08-043

ORIGINAL

ILLINOIS HEALTH FACILITIES PLANNING BOARD

APPLICATION FOR PERMIT

February 2003 EDITION

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"The Illinois Department of Public Health does not discriminate on the basis of handicap in admission or access to, or treatment or employment in its programs and activities in compliance with Section 504 of the Rehabilitation Act of 1973, as amended. The Equal Employment Opportunity Officer is responsible for coordination of compliance efforts; voice (217) 785-2034; TTY (217) 785-2088."

ILLINOIS HEALTH FACILITIES PLANNING BOARD
525 WEST JEFFERSON STREET
SPRINGFIELD, ILLINOIS 62761-0001
(217) 782-3516

RECEIVED

JUN 06 2008

HEALTH FACILITIES PLANNING BOARD

INSTRUCTIONS FOR COMPLETION OF THE APPLICATION FOR PERMIT

The Application for Permit form is to be used for all proposed construction or modification projects (including the acquisition of major medical equipment) subject to the permit requirements of the Illinois Health Facilities Planning Act. Persons making application should have and refer to the Planning Act and the rules promulgated thereunder (77 IAC 1100 et. seq.). This application form does not supersede any of those rules and requirements that are currently in effect.

The application form is divided into several sections, dealing with information requirements and review criteria for Parts 1110 and 1120. Complete and submit ONLY those sections along with the required attachments that are applicable to the type of project proposed. Questions concerning completion of this form may be directed to the Health Facilities Planning Board staff at (217) 782-3516. Copies of this application form are available on computer diskette and by electronic mail.

1. Please observe the following general requirements with respect to completion of the application:

   A. Use this form as written and formatted.

   B. Submit only those sections of the application form that are applicable to the proposed project. Attachments for each section should be appended after the last page of that section. Begin each attachment on a separate sheet and print or type the attachment identification in the lower right-hand corner of each attachment page.

   C. Provide all information upon 8 ½"x11" paper and print or type the information only on one side of the page. All documents must be single sided and size 8 ½" by 11".

   D. Information to be considered must be included with the applicable section attachments. References to appended material not included within the appropriate section will not be considered.

   E. Upon completion of the application, number all pages consecutively at the bottom center of each page.

   F. The application must be signed by the authorized representative(s) of each applicant entity.

   G. If the application is bound, use only three-ring notebooks. It is recommended that only the copy containing the original signatures be placed in such a notebook.

   Failure to follow these general requirements may result in the application being declared incomplete. In addition, failure to provide certain required information (e.g. not providing a site for the proposed project, or having an invalid entity listed as the applicant) may result in the application being declared null and void. Applicants are advised to read Part 1130 with respect to completeness (1130.620(c) and other requirements.

2. In addition to the requirements previously noted, applicants must comply with the following requirements:

   A. FLOOD PLAIN REQUIREMENTS. Before an application for permit involving construction will be deemed complete, the applicant must provide documentation from the Division of Water Resources of the Illinois Department of Transportation (217/333-0447) that the project site is or is not in a flood plain, and that the location of the proposed project complies with the Flood Plain Rule under Executive Order #4, 1979.

   B. HISTORICAL PRESERVATION REQUIREMENTS. In accordance with the requirements of the Illinois Historic Resources Preservation Act, the Health Facilities Planning Board is required to advise the Illinois Historic Preservation Agency of any projects that could affect historic resources. Specifically the Preservation Act provides for a review by the Historic Preservation Agency to determine if certain projects may impact upon historic resources. Such types of projects include:
      i. Projects involving demolition of any structures; or
      ii. Construction of new buildings; or

iii. Modernization of existing buildings.

Should any of these or other types of projects (including those for acquisition of major medical equipment) result in changes in the character or use of historic property or if there is any historic property located in an "area of potential effects," review by the Historic Preservation Agency is required. "Area of potential effects" means the geographical area or areas within which an undertaking may cause changes in the character or use of historic properties.

In order to assure that any proposed construction or modernization project subject to certificate of need review is not delayed by the requirements of the Historic Resources Preservation Act, please submit the following information to the Illinois Historic Preservation Agency (Preservation Services Division, Old State Capitol, Springfield, Illinois 62701) so known or potential cultural resources within the project area can be identified, and the project's effects on significant properties can be evaluated:

i. General project description and address;
ii. Topographic or metropolitan map showing the general location of the project;
iii. Photographs of any standing buildings/structures within the project area;
iv. Addresses for buildings/structures if present.

The Historic Preservation Agency will provide a determination letter concerning the applicability of the Preservation Act. Include the determination letter or comments from the Historic Preservation Agency with the submission of the application for permit. Information concerning the Historic Resources Preservation Act may be obtained by calling (217) 782-4836.

If a determination letter from the Historic Preservation Agency is not submitted, the following information **MUST** be submitted with the application for permit:

i. Detailed map/site plans indicating the complete project area.
ii. 35mm photographs of all buildings/structures within the project area, with addresses and construction date on the back of each photo.
iii. Project narrative, with emphasis on the consequences of the plan on the building/structures within the project area.
iv. Listing of federal and other state agencies which potentially would be involved in the project, either through funding, licensing, permitting or other forms of official support/approval.

Failure to provide a determination letter from the Historic Preservation Agency that the project is not subject to the Historic Resources Preservation Act or failure to provide the required information detailed above may result in delays in processing the application for permit.

3. An application processing fee (refer to 77 IAC 1130.620(f)(1)) for the determination of the application processing fee) is required to be submitted with most applications. If a fee is applicable, an initial fee of $2,500 <u>**MUST**</u> accompany the application. The application is incomplete and review will not be initiated if the initial fee is not submitted. The State Agency will inform applicants of the amount of the fee balance, if any, that must be submitted. **Payment must be by check or money order and must be made payable to the Illinois Department of Public Health.**

4. Submit an original and one copy of all applicable sections of the application, including all attachments thereto. The original must contain original signatures in the certification portion of this form. <u>SUBMIT ALL COPIES TO</u>: Executive Secretary, Illinois Health Facilities Planning Board, 525 West Jefferson Street - Second Floor, Springfield, Illinois 62761-0001

ILLINOIS HEALTH FACILITIES PLANNING BOARD
APPLICATION FOR PERMIT

SECTION I. IDENTIFICATION, GENERAL INFORMATION, AND CERTIFICATION (IDEN)

This section must be completed for all projects.

A. Facility/Project Identification

Facility Name Mercy Hospital and Medical Center

B. Applicant Identification (provide for each co-applicant [refer to Part 1130.220] and insert after this page)

Exact Legal Name Mercy Hospital and Medical Center
Address 2525 S Michigan Ave.
Chicago, IL 60616 Name of Registered Agent Sister Sheila Lyne
Name of Chief Executive Officer Sister Sheila Lyne Title President / CEO
CEO Address 2525 S. Michigan Ave., Chicago, IL 60616 Telephone No. (312) 567-2100
Type of Ownership: ☒ Non-profit Corporation ☐ For-profit Corporation ☐ Limited Liability Company ☐ Partnership ☐ Governmental ☐ Sole Proprietorship ☐ Other (specify)

Corporations and limited liability companies must provide an Illinois certificate of good standing; partnerships must provide the name of the state in which organized and the name and address of each partner specifying whether each is a general or limited partner.

APPEND DOCUMENTATION AS ATTACHMENT IDEN-1 AFTER THE LAST PAGE OF THIS SECTION.

C. Primary Contact Person (person who is to receive correspondence or inquiries during the review period)

Name Richard Cerceo Title Chief Operating Officer
Company Name Mercy Hospital and Medical Center
Address 2525 S. Michigan Ave., Chicago, IL 60616
Telephone No. (312) 567-2255 E-mail rcerceo@mercy-chicago.org
Address 2525 S. Michigan Ave., Chicago, IL 60616 Fax Number (312)567-7089

D. Additional Contact Person (person such as consultant, attorney, financial representative, registered agent, etc. who also is authorized to discuss application and act on behalf of applicant)

Name Tom Garvey Title Chief Financial Officer
Company Name Mercy Hospital and Medical Center
Address 2525 S. Michigan Ave., Chicago, IL 60616
Telephone No. (312) 567-2580
E-mail Address tgarvey@mercy-chicago.org Fax Number (312) 567-7089

E. Post Permit Contact Person (person to whom all correspondence and inquiries pertaining to the project subsequent to permit issuance are to be directed)

Name Richard Cerceo Title Chief Operating Officer
Company Name Mercy Hospital and Medical Center
Address 2525 S. Michigan Ave., Chicago, IL 60616
Telephone No. (312) 567-2255
E-mail Address rcerceo@mercy-chicago.org Fax Number (312) 567-7089

ILLINOIS HEALTH FACILITIES PLANNING BOARD
APPLICATION FOR PERMIT

SECTION I. IDENTIFICATION, GENERAL INFORMATION, AND CERTIFICATION (IDEN)

This section must be completed for all projects.

A. Facility/Project Identification

Facility Name Mercy Hospital and Medical Center

B. Applicant Identification (provide for each co-applicant [refer to Part 1130.220] and insert after this page)

Exact Legal Name Mercy Health System of Chicago
Address 2525 S. Michigan Ave., Chicago, IL 60616
Name of Registered Agent Sister Sheila Lyne
Name of Chief Executive Officer Sister Sheila Lyne Title President/CEO
CEO Address 2525 S. Michigan Ave., Chicago, IL 60616 Telephone No. (312)567-2100
Type of Ownership: ☒ Non-profit Corporation ☐ For-profit Corporation ☐ Limited Liability Company ☐ Partnership ☐ Governmental ☐ Sole Proprietorship ☐ Other (specify)

Corporations and limited liability companies must provide an Illinois certificate of good standing; partnerships must provide the name of the state in which organized and the name and address of each partner specifying whether each is a general or limited partner.

APPEND DOCUMENTATION AS ATTACHMENT IDEN-1 AFTER THE LAST PAGE OF THIS SECTION.

C. Primary Contact Person (person who is to receive correspondence or inquiries during the review period)

Name ____________ Title ____________
Company Name ____________
Address ____________
Telephone No. ( ) ____________ E-mail ____________
Address ____________ Fax Number ( ) ____________

D. Additional Contact Person (person such as consultant, attorney, financial representative, registered agent, etc. who also is authorized to discuss application and act on behalf of applicant)

Name ____________ Title ____________
Company Name ____________
Address ____________
____________ Telephone No. ( ) ____________
E-mail Address ____________ Fax Number ( ) ____________

E. Post Permit Contact Person (person to whom all correspondence and inquiries pertaining to the project subsequent to permit issuance are to be directed)

Name ____________ Title ____________
Company Name ____________
Address ____________
____________ Telephone No. ( ) ____________
E-mail Address ____________ Fax Number ( ) ____________

F. Site Ownership (complete this information for each applicable site and insert after this page)

Exact Legal Name of Person Who Owns Site Mercy Hospital and Medical Center
Address of Site Owner 2525 S. Michigan Ave., Chicago, IL 60616
Street Address or Legal Description of Site 2525 S. Michigan Ave., Chicago, IL 60616

G. Operating Entity/Licensee (complete this information for each applicable facility and insert after this page)

Exact Legal Name Mercy Hospital and Medical Center
Address 2525 S. Michigan Ave., Chicago, IL 60616

Type of Ownership: ☒ Non-profit Corporation ☐ For-profit Corporation ☐ Limited Liability Company ☐ Partnership ☐ Governmental ☐ Sole Proprietorship ☐ Other (specify)

Corporations and limited liability companies must provide an Illinois certificate of good standing; partnerships must provide the name of the state in which organized and the name and address of each partner specifying whether each is a general or limited partner.

APPEND DOCUMENTATION AS ATTACHMENT IDEN-2 AFTER THE LAST PAGE OF THIS SECTION.

H. Organizational Relationships

Provide (for each co-applicant) an organization chart containing the name and relationship of any person who is related (related person is defined in Part 1130.140). If the related person is participating in the development or funding of the project, describe the interest and the amount and type of any financial contribution.

APPEND DOCUMENTATION AS ATTACHMENT IDEN-3 AFTER THE LAST PAGE OF THIS SECTION.

I. Status of Previous Certificate of Need Projects

Provide the project number for any of the applicant's projects that have received permits but are not yet complete (completion is defined in Part 1130.140) and provide the current status of the project. If all projects are complete, indicate NONE:

NONE

J. Flood Plain Requirements (refer to instructions for completion of this application)

Provide documentation regarding compliance with the Flood Plain requirements of Executive Order #4, 1979.

APPEND DOCUMENTATION AS ATTACHMENT IDEN-4 AFTER THE LAST PAGE OF THIS SECTION.

K. Historic Resources Preservation Act Requirements (refer to instructions for completion of this application)

Provide documentation regarding compliance with the requirements of the Historic Resources Preservation Act.

APPEND DOCUMENTATION AS ATTACHMENT IDEN-5 AFTER THE LAST PAGE OF THIS SECTION.

L. Project Classification (check those applicable, refer to Part 1110.40 and Part 1120.20.b)

1. Part 1110 Classification
   - ☒ Substantive
   - ☐ Non-substantive

2. Part 1120 Applicability or Classification: (check one only)
   - ☐ Part 1120 Not Applicable
   - ☐ Category A Project
   - ☐ DHS or DVA Project
   - ☒ Category B Project

M. Narrative Description

Provide in the space below a brief narrative description of the project. Explain what is to be done, NOT why it is being done. Include the rationale as to the project's classification as substantive or non-substantive. If the project site does NOT have a street address, include a legal description of the site.

See Attached.

Section I, Item M. Narrative Description

Mercy Hospital and Medical Center (the "Hospital") is an acute care hospital sponsored by the Sisters of Mercy of the Americas. The Hospital has been serving Chicago since 1852 and currently serves 38% Public Aid patients (75% of the Hospital's Birthing Center patients are Public Aid beneficiaries). The Hospital, together with its corporate member, Mercy Health System of Chicago (collectively, the "Applicants") proposes to modernize its Birthing Center (OB/GYN), the Cardiac Care Unit ("CCU") of its intensive care department, and its Gastrointestinal Laboratories ("GI Labs"). Because two of these units will be relocated in part, the Applicants also plan to renovate a small number of medical/surgical beds and certain non-clinical support space, as these areas are impacted by the modernization of the CCU and the GI Labs, respectively. Due to the renovations, the Hospital is required to update its S-27 Air Handler, a non-clinical project. The final non-clinical portion of the project is the installation of a Hospital-wide sprinkler system and an upgrade to the Hospital's fire alarm system, as required by various legal requirements, discussed below.

This project will not add any beds or new categories of service and is strictly a modernization of portions of the Hospital.

Birthing Center Modernization (OB/GYN)

The modernization to the Hospital's Birthing Center will consist of reconfiguring and renovating the Labor Delivery/Receiving rooms, nursery, and post-partum care areas, in addition to the required support spaces for the unit. Specifically, the Hospital will renovate the unit to add two single post-partum rooms, one of which will be an isolation post-partum room (for a total of 22) and add 2 ante-partum rooms for complicated long stay labor candidates (for a total of 2). The hospital will decrease the number of nursery bassinets by 8 (for a total of 20) as, following the renovation, many newborns will be "rooming-in" in the post-partum rooms. The nursery will also be reconfigured to re-apportion the split between well babies, Special Care and NICU needs. An isolation nursery will be included. The modernization will eliminate one c-section room (for a total of 2), eliminate 2 staff offices (for a total of 4), and eliminate 7 on-call rooms (for a total of 2). Certain staff offices will be relocated to other areas of the building. A new nurse station will be constructed in the core of the birthing area with easy access to all birthing rooms and a small conference area for staff meetings. The number of LDR rooms, the prep/recovery unit, the exam/triage rooms, and the large conference room will not increase or decrease. The LDR rooms will be modernized to include private bathtubs and the post-partum rooms will be modernized to accommodate the "rooming-in" of newborns. In conjunction with the modernization, the HVAC, medical gases system, plumbing, and electrical will be updated to correspond to the renovation. The Hospital has 30 licensed OB/GYN beds; this will not change. The square footage of the unit also will not change. The existing Birthing Center will remain in operation throughout the duration of the renovation.

CCU Modernization (Intensive Care)

The CCU is a specialty care unit within the intensive care unit that is designed to administer care to post-procedure cardiac patients. The modernization of the CCU proposes to relocate a portion of the unit, consolidating the unit at one end of the eleventh floor. The Hospital has 30 licensed intensive care beds, 14 of which are staffed as surgical intensive care beds and 16 of which are currently staffed as CCU intensive care beds. The Hospital proposes to renovate the unit, which will include the addition of three isolation rooms (for a total of four), two of which will be ADA compliant. The patient rooms will be renovated, and a family lounge, conference room, small nurses' station, physician consultation area, and data room will be added. Following the renovation, the Hospital will staff 14 cardiac intensive care beds. In conjunction with the modernization, the mechanical, electrical, lighting, power, and plumbing systems (as well as a few specialized systems, such as the nurse call system, intercom system, and television system) serving the CCU will be updated. The surgical portion of the intensive care unit ("SICU") is not being renovated and the number of licensed intensive care beds (30) will not change. Portions of the CCU will remain in operation throughout the duration of the renovation.

Medical/Surgical Modernization

In conjunction with the CCU modernization, the Applicants propose to renovate five of the adjacent medical/surgical beds vacated by the relocated CCU, as well as a nurses' station. No medical/surgical beds are being added and the Hospital's remaining medical/surgical beds will remain in operation throughout the duration of the renovation.

GI Lab Modernization

The GI Lab Department is a specialty care unit within the Hospital's ambulatory surgery department dedicated solely to performing GI procedures. The modernization of the GI Labs will relocate and consolidate these labs to the east end of the ambulatory surgery unit. Four procedure rooms will be modernized, along with eight induction/recovery bays, a central nurse's station, soiled and clean utility rooms, scope cleaning and storage facilities, and miscellaneous required support functions. In conjunction with the modernization, the mechanical, electrical, lighting, power, and plumbing systems (as well as a few specialized systems, such as the nurse call system, intercom system, and television system) serving the GI Labs will be updated. This modernization will not increase the number of the Hospital's licensed beds, nor will it increase the square footage of the GI Labs. The project will be executed in phases and the GI Labs will remain in operation throughout the modernization.

Non-clinical Modernization

In conjunction with the partial relocation of the GI Labs and the CCU, a staff locker, toilet room, soiled and clean support areas, administrative offices, a storage area, a women's locker room, and a nurses' lounge will be renovated. The Hospital's S-27 Air Handler will also be updated, which is a non-clinical project, as it is required by the Life Safety Code.

Sprinkler System/Fire Alarm Upgrade (Non-clinical)

The project also includes the installation of a Hospital-wide sprinkler system and an upgrade to the Hospital's fire alarm system. This portion is non-clinical and necessary to comply with the Life Safety Code, the Chicago High-Rise Sprinkler Ordinance, and the Life Safety Ordinance of the Chicago Fire Department and Fire Prevention Bureau.

Project Cost

The estimated project cost for the modernization of the Birthing Unit, the GI Labs, the CCU, and the related clinical modernization is $14,966,707. The estimated cost of the non-clinical portion of the project (non-clinical space, sprinklers and fire alarm upgrade) is $14,062,449. The estimated total project cost is $29,029,156.

Project Classification

The project is classified as substantive, as the total project cost of $29,029,156 exceeds the Illinois Health Facilities Planning Board review threshold. The project will be financed by the Department of Housing and Urban Development (HUD) under the Section 242 Mortgage Insurance Program. The first full year of operation for the modernized areas will be 2011.

N. Project Costs and Sources of Funds

Complete the following table listing all costs (refer to Part 1120.110) associated with the project. When a project or any component of a project is to be accomplished by lease, donation, gift, or other means, the fair market or dollar value (refer to Part 1190.40.b) of the component must be included in the estimated project cost. If the project contains components that are not related to the provision of health care, complete an additional table for the portions that are solely for health care and insert that table following this page (e.g. separate a nursing home's costs from the components of a retirement community; separate patient care area costs from a hospital project that includes a parking garage.

HEALTH CARE PROJECT:

PROJECT COST AND SOURCES OF FUNDS	
Preplanning Costs	
Site Survey and Soil Investigation	
Site Preparation	417,318
Off Site Work	
New Construction Contracts	
Modernization Contracts	10,361,630
Contingencies	905,574
Architectural/Engineering Fees	1,146,329
Consulting and Other Fees	77,814
Movable or Other Equipment (not in construction contracts)	2,058,042
Bond Issuance Expense (project related)	
Net Interest Expense During Construction (project related)	
Fair Market Value of Leased Space or Equipment	
Other Costs To Be Capitalized	
Acquisition of Building or Other Property (excluding land)	
ESTIMATED TOTAL PROJECT COST	14,966,707
Cash and Securities	2,135,856
Pledges	
Gifts and Bequests	
Bond Issues (project related)	12,830,851
Mortgages	
Leases (fair market value)	
Governmental Appropriations	
Grants	
Other Funds and Sources	
TOTAL FUNDS	14,966,707

N. Project Costs and Sources of Funds

Complete the following table listing all costs (refer to Part 1120.110) associated with the project. When a project or any component of a project is to be accomplished by lease, donation, gift, or other means, the fair market or dollar value (refer to Part 1190.40.b) of the component must be included in the estimated project cost. If the project contains components that are not related to the provision of health care, complete an additional table for the portions that are solely for health care and insert that table following this page (e.g. separate a nursing home's costs from the components of a retirement community; separate patient care area costs from a hospital project that includes a parking garage.

