under the Medicaid Centennial Care contract, PHP is also subject to retroactive enrollment reconciliation. Under the contract, members whose effective date of Medicaid eligibility is determined prior to HSD's notification date are considered retroactive enrollment. Under the contract, PHP may retain premiums equal to the medical expense and a percentage of total medical expense for administrative costs. Medical expense in excess is reimbursed by HSD. Premiums in excess of medical expense and the percentage for administrative costs is due back to HSD. A liability for the retroactive enrollment reconciliation of approximately $62,391 as of December 31, 2015 is recorded on the accompanying sheets in due to state of New Mexico Human Services Department.

2. Summary of Significant Accounting Policies (continued)

PHP and PIC serve as plan sponsors to offer Medicare Part D prescription drug insurance coverage under a contract with the Centers for Medicare & Medicaid Services (CMS). Premium revenue is recognized ratably over the period in which eligible individuals are entitled to receive prescription drug benefits. Premium revenues are subject to a comprehensive risk reconciliation under which CMS shares in a portion of direct surplus or deficit related to Medicare Part D premiums. In addition to premium revenues, PHP and PIC receive prepayments from CMS related to low income, cost sharing, and catastrophic reinsurance subsidies. PHP and PIC are fully reimbursed by CMS for costs incurred under these contract elements, and, accordingly, there is no insurance risk to either company. Amounts received for these subsidies are not reflected as premium revenue, but rather are accounted for as deposits with the related liability recorded on the combined balance sheets. Pharmacy benefit costs not related to low income, cost sharing, or catastrophic reinsurance subsidies and administrative costs under the contract are expensed as incurred.

The estimated cost of all health services rendered to members through December 31 but not yet paid as of that date, is included in medical claims payable. This claims expense estimate is developed using actuarial assumptions based on historical experience with respect to the timing of payments in relation to the dates of service. Subsequent changes to prior period estimates are reflected in the current period. Losses on contracts are recognized in the period when health care costs are expected to exceed premium revenue.

Patient Service Revenue

PHS has agreements with third-party payors that provide for payments at amounts different from established charges. The basis for payment under these agreements includes prospectively determined rates, cost reimbursement, and negotiated discounts from established charges.

Patient service revenues are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments due to future audits, reviews, and investigations. The differences between the estimated and actual adjustments are recorded as part of patient service revenue in future periods, as the amounts become known, or as years are no longer subject to such audits, reviews, and investigations.

2. Summary of Significant Accounting Policies (continued)

For uninsured patients who do not qualify for charity care, PHS recognizes revenue on the basis of discounted rates, as provided by its policy. On the basis of historical experience, a significant portion of PHS's uninsured patients will be unable or unwilling to pay for the services provided. Thus, PHS records a significant provision for doubtful accounts related to uninsured patients in the period the services are provided. Patient service revenue, net of contractual allowances and discounts (but before the provision for doubtful accounts), is recognized from these major payor sources as follows:

	Year Ended December 31	
	2015	**2014**
Patient service revenue (net of contractual allowances and discounts):		
Third-party payors	**$ 1,007,036**	$ 926,345
Self-pay	**52,407**	75,398
Total	**$ 1,059,443**	$ 1,001,743

Charity Care

As an integral part of its mission, PHS provides care to all patients, regardless of ability to pay for needed services. A patient is classified as a charity patient in accordance with standards established across PHS and its affiliates. Charity care represents services rendered for which no, or only partial, payment is expected and, as such, is not included in revenues on the combined statements of operations.

Excess of Revenues Over Expenses

The combined statements of operations include a measurement for excess of revenues over expenses. Changes in unrestricted net assets, which are excluded from excess of revenues over expenses are primarily related to changes in the pension obligation.

2. Summary of Significant Accounting Policies (continued)

Other Income and Losses

Activities that result in gains or losses and are unrelated to the primary mission of PHS are considered to be other income and losses. Accordingly, investment income, changes in unrealized gains and losses on investments, gains (losses) on debt extinguishment, and unrealized changes in the fair value of interest rate swaps are reported as a component of other (loss) income.

Taxes

PHS and all of its affiliates, except for PNI and its subsidiaries, have been determined to be tax-exempt corporations by the Internal Revenue Service and generally are not subject to federal taxes on income.

The taxable affiliates utilize the liability method in accounting for income taxes. Under this method, deferred income tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the currently enacted tax rates and laws. Valuation allowances are used to reduce deferred tax assets to their estimated net realizable values when management determines ultimate recovery is not probable.

PHP and PIC are required to pay premium taxes to the state based on a percentage of adjusted premiums received related to the Commercial and Medicaid product lines. As a result of paying premium taxes, PHP and PIC are exempt from paying state income taxes. PHP and PIC recorded net premium tax expense totaling approximately $40,656 and $29,892 in 2015 and 2014, respectively. These amounts are included within purchased services and other expenses on the accompanying combined statements of operations. See Note 14.

ASC 740, *Income Taxes*, prescribes criteria for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. ASC 740 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. As of December 31, 2015 and 2014, there was no significant impact on the combined financial statements related to the tax positions taken. There were no significant tax positions taken by management that required accrual as of December 31, 2015 or 2014.

2. Summary of Significant Accounting Policies (continued)

Derivative and Hedging Instruments

In accordance with ASC 815, *Derivatives and Hedging*, derivatives are recognized as either assets or liabilities at fair value on the combined balance sheets, regardless of the purpose or intent for holding them. For those derivatives not designated as hedges under such standards, the changes in fair value are recognized in excess of revenue over expenses. For those derivatives previously designated as hedges under such standards, the effective portion of the changes in fair value previously recognized in unrestricted net assets is being amortized into the excess of revenues over expenses over the remaining lives of the derivative instruments.

Benefit Plans

PHS is the plan sponsor of a defined benefit pension plan (Plan I) and five other limited postretirement benefit plans. The funded status of Plan I is recognized on the combined balance sheets as the difference between the fair value of the investments and the actuarially determined pension obligation. Other required disclosures of ASC 715, *Compensation – Retirement Benefits*, include the accumulated benefit obligation and fair value of the plan's assets, assumptions used in the benefit obligation calculation, contributions, the asset allocation of the plan, and the expected benefits to be paid, which can be found in Note 11.

In addition to Plan I, PHS and PHP sponsor certain defined contribution plans. Contributions to these plans are expensed as earned by the employees.

Use of Estimates

The preparation of combined financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. Actual results could differ from those estimates.

Subsequent Events

In preparing the accompanying combined financial statements, PHS has evaluated subsequent events through April 22, 2016, the date on which the accompanying combined financial statements were issued. PHS further evaluated subsequent events for disclosable events through April 22, 2016.

3. Patient Service Revenue

A summary of payment arrangements with major third-party payors follows:

Medicare – Inpatient acute care and certain outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge or procedure. These rates vary according to patient classification systems based on clinical, diagnostic, and other factors.

Medicaid – The State Medicaid program consists of two primary plans. The larger plan is the Continental Care program. All Medicaid services, including physical health, behavioral health, and long-term care, are provided as part of the New Mexico Centennial Care program effective January 1, 2014. The Medicaid Salud! Plan was terminated by the state on December 31, 2013. PHP was one of four MCOs awarded five-year contracts by the state to administer the New Mexico Centennial Care program. PHS is contracted with each of the four MCOs and will continue to be paid discounted fee-for-service rates. The second plan is a traditional Medicaid plan. PHS facilities and physicians are paid for inpatient acute care services on prospectively determined rates per discharge. Payments for outpatient services are made on a discounted fee-for-service basis.

The Medicare cost report of Presbyterian Hospital has been audited by CMS through December 31, 2010. The Medicare cost reports for Plains Regional Medical Center and Presbyterian Española Hospital have been audited through December 31, 2012. The Medicare cost report of Lincoln Medical Center, Socorro General Hospital, and Dr. Dan C. Trigg Memorial Hospital has been audited by CMS through December 31, 2013. The Medicaid cost reports for Presbyterian Hospital and Presbyterian Española Hospital have been audited through December 31, 2010. The Medicaid cost report for Dr. Dan C. Trigg Memorial Hospital has been audited through December 31, 2011. The Medicaid cost report for Socorro General Hospital, Lincoln Medical Center and Plains Regional Medical Center have been audited through December 31, 2012. Management believes that estimated settlements accrued related to unaudited cost reports are adequate.

Estimates are continually monitored and reviewed, and as settlements are made or estimates adjusted, differences are reflected in current operations. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates could change by a material amount in the near term.

(Dollar Amounts in Thousands)

3. Patient Service Revenue (continued)

Others – PHS has also entered into payment agreements with certain commercial insurance carriers, HMOs, and preferred provider organizations. The basis for payment to PHS under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Amounts received from third-party payors in excess of expected reimbursement are reflected as estimated third-party payor settlements on the accompanying combined financial statements.

As part of the Patient Protection and Affordable Care Act (ACA), eligibility for the Medicaid program was expanded allowing more people to qualify for health care benefits. This change decreased the uninsured patient utilization and subsequently increased the utilization of patients covered by Medicaid.

PHS's major payor utilization percentages, based upon gross patient service revenue, are summarized as follows:

	Year Ended December 31	
	2015	**2014**
Medicare	**40%**	40%
Commercial	**28**	30
Medicaid	**26**	23
Self-pay	**2**	3
Other	**4**	4
	100%	100%

(Dollar Amounts in Thousands)

4. Other Operating Revenues

Other operating revenues consist of the following:

	Year Ended December 31	
	2015	**2014**
Health plan administrative fees	**$ 22,798**	$ 25,845
Contributions and other	**35,482**	32,327
Tax appropriation revenue	**14,157**	12,827
	$ 72,437	$ 70,999

Electronic Health Records Incentive Payments

Starting in 2013, the Medicare and Medicaid programs are providing an incentive payment to eligible hospitals and professionals if meaningful-use certified electronic health record (EHR) technology is adopted. The incentive payment is recognized when management is reasonably assured that PHS has complied with the conditions set forth by Medicare and Medicaid. Approximately $7,220 and $11,110 in incentive payments were recognized in other operating revenue for the years ended December 31, 2015 and 2014, respectively, relating to the Medicare and Medicaid incentive programs. PHS's attestation of compliance with the meaningful use criteria is subject to audit by the federal government or its designee. Additionally, EHR incentive payments are subject to retrospective adjustments upon final settlement of the applicable cost report from which payments were initially calculated.