NON-CLINICAL PROJECT:

PROJECT COST AND SOURCES OF FUNDS	
Preplanning Costs	
Site Survey and Soil Investigation	
Site Preparation	
Off Site Work	
New Construction Contracts	
Modernization Contracts	14,062,449
Contingencies	
Architectural/Engineering Fees	
Consulting and Other Fees	
Movable or Other Equipment (not in construction contracts)	
Bond Issuance Expense (project related)	
Net Interest Expense During Construction (project related)	
Fair Market Value of Leased Space or Equipment	
Other Costs To Be Capitalized	
Acquisition of Building or Other Property (excluding land)	
ESTIMATED TOTAL PROJECT COST	14,062,449
Cash and Securities	
Pledges	
Gifts and Bequests	
Bond Issues (project related)	14,062,449
Mortgages	
Leases (fair market value)	
Governmental Appropriations	
Grants	
Other Funds and Sources	
TOTAL FUNDS	14,062,449

O. Related Project Costs

1. Provide the following information, as applicable, with respect to any land related to the project that will be or has been acquired during the last two calendar years:

   ☒ No land acquisition is related to project; Purchase Price $__________; Fair Market Value$__________

2. Does the project involve establishment of a new facility or a new category of service? ☐ Yes ☒ No

   If yes, provide the dollar amount of all non-capitalized operating start-up costs (including operating deficits) through the first full fiscal year when the project achieves or exceeds the target utilization specified in Part 1100.

   Estimated start-up costs and operating deficit cost is $ __________

P. Project Status and Completion Schedules

1. Indicate the stage of the project's architectural drawings:

   ☐ None or not applicable ☐ Schematics ☒ Preliminary ☐ Final Working

2. Provide the following dates (indicate N/A for any item that is not applicable):

   25% of project costs expended June 2009 50% of project costs expended January 2010
   75% of project costs expended June 2010 95% of project costs expended September 2010
   100% of project costs expended January 2011 Midpoint of construction date January 2010
   Anticipated project completion date (refer to Part 1130.140) January 2011

3. Indicate the following with respect to project expenditures or to obligation (refer to Part 1130.140):
   - ☐ Purchase orders, leases, or contracts pertaining to the project have been executed;
   - ☐ Project obligation is contingent upon permit issuance. Provide a copy of the contingent "certification of obligation" document, highlighting any language related to CON contingencies.
   - ☒ Project obligation will occur after permit issuance.

APPEND DOCUMENTATION AS ATTACHMENT INFO-6 AFTER THE LAST PAGE OF THIS SECTION.

Q. Cost/Space Requirements

Provide in the format of the following example the gross square footage (GSF) and the attributable portion of total project cost for each department/area. Identify each piece of major medical equipment. The sum of the department costs MUST equal the total estimated project costs. Indicate if any space is being reallocated for a different purpose. Include outside wall measurement plus the department or area's portion of the surrounding circulation space. Indicate the proposed use of any vacated space.

		Gross Square Feet		Amount of Proposed Total GSF That Is:			
Department/Area	Cost	Existing	Proposed	New Const.	Remodeled	As is	Vacated Space
Dietary	$1,150,000	3,000	6,000	3,000	1,000	2,000	
Radiation Therapy	3,250,000*	4,000(1)	5,500	5,500			
Medical Records	300,000	2,500	6,500		4,000(1)	2,500	
TOTAL	4,700,000	9,500	18,000	8,500	5,000	4,500	

*Includes $1,500,000 for an 18 MEV linear accelerator
(1) Existing radiation therapy space will be vacated and remodeled and converted to medical records.

APPEND DOCUMENTATION AS ATTACHMENT INFO-7 AFTER THE LAST PAGE OF THIS SECTION.

R. Facility Bed Capacity and Utilization

1. Complete the following chart as applicable. Complete a separate chart for each facility that is part of the project and insert following this page. Provide the existing bed capacity and utilization data for the latest 12 month period for which data is available. Any bed capacity discrepancy from the Inventory will result with the application being deemed incomplete.

FACILITY NAME Mercy Hospital and Medical Center CITY Chicago

REPORTING PERIOD DATES: From January 1, 2007 to December 31, 2007

Category of Service		Existing Beds	Number of Admissions	Patient Days	Bed Changes	Proposed Beds
Medical/Surgical		289	8,595	36,739	0	289
Pediatrics		37	345	3,916	0	37
Obstetrics		30	3,260	6,697	0	30
Intensive Care		30	1,539	5,466	0	30
Neonatal ICU		0	0	0	0	0
Acute Mental Illness		39	1,037	6,793	0	39
Rehabilitation		24	354	3,138	0	24
Nursing Care		0	0	0	0	0
Sheltered Care		0	0	0	0	0
Other (identify)		0	0	0	0	0
Other (identify)		0	0	0	0	0
Other (identify)		0	0	0	0	0
TOTALS		449	15,130	62,749	0	449

2. Is the facility certified for participation in the Medicare "swing bed" (i.e. acute care beds certified for extended care) program? ______Yes ___X___No

3. For the following categories of service, indicate the number of existing beds that are Medicare certified and the number of existing beds that are Medicaid certified (if none, so indicate):

Service	# Medicare Beds	#Medicaid Beds
Nursing Care	0	0
ICF/DD Adult	0	0
Children DD	0	0

S. **Certification**

The application must be signed by the authorized representative(s) of the applicant entity. The authorized representative(s) are in the case of a corporation, any two of its officers or members of its board of directors; in the case of a limited liability company, any two of its managers or members (or the sole manager or member when two or more managers or members do not exist); in the case of a partnership, two of its general partners (or the sole general partner when two or more general partners do not exist); in the case of estates and trusts, two of its beneficiaries (or the sole beneficiary when two or more beneficiaries do not exist); and in the case of a sole proprietor, the individual that is the proprietor. The signature(s) must be notarized. If the application has co-applicants, a separate certification page must be completed for each co-applicant and inserted following this page. One copy of the application must have the ORIGINAL signatures for all persons that sign for the applicant and for each of the co-applicants.

This Application for Permit is filed on behalf of Mercy Hospital and Medical Center *** in accordance with the requirements and procedures of the Illinois Health Facilities Planning Act. The undersigned certifies that he or she has the authority to execute and file this application for permit on behalf of the applicant entity. The undersigned further certifies that the data and information provided herein, and appended hereto, are complete and correct to the best of his or her knowledge and belief. The undersigned also certifies that the permit application fee required for this application is sent herewith or will be paid upon request.**

Sheila Lyne
Signature

Printed Name SR. SHEILA LYNE

Printed Title CEO AND PRESIDENT

Notarization:
Subscribed and sworn to before me
this 16th day of May 2008

Maria Cecilia Jackson
Signature of Notary

Seal

OFFICIAL SEAL
MARIA CECILIA JACKSON
NOTARY PUBLIC - STATE OF ILLINOIS
MY COMMISSION EXPIRES 04/07/12

Thomas J. Garvey
Signature

Printed Name THOMAS J. GARVEY

Printed Title ASSISTANT TREASURER

Notarization:
Subscribed and sworn to before me
this _____ day of _____________

____
Signature of Notary

Seal

*Insert EXACT legal name of the applicant

S. **Certification**

The application must be signed by the authorized representative(s) of the applicant entity. The authorized representative(s) are in the case of a corporation, any two of its officers or members of its board of directors; in the case of a limited liability company, any two of its managers or members (or the sole manager or member when two or more managers or members do not exist); in the case of a partnership, two of its general partners (or the sole general partner when two or more general partners do not exist); in the case of estates and trusts, two of its beneficiaries (or the sole beneficiary when two or more beneficiaries do not exist); and in the case of a sole proprietor, the individual that is the proprietor. The signature(s) must be notarized. If the application has co-applicants, a separate certification page must be completed for each co-applicant and inserted following this page. One copy of the application must have the ORIGINAL signatures for all persons that sign for the applicant and for each of the co-applicants.

This Application for Permit is filed on behalf of Mercy Health System of Chicago *** in accordance with the requirements and procedures of the Illinois Health Facilities Planning Act. The undersigned certifies that he or she has the authority to execute and file this application for permit on behalf of the applicant entity. The undersigned further certifies that the data and information provided herein, and appended hereto, are complete and correct to the best of his or her knowledge and belief. The undersigned also certifies that the permit application fee required for this application is sent herewith or will be paid upon request.**

Sheila Lyne
Signature

Printed Name SR. SHEILA LYNE

Printed Title CEO and President

Notarization:
Subscribed and sworn to before me
this 16th day of May 2008
Maria Cecilia Jackson
Signature of Notary

Seal

OFFICIAL SEAL
MARIA CECILIA JACKSON
NOTARY PUBLIC - STATE OF ILLINOIS
MY COMMISSION EXPIRES:04/07/12

Thomas J. Garvey
Signature

Printed Name THOMAS J. GARVEY

Printed Title ASSISTANT TREASURER

Notarization:
Subscribed and sworn to before me
this ____ day of ____________

Signature of Notary

Seal

*Insert EXACT legal name of the applicant

File Number 0114-154-6

STATE OF ILLINOIS
OFFICE OF THE SECRETARY OF STATE

To all to whom these Presents Shall Come, Greeting:

I, Jesse White, Secretary of State of the State of Illinois, do hereby certify that

MERCY HOSPITAL AND MEDICAL CENTER, A DOMESTIC CORPORATION, INCORPORATED UNDER THE LAWS OF THIS STATE ON JUNE 21, 1852, APPEARS TO HAVE COMPLIED WITH ALL THE PROVISIONS OF THE GENERAL NOT FOR PROFIT CORPORATION ACT OF THIS STATE, AND AS OF THIS DATE, IS IN GOOD STANDING AS A DOMESTIC CORPORATION IN THE STATE OF ILLINOIS.

In Testimony Whereof, *I hereto set my hand and cause to be affixed the Great Seal of the State of Illinois, this* 31ST *day of* MARCH *A.D.* 2008 .

SEAL OF THE STATE OF ILLINOIS AUG. 26TH 1818

Authentication #: 0809100854
Authenticate at: http://www.cyberdriveillinois.com

Jesse White
SECRETARY OF STATE

File Number 5257-458-7

STATE OF ILLINOIS
OFFICE OF THE SECRETARY OF STATE

To all to whom these Presents Shall Come, Greeting:

I, Jesse White, Secretary of State of the State of Illinois, do hereby certify that

MERCY HEALTH SYSTEM OF CHICAGO, A DOMESTIC CORPORATION, INCORPORATED UNDER THE LAWS OF THIS STATE ON NOVEMBER 20, 1981, APPEARS TO HAVE COMPLIED WITH ALL THE PROVISIONS OF THE GENERAL NOT FOR PROFIT CORPORATION ACT OF THIS STATE, AND AS OF THIS DATE, IS IN GOOD STANDING AS A DOMESTIC CORPORATION IN THE STATE OF ILLINOIS.

In Testimony Whereof, *I hereto set my hand and cause to be affixed the Great Seal of the State of Illinois, this* 27TH *day of* MARCH *A.D.* 2008 .

Authentication #: 0808701096

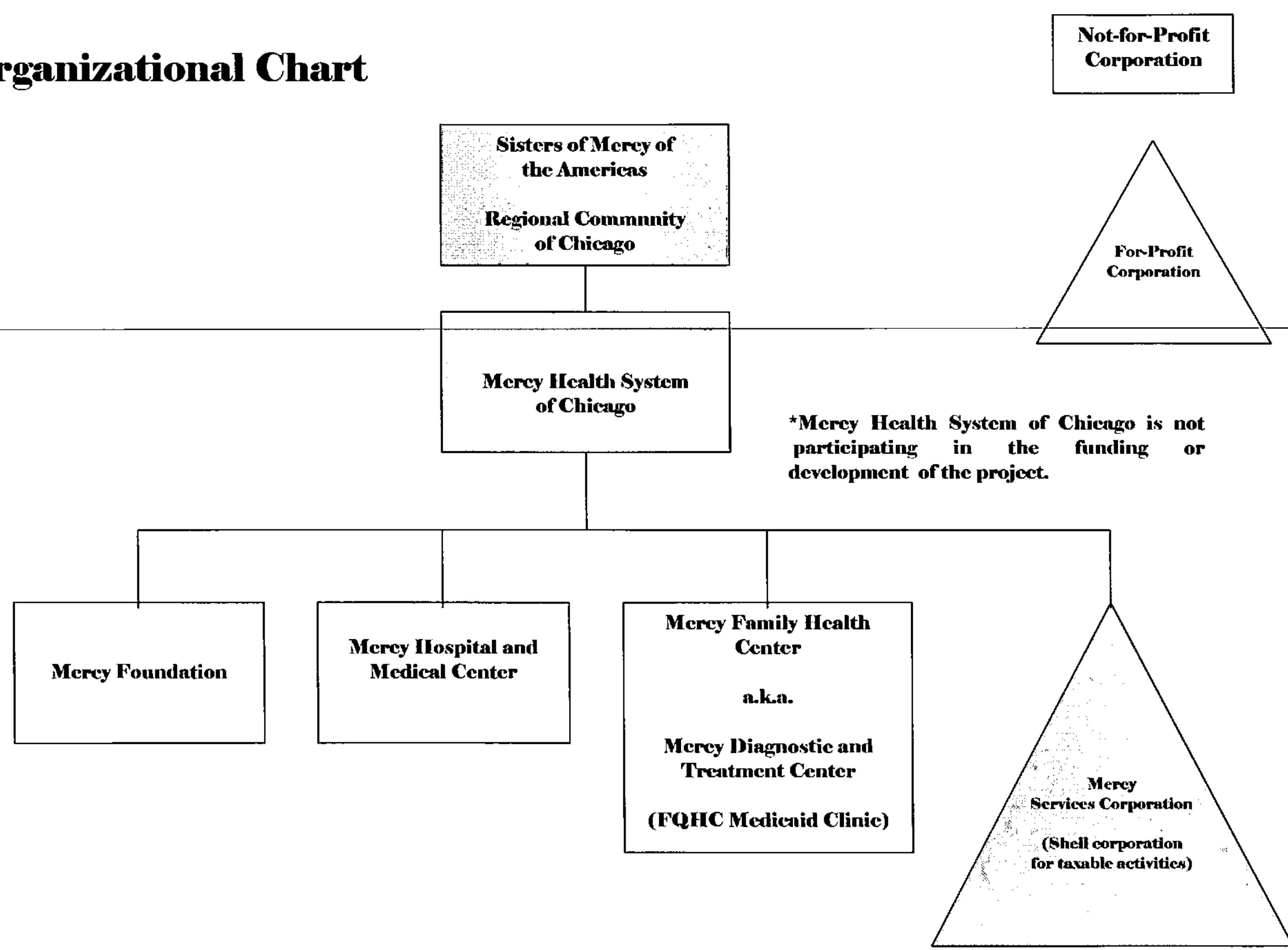
Authenticate at: http://www.cyberdriveillinois.com

Jesse White

SECRETARY OF STATE

ATTACHMENT IDEN-1

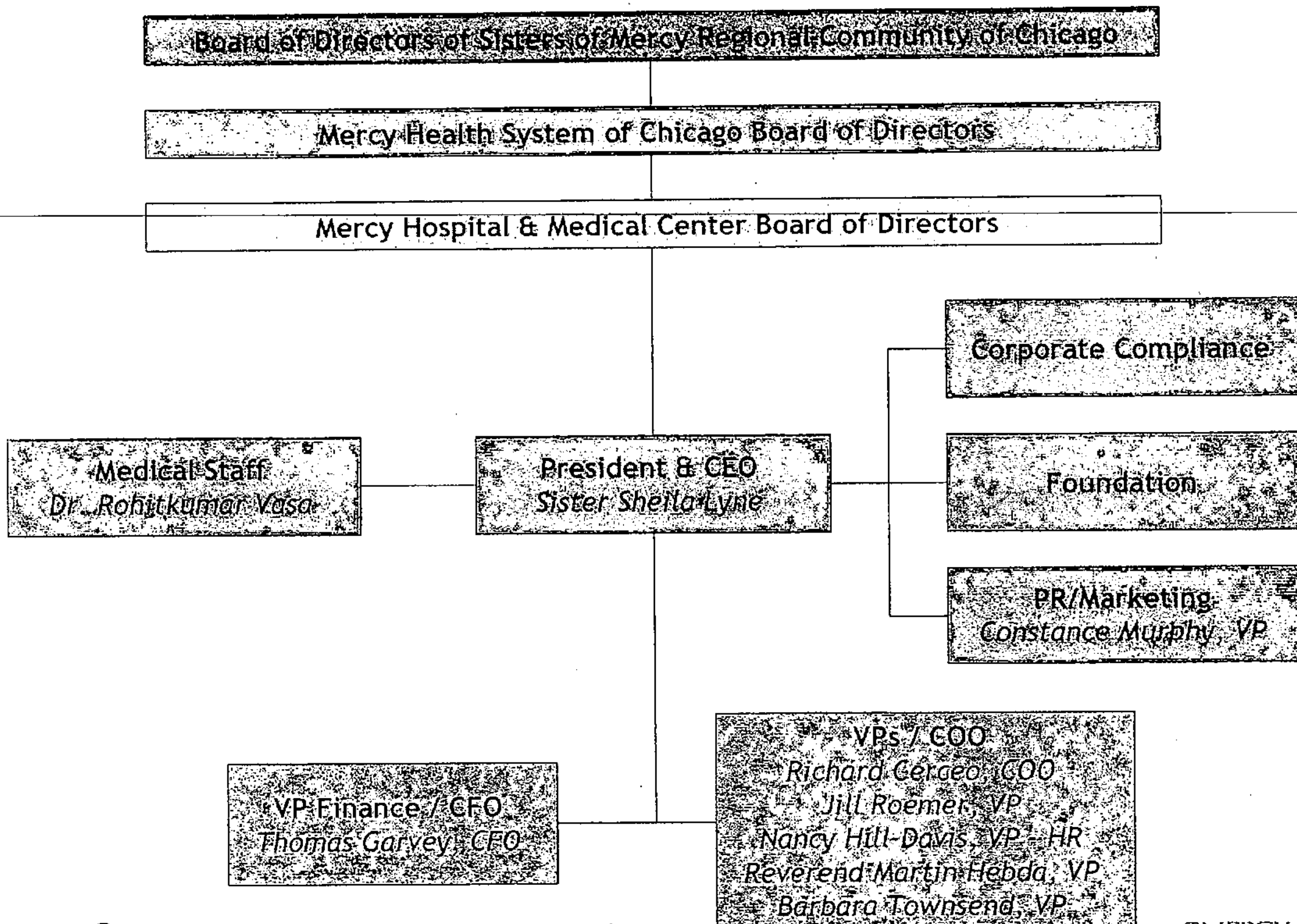
Organizational Chart



*Mercy Health System of Chicago is not participating in the funding or development of the project.

1157257v1

Management Organization Chart



ILLINOIS DEPARTMENT OF NATURAL RESOURCES

Illinois State Water Survey

Main Office • 2204 Griffith Drive • Champaign, IL 61820-7495 • Tel (217) 333-2210 • Fax (217) 333-6540
Peoria Office • P.O. Box 697 • Peoria, IL 61652-0697 • Tel (309) 671-3196 • Fax (309) 671-3106

SWS

Special Flood Hazard Area Determination pursuant to Governor's Executive Order 5 (2006)

(supersedes Governor's Executive Order 4 (1979))

Requester: Richard F. Cerceo, Executive Vice President/Chief Operating Officer
Address: Mercy Hospital & Medical Center, 2525 S. Michigan Ave.
City, state, zip: Chicago, IL 60616-2477 Telephone: (312) 567-2255

Site description of determination:
Site address: 2525 S. Michigan Ave.
City, state, zip: Chicago, IL 60616
County: Cook Sec¼: SE 1/4 of NW 1/4 Section: 27 T. 39 N. R. 14 E. PM: 3rd
Subject area: Area bounded by E. 25th St. on the north, E. 26th St. on the south, S. Michigan Ave. on the west, and Dr. Martin Luther King Jr. Drive on the east.