5. Community Benefit

In support of its mission and philosophy, PHS voluntarily provides free care to patients who cannot afford health care due to inadequate resources and/or patients who are uninsured. Because PHS does not pursue collection of amounts determined to qualify as charity care, such amounts are not reported as patient service revenues. The estimated cost of this voluntary free care less the amount, if any, ultimately received was approximately $16,086 and $13,127 in 2015 and 2014, respectively. Funds received to subsidize charity services for the years ended December 31, 2015 and 2014, were $29 and $30, respectively.

5. Community Benefit (continued)

In addition, PHS provides services to other patients under certain government-reimbursed public aid programs, which pay providers amounts that are generally less than the cost of rendering the services provided to the patients. The estimated unreimbursed cost of this care was approximately \$80,690 and \$58,364 in 2015 and 2014, respectively. These unreimbursed costs and costs of voluntary free care do not include any governmental funds received for providing access to health care to all residents of the local community.

PHS uses information from its cost accounting system and certain cost-to-charge ratios, where applicable, to estimate the cost of financial assistance and other community benefits reported.

PHS, in furtherance of its mission, also commits significant time and resources to endeavors and critical services that meet otherwise unfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. Such programs include health screenings and assessments; cancer and other support groups; hospice programs; free transportation, lodging, meals, and medications for transient patients when needed; funding for homeless health care programs; significant ongoing and temporary donations of office space and telephone systems for nonprofit health care organizations, including the American Heart Association and the Meals on Wheels program; elementary school education on Healthy Choices; free flu vaccine clinics; participation in regular blood drives; and the provision of educational opportunities for students interested in pursuing medical-related or pastoral careers.

(Dollar Amounts in Thousands)

6. Assets Limited as to Use or Restricted

PHS has designated the accumulation of certain funds for future replacement of property and equipment, other capital improvements, debt retirement, self-insurance reserves, and other long-term purposes. Under the terms of the Master Trust Indenture for the outstanding bond issues, funds held by the trustee have been established and legally designated for debt service and qualifying capital expenditures. The following is a summary of assets limited as to use or restricted at fair value, except for certain alternative investments, which are recorded at net asset value using the equity method:

	December 31	
	2015	**2014**
Cash and cash equivalents	**$ 87,531**	$ 41,599
Fixed-income securities	**698,039**	576,689
Equity securities	**732,615**	720,936
Alternative investments	**223,107**	211,640
Government securities and other	**202,734**	201,198
Public master limited partnerships	**59,995**	81,990
	$ 2,004,021	$ 1,834,052

Fixed-Income and Government Securities – This investment class includes investments in various fixed-income instruments that include investment-grade and high-yield domestic and international bonds, mortgage pools, and bonds issued by U.S. government agencies. This investment class also includes investments in common trust funds, mutual funds, exchange-traded funds, and separately managed accounts that hold investments in fixed-income securities. The fixed-income investments are exposed to various kinds and levels of risk, including interest rate risk, credit risk, foreign exchange risk, and liquidity risk.

Equity Securities – This investment class consists primarily of common equity securities of domestic and international companies. These securities trade through the major public domestic and international exchanges. This investment class also includes investments in common trust funds, mutual funds, and exchange-traded funds that hold investments in equity securities. The equity securities investments are exposed to various risks, including market risk; individual security risk; foreign exchange risk; and, for common equity of companies with a small market capitalization, liquidity risk.

(Dollar Amounts in Thousands)

6. Assets Limited as to Use or Restricted (continued)

Alternative Investments – Funds in this class are invested with external investment managers who invest primarily in various alternative categories, including real estate, long and short equity positions, merger and event arbitrage, natural resources, distressed credit, managed futures, fixed-income arbitrage, and foreign exchange. These investments are domestic and international in nature and have varying degrees of illiquidity. The risks associated with these investments are numerous and include liquidity risk, market risk, event risk, interest rate risk, foreign exchange risk, and investment manager risk. In addition, the investment managers are not required to register with the Securities and Exchange Commission and are not subject to regulatory controls. As unregistered investment vehicles, these funds are not required to disclose the holdings in their portfolios to investors. Given the numerous risks involved, these funds have a greater likelihood of losing invested capital.

Public Master Limited Partnerships – This investment class consists of master limited partnerships that invest in various domestic infrastructure assets within the energy industry. The securities held within the limited partnership trade through the major public domestic exchanges and are exposed to various risks, including market risk, individual security risk, regulatory risk, interest rate risk, and liquidity risk.

As of December 31, 2015 and 2014, PHS had a total of $223,107 and $211,640, respectively, invested in alternative investments representing various hedge funds that include limited liability companies and limited liability partnerships, as follows:

	December 31	
	2015	**2014**
Equity long/short	**$ 12,373**	$ 14,462
Event driven	**26,703**	29,865
Relative value	**15,700**	4,000
Tactical trading	**19,032**	19,032
Private equity	**4,609**	5,239
Real assets	**99,992**	96,848
Total cost basis	**178,409**	169,446
Unrealized gain, net	**44,698**	42,194
	$ 223,107	$ 211,640

(Dollar Amounts in Thousands)

6. Assets Limited as to Use or Restricted (continued)

Approximately 98% of these alternative investments represent investments with original lockup periods ranging from one month to five years. The remaining exposure represents investments with longer lockups and limited redemption rights. There were no material unfunded commitments at December 31, 2015.

Investment income on assets limited as to use or restricted (excluding restricted by donor) consists of the following:

	Year Ended December 31	
	2015	**2014**
Interest and dividend income	**$ 37,905**	$ 35,997
Net realized gains on marketable securities and equity hedges	**33,688**	85,132
Total realized income	**71,593**	121,129
Changes in net unrealized gains on marketable securities	**(108,629)**	(43,074)
Changes in net unrealized gains on alternative investments	**2,504**	3,743
	$ (34,532)	$ 81,798

PHS has a hedging strategy related to the equity securities in the investment portfolio using derivatives to provide protection against a downturn in the equity markets. During 2015 and 2014, PHS realized a gain (loss) of $2,984 and ($2,889), respectively, from the hedge positions, which is included in investment income on the combined statements of operations. At December 31, 2015 and 2014, the fair value of the outstanding hedge positions was an asset (liability) of $1,660 and ($597), respectively, which has been included in accrued liabilities on the accompanying combined balance sheets and changes in net unrealized gains on investments in the combined statements of operations. If the liability related to the fair value of the equity hedges were to exceed $40,000, PHS would be required to post a cash deposit for amounts in excess of the threshold as collateral with the counterparty. This collateral threshold would be reduced to $30,000 if PHS's current AA credit rating were to fall to A+, reduced to $20,000 at a rating of A, and further reduced to zero at a credit rating below A.

7. Fair Value Measurements

The following table presents the fair value hierarchy for those financial assets and liabilities measured at fair value on a recurring basis and alternative investments that are carried at net asset value using the equity method as of December 31, 2015:

	Level 1	Level 2*	Level 3	Fair Value	Equity Method	Carrying Value at December 31, 2015	Valuation Technique**
				(In Thousands)			
Designated for long-term purposes							
Money market	$ 14,116	$ –	$ –	$ 14,116	$ –	$ 14,116	a
Government and agencies	139,981	–	–	139,981	–	139,981	a
Bond funds	220,857	164,813	–	385,670	–	385,670	a/c
Corporate and municipal bonds	–	217,034	–	217,034	–	217,034	a
Equity funds	372,448	288,014	–	660,462	–	660,462	a
Other public equities	54,912	–	–	54,912	–	54,912	a
Alternative investments	–	643	9,798	10,441	205,706	216,147	a
Total designated for long-term purposes	$ 802,314	$ 670,504	$ 9,798	$ 1,482,616	$ 205,706	$ 1,688,322	
Designated for self-insurance funds							
Money market	$ 3,177	$ –	$ –	$ 3,177	$ –	$ 3,177	a
Government and agencies	1,866	–	–	1,866	–	1,866	a
Bond funds	25,991	9,402	–	35,393	–	35,393	a/c
Corporate and municipal bonds	–	15,198	–	15,198	–	15,198	a
Equity funds	28,695	30,965	–	59,660	–	59,660	a
Other public equities	4,044	–	–	4,044	–	4,044	
Total designated for self-insurance funds	$ 63,773	$ 55,565	$ –	$ 119,338	$ –	$ 119,338	

7. Fair Value Measurements (continued)

	Level 1	Level 2*	Level 3	Fair Value	Equity Method	Carrying Value at December 31, 2015	Valuation Technique**
				(In Thousands)			
Restricted by donors							
Money market	**$ 267**	**$ –**	**$ –**	**$ 267**	**$ –**	**$ 267**	**a**
Government and agencies	**2,648**	**–**	**–**	**2,648**	**–**	**2,648**	**a**
Bond funds	**4,178**	**3,117**	**–**	**7,295**	**–**	**7,295**	**a/c**
Corporate and municipal bonds	**–**	**4,105**	**–**	**4,105**	**–**	**4,105**	**a**
Equity funds	**7,045**	**5,448**	**–**	**12,493**	**–**	**12,493**	**a**
Other public equities	**1,039**	**–**	**–**	**1,039**	**–**	**1,039**	**a**
Alternative investments	**–**	**428**	**6,532**	**6,960**	**–**	**6,960**	**a**
Total restricted by donors	**$ 15,177**	**$ 13,098**	**$ 6,532**	**$ 34,807**	**$ –**	**$ 34,807**	
Held by trustee							
Money market	**$ 51,838**	**$ –**	**$ –**	**$ 51,838**	**$ –**	**$ 51,838**	**a**
	$ 51,838	**$ –**	**$ –**	**$ 51,838**	**$ –**	**$ 51,838**	
Restricted for statutory requirements							
Money market	**$ 18,133**	**$ –**	**$ –**	**$ 18,133**	**$ –**	**$ 18,133**	**a**
Government and agencies	**58,239**	**–**	**–**	**58,239**	**–**	**58,239**	
Corporate and municipal bonds	**33,344**	**–**	**–**	**33,344**	**–**	**33,344**	**a**
	$ 109,716	**$ –**	**$ –**	**$ 109,716**	**$ –**	**$ 109,716**	
Financial assets (liabilities)							
Interest rate swaps	**$ –**	**$ (26,790)**	**$ –**	**$ (26,790)**	**$ –**	**$ (26,790)**	**a**
Equity hedges	**$ –**	**$ 1,643**	**$ –**	**$ 1,643**	**$ –**	**$ 1,643**	**a**

* Approximately 67% of Level 2 assets consist of commingled funds in which the underlying assets are primarily marketable debt and equity securities that trade on nationally recognized exchanges.