The property described above IS NOT **located in a Special Flood Hazard Area or a shaded Zone X floodzone.**
Floodway mapped: N/A Floodway on property: No
Sources used: FEMA Flood Insurance Rate Map (FIRM, annotated copy attached); cookcountyassessor.com map/photos.
Community name: City of Chicago, IL Community number: 170074
Panel/map number: 17031C0526 F Effective Date: November 6, 2000
Flood zone: X [unshaded] Base flood elevation: N/A ft NGVD 1929

N/A a. The community does not currently participate in the National Flood Insurance Program (NFIP). NFIP flood insurance is not available; certain State and Federal assistance may not be available.
N/A b. Panel not printed: no Special Flood Hazard Area on the panel (panel designated all Zone C or unshaded X).
N/A c. No map panels printed: no Special Flood Hazard Areas within the community (NSFHA).

The primary structure on the property:
N/A d. Is located in a Special Flood Hazard Area. Any activity on the property must meet State, Federal, and local floodplain development regulations. Federal law requires that a flood insurance policy be obtained as a condition of a federally-backed mortgage or loan that is secured by the building.
N/A e. Is located in shaded Zone X or B (500-yr floodplain). Conditions may apply for local permits or Federal funding.
X f. Is not located in a Special Flood Hazard Area or 500-year floodplain area shown on the effective FEMA map.
N/A g. A determination of the building's exact location cannot be made on the current FEMA flood hazard map.
N/A h. Exact structure location is not available or was not provided for this determination.

Note: This determination is based on the current Federal Emergency Management Agency (FEMA) flood hazard map for the community. This letter does not imply that the referenced property will or will not be free from flooding or damage. A property or structure not in a Special Flood Hazard Area may be damaged by a flood greater than that predicted on the FEMA map or by local drainage problems not mapped. This letter does not create liability on the part of the Illinois State Water Survey, or employee thereof for any damage that results from reliance on this determination. This letter does not exempt the project from local stormwater management regulations.

Questions concerning this determination may be directed to Bill Saylor (217/333-0447) at the Illinois State Water Survey. Questions concerning requirements of Governor's Executive Order 5 (2006), or State floodplain regulations, may be directed to John Lentz (847/608-3100 x2022) at the IDNR Office of Water Resources.

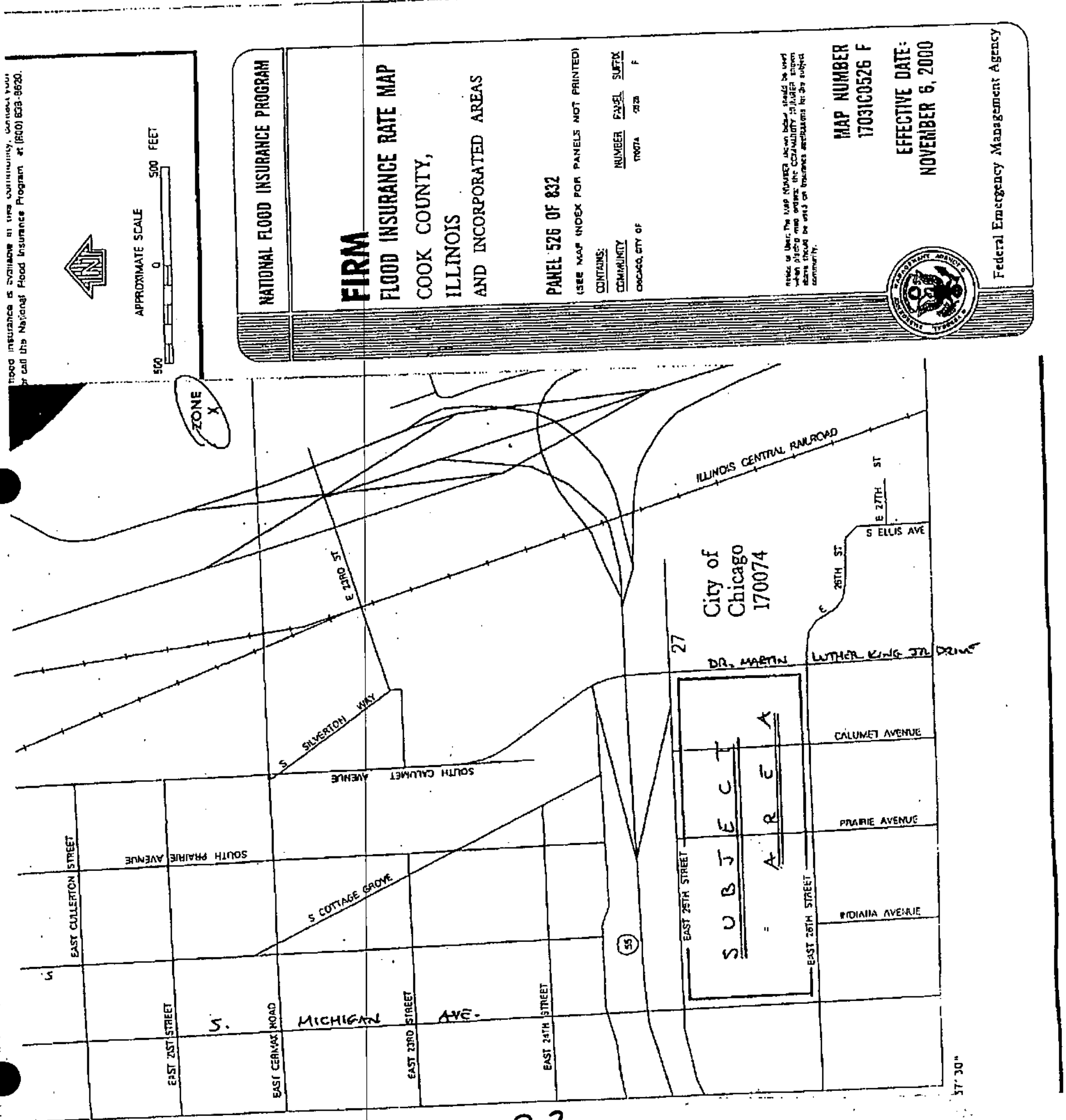
William Saylor
William Saylor, CFM IL-02-00107, Illinois State Water Survey

Title: ISWS Surface Water & Floodplain Information Date: 4/21/2008

Post-it® Fax Note 7671	Date 4/21/2008 # of pages ▶ 3
To Richard Cerceo	From Bill Saylor
Co./Dept. Mercy Hospital	Co. IL State Water Survey
Phone # 312-567-2255	Phone # 217-333-0447

21

ATTACHMENT IDEN-4



ATTACHMENT IDEN-4

LEGEND

SPECIAL FLOOD HAZARD AREAS INUNDATED BY 100-YEAR FLOOD

ZONE A	No base flood elevations determined.
ZONE AE	Base flood elevations determined.
ZONE AH	Flood depths of 1 to 3 feet (usually areas of ponding); base flood elevations determined.
ZONE AO	Flood depths of 1 to 3 feet (usually sheet flow on sloping terrain); average depths determined. For areas of alluvial fan flooding, velocities also determined.
ZONE A99	To be protected from 100-year flood by Federal flood protection system under construction; no base flood elevations determined.
ZONE V	Coastal flood with velocity hazard (wave action); no base flood elevations determined.
ZONE VE	Coastal flood with velocity hazard (wave action); base flood elevations determined.

FLOODWAY AREAS IN ZONE AE

OTHER FLOOD AREAS

ZONE X	Areas of 500 year flood; areas of 100-year flood with average depths of less than 1 foot or with drainage areas less than 1 square mile; and areas protected by levees from 100-year flood.

OTHER AREAS

ZONE X	Areas determined to be outside 500-year floodplain.
ZONE D	Areas in which flood hazards are undetermined, but possible.

UNDEVELOPED COASTAL BARRIERS*

Identified 1983	Identified 1990 or Later	Otherwise Protected Areas Identified 1991 or Later

*Coastal barrier areas are normally located within or adjacent to Special Flood Hazard Areas.

	Floodplain Boundary
	Floodway Boundary
	Zone D Boundary
	Boundary Dividing Special Flood Hazard Zones, and Boundary Dividing Areas of Different Coastal Base Flood Elevations Within Special Flood Hazard Zones.
513	Base Flood Elevation Line; Elevation in Feet**
A — A	Cross Section Line
23 - - - - - 23	Transect Line
(EL 987)	Base Flood Elevation in Feet Where Uniform Within Zone**
RM7 X	Elevation Reference Mark
● M1.5	River Mile

**Referenced to the National Geodetic Vertical Datum of 1929

MAP REPOSITORY

Refer to Repository Listing on Map Index

EFFECTIVE DATE OF COUNTYWIDE FLOOD INSURANCE RATE MAP

NOVEMBER 8, 2000

EFFECTIVE DATE(S) OF REVISION(S) TO THIS PANEL

Please refer to the Listing of Communities table on the FIRM Index for NFIP Initial Identification and Post-FIRM dates for all jurisdictions shown on this map.

To determine if flood insurance is available in this community, contact your insurance agent or call the National Flood Insurance Program at (800) 638-6620.

23

ATTACHMENT IDEN-4

Illinois Historic Preservation Agency

FAX (217) 782-8161

1 Old State Capitol Plaza • Springfield, Illinois 62701-1512 • www.illinois-history.gov

Cook County
Chicago
Renovation - Mercy Hospital and Medical Center
2525 S. Michigan Ave.
IHPA Log #004110807

December 6, 2007

David Larson
VOA Associates Incorporated
224 South Michigan Avenue
Suite 1400
Chicago, IL 60604

Dear Mr. Larson:

We have reviewed the documentation submitted for the referenced project(s) in accordance with 36 CFR Part 800.4. Based upon the information provided, no historic properties are affected. We, therefore, have no objection to the undertaking proceeding as planned.

Please retain this letter in your files as evidence of compliance with section 106 of the National Historic Preservation Act of 1966, as amended. This clearance remains in effect for two years from date of issuance. It does not pertain to any discovery during construction, nor is it a clearance for purposes of the Illinois Human Skeletal Remains Protection Act (20 ILCS 3440).

If you have any further questions, please contact Patrick Gleason, Cultural Resources Manager, Illinois Historic Preservation Agency, 1 Old State Capitol Plaza, Springfield, IL 62701, 217/785-3977.

Sincerely,

Anne E. Haaker

Anne E. Haaker
Deputy State Historic
Preservation Officer

A teletypewriter for the speech/hearing impaired is available at 217-524-7128. It is not a voice or fax line.

ATTACHMENT IDEN-5

Section I, Item Q. Cost/Space Requirements

Department/Area	Cost	Existing GSF	Proposed GSF	GSF: New Construction	GSF: Remodeled	GSF: As Is	GSF: Vacated Space
OB/GYN (Birthing Center)	$6,520,040	34,398	34,398	0	14,371	20,027	0
Intensive Care (Cardiac Intensive Care Project)	$4,362,871	14,066	16,217[1]	0	8,805	7,412	0
Medical/Surgical	$864,809	2,708[2]	2,708	0	2,708	0	0
GI Laboratories	$3,018,987	5,947[3]	5,026	0	5,026	0	0
Non-clinical/ Administrative Space/Staff/ Storage Space	$696,941	3,376[4]	3,376	0	3,376	0	0
Non-clinical/ Fire Alarm	$6,203,060	716,515[5]	716,515	0	716,515	0	0
Non-clinical/ Sprinkler System	$6,868,920	716,515	716,515	0	458,503[6]	258,012	0
Non-clinical/ S-27 Air Handler	$493,528	20,571	20,571	0	20,571	0	0
TOTAL	**$29,029,156**	**1,514,096**	**1,515,326**	**0**	**1,229,875**	**285,451**	0

[1] The Hospital is consolidating the cardiac portion of its intensive care unit ("CCU") into one area of the eleventh floor, as described herein. 4,890 square feet of the existing CCU will remain in place and is being renovated, and 1,764 square feet of the existing CCU space will be vacated (see note 2, below). The remaining 3,915 square feet of the new CCU will include space currently used as medical/surgical space, which will be renovated into CCU space.

[2] This reflects the medical/surgical square footage being renovated. Because of the large size of the Hospital's medical/surgical department, and because the department is spread throughout several floors, obtaining exact square footage for the entire department would be extremely burdensome for the Hospital.

[3] The Hospital is consolidating and renovating the GI portion ("GI Lab") of its ambulatory surgical department. 964 square feet of the old GI Lab space plus 4,062 of former general ambulatory surgical space will be renovated to complete the new relocated GI Lab. The remainder of the old GI space (5,947 square feet existing – 964 existing space being renovated into the new GI Lab = 4,983 square feet of old GI Lab space) will be used as follows: 2,292 renovated for administrative offices, a nurses' lounge, and equipment storage rooms (see note 4). 2,691 square feet of the former GI Lab space within the ambulatory surgical department will be used by that department as general ambulatory surgical space but will not be renovated.

[4] This non-clinical space includes a clean and soiled utility room, administrative offices, a nurses' lounge, storage space, and a staff locker room.

[5] 716,515 is the total square footage of the Hospital.

[6] Certain portions of the sprinkler system have already been completed.

SECTION III. GENERAL REVIEW CRITERIA

This section is applicable to all projects EXCEPT those projects that are solely for discontinuation with no project costs and those projects that are non-substantive and subject only to a Part 1120 review. Refer to Part 1110.40 for the requirement for non-substantive projects.

A. **Criterion 1110.230.a, Location** N/A

Check if the project will result in any of the following: □ establishment of a health care facility: □ establishment of a category of service; □ acquisition of major medical equipment (for treating inpatients) that is not or will not be located in a health care facility and is not being acquired by or on behalf of a health care facility. If NO boxes are checked, this criterion is not applicable. If any box is checked, read the criterion and submit the following:

1. A map (8 ½" x 11") of the area showing:
   a. the location of the applicant's facility or project;
   b. the name and location of all the other facilities providing the same service within the planning area and surrounding planning areas within 30 minutes travel time of the proposed facility;
   c. the distance (in miles) and the travel time (under normal driving conditions) from the applicant's facility to each of the facilities identified in b. above;
   d. an outline of the proposed target population area.
2. For existing facilities, provide patient origin data for all admissions for the last 12 months presented by zip code. Note this information must be based upon the patient's legal residence other than a health care facility for the last 6 months immediately prior to admission. For all other projects for which referrals are required patient origin data for the referrals must be provided.
3. The ratio of beds to population (population will be based upon the latest census data by zip code) within 30 minutes travel time of the proposed project.
4. The status of the project in the zoning process. Provide letter(s) from the appropriate local officials.
5. Evidence of legal site ownership, possession, or option to purchase or lease.

APPEND DOCUMENTATION AS <u>ATTACHMENT GRC-1</u> AFTER THE LAST PAGE OF THIS SECTION.

B. **Criterion 1110.230.b, Background of Applicant**

Read the criterion and submit the following information:

1. A listing of all health care facilities owned or operated by the applicant, including licensing, certification and accreditation identification numbers, if applicable.
2. Proof of current licensing and, if applicable, certification and accreditation of all health care facilities owned or operated by the applicant.
3. A certification from the applicant listing any adverse action taken against any facility owned or operated by the applicant during the three (3) years prior to the filing of the application.

4. Authorization(s) permitting the State Board and Agency access to information in order to verify any documentation or information submitted in response to the requirements of this subsection or to obtain any documentation or information that the State Board or Agency finds pertinent to this subsection. **Failure to provide such authorization shall constitute an abandonment or withdrawal of the application without any action by the State Board.**

APPEND DOCUMENTATION AS ATTACHMENT GRC-2 AFTER THE LAST PAGE OF THIS SECTION.

C. Criterion 1110.230.c, Alternatives to the Proposed Project

Read the criterion and provide the following information:

1. Provide a comparison of all of the alternatives considered including the alternative of doing nothing. The comparison must address cost benefit analyses, patient access, quality, and short and long-term financial benefits.

2. Discuss why the alternative of using other area facilities or resources to meet the needs identified in your project is not feasible.

3. Discuss why the alternative of utilizing underutilized bed or other space in the facility is not feasible.

4. If the alternative selected is based solely or in part on improved quality of care, provide empirical evidence (including quantified outcome data) that verifies improved quality of care.

APPEND DOCUMENTATION AS ATTACHMENT GRC-3 AFTER THE LAST PAGE OF THIS SECTION.

D. Criterion 1110.230.d, Need for the Project

Is the need for the project based upon need assessment per Part 1100 or a variance? ☐ Yes ☒ No.
If no is indicated, read the criterion and submit the following as applicable:

1. Copies of area market studies including explanations regarding how and when these studies were performed.

2. Calculation of the need for the beds or services including the models used to estimate the need (all assumptions used in the model and the mathematical calculations must be included).

3. Identification of the individuals likely to use the proposed beds or service by:

   Provide letters from physicians or hospitals which document how many patients were referred for this service in the past 12 months, where the patients were referred and how many patients will be referred annually to the proposed project.

4. If the project is for the acquisition of major medical equipment that does NOT result in the establishment of a category of service, provide documentation that the equipment will achieve or exceed the applicable target utilization levels specified in Appendix B of Part 1110 within 12 months after acquisition.

APPEND DOCUMENTATION AS ATTACHMENT GRC-4 AFTER THE LAST PAGE OF THIS SECTION.

E. Criterion 1110.230.e, Size of Project

Read the criterion and provide the following:

1. For any department involved in this project that has a square footage which exceeds the State Norm found in Appendix B of Part 1110 or if no State Norm is shown in Appendix B, provide:

   a. a rationale explaining how the proposed square footage was determined;

   b. copies of any standards used to determine appropriate square footage;

   c. architectural drawings showing any design impediments in the existing facility; and

   d. if the project is for the conversion of beds from one category of service to another an explanation as to why the excess space within the facility cannot be more appropriately used for other purposes.

APPEND DOCUMENTATION AS <u>ATTACHMENT GRC-5</u> AFTER THE LAST PAGE OF THIS SECTION.

2. If the project involves a category of service for which the State Board has established utilization targets, provide the following:

   a. projected utilization for the first two years of operation after project completion;

   b. an explanation regarding how these projections were developed;

   c. copies of any contracts with new physicians or professional staff;

   d. a list of any new procedures which will affect the workload of the facility.

APPEND DOCUMENTATION AS <u>ATTACHMENT GRC-6</u> AFTER THE LAST PAGE OF THIS SECTION.

Section III, Item B. Background of Applicant

Applicant: Mercy Hospital and Medical Center

1. Mercy Hospital and Medical Center only owns/operates one health facility (as defined by Section 3 of the Health Facilities Planning Act, 20 ILCS 3960/3), a licensed hospital (Mercy Hospital and Medical Center). The hospital's license number is 0001578.

2. A copy of the hospital's license and accreditation are attached hereto.

3. Attached is a letter certifying that no adverse action has been taken against the Applicant or its hospital for the three (3) years prior to the filing of this application.

4. The attached letter also authorizes the State Board and Agency access to information in order to verify any documentation or information submitted in response to the requirements of this subsection or to obtain any documentation or information that the State Board or Agency finds pertinent to this subsection.

Co-Applicant: Mercy Health System of Chicago

1. Mercy Health System of Chicago does not own or operate any health care facilities.

2. N/A

3. Attached is a letter certifying that no adverse action has been taken against the Co-Applicant for the three (3) years prior to the filing of this application.

4. The attached letter also authorizes the State Board and Agency access to information in order to verify any documentation or information submitted in response to the requirements of this subsection or to obtain any documentation or information that the State Board or Agency finds pertinent to this subsection.

MERCY

Mercy Hospital & Medical Center
2525 South Michigan Avenue
Chicago, Illinois 60616-2477
phone 312.567.2000

March 24, 2008

Mr. Jeffrey Mark
Executive Secretary
Illinois Health Facilities Planning Board
525 W. Jefferson Street – Second Floor
Springfield, IL 62761

Dear Mr. Mark:

In Accordance with Criterion 1110.230.d, Background of the Applicant, we are submitting this letter assuring the Illinois Health Facilities Planning Board that:

1. Mercy Hospital and Medical Center does not have any adverse actions against any facility owned or operated by the applicant during the three (3) year period prior to the filing of this application and

2. Mercy Hospital and Medical Center authorizes the State Board and Agency access to information in order to verify documentation or information submitted in response to the requirements of Criterion 1110.230.d or to obtain any documentation or information which the State Board or Agency finds pertinent to this application

If we can in any way provide assistance to your staff regarding these assurances or any other issue relative to this application, please do not hesitate to call me.

Sincerely,

Sheila Lyne

Sister Sheila Lyne, RSM
President and Chief Executive Officer

SSL/ss

OFFICIAL SEAL
SANDRA A SCHUELER
NOTARY PUBLIC - STATE OF ILLINOIS
MY COMMISSION EXPIRES:03/10/11

Sandra A. Schueler 3/24/08

ATTACHMENT GRC-2

Healthcare Facilities Accreditation Program

HFAP Healthcare Facilities Accreditation Program
ACCREDITING HEALTHCARE FACILITIES FOR OVER 50 YEARS

grants this

CERTIFICATE OF ACCREDITATION

to

Mercy Hospital and Medical Center

Chicago, IL

This Facility has met the applicable HFAP accreditation requirements and is therefore fully accredited by the Healthcare Facilities Accreditation Program

2007-2010

Executive Director
American Osteopathic Association

President
American Osteopathic Association

Chairman
Bureau Healthcare Facilities Accreditation

ATTACHMENT GRC-2

State of Illinois 1849731

Department of Public Health

LICENSE, PERMIT, CERTIFICATION, REGISTRATION

The person, firm or corporation whose name appears on this certificate has complied with the provisions of the Illinois Statutes and/or rules and regulations and is hereby authorized to engage in the activity as indicated below.