** Valuation techniques are described in Note 2.

The following table presents the fair value hierarchy for those financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2014:

	Level 1	Level 2*	Level 3	Fair Value	Equity Method	Carrying Value at December 31, 2014	Valuation Technique**
				(In Thousands)			
Designated for long-term purposes							
Money market	$ 11,752	$ –	$ –	$ 11,752	$ –	$ 11,752	a
Government and agencies	136,271	–	–	136,271	–	136,271	a
Bond funds	180,326	172,945	–	353,271	–	353,271	a/c
Corporate and municipal bonds	–	138,398	–	138,398	–	138,398	a
Equity funds	365,582	279,082	–	644,664	–	644,664	a
Public master limited partnership	74,928	–	–	74,928	–	74,928	a
Alternative investments	–	849	9,059	9,908	195,126	205,034	a/c
Total designated for long-term purposes	$ 768,859	$ 591,274	$ 9,059	$ 1,369,192	$ 195,126	$ 1,564,318	

7. Fair Value Measurements (continued)

	Level 1	Level 2*	Level 3	Fair Value	Equity Method	Carrying Value at December 31, 2014	Valuation Technique**
				(In Thousands)			
Designated for self-insurance funds							
Money market	$ 2,616	$ –	$ –	$ 2,616	$ –	$ 2,616	a
Government and agencies	3,216	–	–	3,216	–	3,216	a
Bond funds	25,887	10,091	–	35,978	–	35,978	a/c
Corporate and municipal bonds	–	13,938	–	13,938	–	13,938	a
Equity funds	30,448	32,606	–	63,054	–	63,054	a
Public master limited partnership	5,526	–	–	5,526	–	5,526	a
Total designated for self-insurance funds	$ 67,693	$ 56,635	$ –	$ 124,328	$ –	$ 124,328	
Restricted by donors							
Money market	$ 241	$ –	$ –	$ 241	$ –	$ 241	a
Government and agencies	2,794	–	–	2,794	–	2,794	a
Bond funds	3,698	3,546	–	7,244	–	7,244	a/c
Corporate and municipal bonds	–	2,838	–	2,838	–	2,838	a
Equity funds	7,498	5,720	–	13,218	–	13,218	a
Public master limited partnership	1,536	–	–	1,536	–	1,536	a
Alternative investments	–	566	6,040	6,606	–	6,606	a/c
Total restricted by donors	$ 15,767	$ 12,670	$ 6,040	$ 34,477	$ –	$ 34,477	
Held by trustee							
Money market	$ 7,244	$ –	$ –	$ 7,244	$ –	$ 7,244	a
Total held by trustee	$ 7,244	$ –	$ –	$ 7,244	$ –	$ 7,244	
Restricted for statutory requirements							
Money market	$ 19,746	$ –	$ –	$ 19,746	$ –	$ 19,746	a
Government and agencies	58,917	–	–	58,917	–	58,917	a
Corporate and municipal bonds	25,022	–	–	25,022	–	25,022	a
Total restricted for statutory requirements	$ 103,685	$ –	$ –	$ 103,685	$ –	$ 103,685	
Financial liabilities							
Interest rate swaps	$ –	$ 26,576	$ –	$ 26,576	$ –	$ 26,576	a
Equity hedges	$ –	$ 597	$ –	$ 597	$ –	$ 597	a

* Approximately 75% of Level 2 assets consist of commingled funds in which the underlying assets are primarily marketable debt and equity securities that trade on nationally recognized exchanges.

** Valuation techniques are described in Note 2.

Fair Value of Long-Term Debt

The fair value of long-term debt is estimated based upon published or quoted market prices (Level 2) for these issues or, where such prices not available, on similar issues and approximated $746,995 and $637,809 at December 31, 2015 and 2014, respectively.

(Dollar Amounts in Thousands)

8. Property and Equipment, Net

Property and equipment, net consists of the following:

	December 31	
	2015	**2014**
Land and improvements	**$ 119,308**	$ 118,888
Buildings and improvements	**943,047**	844,723
Equipment	**587,676**	580,651
Software	**208,604**	187,241
	1,858,635	1,731,503
Less accumulated depreciation and amortization	**1,034,725**	961,859
	823,910	769,644
Construction-in-progress	**33,138**	46,128
	$ 857,048	$ 815,772

Unamortized software was $75,558 and $77,700 as of December 31, 2015 and 2014, respectively. Software amortization expense was $23,196 and $22,195 for the years ended December 31, 2015 and 2014, respectively.

At December 31, 2015, PHS has future capital commitments of $10,030.

PHS capitalized interest costs in the amounts of $2,625 and $1,006 in 2015 and 2014, respectively.

9. Medical Claims Expense

Reserves for medical claims and claims adjustment expenses attributable to insured events of prior years decreased $12,245 and $13,112 in 2015 and 2014, respectively, as a result of changes in estimates of unpaid claims and claims adjustment expenses. These changes generally are the result of ongoing analyses of recent loss development trends. Original estimates are increased or decreased as additional information becomes known regarding individual claims.

(Dollar Amounts in Thousands)

10. Long-Term Debt, Capital Leases, and Interest Rate Swaps

	December 31	
	2015	**2014**
2015 Series A Hospital System Revenue Bonds (New Mexico Hospital Equipment Loan Council), fixed-interest coupon rates from 4.125% to 5.0% at December 31, 2015, payable semiannually on the established interest payment dates, principal payments beginning in 2016 through 2044	**$ 258,535**	$ –
2012 Series A Hospital System Revenue Bonds (New Mexico Hospital Equipment Loan Council), fixed-interest coupon rates from 4.0% to 5.0% at December 31, 2015, payable semiannually on the established interest payment dates, principal payments beginning in 2033 through 2042	**78,415**	78,543
2009 Series A Hospital System Revenue Bonds (New Mexico Hospital Equipment Loan Council), fixed-interest coupon rates from 5.0% to 5.125% at December 31, 2015, payable semiannually on the established interest payment dates, principal payments beginning in 2033 through 2039	**132,553**	132,465
2008 Series A Hospital System Revenue Bonds (New Mexico Hospital Equipment Loan Council), defeased in 2015	**–**	137,306
2008 Series B, C, and D Hospital System Revenue Bonds (New Mexico Hospital Equipment Loan Council), variable-rate demand bonds with interest rate of .01% at December 31, 2015, payable monthly on the established interest payment date, principal payable in annual installments through 2034	**193,150**	200,095
2012 note payable to bank, variable rate, interest payable quarterly at one-month LIBOR plus .90% (1.1% at December 31, 2015) due October 2022	**50,000**	50,000
Capital lease obligations and other	**12,116**	11,347
	724,769	609,756
Less current portion	**14,797**	13,435
	$ 709,972	$ 596,321

10. Long-Term Debt, Capital Leases and Interest Rate Swaps (continued)

The 2015 Series A Revenue Bonds were issued through the New Mexico Hospital Equipment Loan Council in May 2015. A portion of the bonds proceeds were used in 2015 to refund and defease the 2008A Bonds. The remaining portion of the bond proceeds will be used to reimburse PHS for certain prior capital expenditures; for current and future capital projects; and pay certain costs of issuing the 2015A bonds. The 2015 bonds are fixed-rate serial and term bonds and have scheduled maturities and mandatory sinking fund deposits starting in August 2016 and August 2040, respectively and continuing through 2044.

The 2012 Series A Revenue Bonds were issued through the New Mexico Hospital Equipment Loan Council in August 2012. Proceeds of the bonds are being used to fund various health care facilities throughout the PHS system, including a patient tower at the Española Hospital, a cancer center on the Rust Medical Center campus, a physician office building adjacent to Socorro General Hospital, and other general capital improvements, and were also used to pay costs of issuance. The 2012 bonds are fixed-rate term bonds and have scheduled mandatory sinking fund deposits starting in 2013 and continuing through 2042. In August 2012, PHS also obtained a $50,000 taxable bank direct loan (the 2012 Bank Loan), of which $50,000 was outstanding as of December 31, 2015 and 2014. Proceeds of the 2012 Bank Loan were used for a new system corporate office, which was completed in 2014.

The 2009 Series A Revenue Bonds totaling $134,610 of original issue discount bonds were issued through the New Mexico Hospital Equipment Loan Council. Proceeds of the bonds were used to fund a project for the construction of the Rust Medical Center and pay the costs of issuance. The 2009 bonds are fixed-rate term bonds and have scheduled mandatory sinking fund deposits starting in 2033 and continuing through 2039.

The 2008 Revenue Bonds were issued through the New Mexico Hospital Equipment Loan Council in four series (Series A, Series B, Series C, and Series D) (the Series 2008 Bonds) in November 2008. The Series 2008 Bonds were designed to defease the 2005 Series A and B Revenue Bonds ($201,895); to pay off a Wells Fargo Credit Agreement, which defeased the 2004 Series A through D Bonds ($128,655) and the 1993A Bonds ($17,900) during March and April 2008; to reimburse PHS for prior capital expenditures; and to pay certain costs of issuing the Series 2008 Bonds. The Series 2008 A Bonds were refunded in their entirety in 2015 and have been legally defeased. The Series 2008 B through D Bonds are variable-rate demand obligations and bear interest on a weekly rate period at amounts set by a remarketing agent. The

(Dollar Amounts in Thousands)

10. Long-Term Debt, Capital Leases and Interest Rate Swaps (continued)

interest rate mode can be modified under the terms of the legal documents. To secure the tender price of the Series 2008 B Bonds, PHS has entered into standby bond purchase agreements with JPMorgan Chase Bank, N.A., and with Wells Fargo, N.A. for the Series 2008 C and D Bonds. The standby bond purchase agreements expire in November 2017, 2018, and 2016 for the Series 2008 B, C, and D Bonds, respectively.

The Series 2008 B, C, and D Bonds are subject to optional redemption at the discretion of PHS. In addition, the Series 2008 Bonds have a schedule of mandatory sinking fund deposits through 2034.

All of the outstanding bonds are collateralized by a pledge of unrestricted receivables of the Obligated Group, as defined under the Master Trust Indenture. The Master Trust Indenture of the Obligated Group requires, among other things, that certain funds be established and held by a trustee. The Master Trust Indenture also requires certain limitations on additional indebtedness, liens on property, and disposition or transfers of assets, as well as the maintenance of certain cash balances and other financial ratios. The Obligated Group was in compliance with all such covenants at December 31, 2015.

Scheduled principal payments and sinking fund requirements on long-term debt and capital leases at December 31 are as follows:

	Long-Term Debt	Capital Leases	Total
2016	$ 14,247	$ 550	$ 14,797
2017	14,677	–	14,677
2018	15,203	–	15,203
2019	15,764	–	15,764
2020	16,421	–	16,421
Thereafter	644,307	3,600	647,907
	$ 720,619	$ 4,150	$ 724,769

10. Long-Term Debt, Capital Leases, and Interest Rate Swaps (continued)

Interest Rate Swaps

In connection with the Series 2005 Bonds, PHS entered into two floating to fixed-rate swaps (the 2005 Swaps) effective July 28, 2005, for notional amounts of $102,400 and $102,600. On November 25, 2008, PHS refunded the Series 2005 Bonds with the Series 2008 B–D Bonds. The amortization schedule for the Series 2008 B–D Bonds was established to match the amortization of the Series 2005 Bonds. The 2005 Swaps provide that PHS receives a floating amount based on a percentage of one-month LIBOR (58.30% of LIBOR plus 0.36%) and PHS pays a fixed rate of 3.085% based on a notional amount equal to the principal amount of the Series 2005 Bonds. As of and subsequent to April 1, 2007, PHS recognizes the entire change in the fair value of these swaps within the excess of revenue over expenses under ASC 815, as discussed in Note 2. The total outstanding notional amount of the 2005 Swaps at December 31, 2015, was approximately $168,405.

On February 9, 2006, PHS entered into a series of four floating to fixed-rate, forward-dated swaps (the 2006 Swaps) in notional amounts of $38,695, $38,665, $31,460, and $25,720. The 2006 Swaps were effective January 2, 2007, and provide that PHS receives a floating amount based on a percentage of one-month LIBOR (68%) and PHS pays a weighted average fixed rate of 3.564% based on a notional amount equal to the principal amount of the Series 2004 Bonds. On June 5, 2009, PHS terminated the two 2006 Swaps that were initially originated in the notional amounts of $31,460 and $25,720 and partially terminated two of the 2006 Swaps that were initially originated in the notional amounts of $38,695 and $38,665. The remaining portion of the 2006 Swaps match the amortization schedule for the Series 2008 B–D Bonds that are not hedged by the 2005 Swaps. As of and subsequent to April 1, 2007, PHS recognizes the entire change in the fair value of these swaps within the excess of revenue over expenses under ASC 815, as discussed in Note 2. The total outstanding notional amount of the 2006 Swaps at December 31, 2015, is approximately $27,745.

All derivatives that are being measured by PHS under ASC 820 are considered Level 2 assets (liabilities) because a quoted price can be obtained from a number of dealer counterparties and other market sources based on observable interest rates and yield curves for the full term of the asset or liability. In order to measure the fair value of municipal derivatives under ASC 820, PHS adjusted its mid-market periodic values of the swaps outstanding to incorporate non-performance risk by PHS (when the financial instrument is a liability) or the counterparty (when the financial

10. Long-Term Debt, Capital Leases, and Interest Rate Swaps (continued)

instrument is an asset). In order to determine the risk of non-performance when the financial instrument is a liability, PHS has determined the change in the credit market for debt issues by entities with the same credit characteristics as PHS. To determine non-performance risk when the instrument is an asset, PHS determines the change in the credit market for debt issues by the counterparty.

As of December 31, 2015 and 2014, the fair value of the 2005 and 2006 Swaps was a net liability of $26,790 and $26,576, respectively, and is included in other liabilities on the accompanying combined balance sheets.

If the liability related to the swaps were to exceed $40,000, PHS would be required to post a cash deposit for amounts in excess of the threshold as collateral with the counterparty. This collateral threshold would be reduced to $30,000 if PHS's current AA credit rating were to fall to A+, reduced to $20,000 at a rating of A, and further reduced to zero at a credit rating below A.

Interest expense included approximately $5,346 and $5,582 in 2015 and 2014, respectively, related to net periodic payments to the counterparty.

11. Employee Benefit Plans

PHS has a defined benefit pension plan (Plan I) that previously covered substantially all of the employees of its related organizations, except employees of PNI. Effective January 1, 2006, Plan I was closed to new entrants, but it continued to accrue benefits for those employees in the plan as of December 31, 2005 until December 31, 2012, when Plan I was amended to cease future benefit accruals. Any benefits earned by participants under Plan I at December 31, 2012, will be preserved and will be payable based on Plan I's provisions.

PHS contributes such amounts as necessary on an actuarial basis to provide Plan I with assets sufficient to meet the benefits to be paid to Plan I participants. PHS contributed $8,004 and $9,850 in 2015 and 2014, respectively to Plan I.

(Dollar Amounts in Thousands)

11. Employee Benefit Plans (continued)

A summary of Plan I's benefit obligation, assets, and funded status is as follows:

	Year Ended December 31	
	2015	**2014**
Change in benefit obligation:		
Benefit obligation at beginning of year	**$ 580,068**	$ 471,539
Service cost	**2,100**	2,100
Interest cost	**24,767**	24,509
Actuarial (gain) loss	**(39,337)**	116,672
Benefits paid and plan expenses	**(22,997)**	(34,752)
Benefit obligation at end of year	**$ 544,601**	$ 580,068
Change in assets:		
Fair value of assets at beginning of year	**$ 422,509**	$ 411,949
Actual return on assets	**(16,822)**	35,462
Employer contribution	**8,004**	9,850
Benefits paid and plan expenses	**(22,997)**	(34,752)
Fair value of plan assets at end of year	**$ 390,694**	$ 422,509
Funded status at year-end	**$ (153,907)**	$ (157,559)
Amounts not yet reflected in net periodic benefit cost and included in net assets:		
Accumulated loss	**$ (178,285)**	$ (175,283)
Cumulative changes in unrestricted net assets	**(178,285)**	(175,283)
Cumulative employer contributions in excess of net periodic benefit cost	**24,378**	17,724
Net amount recognized in the combined balance sheets	**$ (153,907)**	$ (157,559)

The actuarial gain recorded in 2015 was primarily due to PHS using new mortality tables in the projected benefit obligation calculation. The new mortality tables were issued by the Society of Actuaries during 2015.

(Dollar Amounts in Thousands)

11. Employee Benefit Plans (continued)

A summary of the projected benefit obligation, accumulated benefit obligation, and fair value of plan assets is as follows:

	2015	2014
Projected benefit obligation	**$ 544,601**	$ 580,068
Accumulated benefit obligation	**544,601**	580,068
Fair value of plan assets	**390,694**	422,509

Net periodic benefit cost includes the following components:

	2015	2014
Service cost – benefits earned during the year	**$ 2,100**	$ 2,100
Interest cost on projected benefit obligation	**24,767**	24,509
Expected return on Plan I assets	**(29,842)**	(29,335)
Amortization of prior service credit	**–**	–
Recognized net actuarial loss	**4,326**	1,189
Net periodic pension benefit	**$ 1,351**	$ (1,537)

Assumptions used to determine benefit obligation as of the measurement date are as follows:

	2015	2014
Discount rate at end of year	**4.75%**	4.34%
Rate of increase in compensation levels	**N/A**	N/A

Assumptions used to determine net periodic pension cost are as follows:

	2015	2014
Discount rate at beginning of year	**4.34%**	5.29%
Rate of increase in compensation levels	**–**	N/A
Expected long-term rate of return on assets	**7.50%**	7.50%

(Dollar Amounts in Thousands)

11. Employee Benefit Plans (continued)

Contributions expected to be made during 2016 have not been finalized but are expected to be approximately $9,468.

The expected return on Plan I assets has been developed using both historical and future expected returns for each asset class. Based on the target asset mix as of December 31, 2015, PHS has selected a long-term rate of return of 7.0% using this approach.

The asset allocation for Plan I by asset class at the measurement date was as follows:

	2015	**2014**
Cash and cash equivalents	**1%**	1%
Fixed-income securities	**45**	45
Common stock and equity	**44**	44
Absolute return, hedge funds, and other	**10**	10
	100%	100%

Plan I assets have historically been invested in a portfolio designed to preserve principal and obtain competitive investment returns and long-term investment growth, consistent with actuarial assumptions, while minimizing unnecessary investment risk. Diversification is achieved by retaining multiple investment managers with complementary philosophies, styles, and approaches.