DAMON T. ARNOLD, M.D.
DIRECTOR

Issued under the authority of
The State of Illinois
Department of Public Health

EXPIRATION DATE	CATEGORY	I.D. NUMBER
12/31/08	BGBD	0001578

FULL LICENSE

GENERAL HOSPITAL

EFFECTIVE: 01/01/08

BUSINESS ADDRESS

MERCY HOSPITAL & MEDICAL CENTER
2525 SOUTH MICHIGAN AVENUE
CHICAGO IL 60616 2477

The face of this license has a colored background. Printed by authority of the State of Illinois • 4/97 •

DISPLAY THIS PART IN A CONSPICUOUS PLACE

REMOVE THIS CARD TO CARRY AS AN IDENTIFICATION

State of Illinois 1849731

Department of Public Health

LICENSE, PERMIT, CERTIFICATION, REGISTRATION

MERCY HOSPITAL & MEDICAL CENTER

EXPIRATION DATE	CATEGORY	I.D. NUMBER
12/31/08	BGBD	0001578

FULL LICENSE

GENERAL HOSPITAL

EFFECTIVE: 01/01/08

11/03/07

MERCY HOSPITAL & MEDICAL CENTER
2525 SOUTH MICHIGAN AVENUE
CHICAGO IL 60616 2477

FEE RECEIPT NO.

ATTACHMENT GRC-2

CITY OF CHICAGO

LICENSE CERTIFICATE

NON-TRANSFERABLE

BY THE AUTHORITY OF THE **CITY OF CHICAGO**, THE FOLLOWING SPECIFIED LICENSE IS HEREBY GRANTED TO

NAME: RELIGIOUS SISTERS/MERCY/CHICAGO

DBA: MERCY HOSPITAL/MEDICAL CENTER

AT: 2510 S. DR MARTIN LUTHER KING JR DR., Apt./Suite
CHICAGO, IL 60616
1

LICENSE NO: 11727 CODE: 1375 FEE: $****916.67

LICENSE: Hospital

1000 Beds Max.
PRESIDENT:CHARLES B. VAN VORST
SECRETARY:SR. LENORE MULUIHILL, RSM

PRINTED ON : 08/16/2007 $****916.67

THIS LICENSE IS ISSUED AND ACCEPTED SUBJECT TO THE REPRESENTATIONS MADE ON THE APPLICATION THEREFOR, AND MAY BE SUSPENDED OR REVOKED FOR CAUSE AS PROVIDED BY LAW. LICENSEE SHALL OBSERVE AND COMPLY WITH ALL LAWS, ORDINANCES, RULES AND REGULATIONS OF THE UNITED STATES GOVERNMENT, STATE OF ILLINOIS, COUNTY OF COOK, CITY OF CHICAGO AND ALL AGENCIES THEREOF.

WITNESS THE HAND OF THE MAYOR OF SAID CITY AND THE CORPORATE SEAL THEREOF

THIS 15 DAY OF AUGUST, 2007

EXPIRATION DATE: June 15, 2008

ATTEST:

Richard M Daley
MAYOR

Miguel del Valle
CITY CLERK

CITY OF CHICAGO INCORPORATED 4th MARCH 1837

DREV NO. 51184 SITE 1

TRANS NO.

THIS LICENSE MUST BE [illegible] IN A CONSPICUOUS PLACE UPON THE LICENSED PREMISES.

THE FACE OF TH[illegible]CUMENT HAS A MULTI-COLORED DOCUMENT ON WHITE PAPER

ATTACHMENT GRC-2

MERCY
MERCY HOSPITAL & MEDICAL CENTER
2525 SOUTH MICHIGAN AVENUE
CHICAGO, ILLINOIS 60616-2477
phone 312.567.2000

March 24, 2008

Mr. Jeffrey Mark
Executive Secretary
Illinois Health Facilities Planning Board
525 W. Jefferson Street – Second Floor
Springfield, IL 62761

Dear Mr. Mark:

In Accordance with Criterion 1110.230.d, Background of the Applicant, we are submitting this letter assuring the Illinois Health Facilities Planning Board that:

1. Mercy Health System of Chicago does not have any adverse actions against any facility owned or operated by the applicant during the three (3) year period prior to the filing of this application and

2. Mercy Health System of Chicago authorizes the State Board and Agency access to information in order to verify documentation or information submitted in response to the requirements of Criterion 1110.230.d or to obtain any documentation or information which the State Board or Agency finds pertinent to this application

If we can in any way provide assistance to your staff regarding these assurances or any other issue relative to this application, please do not hesitate to call me.

Sincerely,

Sheila Lyne

Sister Sheila Lyne, RSM
President and Chief Executive Officer

SSL/ss

OFFICIAL SEAL
SANORA A SCHUELER
NOTARY PUBLIC - STATE OF ILLINOIS
MY COMMISSION EXPIRES:03/10/11

Sandra A. Schueler 3/24/08

ATTACHMENT GRC-2

Section III, Item C. Alternatives to the Proposed Project

The proposed project requires modernization of three main areas of the Hospital: the Birthing Center, the Cardiac Care Unit ("CCU"), and the Gastrointestinal Laboratory ("GI Labs"), as well as certain related renovations to space vacated by the relocation of the CCU and the GI Labs (including renovations to certain medical/surgical beds and certain non-clinical space). The project also proposes to add sprinklers to the Hospital, to upgrade the fire alarm system, and to upgrade the S-27 air handler; this aspect is considered to be non-clinical and is required in order to comply with various regulations. Please note that the project does not propose to add a category of service, does not propose to add beds, and does not propose any new construction or expansion of the square footage of the Hospital.

The primary alternatives considered with respect to this project included: (i) doing nothing and maintaining the Birthing Center, the CCU, and the GI Lab "as is;" (ii) using other area facilities; (iii) using underutilized bed or other space in the hospital; and (iv) modernizing the Hospital's Birthing Center, the CCU, and the GI Lab.

Birthing Center (OB/GYN)

The Hospital's Birthing Center consists of twenty-two (22) post partum patient rooms, nine (9) labor delivery rooms, twenty (20) nursery bassinets and two (2) c-Section rooms. Seventy-five percent (75%) of the Hospital's Birthing Center patients are Public Aid beneficiaries. With the impending closing of Michael Reese Hospital and the continuous increases in deliveries the Hospital faces each year, the Birthing Center serves a vital community need.

1. Do Nothing/Maintain Status Quo

The existing physical infrastructure of the Hospital is 40 years old and the Birthing Center has never been renovated. The Hospital currently has semi-private patient rooms in its Birthing Center. Double occupancy is not only a big patient dissatisfaction (as identified by the Hospital's patient satisfaction surveys), but patient confidentiality is compromised in a semi-private room. The industry standard and patient's expectations clearly have shifted to the use of private post-partum rooms.

Under the "do nothing/maintain status quo" alternative, the Applicants would continue operating in the existing Birthing Center without any modernization. Such a course of action would ignore the existing condition of the facilities, the legal requirements for patient confidentiality, and the obvious healthcare need of patients and the community. The existing Birthing center presents serious deficiencies to accommodate the needs of patients (e.g., noise issues, privacy concerns, etc.).

Since the need for obstetrics services is expected to continue to increase in the coming years, particularly with the anticipated closure of Michael Reese Hospital, the Applicants determined that "doing nothing" is infeasible. Although "doing nothing" will not cost anything, continued utilization of the Birthing Center without modernization will not address the age of the facility, the patients' desire for private rooms, and the legal requirements for patient confidentiality. As a result, the alternative of doing nothing/maintaining the status quo was considered and rejected.

2. Use Other Area Facilities

The Hospital has seen significant growth in community demand for women's health services in our market. Unlike most other inpatient admissions, women plan their obstetric hospitalizations and are seen on a regular basis in our affiliated clinics. Many of our patients select the Hospital because they live in our primary service area. The level and breadth of our healthcare services, including pre-natal care, is available in convenient satellite locations. As stated previously, the Hospital's obstetrics patients are primarily Public Aid beneficiaries (75%).

The Hospital considered the alternative of using other area facilities rather than modernizing its Birthing Center. The Hospital has experienced a dramatic increase in deliveries during the past four years. Cumulative growth during the past four fiscal years through 2007 was 42.62%, averaging 10.7% annually. In fiscal year 2007, the Hospital had 3,067 deliveries, which represents a 17.2% increase from the 2,618 deliveries in fiscal year 2006. Deliveries through the first eight months of Fiscal Year 2008 (through Feb. 2008) are 6.9% above last year's levels. A forecast of 3,278 deliveries is projected for the full fiscal year ending June 30, 2008. In addition, with the impending closure of Michael Reese Hospital, which performed 894 deliveries in 2006, more patients in the local community will be coming to the Hospital's Birthing Center.

Due to the continued increase in obstetrics demand, the impending closure of Michael Reese in the Hospital's community, the fact that the Hospital serves 75% Public Aid beneficiaries for obstetrics services, and the fact that patients' physicians may only have privileges at the Hospital, referring obstetrics patients to other facilities is not a viable option.

3. Use Underutilized Bed/Other Hospital Space

This alternative does not apply to the proposed project, as the proposed project does not require constructing new space for the Birthing Center but, rather, proposes renovating the Hospital's existing Birthing Center.

4. Modernize Birthing Center

In the final analysis, the Applicants determined that the best option to ensure the availability of quality and confidential obstetrics services is to obtain a Certificate of Need for the modernization of the Hospital's Birthing Center. This project is the most efficient and cost-effective alternative to preserve the quality of services provided by the Hospital and to continue to serve the community, particularly the Public Aid beneficiaries in need of obstetrics services. This project proposes to modernize the Birthing Center and allow the Hospital to accommodate significant growth in obstetrics and meet the projected need in our community.

As discussed above, the Hospital has experienced a dramatic increase in deliveries during the past four years and anticipates that deliveries will continue to increase in the coming years as the neighborhood surrounding the Hospital is being gentrified with the addition of new residential space. With the closure of Michael Reese Hospital, providing obstetrics services to the community serves a vital need. As the Hospital's facilities are 40 years old and have not been renovated, and as semi-private post partum rooms are no longer the standard for obstetrics services, the Applicants determined that modernization of the Birthing Center was the best alternative. This allows the Hospital to continue to provide access to obstetrical services and to continue to serve a high amount of Public Aid beneficiaries. Modernizing the Birthing Center increases patient confidentiality and decreases noise and disruption, as the improved efficiencies caused by the proposed renovations allow the Hospital to run the Birthing Center's room as private rooms. The modernization will allow the Birthing Center to meet new regulatory standards including the requirements of the Americans with Disabilities Act. The modernization is necessary to provide an efficient and safe environment for patient care and will bring the Hospital up to the latest healthcare regulatory and safety standards.

The proposed modernization does not require new construction or the addition of beds, which keeps the cost of the project down. It will result in a Birthing Center containing 22 private post-partum rooms, 9 labor delivery rooms, and a supporting nursery. By allowing mothers requiring a long labor time to be accommodated in rooms separate from the LDR, the average length of stay will be reduced and the number of births that can be accommodated by the LDR suites will increase. This will address the increase in community demand and accommodate nearly 4,000 deliveries per year. This option will improve operating efficiencies, safety, security, and patient confidentiality.

As the Hospital provides obstetrics services to a high amount of Public Aid beneficiaries (75% of obstetrics services are provided to Public Aid beneficiaries), the Hospital serves a vital community need and the Hospital requests approval of the modernization of its Birthing Center so that it can continue to care for patients and provide them quality services while protecting their confidentiality.

Cardiac Care Unit (Intensive Care)

The Hospital's intensive care unit is divided into two sub-units: the surgical intensive care unit and the cardiac intensive care unit. The cardiac intensive care unit is designed to administer care to post-procedure cardiac patients. The intensive care portion of the Cardiac Care Unit ("CCU") currently consists of 16 cardiac intensive care beds. The Hospital is approved for 30 intensive care beds and the proposed project will not increase the number of approved beds. The Hospital currently staffs 14 surgical intensive care beds and 16 cardiac intensive care beds. Following the modernization, the Hospital will have 28 staffed intensive care beds (14 surgical intensive care and 14 cardiac intensive care) out of the 30 authorized intensive care beds.

1. Do Nothing/Maintain Status Quo

The existing physical infrastructure of the Hospital is 40 years old. The current CCU has been in place for over 20 years and has never been renovated. The space provided within the CCU is poorly configured to accommodate the needs of physicians and staff members, as well as patients and their family members. The layout is not efficient and does not adequately accommodate space needs for new technology for care of patients in this area. For example, the current CCU rooms are too small to accommodate the C-ARM units. Because this technology does not fit into the patient's room, the patient must be wheeled down to the cath lab for the C-ARM procedure. In order to have an up-to-date CCU, the unit's individual rooms need to be larger to meet current regulatory standards and clinical needs. For example, the Hospital's current CCU does not have isolation rooms that are ADA-compliant.

Under the "do nothing/maintain status quo" alternative, the Applicants would continue operating in the existing CCU without any modernization. Although such a course of action does not cost anything for the Hospital, it would ignore the existing condition of the facilities, the inefficient layout, and the inadequate size of patient rooms. For the above reasons, the Applicants determined that the "do nothing/maintain status quo" option is not a viable alternative.

2. <u>Use Other Area Facilities</u>

The Hospital considered referring CCU patients to other area facilities, but determined that this was not a viable option. The Hospital's CCU serves post-procedure cardiac intensive care patients. Transferring these patients to another facility following cardiac surgery is not a feasible option, as these patients are too unstable to transfer.

3. <u>Modernize Cardiac Care Unit./Use Underutilized Hospital Space</u>

The existing intensive care portion of the CCU consists of 16 staffed intensive care beds. The expanded area renovates currently underutilized Hospital space. The program for the renovation of the CCU is to improve the facilities for the existing comprehensive cardiac care (recovery) unit, consolidating the CCU beds at one end of the floor. The overarching goals of this renovation are to improve workflow and staff efficiencies while improving the continuum of care and ultimately, clinical results. The renovation will include the addition of three isolation rooms (for a total of four), two of which will be ADA compliant. The patient rooms will be renovated, and a family lounge, conference room, small nurses' station, physician consultation area, and data room will be added. In conjunction with the modernization, the mechanical, electrical, lighting, power, and plumbing systems (as well as a few specialized systems, such as the nurse call system, intercom system, and television system) serving the CCU will be updated.

The modernization alternative is the preferred alternative because it is the most cost-efficient, renovating existing space within the Hospital and reorganizing the intensive care unit so that the cardiac care portion is consolidated. Allowing all of the cardiac patients and staff to be located in the same space saves time and provides better quality care. For these reasons, modernizing the cardiac care portion of the Hospital's existing intensive care unit is the preferred alternative.

Gastrointestinal ("GI") Laboratories

The Hospital currently has four (4) GI labs spread throughout the same day surgical division of the Hospital's first floor. The project does not propose the addition of more GI labs, but rather proposes to consolidate and modernize the labs. The Hospital intends to relocate the GI labs to the east end of the same day surgery unit.

1. Do Nothing/Maintain Status Quo

The existing physical infrastructure of the Hospital is 40 years old and the GI labs have never been renovated. The current GI labs are not configured to handle the projected increase volume in an efficient manner because they are spread across the same day surgery wing and not centralized, which is inefficient for staff, physicians, and patients. The existing GI labs do not have dedicated toilets or a dedicated nurses' station. Further, the labs must be updated to meet current regulatory standards and to comply with the requirements of the Americans with Disabilities Act.

Under the "do nothing/maintain status quo" alternative, the Applicants would continue operating the GI labs in their current location and would not modernize the labs. Such a course of action would ignore the existing condition of the facilities, the inefficient layout, and would prevent the Hospital from having an area dedicated to GI procedures. For the above reasons, the Applicants determined that the "do nothing/maintain status quo" option is not a viable alternative.

2. Use Other Area Facilities

The Hospital's GI Labs are an integral part of the services the Hospital provides and referring patients to another facility for these services is not a viable option, particularly due to the anticipated closure of Michael Reese Hospital.

The Hospital has a large cancer program, as cancer is the second highest diagnosis the Hospital treats. GI services are an integral part of the cancer screening and cancer care program and an integral part of the Hospital's operations. The Hospital has experienced a dramatic increase in cancer procedures and screenings, especially GI cases. Cumulative growth during the past four (4) fiscal years through 2007 was 23.5% averaging 5.9% annually. GI cases through the first 8 months of fiscal year 2008 (through Feb 2008) are 10.3% above last year's levels. A forecast of 4,061 GI cases is projected for the full fiscal year ending June 30, 2008.

The American Cancer Society estimates that 104,950 colon and 40,340 rectal cancers were diagnosed in 2005. 56,290 patients are estimated to have died of colorectal cancer in 2005. Colorectal cancer accounts for 10-11% of all new cancers and 10% of cancer deaths in both men and women. In 2005, colorectal cancer accounted for 14% of all newly diagnosed cancers in men and 12% of newly diagnosed cancers in women at the Hospital. Based on our historical trend data and higher national estimates for colon and rectal cancers, we are projecting to attain a volume in excess of 5,000 GI cases per year.

For these reasons, referring GI patients to another area facility is not a feasible option.

3. Use Underutilized Bed/Other Hospital Space

This alternative does not apply to the proposed project, as the proposed project does not require constructing new space for the GI Laboratories but, rather, proposes renovating the Hospital's existing space.

4. Modernize GI Laboratories

This modernization project will relocate the four (4) GI laboratories to the east end of the outpatient surgery center. This area will be modernized to include support areas for scope cleaning, storage, charting, a nurses' station and a conference room. The modernization allows for the creation of eight (8) dedicated prep/hold/recovery rooms for individual patients. The Hospital currently has no dedicated prep/hold/recovery rooms. These renovations will allow the GI labs to be more efficient, as they will be centralized in one area, which is convenient for patients and staff and which is designed to improve efficiency and care and to allow the Hospital to meet the anticipated increases in demand for GI services, as discussed above. The renovations will also allow the hospital to have space for pre- and post-care of patients, as currently patients recover in the actual GI Lab, which is not efficient. Consolidating the space also increases the protections of patient confidentiality and is convenient for patients and staff.

Rather than building out and expanding the GI laboratories, relocating the unit and modernizing existing hospital space is the most cost-effective alternative. The Hospital expects the efficiencies created by the new layout to add to staff efficiencies and to increase patient safety and quality of care. Further, the renovated rooms provide more space for technology.

Relocating and modernizing the GI laboratories is the preferred alternative, as this option will address the Hospital's anticipated volume increases for this important service line.

Medical/Surgical Modernization

The Applicants propose to renovate five (5) medical/surgical rooms on the eleventh floor of the Hospital that will be vacated by the partial relocation of the cardiac intensive care unit, as well as a nurses' station.

1. Do Nothing/Maintain Status Quo

Following the relocation of a portion of the CCU, five (5) patient rooms that are currently being used as CCU rooms will be vacated. Under the "do nothing/maintain status quo" alternative, the Applicants would use these rooms for medical/surgical patients in the existing space without reconfiguring the rooms to meet the needs of medical/surgical patients and staff. Currently, these rooms comprise a four (4) bed ward and a six (6) bed ward within the CCU. The renovations will modify these areas to turn the four (4) bed ward into two (2) private patient rooms, and the six (6) bed ward into three (3) patient rooms.

Although "doing nothing" will not cost anything, utilizing the vacated CCU space without the necessary minor renovations would not allow the hospital to have five (5) private medical/surgical patient rooms. Michael Reese Hospital is anticipated to close in the coming months. Further, the Hospital has a transfer agreement with the University of Chicago whereby the Hospital receives patients in need of non-specialized care, which has increased the Hospital's ADC by ten (10) to twelve (12) per day. As a result, the alternative of doing nothing/maintaining the status quo was considered and rejected.

2. Use Other Area Facilities

As the renovations to these beds were driven by the relocation of the CCU, the alternative of using other area facilities does not apply.

3. Modernize Certain Medical/Surgical Beds/Use Underutilized Hospital Space

In the final analysis, the Applicants determined that the best option to ensure the availability of quality services is to modernize certain medical/surgical beds from the former CCU space. This project is the most efficient and cost-effective alternative to make use of the Hospital's existing resources. Due to the Hospital's increasing utilization and need for staffed medical/surgical beds, the minor renovations necessary to convert former CCU space to medical/surgical beds were deemed to be worth the limited cost of the renovations.

Support Space (Non-Clinical)

The Applicants propose to renovate non-clinical support space (including a clean and soiled utility room, administrative offices, a nurses' lounge, storage space, and a staff locker room), some of which was vacated by the relocation of the CCU and the GI Labs. While the Applicants considered the alternative of leaving this space as is, in order for the space to be usable, renovation is required. Therefore, the Applicants chose the alternative of renovating this non-clinical space in order to make the Hospital as functional as possible.

Hospital-wide Sprinkler Installation and Fire Alarm Upgrade (Non-Clinical)

The hospital is required to comply with the Life Safety Ordinance of the Chicago Fire Department and Fire Prevention Bureau to update the facility with installation of a hospital-wide fire sprinkler system and fire alarm upgrade. This is a non-clinical project.

Renovation of S-27 Air Handler (Non-Clinical)

Due to the renovations to the CCU, the Hospital is required by the Life Safety Code to update the S-27 Air Handler. This is a non-clinical project.

Section III, Item D. Need for the Project

This project is not based upon a need assessment per Part 1100 of the Planning Board Rules or a variance because the Applicants are not proposing to create a new category of service or add any beds beyond those previously authorized and is strictly a modernization of portions of the Hospital.

1. Area market studies

During its analysis of whether or not to renovate the Hospital's Birthing Center, the Cardiac Care Unit ("CCU"), and the Gastrointestinal Laboratory ("GI Labs"), as well as certain related renovations to five (5) medical/surgical beds and a nurses' station in space vacated by the relocation of the CCU, the Applicants did not conduct formal area market studies, but instead based its decision to modernize portions of the Hospital on its current utilization rates, on the age and functionality of the facilities, and the projected increases the Hospital expects due to the impending closure of Michael Reese Hospital.

2. Calculation of the need for the beds or services

a. Birthing Center

The Hospital's obstetrics occupancy rate for 2007 is 59%. Due to the impending closure of Michael Reese, as well as the continued increase in Birthing Center volume, the Hospital conservatively anticipates that its occupancy will increase in the coming years by an estimated 3% per year.

b. CCU

The Hospital's CCU occupancy rate for 2007 is 67%, which is above the State utilization standard for ICU (60%). The Hospital's total ICU occupancy rate for 2007 is 71%, which is also above the State standard. The Hospital anticipates its ICU occupancy rate will continue to increase.

c. GI Labs

The State does not have a utilization standard for the GI Labs. The Applicants determined that it needed to develop a more efficient floor plan for the GI Labs in order to accommodate an increase in patient volume partially stemming from the impending closure of Michael Reese Hospital. The proposed renovations consolidate the GI Labs in one area of the ambulatory surgery department, which provides for greater staff efficiency, greater patient convenience, and greater patient confidentiality.

d. Medical/Surgical

The Hospital's medical/surgical occupancy rate for 2007 is 34%. Due to the impending closure of Michael Reese, as well as the continued increase in inpatient volume, the Hospital conservatively anticipates that its occupancy will increase in the coming years by an estimated 3% per year.

3. Identification of individuals likely to use the proposed beds or service

This project is a modernization and does not propose the addition of any beds or services. The Applicants anticipate that the future volume for the Birthing Center, CCU and GI Labs (as well as for the five (5) renovated medical/surgical beds will come from the population living in the established service areas of the Hospital. The Applicants anticipate that the Hospital will continue to serve a high percentage of Medicaid beneficiaries. In particular, the zip codes in the Hospitals primary and secondary service areas include:

	Zip	Community
New	60604	Loop
New	60605	South Loop
New	60606	Loop
New	60607	West Loop/Near West
Core	60608	Pilsen/Lower West Side
Core	60609	Stockyards
SSA	60615	Hyde Park
Core	60616	22nd Street
SSA	60619	Greater Grand Crossing
SSA	60620	Auburn Park
SSA	60621	Englewood
SSA	60623	South Lawndale
SSA	60628	Roseland
SSA	60629	Chicago Lawn
SSA	60632	Eldson (5th)
SSA	60636	Ogden Park
SSA	60637	Jackson Park
SSA	60649	South Shore
Core	60653	Hyde Park
New	60661	Loop

Attached to this Attachment GRC-4 is a letter from Carmen Velasquez, Executive Director, Alivio Medical Center, demonstrating the need for the modernization of the Hospital's Birthing Center. Ms. Velasquez's letter highlights how the Birthing Center serves a large number of low-income, Spanish-speaking mothers.

Also attached is a letter from John McCarthy, Chair of the Board of the Hospital, supporting the proposed modernization and outlining the Hospital's inpatient and outpatient growth and need for up-to-date, quality facilities to provide the best level of care to the community.

4. This project does not include the acquisition of major medical equipment.

This section does not analyze the need for the non-clinical aspects of the project, such as the minor renovations to certain of the Hospital's non-clinical space, the installation of a sprinkler system, or the upgrade to the fire alarm system. The sprinkler/fire alarm projects are necessary to comply with the Life Safety Code, the Chicago High-Rise Sprinkler Ordinance, and the Life Safety Ordinance of the Chicago Fire Department and Fire Prevention Bureau. The S-27 Air Handler project is necessary to comply with the requirements of the Life Safety Code. The minor non-clinical renovations are necessary to enable the Hospital to utilize space vacated by the consolidations of the CCU and the GI Labs.

ALIVIO MEDICAL CENTER

An Active Presence for a Strong Community

Mr. Jeffrey S. Mark
Executive Secretary
Illinois Health Facilities Planning Board
525 W. Jefferson St. – 2nd floor
Springfield, IL 62761

Dear Mr. Mark.

I am writing this letter to you to express my support for the modernization of the Birthing Center at Mercy Hospital and Medical Center. Alivio Medical Center and Mercy Hospital has worked closely together to address access to health care to many low income Spanish speaking, and predominantly Mexican immigrants in our community.

In FY 2007, (July 1, 2006-June 30,2007), 1,154 of Alivio patients delivered their babies at Mercy Hospital.

Mercy Hospital is an important partner in providing desperately needed quality health care to our community.

As Executive Director of Alivio Medical Center, I urge the Illinois Health Facilities Planning Board to approve this essential modernization of the Birthing Center at Mercy Hospital and Medical Center.

Thank you very much for your attention to this matter.

Sincerely,

Carmen Velasquez

Carmen Velasquez
Executive Director
Alivio Medical Center

Joint Commission National Quality Approval

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Mr. Jeffrey S. Mark
Executive Secretary
Illinois Health Facilities Planning Board
525 W. Jefferson St. – 2nd floor
Springfield, IL 62761

Dear Mr. Mark :

I am writing this letter to you to express my support for the modernization projects at Mercy Hospital and Medical Center. The projects include necessary updating of facilities for our Birthing Center, Cardiac Care Unit (CCU), GI Laboratories, and Fire Sprinklers and Fire Alarm upgrades.

Mercy Hospital and Medical Center has experienced a dramatic increase in in-patient admissions and outpatient cases during the past four fiscal years. Cumulative growth during the past four fiscal years through 2007, for inpatient admissions was 23% averaging 7.1% annually. Outpatient services increased during the same period increase with a cumulative of 17.7% averaging 5.9%annually.

It is apparent from the above utilization rates that Mercy Hospital and Medical Center must maintain modern, up to date, healthcare facilities for the efficient, high quality care for our patients.

If I can provide any further information in support of this endorsement of this project, please do not hesitate to call my office.

Sincerely,

John C. McCarthy

John McCarthy
Chair of the Board
Mercy Hospital and Medical Center

ATTACHMENT GRC-4

Received as original on 5/20/08

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OFFICIAL SEAL
SANDRA A SCHUELER
NOTARY PUBLIC - STATE OF ILLINOIS
MY COMMISSION EXPIRES:03/10/11

Sandra A. Schueler

Section III, Item E. Size of the Project

1. For any department that has a square footage that exceeds the State Norm or if no State Norm is shown:

Birthing Center (OB/GYN/LDR/Newborn Nursery)

The State Norm for OB/GYN beds is 476 square feet per bed. The Hospital has 30 OB/GYN beds (the modernization will not change the number of OB/GYN beds).

476 x 30 = 14,280 square feet

The State Norm for Labor-Delivery-Recovery is 23 square feet per bed or 4.6 square feet per procedure or 1975 square feet per needed delivery room (based upon 750 live births per delivery room). The Hospital has 9 LDRs (the modernization will not change the number of LDRs). The Hospital has 449 beds (the modernization will not change the number of Hospital beds).

23 x 449 = 10,327

The State Norm for a newborn nursery is 152 square feet per obstetrics bed. The Hospital has 30 OB beds (the modernization will not change the number of OB beds).

152 x 30 = 4,560 square feet

Birthing Center State Norm: 14,280 + 10,327 + 4,560 = 29,167 square feet

The existing Birthing Center is 34,398 square feet; this number will not change following the proposed modernization. The Birthing Center will remain slightly larger than the State Norm. This is due in part to the patient preference for private rooms. This is also necessary to help maintain patient confidentiality and to decrease noise in the unit.

CCU (Intensive Care Unit)

The State Norm for intensive care beds is 603 square feet per bed. The Hospital is licensed for and currently operates 30 intensive care beds (14 surgical intensive care beds and 16 cardiac intensive care beds). Following the proposed modernization, the Hospital will operate 28 intensive care beds (14 surgical and 14 cardiac).

603 x 28 = 16,884 square feet

Proposed square footage of ICU following modernization: 16,217 square feet

The renovated intensive care unit meets the State Norm for square footage, as the proposed intensive care unit will be slightly under the allowed 16,884 square feet.

GI Unit (Ambulatory Care)

There is no State Norm for dedicated GI Laboratories. The Hospital's current GI Labs occupy 5,947 square feet, and the modernized GI Labs will occupy 5,026 square feet.

Section III, Item E. Size of the Project, Continued

2. If the project involves a category of service for which the Board has established utilization targets, provide the following:

   (a) projected utilization for the first two years of operation after project completion

      (i) Birthing Center (OB/GYN)

The first full year of operation of the areas that the Hospital proposes to modernize will be 2011. The State Standard is 78% occupancy for OB/GYN beds. The Birthing Center currently operates at 59% utilization. The Hospital anticipates that the Birthing Center will operate at 71% utilization in 2011 and at 74% utilization in 2012 due to the impending closure of Michael Reese Hospital and the Hospital's continued increases in births.

      (ii) CCU (Intensive Care)

The first full year of operation of the areas that the Hospital proposes to modernize will be 2011. The State Standard is 60% occupancy for ICU beds. The Hospital's ICU currently operates at 71%, and the cardiac portion of the ICU currently operates at 67%. The Hospital anticipates that the ICU will continue to operate over the State Standard in 2011 and 2012 due to the impending closure of Michael Reese Hospital and the Hospital's continued increase in patients. The Hospital anticipates that the cardiac portion of its ICU will be utilized at an even higher degree than the overall ICU in 2011 and 2012.

      (iii) GI Labs

There is no State Standard for utilization of dedicated GI Laboratories. The Applicants forecast that the Hospital will perform 4,061 GI cases in the fiscal year ending June 30, 2008.

      (iv) Medical/Surgical

The first full year of operation of the areas that the Hospital proposes to modernize will be 2011. The State Standard is 88% occupancy for medical/surgical beds. The Hospital's medical/surgical department currently operates at 34%. The Hospital anticipates that the medical/surgical department will operate at 46% in 2011 and at 49% in 2012 due to the impending closure of Michael Reese Hospital and the Hospital's continued increase in patients. Please note that the Hospital only proposes to renovate five (5) medical/surgical beds and a nurses' station. These renovations are necessary due to the partial relocation of the cardiac intensive care unit.

   (b) an explanation regarding how these projections were developed

The Applicants developed the projected utilization of each unit by factoring in its trend of recent patient increases (a 23% increase in inpatient admissions over the past four fiscal years and a 17.7% increase in outpatient admissions over the same period), the impending closure of Michael Reese Hospital, and other reasons, including population growth and gentrification of the Hospital's service area. The Hospital's market survey showed a 19% increase in outpatients and a 9% increase in inpatients. The actual projections are based upon a 3% increase each year, which the Applicants view as a conservative projection.

(c) copies of any contracts with new physicians or professional staff

While the Hospital does not have any particular contracts with new physicians that drive the proposed renovation, the Hospital's continuing relationship with the University of Chicago continues to increase the Hospital's utilization. The Hospital has a transfer agreement with the University of Chicago whereby the Hospital receives the overflow from the University of Chicago's emergency room and receives referrals of patients in need of non-specialized care and psychiatric services. These patients increase the Hospital's ADC by ten (10) to twelve (12) per day.

(d) list of any new procedures which will affect the workload of the facility.

The Hospital does not anticipate any new procedures in the areas being renovated.

SECTION VII. REVIEW CRITERIA RELATING TO ALL MODERNIZATION PROJECTS (MOD)

This section is applicable to all projects proposing modernization. Modernization includes, but is not limited to: expanding a department, acquiring major medical equipment, remodeling, or constructing additions or new buildings.

A. Specific Information Requirements

Indicate if the following areas or departments are to be modernized and provide the information as applicable.

1. AMBULATORY CARE (Include all outpatient clinics) -- Is this area being modernized? Yes ☐ No ☒

   If yes, provide:

   a. The number of visits for each of the last three years:

Year			
Number			

   b. The number of treatment/examination rooms: Existing _______ Proposed _______

2. AMBULATORY SURGERY TREATMENT CENTERS-- Is this area being modernized? Yes ☐ No ☒

   If yes, provide:

   a. The number of procedures for each of the last three years:

Year			
Number			

   b. The number of visits for each of the last three years:

Year			
Number			

   c. The number of operating rooms for each of the last three years:

Year			
Number			

3. CARDIAC CATHETERIZATION -- Is this area being modernized? Yes ☐ No ☒

   If yes, provide the number of inpatient, outpatient, and total procedures (patient visits) performed on adults and on pediatric patients for each of the past three years:

	ADULT				PEDIATRIC		
Year				Year			
Inpatient				Inpatient			
Outpatient				Outpatient			
Total				Total			

4. EEG DEPARTMENT OR AREA -- Is this area being modernized? Yes ☐ No ☒

If yes, provide the number of inpatient, outpatient, and total procedures for each of the past three years:

Year			
Inpatient			
Outpatient			
Total			

5. EKG DEPARTMENT OR AREA -- Is this area being modernized? Yes ☐ No ☒

If yes, provide the number of inpatient, outpatient, and total procedures for each of the past three years:

Year			
Inpatient			
Outpatient			
Total			

6. HEMODIALYSIS SERVICES -- Is this area being modernized? Yes ☐ No ☒

If yes, provide the following information:

a. The number of treatment stations: existing ______ proposed ______

b. The number of treatments performed for each of the last three years:

Year			
Treatments			

7. LABOR-DELIVERY-RECOVERY -- Is this area being modernized? Yes ☒ No ☐

If yes, provide the following information: **

a. The number of

Labor rooms	0
Delivery/birthing rooms	0
Recovery stations	3
LDR's	9
LDRP rooms	0

b. The number of procedures and deliveries for each of the last three years:

Year	FY 2007	FY 2006	FY 2005
Procedures	0	0	0
Deliveries	3067	2618	2547

**Please note that this project is a modernization only and does not request the addition of any new OB/GYN beds.

8. LABORATORY SERVICES -- Is this area being modernized? Yes ☐ No ☒

If yes, provide the number of equivalent full-time employees (FTE's) employed in the laboratory______

9. MAGNETIC RESONANCE IMAGING -- Is this area being modernized? Yes ☐ No ☒

If yes, provide the following information for each of the last three years:

Year			
Number of visits			
Number of scans			

10. NURSERY (other than neonatal intensive care units) -- Is this area being modernized? Yes ☒ No ☐
If yes, provide the following for each of the last three years: *

Year	FY 2007	FY 2006	FY 2005
Number of newborns	3103	2645	2571
Number of patient days	6509	5509	5207

*Please note that this project is a modernization only and does not request the expansion of the nursery.

11. OCCUPATIONAL THERAPY -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the following information for each of the last three years:

Year			
Inpatient treatments			
Outpatient treatments			
Number of visits			

12. PHYSICAL THERAPY -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the following information for each of the last three years.

Year			
Inpatient treatments			
Outpatient treatments			
Total treatments			
Number of visits			

13. PULMONARY FUNCTION -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the following information for each of the last three years.

Year			
Inpatient procedures			
Outpatient procedures			
Total procedures			
Number of visits			

14. RECOVERY (SURGICAL) -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the existing and proposed number of stations by type:

	Existing	Proposed
Inpatient		
Outpatient Stage I		
Outpatient Stage II		

15. RESPIRATORY THERAPY -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the following information for each of the last three years.

Year			
Inpatient treatments			
Outpatient treatments			
Total treatments			
Number of visits			

16. DIAGNOSTIC RADIOLOGY -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the following information classifying procedure rooms as general or special according to the type of machines employed.

General machines are:
- -Radiographic
- -Fluoroscopic
- -Radiographic/Flouroscopic
- -Tomographic (linear)
- -Tomographic (multi-directional)

Special machines are:
- -Angiographic
- -CT Scanner
- -Mammography
- -Sonographic (ultrasound)

a. Provide the number of existing and proposed general procedure rooms by machine type.

b. Provide the number of existing and proposed special procedure rooms by machine type.

APPEND DOCUMENTATION AS ATTACHMENT MOD-1A AFTER THE LAST PAGE OF THIS SECTION.

17. EMERGENCY SERVICES -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the following information:

a. The number of existing and proposed treatment/examination rooms;

b. A list of any of the above rooms that are or will be used for purposes other than general treatment;

c. The number of visits for each of the last three years.

APPEND DOCUMENTATION AS ATTACHMENT MOD-1B AFTER THE LAST PAGE OF THIS SECTION.

18. INPATIENT BED AREA -- Is this area being modernized? Yes ☒ No ☐
If yes, provide the following information: *

a. The number of existing and proposed private rooms, semi-private rooms, and three or more occupancy rooms (by category of service for each type of room) for the entire facility and for the project;

b. Line drawings showing the configuration of the unit(s) being modernized.

*Please note that this project is a modernization only and does not request the addition of any new inpatient beds.

APPEND DOCUMENTATION AS ATTACHMENT MOD-1C AFTER THE LAST PAGE OF THIS SECTION.

19. NUCLEAR MEDICINE -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the following information:

a. A list of the existing and proposed major pieces of equipment;

b. The existing and proposed number of procedure rooms;

c. The number of inpatient, outpatient, and total procedures done for each of the last three years;

d. A breakdown of the procedures into types of procedures and machine time/procedure for the last year.

APPEND DOCUMENTATION AS ATTACHMENT MOD-1D AFTER THE LAST PAGE OF THIS SECTION.

20. RADIATION THERAPY -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the following information:

a. The number of treatments and the number of "courses of treatment" for each of the last three years;

b. A list of the existing and proposed pieces of megavoltage equipment.

APPEND DOCUMENTATION AS ATTACHMENT MOD-1E AFTER THE LAST PAGE OF THIS SECTION.

21. SURGERY -- Is this area being modernized? Yes ☐ No ☒
If yes, provide the following information:

a. The existing and proposed number of procedure rooms. Indicate the use of these rooms such as general, open heart, eye, endoscopy, and cystology. Indicate how many rooms are dedicated solely to outpatient surgery, solely to inpatient surgery, and how many are used for both.

b. The inpatient, outpatient, and total hours of utilization (including clean-up and set-up time) for each of the last three years;

c. The total hours of utilization (including clean-up and set-up time) for each type of procedure room for each of the last three years;

d. The number of inpatient, outpatient, and total surgical visits for each type of surgical specialty for each of the last three years.

APPEND DOCUMENTATION AS ATTACHMENT MOD-1F AFTER THE LAST PAGE OF THIS SECTION.

22. OTHER DEPARTMENTS OR AREAS – Are any other areas being modernized? Yes ☒ No ☐
If yes, identify the area(s) and provide workload data for each area for each of the last three years.*
Please see Attachment MOD-A(22).

APPEND DOCUMENTATION AS ATTACHMENTS MOD-1G, MOD-1H, MOD-1I, MOD 1J, etc. AFTER THE LAST PAGE OF THIS SECTION.

B. Criterion 1110.420.b, Modern Facilities

A criterion must be claimed for EACH department or area to be modernized. The justification for each department or area must be on a separate page. Choose the criterion or criteria which most clearly approximates the reason for proposing the modernization.

At least ONE of the following two criteria must be claimed for EACH department or area proposed for modernization.

1. Read criterion 1110.420.b.1. **This criterion cannot be used to justify any increase in square footage. If expansion of a department is proposed, criterion 1110.420.b.2 must be claimed.**

Indicate if this criterion is claimed and submit the following:

a. the age of the building or piece of equipment;

b. the downtime experienced on the piece of equipment for each of the last three years;

c. the cost of repair experienced on the piece of equipment for each of the last three years;

d. a detailed explanation of why and how it was determined that the building or piece of equipment was deteriorated and needs to be replaced;

e. provide copies of any licensing, certification, or fire protection citations.