Plan I asset allocation targets at the measurement date were as follows:

	Target	**Range**
Cash and cash equivalents	1%	0%–6%
Fixed-income securities	44%	39%–49%
Domestic equity securities	20%	15%–25%
International equity securities	20%	15%–25%
Other	15%	7%–25%

(Dollar Amounts in Thousands)

11. Employee Benefit Plans (continued)

The fair values of PHS's Plan I assets at December 31, by asset category, are as follows:

Asset Category	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Carrying Value	Valuation Technique (a, b, c)*
2015					
Money market	**$ 3,337**	**$ –**	**$ –**	**$ 3,337**	**a**
Bond funds	**17,682**	**157,308**	**–**	**174,990**	**a/c**
Public master limited partnership	**17,711**	**–**	**–**	**17,711**	**a**
Equity funds	**83,645**	**69,754**	**–**	**153,399**	**a**
Alternative investments	**–**	**–**	**41,257**	**41,257**	**a, c**
	$ 122,375	**$ 227,062**	**$ 41,257**	**$ 390,694**	
2014					
Money market	$ 2,059	$ –	$ –	$ 2,059	a
Bond funds	25,482	166,392	–	191,874	a/c
Public master limited partnerships	24,341	–	–	24,341	a
Equity funds	87,838	74,893	–	162,731	a
Alternative investments	–	–	41,504	41,504	a, c
	$ 139,720	$ 241,285	$ 41,504	$ 422,509	

* Valuation techniques are described in Note 2.

Expected benefits to be paid to the Plan I participants and beneficiaries are as follows:

2016	$ 20,390
2017	21,889
2018	23,202
2019	24,813
2020	26,272
2021–2025	152,329

(Dollar Amounts in Thousands)

11. Employee Benefit Plans (continued)

In addition to Plan I, PHS also has five other limited postretirement benefit plans subject to the funded status recognition provisions of ASC 715. Plan I is funded, and the other postretirement plans are unfunded. During 2015, unrestricted net assets decreased by approximately $2,015, and during 2014, unrestricted net assets decreased by approximately $112,520 for changes in the funded status of Plan I and the other postretirement benefit plans.

PHS has a defined contribution Plan (Plan II), which consists of a Section 403(b) plan and a Section 401(a) plan under the Internal Revenue Code. Plan II requires PHS to pay a basic employer contribution, as well as match participant contributions up to a stated maximum percentage of the participant's salary. Contributions to Plan II are expensed as earned by employees and approximated $25,697 and $23,892 in 2015 and 2014, respectively.

PHP has a 401(k) defined contribution plan (Plan III) for PHP employees. Plan III requires PHP to match participant contributions up to a stated maximum percentage of the participant's salary. Plan III additionally provides an employer contribution for all employees regardless of whether the employee individually contributes to the Plan III. PHP contributions to Plan III are expensed as earned by employees and approximated $2,404 and $2,072 in 2015 and 2014, respectively.

12. Restricted Net Assets

Permanently or temporarily restricted net assets are recorded in accordance with the intent of the donor. Restricted net assets are available for the following purposes as of December 31:

	2015		2014	
	Temporarily	**Permanently**	**Temporarily**	**Permanently**
Program services and facility improvements	**$ 22,435**	**$ 9,218**	$ 23,419	$ 6,754
Education	**3,562**	**1,633**	3,724	1,612
	$ 25,997	**$ 10,851**	$ 27,143	$ 8,366

(Dollar Amounts in Thousands)

13. Concentration of Credit Risk

PHS provides health care services through its inpatient and outpatient care facilities throughout New Mexico. PHS grants credit to patients, most of whom are insured under third-party payor agreements, without requiring collateral or other security in extending credit to patients. However, PHS routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits payable under their health insurance programs, plans, or policies (e.g., Medicare, Medicaid, HMOs, and commercial insurance policies). The following table summarizes the percentage of net patient accounts receivable from all payors:

	December 31	
	2015	**2014**
Managed care and other third-party payors	**71%**	68%
Government	**23**	24
Self-pay	**6**	8
Total	**100%**	100%

Managed care and other third-party payors consist of receivables from various payors, including contracted third-party payors providing commercial and government programs. Management does not believe there is any significant concentration of credit risks associated with accounts receivable. Furthermore, management continually monitors and adjusts its allowances (contractual and doubtful accounts) associated with these receivables.

14. Commitments and Contingencies

Litigation and Other Contingent Liabilities

PHS is subject to pending and threatened legal actions arising during the ordinary course of business. Management and legal counsel periodically assess whether losses have been incurred related to pending or threatened litigation, claims, and assessments. Loss estimates are continually monitored and reviewed, and as estimates are adjusted, changes in estimated losses are reflected in current operations. Losses incurred due to the actual results of litigation could differ from estimates recorded. In management's opinion, upon consultation with legal counsel,

14. Commitments and Contingencies (continued)

these matters should not have a material adverse effect on PHS's combined financial condition, results of operations, or cash flows. However, PHS's evaluation of the likely effects of these actions could change in the future, and an unfavorable outcome, depending upon the amount and timing, could have a material effect on PHS's combined results of operations or cash flows of a future period.

Patient Protection and Affordable Care Act

The ACA, signed into law on March 23, 2010, has created significant changes and will continue to create significant changes for health insurance markets, including changes to Medicare Advantage payments and the Medical Loss Ratio (MLR) provision that requires insurers to pay rebates to customers when insurers do not meet or exceed the specified MLR thresholds. Most of the provisions of ACA with more significant effects on the health insurance marketplace, both state and federal, went into effect on January 1, 2014, including a requirement that insurers guarantee the issuance of coverage to all individuals regardless of health status, strict rules on how health insurance is rated, the assessment of new taxes and fees (including annual fees on health insurance companies), the creation of new insurance exchanges for individuals and small groups, the availability of premium subsidies for certain individual products, and substantial expansions in eligibility for Medicaid. Implementation of ACA brings with it significant oversight responsibilities by health insurers that may result in increased governmental audits, increased assertions of False Claims Act violations, and an increased risk of other litigation.

Despite significant preparation for the advent of the new federal and state health insurance exchanges, there have been many technical difficulties in the implementation of the exchanges, which entail uncertainties associated with mix and volume of business. In November 2013, CMS notified the various state insurance commissioners that, under a transitional policy, health insurance coverage in the individual or small group market that is renewed for a policy year starting between January 1, 2014 and October 1, 2014, and that would otherwise have been deemed non-compliant with certain market reforms under Health Care Reform, will nonetheless not be considered by CMS to be out of compliance with respect to such market reforms, provided certain conditions are met. CMS further encouraged state agencies responsible for enforcing the specified market reforms to adopt the same transitional policy with respect to this coverage. The state of New Mexico has taken the position that individual policies have no transition period and should be renewed to be compliant by January 1, 2015. For small group policies, the state has taken the position of allowing a transition period through December 31, 2015, and policies must be renewed to be compliant by January 1, 2016.

14. Commitments and Contingencies (continued)

Due to the impact of the transitional policy, PHS may be adversely selected by individuals who will have a higher acuity level than the anticipated pool of participants in the exchange markets. In addition, the risk adjustment, reinsurance, and risk corridor premium stabilization programs of Health Care Reform, or Health Care Reform Premium Stabilization Programs, established to apportion risk among insurers, may not be effective in appropriately mitigating the financial risks related to PHS's exchange products. These factors, along with the limited information about the individuals who have access to these newly established exchanges that was available when PHS established premiums, may have a material adverse effect on PHS's combined results of operations if premiums are not adequate or do not appropriately reflect the acuity of these individuals. Any variation from PHS's expectations regarding acuity, enrollment levels, adverse selection, or other assumptions utilized in setting adequate premium rates could have a material adverse effect on PHS's combined results of operations, financial position, and cash flows.

Health Insurer Fee

ACA Section 9010 imposes a mandatory annual fee on health insurers that write certain types of health insurance on U.S. risks for each calendar year beginning on or after January 1, 2014. The annual fee is allocated to health insurers based on the ratio of the amount of an insurer's premium written during the preceding calendar year to the amount of health insurance for all U.S. health risk for those certain lines of business that is written during the preceding calendar year. This fee is nondeductible for income tax purposes. The fee is estimated and recorded in the financial statements of health insurers in full once the insurer provides qualifying health insurance in the applicable calendar year in which the fee is payable, with a corresponding deferred cost that is amortized to expense using a straight-line method of allocation. The health insurer fee of $31,337 was paid in 2015, based upon premiums written in 2014, and is included in 2015 purchased services and other expenses. The health insurer fee payable for 2016 is currently estimated to be approximately $31,330.

Health Care Regulatory Environment

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Violations of these laws and regulations could result in exclusion from government health care programs, together with the

14. Commitments and Contingencies (continued)

imposition of significant fines and penalties, as well as significant repayments for patient services previously billed and paid. Management believes that it has established adequate reserves to investigate, defend, and ultimately resolve any alleged instances of noncompliance. Compliance with such laws and regulations can be subject to future government review, as well as regulatory actions unknown or unasserted at this time.

Self-Insurance Plans

PHS is self-insured for professional and general liability, workers' compensation, and employee health insurance. PHS purchases claims-made insurance to cover professional liability and workers' compensation claims in excess of the self-insured limits. There are known claims and incidents that may result in the assertion of additional claims, as well as claims for unknown incidents that may be asserted arising from services provided to patients. PHS has engaged independent actuaries to estimate the ultimate costs, if any, of the settlement of such claims. Accrued professional liability, general liability, and workers' compensation losses of $139,794 and $118,326 at December 31, 2015 and 2014, respectively, have been discounted at 2.72% and 2.28%, respectively, and in management's opinion, such amounts provide an adequate reserve for loss contingencies. The increase in the accrued liability can be attributed to adverse claim development. The accrued liability relating to professional and general liability and workers' compensation at December 31, 2015 and 2014, is reported on a gross basis and therefore has not been reduced by estimated insurance recoveries of $21,326 and $11,740, respectively, which are reported in other receivables. The accrued liability for estimated employee health claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported.