APPEND DOCUMENTATION AS ATTACHMENT MOD-2 AFTER THE LAST PAGE OF THIS SECTION.

2. Read Criterion 1110.420.b.2. Identify if this criterion is claimed and submit the following information:

a. a detailed explanation of why and how it was determined that expansion of the department or area was necessary;

b. a discussion of the alternatives considered to expanding the department (e.g. increasing the hours or days of operation) and why the alternatives were rejected.

APPEND DOCUMENTATION AS ATTACHMENT MOD-3 AFTER THE LAST PAGE OF THIS SECTION.

C. Criterion 1110.420.c, Major Medical Equipment N/A

Read Criterion 1110.420.c and provide documentation that the equipment will achieve or exceed the applicable target utilization levels specified in Appendix B of Part 1110 within 12 months after becoming operational.

APPEND DOCUMENTATION AS ATTACHMENT MOD-4 AFTER THE LAST PAGE OF THIS SECTION.

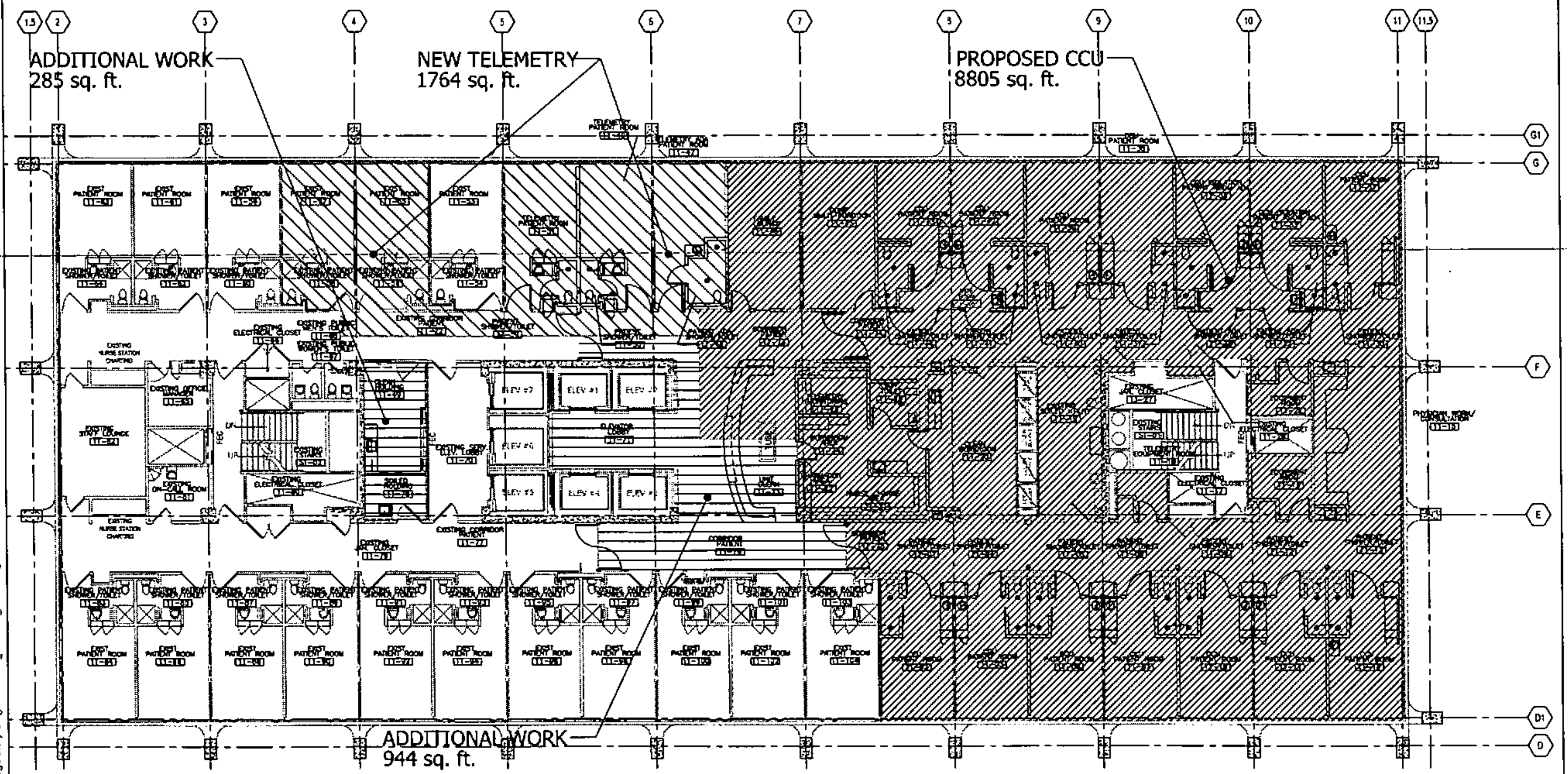
Section VII, Item A(18). Inpatient Bed Area

The Hospital currently has the following rooms:

Category	Private Rooms	Semi-private Rooms	3+ Occupancy	Total Rooms
Medical/Surgical	37	126	0	**163**
Obstetric	12	9	0	**21**
Intensive Care	26	2	0	**28**
Neonatal ICU	0	0	0	**0**
Pediatric	5	16	0	**21**
Rehabilitation	0	12	0	**12**
Mental Illness	1	19	0	**20**
Long Term Care	0	0	0	**0**
Total	**81**	**184**	**0**	**265**

Following the proposed renovation, the number of beds will remain the same. The room count will be as follows:

Category	Private Rooms	Semi-private Rooms	3+ Occupancy	Total Rooms
Medical/Surgical	37	126	0	**163**
Obstetric	12	9	0	**30**
Intensive Care	28	0	0	**28**
Neonatal ICU	0	0	0	**0**
Pediatric	5	16	0	**21**
Rehabilitation	0	12	0	**12**
Mental Illness	1	19	0	**20**
Long Term Care	0	0	0	**0**
Total	**83**	**182**	**0**	**265**

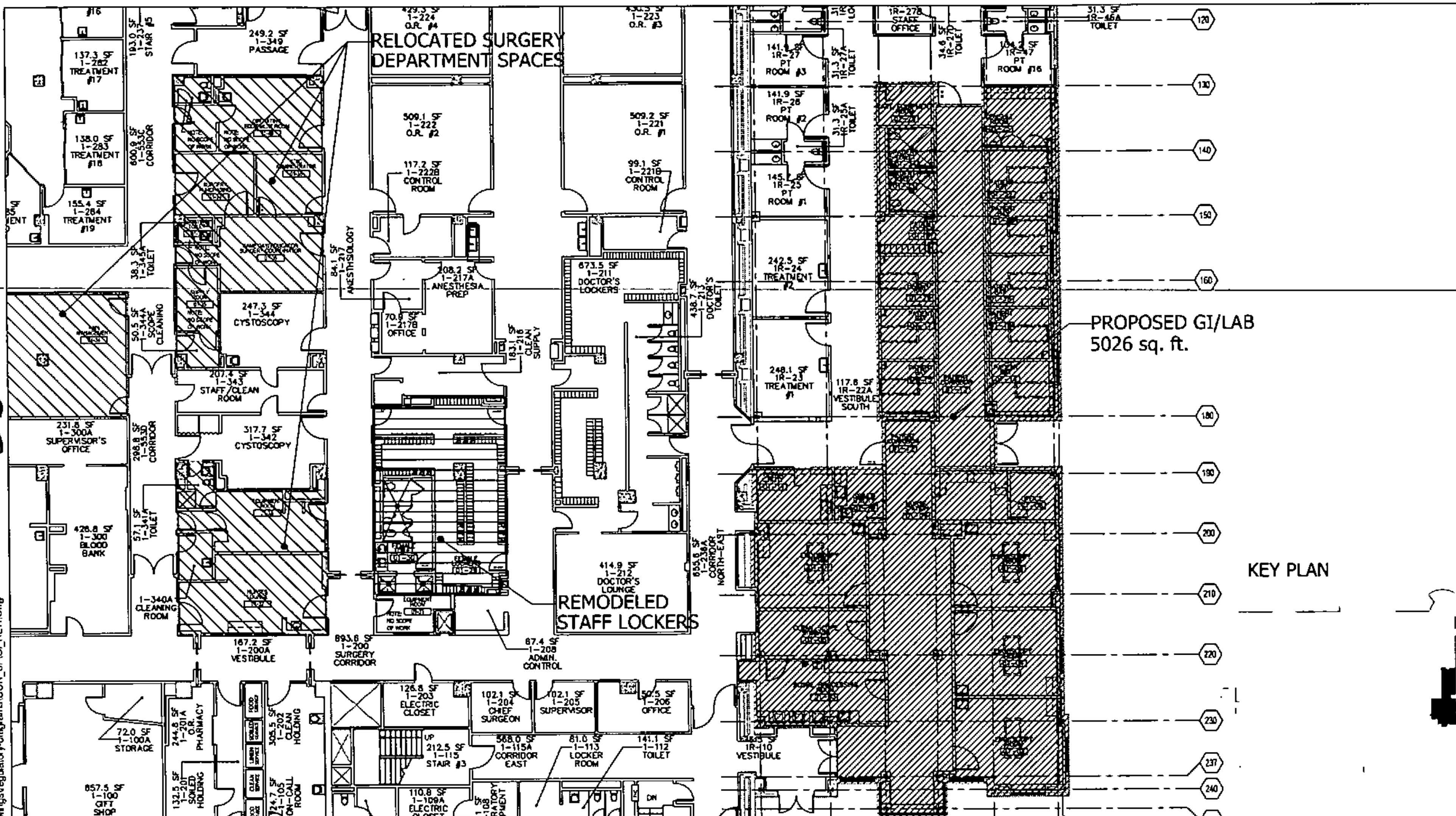


VOA ASSOCIATES, INC. Architecture/Planning/Interior Design 224 South Michigan Avenue #1400 Chicago, Illinois 60604 PH: (312)554-1400 FAX:(312)554-1412	DRAWING ISSUE/REVISION LOG (NO. / DESCRIPTION / DATE)	MERCY HOSPITAL & MEDICAL CENTER CHICAGO, IL	DRAWN BY: LR	SCALE: 1/16" = 1'-0"	SHEET: SK.3
		11TH FLOOR: PROPOSED CCU	CHECKED BY: DL	DATE: 04/11/2008	

FILE: U:\2519a-00\Drawings\regulatory-diagrams\CON_SF\CCU_NEW.dwg

PRINTED: 04/23/2008

ATTACHMENT MOD-1C



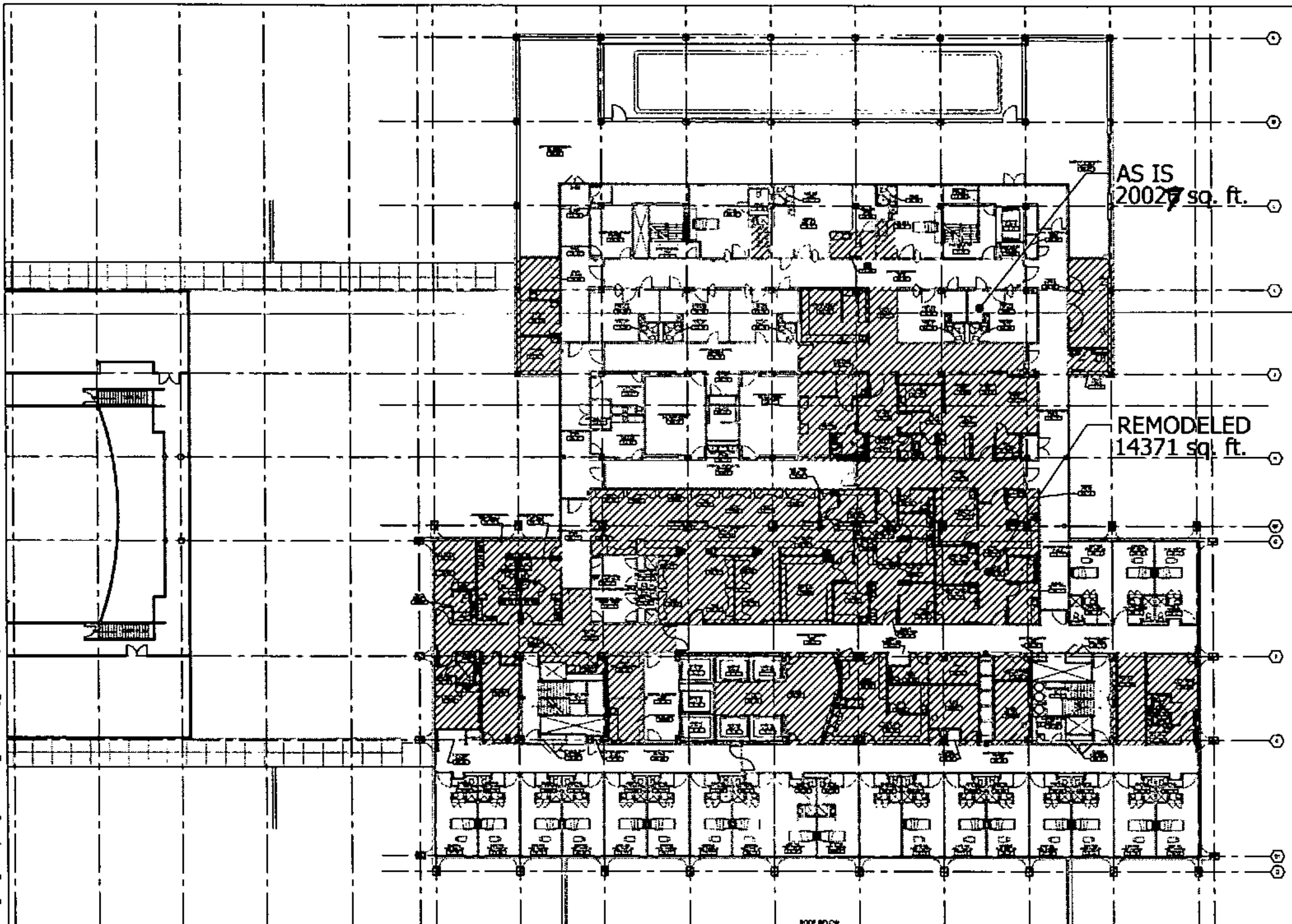
VOA ASSOCIATES, INC. Architecture/Planning/Interior Design 224 South Michigan Avenue #1400 Chicago, Illinois 60604 PH: (312)554-1400 FAX:(312)554-1412	DRAWING ISSUE/REVISION LOG NO. DESCRIPTION DATE	MERCY HOSPITAL & MEDICAL CENTER CHICAGO, IL 1ST FLOOR: PROPOSED GI/LAB	DRAWN BY: LR CHECKED BY: DL	SCALE: 1/16" = 1'-0" DATE: 04/11/2008	SHEET: SK.7

FILE: U:\2519a-000\Drawings\Regulatory-diagrams\CON_SF\GI_NEW.dwg

PRINTED: 04/11/2008

59

ATTACHMENT MOD-1C



FILE: U:\25198-00\Drawings\regulatory-diagrams\CON_SF\Birthing_New.dwg

VOA

VOA ASSOCIATES, INC.
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DRAWING ISSUE/REVISION LOG

NO.	DESCRIPTION	DATE

MERCY HOSPITAL & MEDICAL CENTER
CHICAGO, IL

3RD FLOOR: PROPOSED BIRTHING CENTER

DRAWN BY: LR

CHECKED BY: DL

SCALE: 1" = 30'

DATE: 04/11/2008

SHEET: SK.5

PRINTED: 04/11/2008

ATTACHMENT MOD-1C

Section VII, Item A(22). Other Departments or Areas

The other area being modernized is the Hospital's GI laboratories.

The workload data for the GI Labs for each of the last three years is as follows:

FY2007: 3,681 procedures

FY2006: 3,682 procedures

FY2005: 3,251 procedures

Section VII, Item B. Modern Facilities

Birthing Center and GI Labs:

1. The Applicants propose to modernize its Birthing Center, GI labs, and five (5) of its medical/surgical beds (as well as a nurses' station) based on the rationale listed in criterion 1110.420(b)(1). The proposed project does not increase the square footage of the Birthing Center or the GI labs.

   (a) The Hospital building is 40 years old and the Birthing Center, GI labs, and medical/surgical beds have never been renovated.

   (b) N/A

   (c) N/A

   (d) The Applicants determined that the projects are necessary as detailed below:

      i. <u>Birthing Center</u>

      Modernizing the Birthing Center is the most efficient and cost-effective alternative to preserve the quality of services provided by the Hospital and to continue to serve the community, particularly the Public Aid beneficiaries in need of obstetrics services. With the closure of Michael Reese Hospital, continuing to provide obstetrics services to the community serves a vital need. As the Hospital's facilities are 40 years old and have not been renovated, and as the Hospital's existing semi-private post partum rooms are no longer the standard for obstetrics services, the Applicants determined that modernization of the Birthing Center was necessary. Modernizing the Birthing Center increases patient confidentiality and decreases noise and disruption, as the efficiencies created by the proposed renovations will allow the Birthing Center rooms to be run as private post-partum rooms. The modernization will allow the Birthing Center to meet new regulatory standards including the requirements of the Americans with Disabilities Act. The modernization is necessary to provide an efficient and safe environment for patient care and will bring the Hospital up to the latest healthcare regulatory and safety standards. This project will improve operating efficiencies, safety, security, and patient confidentiality.

ii. GI Labs

As discussed above, the Hospital's facilities are 40 years old and have not been renovated. The relocation and modernization of the GI laboratories is necessary to increase efficiency of the labs and to provide for adequate space for new technology. The modernization is also necessary to better protect patient confidentiality. These renovations will allow the GI labs to be more efficient, as they will be consolidated, saving staff and physician time. With the addition of dedicated prep/hold/recovery rooms, the Hospital will be able to meet the anticipated increases in demand for GI services, as these functions currently take place in the GI labs, which is inefficient.

iii. Certain Medical/Surgical Beds/Nurses' Station

As discussed previously, the Hospital's facilities are 40 years old and have not been renovated. Due to the consolidation and partial relocation of the cardiac care portion of the intensive care unit ("CCU"), five (5) formerly intensive care patient rooms were vacated. The modernization of these rooms is necessary to make them functional medical/surgical rooms. A nurses' station is also being renovated to better serve the floor.

iv. Sprinklers/Fire Alarm

The hospital is required to comply with the Life Safety Ordinance of the Chicago Fire Department and Fire Prevention Bureau to update the facility with installation of a hospital-wide fire sprinkler system and fire alarm upgrade. This is a non-clinical project.

v. S-27 Air Handler

The hospital is required to comply with the Life Safety Code to update the S-27 Air Handler. This is a non-clinical project.

vi. Other Non-clinical Space

The Hospital also plans to renovate a clean and soiled utility room, administrative offices, a nurses' lounge, storage space, and a staff locker room. This is a non-clinical project.

(e) The sprinkler/fire alarm and the S-27 air handler project are required by various regulations and the Life Safety Code, but none of the renovations are driven by citations.

Section VII, Item B. Modern Facilities

Cardiac Care Unit ("CCU"):

2. The Applicants propose to modernize its CCU based on the rationale listed in criterion 1110.420(b)(2).

(a) The hospital determined that the minor expansion of the CCU division of the intensive care unit was necessary because the Hospital's facilities are 40 years old and have not been renovated. The proposed renovation of the CCU is necessary to improve the facilities for the existing comprehensive cardiac care (recovery) unit and to consolidate the CCU beds at one end of the floor. This renovation will improve workflow and staff efficiencies while improving the continuum of care and ultimately, clinical results.

In order to have an up-to-date CCU, the unit's individual rooms need to be larger to meet current regulatory standards and clinical needs. For example, the Hospital's current CCU does not have isolation rooms that are ADA-compliant.

The modernization is cost-efficient, renovating existing space within the Hospital and reorganizing the intensive care unit so that the cardiac care portion is consolidated. Allowing all of the cardiac patients and staff to be located in the same space saves time and provides better quality care.

(b) In debating whether to expand the CCU, the Hospital considered and rejected the following alternatives:

Do Nothing. The Hospital considered doing nothing to the existing CCU, but rejected this alternative because the current CCU has been in place for over 20 years and has never been renovated. The current space is poorly configured to accommodate the needs of physicians, staff, patients, and family members. The layout is not efficient, as it is spread out rather than centralized, and the patient rooms are too small and do not accommodate new equipment and other clinical needs. For example, the Hospital's current CCU does not have isolation rooms that are ADA-compliant. For these reasons, the Hospital decided against doing nothing.

Use Other Area Facilities. The Hospital considered referring CCU patients to other area facilities, but determined that this was not a viable option. The Hospital's CCU serves post-procedure cardiac intensive care patients. Transferring these patients to another facility following cardiac surgery is not a feasible option.