At December 31, 2015 and 2014, PHS had an available line of credit to collateralize the workers' compensation coverage of approximately $9,300 of which none was outstanding.

Surety Bond

The Medicaid Centennial Care Contract requires PHP to provide a performance bond equal to 90% of the average of the past three months capitation payments made to PHP from HSD. As of December 31, 2015 and 2014, PHP met this requirement through a surety bond issued by an unrelated insurance company in the amount of $90,245 and $78,839, respectively. PHP has indemnified the issuer of the bond for any and all losses.

(Dollar Amounts in Thousands)

14. Commitments and Contingencies (continued)

Operating Leases

Future minimum rental payments required for the next five years and thereafter for all operating leases that have initial or remaining noncancelable lease terms in excess of one year at December 31, 2015, are as follows:

2016	$ 1,972
2017	1,777
2018	1,767
2019	1,763
2020	448
Thereafter	612
	$ 8,339

Rent expense under operating leases for the years ended December 31, 2015 and 2014, totaled approximately $8,303 and $9,459, respectively.

15. Functional Expenses

PHS provides general health care services to residents within its geographic region. Expenses related to providing these services are as follows:

	Year Ended December 31	
	2015	**2014**
Health care services	**$ 2,318,284**	$ 2,055,508
Non-clinical and support services, including general and administrative	**451,656**	426,037
	$ 2,769,940	$ 2,481,545

(Dollar Amounts in Thousands)

16. Income Taxes

The components of the provision for income taxes at December 31 are as follows:

	2015	2014
Current	**$ 43,783**	$ 53,584
Deferred	**(8,697)**	(1,012)
Total provision for income taxes	**$ 35,086**	$ 52,572

The differences between the actual and expected provision for income taxes or benefit computed by applying the federal corporate income tax rate of 35% in 2015 and 2014, plus a state rate of 4.8% to income before income taxes for the years ended December 31 are as follows:

	2015	2014
Computed tax expense at combined rate	**$ 24,237**	$ 46,855
ACA health provider fee	**10,968**	6,309
Change in valuation allowance	**(147)**	(148)
Other permanent differences	**(466)**	(665)
Provision to return – permanent items	**303**	(32)
State taxes and other	**191**	253
	$ 35,086	$ 52,572

Deferred tax assets (liabilities) comprised the following at December 31:

	2015	2014
Deferred tax assets:		
Medical liabilities and other reserves	**$ 4,213**	$ 4,202
Medical claims payable (incurred but not reported)	**417**	511
Premium deficiency reserve	**7,190**	–
Deferred compensation	**840**	924
Investments	**424**	463
Unrealized loss on sale of securities	**914**	298
Unrealized loss on investments	**130**	–
Net operating loss carryforwards	**541**	689
Total deferred tax assets	**14,669**	7,087

(Dollar Amounts in Thousands)

16. Income Taxes (continued)

	2015	2014
Deferred tax liabilities:		
Amortization of intangibles	**$ (20,462)**	$ (20,007)
Prepaid insurance	**(2,869)**	(2,331)
Depreciation	**(36)**	(46)
Partnership – book/tax difference	**(255)**	(350)
Gains on sale of securities	**(1,167)**	(911)
Unrealized gains on investments	**(5,420)**	(7,532)
Total deferred tax liabilities	**(30,209)**	(31,177)
Valuation allowance	**(541)**	(689)
Deferred tax liabilities, net	**$ (16,081)**	$ (24,779)

At December 31, 2015 and 2014, PNI had no federal net operating loss carryforwards. PNI is subject to state income tax and has state net operating loss carryforwards at December 31, 2015 and 2014, of approximately $11,273 and $14,344, respectively, of which a portion is expiring each year.

At December 31, 2015 and 2014, a valuation allowance in the amount of $541 and $689, respectively, was established against the deferred tax asset related to the state net operating loss carryforwards, as management currently believes that the benefit from some or all of this deferred tax asset may not be realized.

In the normal course of business, PNI is subject to examination by taxing authorities, and PNI is no longer subject to U.S. federal, state, or local income tax examinations for years before 2010. PNI does not have any current federal tax disputes.

Supplementary Information

Presbyterian Healthcare Services and Affiliates

Combining Balance Sheet

December 31, 2015

	Obligated Group	Presbyterian Network, Inc.	Other Non-Obligated Group Members	Eliminations	Combined
			(In Thousands)		
Assets					
Current assets:					
Cash and cash equivalents	$ 115,258	$ 169,882	$ 756	$ –	$ 285,896
Accounts receivable, net	128,753	–	5,340	(20,726)	113,367
Other receivables	64,068	73,575	1,429	(19,114)	119,958
Inventories, prepaid expenses, and other current assets	30,813	17,261	1,394		49,468
Total current assets	338,892	260,718	8,919	(39,840)	568,689
Assets limited as to use or restricted:					
Designated for long-term purposes	1,319,336	368,425	561	–	1,688,322
Designated for self-insurance funds	119,338	–	–	–	119,338
Restricted by donors	34,807	–	–	–	34,807
Held by trustee	51,838	–	–	–	51,838
Restricted for statutory requirements	–	109,716	–	–	109,716
	1,525,319	478,141	561	–	2,004,021
Property and equipment, net	816,554	477	40,017	–	857,048
Goodwill	3,125	52,501	–	–	55,626
Intercompany (payables) receivables	(15,571)	9,974	30,982	(25,385)	–
Other assets	64,631	5,897	134,665	(119,920)	85,273
Total assets	$2,732,950	$ 807,708	$ 215,144	$ (185,145)	$ 3,570,657

See accompanying note.

Presbyterian Healthcare Services and Affiliates

Combining Balance Sheet (continued)

	Obligated Group	Presbyterian Network, Inc.	Other Non-Obligated Group Members	Eliminations	Combined
			(In Thousands)		
Liabilities and net assets					
Current liabilities:					
Accounts payable	$ 51,800	$ 4,471	$ 1,511	$ –	$ 57,782
Due under Medicaid contract	–	168,296	–	–	168,296
Accrued liabilities	140,236	84,312	4,321	(67,299)	161,570
Medical claims payable	–	143,238	–	(3,841)	139,397
Estimated third-party payor settlements	1,731	–	95	–	1,826
Current portion of long-term debt and capital leases	14,797	–	–	–	14,797
Total current liabilities	208,564	400,317	5,927	(71,140)	543,668
Long-term debt and capital leases, net of current portion	709,972	–	–	–	709,972
Employee benefit plans	198,511	–	–	–	198,511
Self-insurance plans	145,092	–	–	–	145,092
Other liabilities	75,017	30,228	1,787	–	107,032
Total liabilities	1,337,156	430,545	7,714	(71,140)	1,704,275
Net assets:					
Unrestricted	1,358,946	377,163	207,430	(114,005)	1,829,534
Temporarily restricted	25,997	–	–	–	25,997
Permanently restricted	10,851	–	–	–	10,851
Total net assets	1,395,794	377,163	207,430	(114,005)	1,866,382
Total liabilities and net assets	$2,732,950	$ 807,708	$ 215,144	$ (185,145)	$ 3,570,657

See accompanying note.

Presbyterian Healthcare Services and Affiliates

Combining Statement of Operations

Year Ended December 31, 2015

	Obligated Group	Presbyterian Network, Inc.	Other Non-Obligated Group Members	Eliminations	Combined
			(In Thousands)		
Revenues:					
Net premium	$ 406,943	$ 1,814,706	$ –	$ (401,793)	$ 1,819,856
Patient service revenue	1,273,838	–	55,781	(270,176)	1,059,443
Less provision for doubtful accounts	(53,500)	–	(2,981)	–	(56,481)
Net patient service revenue	1,220,338	–	52,800	(270,176)	1,002,962
Other operating revenues	69,712	28,137	9,834	(35,246)	72,437
Total operating revenues	1,696,993	1,842,843	62,634	(707,215)	2,895,255
Expenses:					
Medical claims	199,925	1,516,259	–	(672,092)	1,044,092
Salaries, wages, and employee benefits	774,786	76,754	26,995	(4,898)	873,637
Purchased services and other	274,012	185,644	24,445	(30,225)	453,876
Supplies	239,275	619	894	–	240,788
Professional fees	35,719	1	2,329	–	38,049
Depreciation and amortization	88,805	660	5,147	–	94,612
Interest	24,827	–	59	–	24,886
Total expenses	1,637,349	1,779,937	59,869	(707,215)	2,769,940
Operating income	59,644	62,906	2,765	–	125,315
Other (loss) income:					
Investment income	55,987	14,459	1,147	–	71,593
Changes in unrealized gains on investments	(98,008)	(8,117)	–	–	(106,125)
Loss on bond defeasance	(24,061)	–	–	–	(24,061)
Change in fair value of interest rate swaps	(149)	–	–	–	(149)
Total other (loss) income	(66,231)	6,342	1,147	–	(58,742)
Excess of revenues over expenses before income taxes	(6,587)	69,248	3,912	–	66,573
Provision for income taxes	–	35,081	5	–	35,086
Excess of revenues over expenses	$ (6,587)	$ 34,167	$ 3,907	$ –	$ 31,487

See accompanying note.