Use Underutilized Hospital Space/Modernize Cardiac Care Unit. The Hospital chose the alternative of renovating the CCU to improve the facilities for the existing comprehensive cardiac care (recovery) unit and to consolidate the CCU beds at one end of the floor. This alternative is intended to improve CCU workflow and staff efficiencies while improving the continuum of care and ultimately, clinical results. The renovation will include the addition of three isolation rooms (for a total of four), two of which will be ADA compliant. The patient rooms will be renovated, and a family lounge, conference room, small nurses' station, physician consultation area, and data room will be added.

The modernization alternative is the preferred alternative because it is the most cost-efficient, renovating existing space within the Hospital and reorganizing the intensive care unit so that the cardiac care portion is consolidated. The expanded square footage of the CCU renovates underutilized hospital space. Allowing all of the cardiac patients and staff to be located in the same space saves time and provides better quality care. For these reasons, modernizing the cardiac care portion of the Hospital's existing intensive care unit is the preferred alternative.

The sprinkler/fire alarm and the S-27 air handler project are required by various regulations and the Life Safety Code, but none of the renovations are driven by citations.

SECTION XXIV. REVIEW CRITERIA RELATING TO FINANCIAL FEASIBILITY (FIN)

This section is applicable to all projects subject to Part 1120.

Does the applicant (or the entity that is responsible for financing the project or is responsible for assuming the applicant's debt obligations in case of default) have a bond rating of "A" or better? Yes ☐ No ☒

If yes is indicated, submit proof of the bond rating of "A" or better (that is less than two years old) from Fitch's, Moody's or Standard and Poor's rating agencies and go to Section XXX. If no is indicated, submit the most recent three years' audited financial statements including the following:

1. **Balance sheet**
2. **Income statement**
3. **Change in fund balance**
4. **Change in financial position**

APPEND THE REQUIRED DOCUMENTS AS <u>ATTACHMENT FINANCIALS</u> AND PLACE AFTER ALL OTHER APPLICATION ATTACHMENTS INCLUDING THE REMAINING ATTACHMENTS FOR THIS SECTION AND FOR SECTION XXX.

A. Criterion 1120.210.a, Financial Viability

1. Viability Ratios

If proof of an "A" or better bond rating has not been provided, read the criterion and complete the following table providing the viability ratios for the most recent three years for which audited financial statements are available. Category B projects must also provide the viability ratios for the first full fiscal year after project completion or for the first full fiscal year when the project achieves or exceeds target utilization (per Part 1100), whichever is later.

Provide Data for Projects Classified as:	Category A or Category B (last three years)			Category B
Enter Historical and/or Projected Years:	FY2005	FY2006	FY2007	FY2012
Current Ratio	.8	.9	1.6	1.5
Net Margin Percentage	2.3%	2.9%	9.0%	1.2%
Percent Debt to Total Capitalization	85%	71%	52%	53.7%
Projected Debt Service Coverage	1.79	2.56	6.54	2.87
Days Cash on Hand	45	54.6	45	60
Cushion Ratio	2.4	3.9	5.1	6.0

Provide the methodology and worksheets utilized in determining the ratios detailing the calculation and applicable line item amounts from the financial statements. Complete a separate table for each co-applicant and provide worksheets for each. Insert the worksheets after this page.

2. Variance

Compare the viability ratios provided to the Part 1120 Appendix A review standards. If any of the standards for the applicant or for any co-applicant are not met, provide documentation that a person or organization will assume the legal responsibility to meet the debt obligations should the applicant default. The person or organization must demonstrate compliance with the ratios in Appendix A when proof of a bond rating of "A" or better has not been provided.

APPEND DOCUMENTATION AS <u>ATTACHMENT FIN-1</u> AFTER THE LAST PAGE OF THIS SECTION.

B. Criterion 1120.210.b, Availability of Funds

If proof of an "A" or better bond rating has not been provided, read the criterion and document that sufficient resources are available to fund the project and related costs including operating start-up costs and operating deficits. Indicate the dollar amount to be provided from the following sources:

2,135,856.00 Cash & Securities
Provide statements as to the amount of cash/securities available for the project. Identify any security, its value and availability of such funds. Interest to be earned or depreciation account funds to be earned on any asset from the date of application submission through project completion are also considered cash.

________ Pledges
For anticipated pledges, provide a letter or report as to the dollar amount feasible showing the discounted value and any conditions or action the applicant would have to take to accomplish goal. The time period, historical fund raising experience and major contributors also must be specified.

________ Gifts and Bequests
Provide verification of the dollar amount and identify any conditions of the source and timing of its use.

26,893,300.00 Debt Financing (indicate type(s) FHA insured mortgage under Section 242)
For general obligation bonds, provide amount, terms and conditions, including any anticipated discounting or shrinkage) and proof of passage of the required referendum or evidence of governmental authority to issue such bonds;
For revenue bonds, provide amount, terms and conditions and proof of securing the specified amount;
For mortgages, provide a letter from the prospective lender attesting to the expectation of making the loan in the amount and time indicated;
For leases, provide a copy of the lease including all terms and conditions of the lease including any purchase options.

________ Governmental Appropriations
Provide a copy of the appropriation act or ordinance accompanied by a statement of funding availability from an official of the governmental unit. If funds are to be made available from subsequent fiscal years, provide a resolution or other action of the governmental unit attesting to such future funding.

________ Grants
Provide a letter from the granting agency as to the availability of funds in terms of the amount, conditions, and time or receipt.

________ Other Funds and Sources
Provide verification of the amount, terms and conditions, and type of any other funds that will be used for the project.

29,029,156.00 TOTAL FUNDS AVAILABLE

APPEND DOCUMENTATION AS ATTACHMENT FIN-2 AFTER THE LAST PAGE OF THIS SECTION.

C. Criterion 1120.210.c, Operating Start-up Costs

If proof of an "A" or better bond rating has not been provided, indicate if the project is classified as a Category B project that involves establishing a new facility or a new category of service? Yes ☐ No ☒. If yes is indicated read the criterion and provide in the space below the amount of operating start-up costs (the same as reported in Section I of this application) and provide a description of the items or components that comprise the costs. Indicate the source and amount of the financial resources available to fund the operating start-up costs (including any initial operating deficit) and reference the documentation that verifies sufficient resources are available.

MERCY HOSPITAL AND MEDICAL CENTER
Section XXIV - Review Criteria Related to Financial Feasibility
Part 1120.210a-Financial Viability
Viability Ratio-Support
(000's OMITTED)

	ACTUAL FYE JUN 05	ACTUAL FYE JUN 06	ACTUAL FYE JUN 07	PROJECTED FYE JUN 12	STATE GUIDELINES
CURRENT RATIO					
CURRENT ASSETS	$37,351	$39,936	$62,110	$56,334	
CURRENT LIABILITIES	$45,310	$44,714	$38,795	$37,768	
RATIO	.8	.9	1.6	1.5	1.5 MIN
NET MARGIN PERCENTAGE					
NET INCOME	$4,304	$5,124	$19,961	$2,811	
NET OPERATING REVENUE	$187,724	$178,502	$222,148	$223,304	
RATIO	2.3%	2.9%	9.0%	1.2	3.5% MIN
PERCENT DEBT TO TOTAL CAPITALIZATION					
LONG-TERM DEBT	$32,815	$31,313	$36,213	$67,439	
UNRESTRICTED FUND BALANCE	$5,811	$12,970	$32,984	$58,213	
TOTAL	$38,626	$44,283	$69,197	$125,652	
RATIO	85%	71%	52%	53.7%	60% MAX
PROJECTED DEBT SERVICE COVERAGE					
NET INCOME	$4,304	$5,124	$19,961	$2,811	
DEPRECIATION	$8,419	$8,374	$8,278	$9,853	
INTEREST.NET	$3,725	$2,743	$2,816	$4,665	
TOTAL	$16,448	$16,241	$31,055	$17,329	
PRINCIPAL PAYMENTS	$4,956	$3,714	$1,817	$1,364	
NET INTEREST PAYMENTS	$4,252	$2,639	$2,931	$4,665	
ANNUAL DEBT SERVICE	$9,208	$6,353	$4,748	$6,029	
DEBT SERVICE RATIO	1.79	2.56	6.54	2.87	1.75 MIN
MAXIMUM ANNUAL DEBT SERVICE	$9,208	$6,353	$4,748	$6,029	
MAXIMUM DEBT SERVICE RATIO	1.79	2.56	6.54	2.87	1.75MIN
DAYS CASH ON HAND					
CASH & EQUIVALENTS	$9,578	$10,867	$10,632	$13,035	
INVESTMENTS & BOARD DESIGNATED FUNDS	$12,088	$14,050	$13,794	$23,132	
TOTAL ASSETS AVAILABLE	$21,666	$24,917	$24,426	$36,167	
TOTAL EXPENSES	$184,002	$174,984	$206,546	$229,359	
LESS DEPRECIATION	$8,419	$8,374	$3,278	$9,853	
NET EXPENSES	$175,583	$166,610	$203,268	$219,506	
AVERAGE DAILY EXPENSE	$481	$456	$542	$601	
DAYS CASH ON HAND	45.0	54.6	45.0	60	90 MIN
CUSHION RATIO					
CASH & EQUIVALENTS	$9,578	$10,867	$10,632	$13,035	
INVESTMENTS & BOARD DESIGNATED FUNDS	$12,088	$14,050	$13,794	$23,132	
TOTAL ASSETS AVAILABLE	$21,666	$24,917	$24,426	$36,167	
MAXIMUM ANNUAL DEBT SERVICE	$9,208	$6,353	$4,748	$6,029	
CUSHION RATIO	2.4	3.9	5.1	6.0	5 MIN

Section XXIV, Item A. Financial Viability

Please note that the co-applicant, Mercy Health System of Chicago, did not separately complete the ratios, as it has only limited assets, as further outlined in the attached consolidated financial statements.

As it is insuring the Hospital's mortgage, the U.S. Department of Housing and Urban Development is assuming the legal responsibility to meet the Hospital's mortgage obligations should the Hospital default.

Section XXIV, Item B. Availability of Funds

Attached is information on the debt financing related to the project.

JPMorgan

Timothy Wons
Executive Director
J.P. Morgan Securities Inc.
Tax Exempt Capital Markets
10 S. Dearborn St. 32nd Floor
Chicago, IL 60670
Tel: 312-385-8455
Fax: 312-732-2400

Jay Shah
Vice President
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Chicago, IL 60670
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Fax: 312-732-2400

June 3, 2008

Thomas J. Garvey
Vice President of Finance and Chief Financial Officer
Mercy Hospital & Medical Center
2525 South Michigan Avenue
Chicago, IL 60616-2477

Dear Tom,

J.P. Morgan Securities Inc. has been retained to assist Mercy Hospital & Medical Center ("Mercy") in obtaining permanent financing in an amount up to $85,000,000 for the purpose of renovating and equipping its existing facilities in Chicago, Illinois. As part of our engagement, we are providing the attached preliminary term sheet outlining a potential approach to this financing.

Please note that the attached term sheet does not represent a commitment to lend money on the part of J.P. Morgan Securities Inc. A commitment to finance or underwrite these bonds would require formal credit approval and would be subject to additional due diligence.

We look forward to this opportunity to assist Mercy.

Timothy Wons
Executive Director

ATTACHMENT FIN-2

JPMorgan

Proposed Term Sheet

Transaction	FHA 242 insured mortgage securing an issuance of tax-exempt bonds pursuant to a Master Trust Indenture and associated bond documentation among Trustee, Issuer and Obligor
Amount	Up to $85,000,000
Use of Bond Proceeds	1) Funding the construction and equipment of renovations to the existing facilities including a birthing center, GI lab, Cardiac Care Unit and hospital wide sprinkler system 2) Funding of a debt service reserve fund 3) Paying for costs of issuance
Interest Rate	To be determined
Term	To be determined - not to exceed 30 years
Closing Date	The Series 2008 bonds are anticipated to be delivered as soon as reasonably possible upon receipt of a Certificate of Need and related approvals
Rating	The bonds will be carry the ratings associated with the FHA mortgage insurance ("AA")
Debt Service Reserve Fund	A Debt Service Reserve Fund will be required
Security	Pledge of general revenues and a mortgage on all real property that comprises the core operations of the obligor
Financial Covenants	Usual and customary with threshold levels to be negotiated with the hospital

SECTION XXV. REVIEW CRITERIA RELATING TO ECONOMIC FEASIBILITY (ECON)

This section is applicable to all projects subject to Part 1120.

A. Criterion 1120.310.a, Reasonableness of Financing Arrangements

Is the project classified as a Category B project? Yes ☒ No ☐. If no is indicated this criterion is not applicable. If yes is indicated, has proof of a bond rating of "A" or better been provided? Yes ☐ No ☒. If yes is indicated this criterion is not applicable, go to item B. If no is indicated, read the criterion and address the following:

Are all available cash and equivalents being used for project funding prior to borrowing? ☐ Yes ☒ No

If no is checked, provide a notarized statement signed by two authorized representatives of the applicant entity (in the case of a corporation, one must be a member of the board of directors) that attests to the following:

1. a portion or all of the cash and equivalents must be retained in the balance sheet asset accounts in order that the current ratio does not fall below 2.0 times; or
2. borrowing is less costly than the liquidation of existing investments and the existing investments being retained may be converted to cash or used to retire debt within a 60-day period.

APPEND DOCUMENTATION AS <u>ATTACHMENT ECON-1</u> AFTER THE LAST PAGE OF THIS SECTION.

B. Criterion 1120.310.b, Conditions of Debt Financing

Read the criterion and provide a notarized statement signed by two authorized representatives of the applicant entity (in the case of a corporation, one must be a member of the board of directors) that attests to the following as applicable:

1. The selected form of debt financing the project will be at the lowest net cost available or if a more costly form of financing is selected, that form is more advantageous due to such terms as prepayment privileges, no required mortgage, access to additional debt, term (years) financing costs, and other factors;
2. All or part of the project involves the leasing of equipment or facilities and the expenses incurred with such leasing are less costly than constructing a new facility or purchasing new equipment.

APPEND DOCUMENTATION AS <u>ATTACHMENT ECON-2</u> AFTER THE LAST PAGE OF THIS SECTION.

C. Criterion 1120.310.c, Reasonableness of Project and Related Costs

Read the criterion and provide the following:

1. Identify each department or area impacted by the proposed project and provide a cost and square footage allocation for new construction and/or modernization using the following format (insert after this page).

COST AND GROSS SQUARE FEET BY DEPARTMENT OR SERVICE

Department (list below)	A Cost/Square Foot New	B Mod.	C Gross Sq. Ft. New	D Circ.*	E Gross Sq. Ft. Mod.	F Circ.*	G Const. $ (A x C)	H Mod. $ (B x E)	Total Cost (G + H)
Contingency									
TOTALS									

*Include the percentage (%) of space for circulation

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Section XXV, Item C. Reasonableness of Project and Related Costs

1. Cost and Gross Square Feet by Department or Service

	A	B	C	D	E	F	G	H	Total
Department	Cost/Square Foot New	Mod.	Gross Square Feet New	Circ.	Gross Square Feet Mod.	Circ.	Const. $ (A x C)	Mod. $ (B x E)	(G + E)
OB/GYN	0	$263.4982*	0	0	14,371	19%	0	3,786,733	3,786,733
ICU	0	$439.305*	0	0	8,805	22%	0	3,868,081	3,868,081
Med/Surg	0	$319.3535*	0	0	2,708	0	0	864,809	864,809
GI Labs	0	$449.5274*	0	0	5,026	27%	0	2,259,325	2,259,325
Non-clinical (Admin, staff lounges/ locker rooms, etc.)	0	$206.44	0	0	3,376	0	0	696,941	696,941
Non-clinical fire alarm	0	$5.07697	0	0	716,515	0	0	3,637,732	3,637,732
Non-clinical sprinkler	0	$20.13	0	0	458,503	0	0	9,234,248	9,234,248
Non-clinical S-27 Air Handler	0	$23.9914	0	0	20,571	0	0	493,528	493,528
Contingency	0	$1.26	0	0	716,515	0	0	905,574	905,574
TOTALS	**0**	**1728.58247**	**0**	**0**	**1,943,960**	**68%**	**0**	**25,746,971**	**25,746,971**

* This amount includes the cost of site preparation.

2. For each piece of major medical equipment included in the proposed project, the applicant must certify one of the following:

   a. that the lowest net cost available has been selected; or

   b. that the choice of higher cost equipment is justified due to such factors as, but not limited to, maintenance agreements, options to purchase, or greater diagnostic or therapeutic capabilities.

APPEND DOCUMENTATION AS ATTACHMENT ECON-3 AFTER THE LAST PAGE OF THIS SECTION.

3. List the items and costs included in preplanning, site survey, site preparation, off-site work, consulting, and other costs to be capitalized. If any project line item component includes costs attributable to extraordinary or unusual circumstances, explain the circumstances and provide the associated dollar amount. When fair market value has been provided for any component of project costs, submit documentation of the value in accordance with the requirements of Part 1190.40.

APPEND DOCUMENTATION AS ATTACHMENT ECON-4 AFTER THE LAST PAGE OF THIS SECTION.

D. Criterion 1120.310.d, Projected Operating Costs

Read the criterion and provide in the space below the facility's projected direct annual operating costs (in current dollars per equivalent patient day or unit of service, as applicable) for the first full fiscal year of operation after project completion or for the first full fiscal year when the project achieves or exceeds target utilization pursuant to 77 Ill. Adm. Code 1100, whichever is later. If the project involves a new category of service, also provide the annual operating costs for the service. Direct costs are the fully allocated costs of salaries, benefits, and supplies. Indicate the year for which the projected operating costs are provided.

E. Criterion 1120.310.e, Total Effect of the Project on Capital Costs

Is the project classified as a category B project? Yes ☒ No ☐. If no is indicated, go to item F. If yes is indicated, provide in the space below the facility's total projected annual capital costs as defined in Part 1120.130.f (in current dollars per equivalent patient day) for the first full fiscal year of operation after project completion or for the first full fiscal year when the project achieves or exceeds target utilization pursuant to 77 Ill. Adm. Code 1100, whichever is later. Indicate the year for which the projected capital costs are provided.

F. Criterion 1120.310.f, Non-patient Related Services

Is the project classified as a category B project and involve non-patient related services? Yes ☐ No ☒. If no is indicated, this criterion is not applicable. If yes is indicated, read the criterion and document that the project will be self-supporting and not result in increased charges to patients/residents or that increased charges are justified based upon such factors as, but not limited to, a cost benefit or other analysis that demonstrates the project will improve the applicant's financial viability.

APPEND DOCUMENTATION AS ATTACHMENT ECON-5 AFTER THE LAST PAGE OF THIS SECTION.

D: FY2012: $146,483,000; operating cost per equivalent patient day: 146,483,000/101,105 = $1,449. These costs include salaries and wages ($93,977,000), employee benefits ($19,181,000) and supplies and pharmaceuticals ($33,325,000).

E: FY2012: $14,518,000; capital cost per equivalent patient day: 14,518,000/101,105 = $143.59.

MERCY

Mercy Hospital & Medical Center
2525 South Michigan Avenue
Chicago, Illinois 60616-2477
phone 312.567.2000

May 19, 2008

Health Facilities Planning Board
525 West Jefferson
2nd Floor
Springfield, Illinois 62761

Re: Debt Financing, Modernization of Mercy Hospital

To Whom It May Concern:

We are writing this letter in accordance with the requirements of Certificate of Need Criterion 1120.310.a – Reasonableness of Financing Arrangements. We hereby attest to the fact that borrowing is less costly than the liquidation of existing investments and the existing investments being retained may be converted to cash or used to retire debt within a 60-day period.

Sincerely,

Name: Sister Sheila Lyne
Title: President / CEO

Name: John McCarthy
Title: Chair of the Board of Directors

Subscribed and Sworn to before me this
19th day of May, 2008

Sandra A. Schueler
Notary

OFFICIAL SEAL
SANDRA A SCHUELER
NOTARY PUBLIC - STATE OF ILLINOIS
MY COMMISSION EXPIRES:03/10/11

ATTACHMENT ECON-1

MERCY

Mercy Hospital & Medical Center
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Chicago, Illinois 60616-2477
phone 312.567.2000

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NOTARY PUBLIC - STATE OF ILLINOIS
MY COMMISSION EXPIRES:03/10/11

MERCY

MERCY HOSPITAL & MEDICAL CENTER
2525 SOUTH MICHIGAN AVENUE
CHICAGO, ILLINOIS 60616-2477
phone 312.567.2000

May 19, 2008

Health Facilities Planning Board
525 West Jefferson
2nd Floor
Springfield, Illinois 62761

Re: Debt Financing, Modernization of Mercy Hospital

To Whom It May Concern:

We are writing this letter in accordance with the requirements of Certificate of Need Criterion 1120.310.b – Conditions of Debt Financing. We hereby attest to the fact that the selected form of debt financing for the proposed project represents the lowest net cost available. The project does not involve the leasing of equipment or facilities.