EY | Assurance | Tax | Transactions | Advisory

Annual Operating Information

Presbyterian Healthcare Services
All Hospitals
Operating Disclosure Data

	Year Ended				
	2011	**2012**	**2013**	**2014**	**2015**
Hospital Data					
Total Inpatient Discharges	50,724	51,429	53,216	53,078	52,218
Newborn Discharges	7,256	7,302	7,191	6,791	6,787
Inpatient Surgery Discharges	11,142	10,609	10,916	10,536	10,540
Open Heart Surgery Discharges	434	432	440	427	405
ER Visits Resulting in an Admit	19,597	21,397	22,848	25,379	25,528
Observation Discharges	4,216	6,111	5,488	8,404	10,471
Total Inpatient Days	213,390	217,356	234,465	235,817	232,121
Newborn Days	27,527	29,868	28,598	28,649	27,622
Inpatient Surgery Days	53,313	51,962	54,389	55,755	53,804
Total Outpatient Visits	522,791	551,538	556,958	600,966	634,476
ER Visits	194,295	202,849	212,023	228,789	242,964
OP Surgeries	20,157	22,039	22,993	23,043	22,515
Licensed Beds	1,159	1,173	1,171	1,151	1,086
Beds in Service	998	977	973	973	947
Average Length of Stay (days)	4.21	4.23	4.41	4.44	4.45
Percentage Occupancy (of beds in service)	58.7%	61.1%	66.0%	66.4%	67.1%
Medicare Case Mix Index	1.44	1.47	1.57	1.45	1.38
PMG Albuquerque Visits	1,169,003	1,305,928	1,481,555	1,670,274	1,842,565

Presbyterian Healthcare Services
Obligated Group
Operating Disclosure Data

Year Ended

	2011	2012	2013	2014	2015
<u>**Hospital Data**</u>					
Total Inpatient Discharges	48,723	49,413	51,202	51,033	50,243
Newborn Discharges	6,893	6,903	6,828	6,455	6,428
Inpatient Surgery Discharges	10,673	10,270	10,615	10,354	10,312
Total Inpatient Days	208,406	212,215	229,267	230,320	226,560
Newborn Days	27,015	29,250	28,080	28,160	27,087
Inpatient Surgery Days	52,063	51,048	53,640	55,237	53,246
Total Outpatient Visits	469,363	504,154	511,081	556,080	589,913
ER Visits	176,185	183,913	193,740	211,041	224,845
OP Surgeries	18,921	20,719	21,580	22,206	21,953
Licensed Beds	1,106	1,120	1,118	1,098	1,033
Beds in Service	945	924	920	920	894
Average Length of Stay (days)	4.28	4.29	4.48	4.51	4.51
Percentage Occupancy (of beds in service)	60.6%	63.1%	68.3%	68.6%	69.4%
Medicare Case Mix Index	1.46	1.49	1.59	1.47	1.40

Presbyterian Healthcare Services
Central New Mexico
Operating Disclosure Data

	Year Ended				
	2011	**2012**	**2013**	**2014**	**2015**
Hospital Data					
Total Inpatient Discharges	39,119	39,804	41,979	42,261	41,791
Newborn Discharges	5,078	5,185	5,091	4,787	4,798
Inpatient Surgery Discharges	8,721	8,479	8,849	8,828	8,827
Total Inpatient Days	180,415	183,812	195,080	204,265	202,225
Newborn Days	23,714	25,983	24,664	24,915	24,097
Inpatient Surgery Days	43,932	43,685	47,169	49,305	47,749
Total Outpatient Visits	315,653	352,370	377,044	405,620	433,817
ER Visits	116,746	123,209	133,068	146,379	157,723
OP Surgeries	14,236	15,978	17,170	18,244	18,841
Licensed Beds	868	882	886	882	801
Beds in Service	712	691	693	711	692
Average Length of Stay (days)	4.61	4.62	4.65	4.83	4.84
Percentage Occupancy (of beds in service)	69.6%	73.1%	77.1%	78.9%	80.1%
Medicare Case Mix Index	1.52	1.55	1.62	1.54	1.48

Presbyterian Healthcare Services
Regional Hospitals
Operating Disclosure Data

Year Ended

	2011	2012	2013	2014	2015
Hospital Data					
Total Inpatient Discharges	11,605	11,625	11,237	10,817	10,427
Newborn Discharges	2,178	2,117	2,100	2,004	1,989
Inpatient Surgery Discharges	2,421	2,130	2,067	1,708	1,713
Total Inpatient Days	32,975	33,544	39,385	31,552	29,896
Newborn Days	3,813	3,885	3,934	3,734	3,525
Inpatient Surgery Days	9,381	8,277	7,220	6,450	6,055
Total Outpatient Visits	207,138	199,168	179,914	195,346	200,659
ER Visits	77,549	79,640	78,955	82,410	85,241
OP Surgeries	5,921	6,061	5,823	4,799	3,674
Licensed Beds	291	291	285	269	285
Beds in Service	286	286	280	262	255
Average Length of Stay (days)	2.84	2.89	3.50	2.92	2.88
Percentage Occupancy (of beds in service)	31.7%	32.2%	38.5%	33.0%	32.1%
Medicare Case Mix Index	1.11	1.14	1.21	1.04	0.99

Presbyterian Healthcare Services
PHP Membership
Operating Disclosure Data

Year Ended

	2011	2012	2013	2014	2015
PHP Membership					
Commercial	90,010	98,926	95,569	86,760	82,615
Medicare Advantage	31,325	34,040	36,902	38,852	42,585
Medicaid	169,787	166,222	163,502	193,114	213,116
Administrative Services Only	109,416	117,414	123,940	124,329	121,159
Total PHP Membership	400,538	416,602	419,913	443,055	459,475

Presbyterian Healthcare Services
Payor Mix Based on Net Revenue
All Facilities

	2011	2012	2013	2014	2015
COMMERCIAL	41.9%	46.3%	46.4%	44.8%	43.1%
MEDICAID	20.2%	16.6%	15.7%	19.8%	21.5%
MEDICARE	31.3%	30.0%	31.7%	29.7%	30.3%
OTHER	4.4%	4.7%	4.1%	4.2%	3.8%
SELF PAY	2.2%	2.4%	2.1%	1.5%	1.3%

Presbyterian Healthcare Services
Payor Mix Based on Net Revenue
Obligated Group

	2011	2012	2013	2014	2015
COMMERCIAL	42.2%	46.6%	46.8%	44.2%	43.3%
MEDICAID	19.9%	16.4%	15.6%	19.7%	21.2%
MEDICARE	31.4%	29.9%	31.5%	29.5%	30.4%
OTHER	4.4%	4.8%	4.1%	4.1%	3.9%
SELF PAY	2.1%	2.3%	2.0%	2.5%	1.2%

Historic and Pro Forma Coverage of Maximum Annual Debt Service
of the Obligated Group
(dollars in thousands)

	Years Ended December 31				
	2011	2012	2013	2014	2015
Income available for debt service:					
Excess of revenues over expenses	$ (13,123)	$ 137,980	$ 185,637	$ 103,050	$ (6,587)
Plus: Depreciation and amortization	67,931	77,959	80,579	86,379	88,805
Plus: Interest	19,982	23,925	24,135	25,662	24,827
Plus: Loss on bond defeasance	-	-	-	-	24,061
Plus: Changes in unrealized gains and losses on investments, loss on bond defeasance and change in fair market value of swaps	63,233	(67,499)	(71,968)	48,263	98,157
Total income available for debt service	$ 138,023	$ 172,365	$ 218,383	$ 263,354	$ 229,263
Maximum annual debt service ("MADS")	$ 35,534	$ 39,758	$ 39,758	$ 39,758	$ 43,591
Coverage of Historic MADS	3.9	4.3	5.5	6.6	5.3

Debt to Capitalization of the Obligated Group
(dollars in thoursands)

	As of December 31				
	2011	2012	2013	2014	2015
Series 2008A Bonds (1)	151,348	145,957	142,271	137,306	-
Series 2008B Bonds	73,245	71,125	68,945	66,695	64,380
Series 2008C Bonds	73,245	71,125	68,945	66,695	64,380
Series 2008D Bonds	73,255	71,135	68,950	66,705	64,390
Series 2009A Bonds (2)	132,204	132,291	132,378	132,465	132,553
Series 2012A Bonds (3)	-	78,800	78,672	78,543	78,415
Series 2015A Bonds (4)	-	-	-	-	258,535
Note payable to bank	-	15,000	41,000	50,000	50,000
Other, including capital lease obligations and other long term debt	12,226	10,495	8,815	11,347	12,116
Subtotal	515,523	596,928	609,976	609,756	724,769
Less current portion	12,633	13,064	12,973	13,435	14,797
Total long-term debt	502,890	583,864	597,003	596,321	709,972
Unrestricted net assets	618,709	842,323	1,374,812	1,367,161	1,358,946
Total Capitalization	$ 1,121,599	$ 1,426,187	$ 1,971,815	$ 1,963,482	$ 2,068,918
Long-term debt to capitalization	45%	41%	30%	30%	34%

(1) Amount is net of discounts.
(2) Amount is net of discounts. The outstanding par amount of the Series 2009A Bonds is $134,610,000.
(3) Amount includes preminums. The outstanding par amount of the Series 2012A Bonds is $75,000,000.
(4) Amount includes premiums. The outstanding par amount of the Series 2015A Bonds is $237,160,000.

Obligated Group Financial Indicators

Year Ended December 31

		2011	2012	2013	2014	2015
Operating Margin		0.9%	1.3%	2.7%	2.8%	3.5%
Excess Margin	(1)	-1.1%	9.3%	11.4%	6.3%	-0.4%
Adjusted Excess Margin	(2)	3.9%	5.0%	7.3%	9.0%	6.8%
Unrestricted days cash on hand		298	307	353	359	338
Debt to cash flow		4.4	4.0	3.1	2.6	3.5

(1) Includes investment income, changes in unreallized gains and losses on investments, loss on bond defeasance and change in fair market value of interest rate swaps relating to the Series 2008B/C/D Bonds

(2) Excludes changes in unrealized gains and losses on investments, loss on bond defeasance and change in fair market value of interest rate swaps relating to the Series 2008 B/C/D Bonds.

Presbyterian Healthcare Services and Affiliates

Summary Combined Balance Sheet of the Obligated Group

December 31, 2015 and 2014

	2015	2014
	(In Thousands)	
Assets		
Current assets:		
Cash and cash equivalents	$ 115,258	128,359
Accounts receivable, net	128,753	123,864
Other receivables	64,068	43,867
Inventories, prepaid expenses and other	30,813	25,871
Total current assets	338,892	321,961
Assets limited as to use or restricted:		
Designated for long-term purposes	1,319,336	1,282,381
Designated for self-insurance funds	119,338	124,328
Restricted by donors	34,807	34,477
Held by trustee	51,838	7,244
	1,525,319	1,448,430
Property and equipment, net	816,554	773,569
Goodwill	3,125	5,088
Other assets and Intercompany Balances	49,060	41,722
Total assets	$ 2,732,950	2,590,770
Liabilities and net assets		
Current liabilities:		
Accounts payable	$ 51,800	48,693
Accrued liabilities	140,236	126,155
Estimated third-party payer settlements	1,731	2,964
Current portion of long-term debt and capital leases	14,797	13,435
Total current liabilities	208,564	191,247
Long-term debt and capital leases, net of current portion	709,972	596,315
Pension liability	198,511	201,850
Other liabilities	220,109	198,688
Total liabilities	1,337,156	1,188,100
Net assets:		
Unrestricted	1,358,946	1,367,161
Temporarily restricted	25,997	27,143
Permanently restricted	10,851	8,366
Total net assets	1,395,794	1,402,670
Total liabilities and net assets	$ 2,732,950	2,590,770

Presbyterian Healthcare Services and Affiliates

Summary Combined Income Statement of the Obligated Group

	For the Year Ended	
	12/31/2015	12/31/2014
	(In Thousands)	
Revenues		
Net premium	$ 406,943	$390,346
Patient service	1,273,838	1,195,797
Provisions for bad debts	(53,500)	(86,057)
Net patient service	1,220,338	1,109,740
Other operating	69,712	65,097
Total operating revenues	1,696,993	1,565,183
Expenses		
Medical claims	199,925	178,943
Salaries, wages and employee benefits	774,786	728,197
Purchased services and other	274,012	255,932
Professional fees	35,719	35,712
Supplies	239,275	210,438
Depreciation and amortization	88,805	86,379
Interest	24,827	25,662
Total expenses	1,637,349	1,521,263
Operating income	59,644	43,920
Other income:		
Investment income	55,987	107,393
Changes in unrealized gains on investments	(98,008)	(40,330)
Loss on bond defeasance	(24,061)	-
Change in fair value of interest rate swaps	(149)	(7,933)
Total other income	(66,231)	59,130
Excess of revenues over expenses before income taxes	(6,587)	103,050
Provision for income taxes	-	-
Excess of revenues over expenses	$ (6,587)	$103,050

Results of Operations

Years Ended December 31, 2015 and 2014

For the year ended December 31, 2015 total operating income decreased by $45.8 million to $125.3 million (4.3% operating margin) from $171.1 million (6.5% operating margin) in 2014.

Total operating revenue for the year increased by $242.6 million to $2.89 billion from $2.65 billion in 2014. This increase is due to a $148.0 million or 8.9% increase in net premium revenue related primarily to Centennial Care and an increase in net patient service revenue of $93.2 million or 10.2%. The increase in net patient service revenue is due to higher volumes throughout the system driven primarily by outpatient visits and emergency room and lower provision for bad debts.

During 2015, total inpatient discharges for PDS decreased by (1.6%) or (860) discharges compared to 2014 while total inpatient days decreased by (1.6%) or (3,696) days. Total outpatient visits increased by 5.6% or 33,510 visits. Outpatient volumes throughout the system continue to benefit from the shifting of services to an outpatient setting from an inpatient setting as well as an increase in the number of clinics and providers.

Inpatient discharges for the Obligated Group decreased (1.5%) or (790) discharges during 2015 compared to 2014. Inpatient days decreased during this period by (1.6%) or (3,760) days. Outpatient visits increased by 6.0% or 33,833 visits.

Inpatient discharges within CDS decreased during 2015 by (1.1%) or (470) discharges. Inpatient Days were down from prior year by (1.0%) or (2,040) days. Total Outpatient Visits in CDS increased by 7.0% or 28,197 visits.

Inpatient discharges in RDS decreased during 2015 compared to 2014 by (3.6%) or (390) discharges, while total inpatient days decreased by (5.2%) or (1,656) days on a slightly lower average length of stay. Inpatient volumes in the regional hospitals continue to be impacted by provider vacancies. Outpatient visits increased by 2.7% or 5,313 visits during the year, consistent with the overall system trend.

Other operating revenue increased during 2015 compared 2014 by $1.4 million or 2.0% related to an increase in mill levy and gross receipts tax support for the Rust Hospital and certain regional hospitals and more administrative services revenues at the Health Plan, partially offset by less meaningful use dollars received.

The payer mix for PHS experienced a (1.7%) decrease in Commercial net revenue during 2015 compared 2014. Medicaid increased 1.7% while Medicare increased 0.6%. The increase in

Medicaid is due to the coverage expansion built into the Centennial Care program and was the main driver in a (0.6%) decrease in the self pay and other categories.

For the year ended December 31, 2015 total operating expenses increased $288.4 million to $2.77 billion from $2.48 billion in 2014. Medical claims increased $153.8 million or 17.3% due primarily to the expanded Medicaid program under Centennial Care. Salary expense increased $63.0 million or 7.8% compared to 2014 due to increased staffing levels in the Health Plan in support of Centennial Care, higher staffing levels in the hospitals and clinics, and additional medical and support staff for new clinics in Rio Rancho and Santa Fe. Purchased services increased $41.3 million or 10.0% and is due to increased medical malpractice reserves and health plan costs including premium and Affordable Care Act taxes as well as contractual fees and penalties in connection with Centennial Care. Supplies expense increased $29.1 million or 13.7% due to higher drug costs, particularly for drugs to treat hepatitis C and pneumonia. The PHS specialty pharmacy volumes also contributed to the increase in supply costs during 2015. Professional fees were relatively unchanged year over year. Depreciation and amortization expense increased $2.1 million in 2015 compared to 2014 related primarily to the goodwill impairment charge for the Clovis, New Mexico ambulatory surgery center. Interest expense decreased ($0.9) million in 2015 being favorably impacted by the issuance of the 2015A bonds in May 2015 and the refunding of the 2008A bonds which slightly lowered the overall effective interest rate on long term debt.

Investment Income

The Investment Subcommittee of the PHS Board works with an investment consultant to review asset class allocations, select and monitor various professional investment managers and to oversee Presbyterian's investment portfolios in accordance with the investment policy and guidelines.

The unrestricted cash and investments of the Obligated Group at December 31, 2015 consisted of the following:

(In Millions)

Asset Class	Target PHS	PHS	Target Foundation	Foundation	Total
Large Cap Equity	16%	$ 233.0	18%	$ 15.2	$ 248.2
Small Cap Equity	4%	57.1	4.5%	4.4	61.5
International and Emerging Markets	20%	259.6	22.5%	15.8	275.4
Alternatives	20%	259.2	27.5%	21.1	280.3
Fixed income	35%	468.2	27.5%	21.1	489.3
Cash	5%	112.3	- %	2.4	114.7
Total	100%	1,389.4	100%	80.0	1,469.4
Less Restricted Net Assets		-		(34.8)	(34.8)
Total Unrestricted Obligated Group		$ 1,389.4		$ 45.2	$ 1,434.6

Total unrestricted investments for the Obligated Group include the PHS Corporate portfolio and the PHS Foundation portfolio. At December 31, 2015 the unrestricted Obligated Group portfolio totaled $1.43 billion.

Realized investment gains for PHS totaled $30.4 million and $35.4 million for the three month periods ended December 31, 2015 and 2014, respectively, and $71.6 million and $121.1 million for the years ended December 31, 2015 and 2014, respectively. The combined investment income and changes in unrealized gains on investments for 2015 was a loss of ($34.5) million compared to a gain of $81.8 million for 2014. The investment returns for the PHS Corporate and Foundation portfolios were 1.39% and 1.30%, respectively for the quarter ended December 31, 2015 and (2.21%) and (2.04%), respectively, for the years ended December 31, 2015 and 2014.

Liquidity and Capital Resources

On a combined basis, unrestricted cash and investments of PHS totaled $1.97 billion as of December 31, 2015, an increase of $165 million from December 31, 2014.

On May 19, 2015 PHS issued the 2015 Series A Revenue Bonds with a par value of $237.2 million. Proceeds of the bonds were used to refund and defease the majority of the 2008A Revenue Bonds and provide approximately $118 million to fund the construction or improvement of various healthcare facilities throughout the PHS system. Prior to the issuance of the 2015A bonds PHS used $18 million of existing cash to fund an escrow account to refund and defease the 2008A Revenue Bonds not refunded and defeased by the 2015A bonds. The pre-refunding of the 2008A bonds resulted in a loss on early redemption of $24.1 million which is included in non-operating income (loss) on the statement of operations. The long term savings of the lower effective interest rate of the 2015A bonds produced a net present value of $10 million which will be realized through a lower effective interest rate going forward. At December 31, 2015, the unspent funds remaining in the restricted project account totaled $51.8 million.

Cash provided by operating activities totaled $134.2 million for the year ended December 31, 2015 compared to $212.0 million in 2014. Net cash used in investing activities was $184.5 million, including capital expenditures of $133.9 million, during 2015 compared to a net used of $96.4 million, including capital expenditures of $116.8 million, for 2014. Total capital expenditures for fiscal 2016 are expected to approximate $150 million which are anticipated to be financed from a combination of cash flow from operations, and the remaining proceeds from the 2015A Bonds.

Days cash on hand for PHS and the Obligated Group was 269 days and 338 days, respectively, as of December 31, 2015, compared to 276 days and 359 days, respectively, at December 31, 2014.