Sincerely,

Name: Sister Sheila Lyne
Title: President/CEO

Name: John McCarthy
Title: Chair of the Board of Directors

Subscribed and Sworn to before me this
19th day of May, 2008

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Sincerely,

Sheila Lyne

Name: Sister Sheila Lyne
Title: President/CEO

John McCarthy

Name: John McCarthy
Title: Chair of the Board of Directors

Subscribed and Sworn to before me this
19th day of May, 2008

OFFICIAL SEAL
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NOTARY PUBLIC - STATE OF ILLINOIS
MY COMMISSION EXPIRES:03/10/11

Sandra A. Schueler
Notary

Section XXV, Item C. Reasonableness of Project and Related Costs, Continued

2. N/A. No major medical equipment is included in the proposed project.

Section XXV, Item C. Reasonableness of Project and Related Costs, Continued

3. The project does not require preplanning, site survey, or off-site work. The site preparation costs to be capitalized are $417,318. The consulting costs to be capitalized are $77,814.

Section XXIV, Financials

Attached are the audited financial statements for the past three years. Please note that these are consolidated financial statements; the applicants, Mercy Hospital and Medical Center and Mercy Health System of Chicago, do not have separate audited financial statements.

Mercy Health System of Chicago and Subsidiaries

Consolidated Financial Report

June 30, 2007

ATTACHMENT FINANCIALS

Contents

McGladrey & Pullen
Certified Public Accountants

Independent Auditor's Report on the Financial Statements

To the Board of Directors
Mercy Health System of Chicago
Chicago, Illinois

We have audited the accompanying consolidated balance sheets of Mercy Health System of Chicago and subsidiaries (the "Corporation") as of June 30, 2007 and 2006, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mercy Health System of Chicago and subsidiaries as of June 30, 2007 and 2006, and the results of their operations and changes in net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

McGladrey & Pullen, LLP

Chicago, Illinois
October 30, 2007

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ATTACHMENT FINANCIALS

Mercy Health System of Chicago and Subsidiaries

Consolidated Balance Sheets
June 30, 2007 and 2006

	2007	2006
Assets		
Current Assets		
Cash and cash equivalents	$ 6,786,970	$ 7,291,637
Investments and assets limited as to use		
Internally designated under self-insurance program	30,636	127,211
Short-term investments	3,846,092	1,826,802
Patient accounts receivable, net of allowance for doubtful accounts of $8,933,000 in 2007 and $11,362,000 in 2006	33,141,041	26,568,161
Due from related party	423,755	-
Inventories	2,153,453	2,147,405
Medicaid assessment revenue receivable	12,596,005	-
Grant receivable	1,000,000	-
Other current assets	2,132,123	1,974,922
Total current assets	62,110,075	39,936,138
Investments and Assets Limited as to Use, net of amounts required to meet current obligations		
Pledged under debt agreement	12,041,020	12,040,542
Externally designated under lease agreement	-	717,662
Internally designated under self-insurance program	1,933,333	2,009,888
Other Investments	1,632,059	2,682,589
	15,606,412	17,450,681
Property and Equipment		
Land and land improvements	8,486,591	8,753,112
Buildings and fixtures	109,443,733	106,443,732
Equipment	120,906,482	117,627,148
Construction in progress	5,103,306	4,183,699
	243,940,112	237,007,691
Less accumulated depreciation	(186,210,094)	(178,250,906)
	57,730,018	58,756,785
Other Assets		
Deferred financing costs, net	207,978	474,253
Investment in joint venture and other	1,723,356	1,212,436
	1,931,334	1,686,689
Total assets	$ 137,377,839	$ 117,830,293

See Notes to Consolidated Financial Statements.

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	2007	2006
Liabilities and Net Assets		
Current Liabilities		
Accounts payable	$ 15,366,826	$ 18,195,144
Accrued expenses	8,303,295	8,033,457
Due to third-party payors	573,583	6,257,664
Current portion of long-term debt	914,253	6,522,676
Medicaid assessment tax payable	6,039,734	-
Current portion of professional liability	6,472,666	5,580,667
Current portion of deferred grant revenue	1,125,000	125,000
Total current liabilities	38,795,357	44,714,608
Noncurrent Liabilities		
Long-term debt, less current portion	36,213,018	31,313,062
Professional liability, less current portion	17,491,667	17,604,333
Financing obligation arising from sale-leaseback transaction	7,537,158	7,331,968
Deferred grant revenue, less current portion	1,821,323	1,978,562
Total liabilities	101,858,523	102,942,533
Commitments and Contingencies (Notes 9 and 14)		
Net Assets:		
Unrestricted	32,983,553	12,970,267
Temporarily restricted	2,223,203	1,604,933
Permanently restricted	312,560	312,560
Total net assets	35,519,316	14,887,760
Total liabilities and net assets	$ 137,377,839	$ 117,830,293

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Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets
Years Ended June 30, 2007 and 2006

	2007	2006
Revenue:		
Net patient service revenue	$ 190,180,524	$ 171,780,631
Medicaid assessment revenue	25,192,010	-
Capitation revenue	1,904,432	1,698,339
Contributions	994,439	867,944
Other	3,515,005	3,826,466
Net assets released from restriction - used for operations	361,601	328,519
	222,148,011	178,501,899
Expenses:		
Salaries and benefits	97,504,896	90,200,686
Supplies	29,315,853	25,775,952
Insurance, net (Note 11)	4,766,676	(2,242,683)
Depreciation and amortization	8,278,329	8,373,976
Provision for uncollectible accounts	11,631,073	14,323,749
Interest	2,815,971	2,743,940
Professional fees	6,295,101	5,473,887
Repairs, utilities and rent	13,320,459	11,615,181
Purchased services	17,229,098	14,543,733
Medicaid assessment tax	12,079,468	-
Other	3,309,598	4,175,355
	206,546,522	174,983,776
Operating income	15,601,489	3,518,123
Nonoperating income:		
Gain on sale of property	2,932,909	848,808
Investment income	1,057,432	757,905
Income from joint venture	369,449	-
	4,359,790	1,606,713
Excess of revenue over expenses	$ 19,961,279	$ 5,124,836

(Continued)

ATTACHMENT FINANCIALS

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Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets (Continued)
Years Ended June 30, 2007 and 2006

	2007	2006
Unrestricted net assets		
Excess of revenue over expenses	$ 19,961,279	$ 5,124,836
Net change in unrealized gains and losses on investments	52,007	(2,543)
Forgiveness of note payable	-	2,075,000
Increase in unrestricted net assets	**20,013,286**	7,197,293
Temporarily restricted net assets		
Contributions	979,871	415,610
Net assets released from restrictions - used for operations	(361,601)	(328,519)
Increase in temporarily restricted net assets	**618,270**	87,091
Increase in net assets	**20,631,556**	7,284,384
Net assets:		
Beginning of year	14,887,760	7,603,376
End of year	$ 35,519,316	$ 14,887,760

See Notes to Consolidated Financial Statements.

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ATTACHMENT FINANCIALS

Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Cash Flows
Years Ended June 30, 2007 and 2006

	2007	2006
Cash Flows from Operating Activities		
Increase in net assets	$ 20,631,556	$ 7,284,384
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Net change in unrealized gains and losses on investments	(52,007)	2,543
Depreciation	7,959,188	8,115,478
Amortization	319,141	258,498
Provision for uncollectible accounts	11,631,073	14,323,749
Gain on sale of property	(2,932,909)	(848,808)
Amortization of deferred grant revenue	(157,239)	(189,478)
Interest added to financing obligation arising from sale-leaseback transaction	205,190	285,327
Forgiveness of note payable	-	(2,075,000)
Changes in operating assets and liabilities:		
Accounts receivable	(18,203,953)	(16,797,611)
Medicaid assessment tax receivable and payable	(6,556,271)	-
Grant receivable	(1,000,000)	-
Other assets	(727,035)	(108,905)
Accounts payable and accrued expenses	(1,955,784)	1,400,048
Due to third-party payors	(5,684,081)	1,227,373
Professional liability	779,333	(4,601,000)
Deferred grant revenue	1,000,000	-
Net cash provided by operating activities	5,256,202	8,276,598
Cash Flows from Investing Activities		
Purchases of property and equipment	(6,182,263)	(8,148,311)
Payments of accounts payable for the purchase of property and equipment	(1,613,701)	-
Purchases of investments and assets limited as to use and other investments	(5,160,976)	(3,123,554)
Proceeds from sale of property	3,193,756	1,065,391
Proceeds from sale/maturity of investments and assets limited to use	5,134,537	3,941,946
Repayment from related party	-	234,573
Advances to affiliate	(423,755)	-
Net cash (used in) investing activities	(5,052,402)	(6,029,955)
Cash Flows from Financing Activities		
Net proceeds from long-term debt	299,956	-
Payments on long-term debt	(1,008,423)	(2,422,015)
Payment of deferred financing costs	-	(253,098)
Proceeds from grant, for property and equipment	-	32,239
Net cash (used in) financing activities	(708,467)	(2,642,874)
Net (decrease) in cash and cash equivalents	(504,667)	(396,231)

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ATTACHMENT FINANCIALS

(Continued)

Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Cash Flows (Continued)
Years Ended June 30, 2007 and 2006

		2007		2006
Cash and cash equivalents:				
Beginning	$	7,291,637	$	7,687,868
Ending	$	6,786,970	$	7,291,637
Supplemental Disclosures of Cash Flow Information				
Cash paid for interest, net of amounts capitalized of $288,500 in 2007 and $259,000 in 2006	$	2,855,602	$	2,636,915
Supplemental Schedule of Noncash Investing and Financing Activities				
Property and equipment additions included in accounts payable	$	1,011,005	$	1,613,701

See Notes to Consolidated Financial Statements.

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Note 1. Nature of Business and Significant Accounting Policies

Organization and nature of business: The accompanying consolidated financial statements represent the accounts of Mercy Health System of Chicago ("Parent") and its subsidiaries (jointly, the "Corporation"). The Corporation is sponsored by the Sisters of Mercy of the Americas, Regional Community of Chicago ("Sisters of Mercy"), a religious institute. Subsidiaries of the Parent include Mercy Health Care Rehabilitation Center ("Center"), Mercy Services Corporation ("MSC"), Mercy Hospital and Medical Center ("Hospital"), and Mercy Foundation, Inc. ("Foundation").

The Hospital is a licensed 479-bed acute care facility with its primary market in the south and southwest side of Chicago, Illinois, and adjacent suburbs. In addition to the main facility, the Hospital has a network of hospital-owned primary care centers, private physician offices, and a number of satellites throughout the City of Chicago.

All of MSC's stock is owned by the Parent. MSC has been inactive since the transfer of its operations to the Hospital.

The Foundation was organized for the purpose of collecting, earning, and receiving funds from public and private sources, accumulating such funds, and making distributions of income to the Parent or related entities properly designated by the Parent.

The Center's assets were sold in December 2001. According to the sale agreement, $300,000 was placed into a trust account to be used to offset Medicare and Medicaid audit adjustments related to periods prior to the sale. Unused funds were released to the Hospital in February 2005. Other than recognizing interest income and expenses related to the release of the trust monies, the Center has been inactive.

The Corporation is a 51% owner of Mercy Heart and Vascular, LLC, a for-profit corporation, which was established for the purpose of subleasing computed tomography (CT) space and equipment for the overall purpose of promoting health and providing quality health care services to a broad section of the community. The Corporation accounts for this joint venture using the equity method.

A summary of significant accounting policies follows:

Principles of consolidation: The accompanying consolidated financial statements include the Parent, Center, MSC, Hospital and Foundation. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of estimates: The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The use of estimates and assumptions in the preparation of the accompanying financial statements is primarily related to the determination of the net patient accounts receivable and settlements with third-party payors and the accrual for professional liability. Due to uncertainties inherent in the estimation and assumption process, it is at least reasonably possible that changes in these estimates and assumptions in the near-term would be material to the financial statements.

Basis of presentation: The Corporation may classify its net assets into three categories, which are unrestricted, temporarily restricted and permanently restricted.

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Unrestricted net assets are reflective of revenues and expenses associated with the principal operating activities of the Corporation and are not subject to donor-imposed stipulations.

Temporarily restricted net assets are subject to donor-imposed stipulations that may or will be met either by actions of the Corporation and/or the passage of time. As of June 30, 2007 and 2006, temporarily restricted net assets were restricted by donors primarily for patient care, community service, education, research, and purchase of equipment. Income earned on donor-restricted marketable securities, unless restricted by donors, is reflected in investment income. When a donor restriction expires, temporarily restricted net assets are classified as unrestricted net assets and reported in the statement of operations and changes in net assets as other revenue.

Permanently restricted net assets have been restricted by donors to be maintained by the Corporation in perpetuity. The income earned on permanently restricted net assets has been restricted by donors to provide care for the poor.

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

Cash and cash equivalents: All investments that are not limited as to use with an original maturity of three months or less at the time of acquisition are reflected as cash equivalents.

Throughout the year, the Corporation may have amounts on deposit with financial institutions in excess of those insured by the FDIC. Management does not believe this presents a significant risk to the Corporation.

Patient accounts receivable, provision for doubtful accounts and due from/to third party-payors: The collection of receivables from third-party payors and patients is the Corporation's primary source of cash for operations and is critical to its operating performance. The primary collection risks relate to uninsured patient accounts and patient accounts for which the primary insurance payor has paid, but patient responsibility amounts (deductibles and co-payments) remain outstanding. Patient receivables, where a third-party payor is responsible for paying the amount, are carried at a net amount determined by the original charge for the service provided, less an estimate made for contractual adjustments or discounts provided to third-party payors.

Patient receivables due directly from the patients are carried at the original charge for the service provided less amounts covered by third-party payors and less an estimated allowance for uncollectible receivables. Management estimates this allowance based on the aging of its accounts receivable and its historical collection experience for each payor type. Recoveries of receivables previously written off are recorded as a reduction of the provision for uncollectible accounts when received.

The past due status of receivables is determined on a case-by-case basis depending on the payor responsible. Interest is generally not charged on past due accounts.

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Receivables or payables related to estimated settlements on various payor contracts, primarily Medicare, are reported as amounts due from or to third-party payors. Significant changes in payor mix, business office operations, economic conditions or trends in federal and state governmental health care coverage could affect the Corporation's collection of accounts receivable, cash flows and results of operations.

Inventories: Inventories are stated at cost (first-in, first-out method). Inventories consist primarily of supplies inventories.

Investments and assets limited as to use: Investments are recorded at fair value based on quoted market prices. Realized investment income is included in excess of revenue over expenses unless the income or loss is restricted by donor or law. The change in unrealized appreciation in fair value of investments is recognized as a change in net assets.

Investments are regularly evaluated for impairment. The Corporation considers factors affecting the investee, factors affecting the industry the investee operates within, and general debt and equity trends. The Corporation considers the length of time an investment's fair value has been below carrying value, the near-term prospects for recovery to carrying value, and the intent and ability to hold the investment until maturity date or market recovery is realized. If and when a determination is made that a decline in fair value below the cost basis is other than temporary, the related investment is written down to its estimated fair value and included as a realized loss in excess of revenue over expenses.

Assets limited as to use consist of investments set aside by the Board for self-insurance over which the Board retains control and may, at its discretion, subsequently use for other purposes. Assets limited as to use also include investments externally designated under debt and lease agreements.

Property and equipment: Property and equipment are recorded at cost and depreciated on the straight-line method over their estimated useful lives. The assets' lives are as follows:

Land improvements	5 years
Buildings and fixtures	5 - 40 years
Furniture and equipment	3 - 20 years
Automobiles	3 - 4 years
Leasehold improvements	15 - 20 years

Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

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

Accrued professional liability: The provision for accrued professional liability includes estimates of the ultimate costs for claims incurred but not reported. The provision is actuarially determined. The Corporation is completely self-insured for all claims incurred on and after July 1, 2002.

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Deferred financing costs: Costs incurred in connection with the issuance or refinancing of long-term debt are deferred and amortized over the term of the related financing on a method that approximates the effective yield method.

Community commitment: Community commitment includes patient charity care rendered to the community at a reduced rate or at no fee based upon community need or the inability of the individual to pay for services. Because the Corporation does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Net patient service revenue: The Corporation has agreements with third-party payors that provide for payments to the Corporation at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Capitation revenue: The Corporation has an agreement with Independent Physician Association at Mercy (IPA@M), an independent physician association (IPA), to provide outpatient diagnostic services for a monthly capitation fee. IPA@M receives capitation payments from various health maintenance organizations (HMOs) and sub-capitates to the Hospital for outpatient diagnostic services. Under this agreement, the Corporation receives monthly capitation payments based on the number of the IPA's participants, regardless of the outpatient diagnostic services actually performed by the Corporation.

Operating income: The consolidated statements of operations and changes in net assets include operating income. Changes in unrestricted net assets, which are excluded from operating income, include investment income, gains and losses from sales of property and equipment, and other income and expense which management views as outside of normal activity.

Excess of revenues over expenses: The consolidated statements of operations and changes in net assets include excess of revenue over expenses that represents the results of operations. Changes in unrestricted net assets that are excluded from excess of revenues over expenses, consistent with industry practice, include the change in net unrealized appreciation in fair value of investments, and forgiveness of notes payable by related parties.

Income taxes: The Parent, the Hospital, the Center, and the Foundation have received determination letters from the Internal Revenue Service stating that they are exempt from the payment of federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

At June 30, 2007, MSC had approximately $1,566,000 of net operating tax loss carryforwards available for use against future taxable income, which begin to expire in 2012. As a result of the net operating tax loss carryforwards, there is no income tax provision in 2007 and 2006. Due to the uncertain future realization of these loss carryforwards, the related tax assets have been fully reserved by a valuation allowance in the accompanying consolidated balance sheets.

Reclassifications: Certain amounts within the 2006 consolidated financial statements have been reclassified to conform with the 2007 presentation with no effect on net assets.

Note 2. Net Patient Service Revenue

The Corporation has agreements with third-party payors which provide for reimbursement to the Corporation at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Corporation's billings at list price and the amounts reimbursed by Medicare, Medicaid, Blue Cross, and certain other third-party payors, and any differences between estimated third-party reimbursement settlements for prior years and subsequent final settlements. Contractual adjustments under third-party reimbursement programs are accrued on an estimated basis in the period the related services are rendered and are adjusted in future periods as final settlements are determined. A summary of the basis of reimbursement with major third-party payors follows:

Medicare: The Corporation is paid for inpatient acute care and outpatient care services rendered to Medicare program beneficiaries under prospectively determined rates per discharge (Prospective Payment Systems). These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient non-acute services and defined capital and medical education costs related to Medicare beneficiaries are paid based upon either a cost reimbursement method or established fee screens, or a combination thereof. The Corporation's classification of patients under Prospective Payment Systems and the appropriateness of the patient's admissions are subject to validation reviews. The Corporation is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual reimbursement reports by the Corporation and audits by the Medicare fiscal intermediary.

For the years ended June 30, 2007 and 2006, the Corporation recognized approximately $169,765,000 and $158,854,000, respectively, of gross patient service revenues from services provided to Medicare beneficiaries. Changes in Medicare reimbursement as a result of the Centers for Medicare and Medicaid Services' implementation of the provisions of future Medicare legislation may have an adverse effect on the Corporation's net patient service revenue. Fiscal year 2008 will represent the first of a three-year phase-in period for implementation of a revised Medicare Diagnosis Related Group (DRG) reimbursement system. This new payment methodology makes meaningful refinements to the current CMS classification system to increase recognition of severity of illness. However, there will be a limited impact on payments in specific DRGs because of the simultaneous implementation of incremental reforms for cost-based and severity-based payments.

Laws and regulations governing the Medicare program are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near-term. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare program. Net patient service revenue in 2007 and 2006 increased by the effect of third-party payor settlements by approximately $284,000 and $1,200,000, respectively. At June 30, 2006, the Hospital recorded a liability of approximately $3,500,000 in connection with the Medicare disproportionate share (DSH) settlements related to fiscal years ended June 30, 2006, 2005 and 2004. In fiscal year 2007, approximately $3,200,000 of the 2006 liability was reversed as the Federal Centers of Medicare and Medicaid Services (CMS) is now allowing Title 21 days.

Note 2. Net Patient Service Revenue (Continued)

Medicaid: The Corporation is reimbursed at prospectively determined rates for each Medicaid inpatient discharge. Outpatient services are reimbursed based on established fee screens. For inpatient acute care services, payment rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. The prospectively determined rates are not subject to retroactive adjustment. As described below, the Corporation also receives incremental Medicaid reimbursement for specific programs and services at the discretion of the State of Illinois Medicaid Program. Medicaid reimbursement may be subject to periodic adjustment, as well as to changes in existing payment levels and rates, based on the amount of funding available to the Medicaid program.

For the years ended June 30, 2007 and 2006, the Corporation recognized approximately $122,424,000 and $104,234,000, respectively, of gross patient service provided to Medicaid patients. Due to the Hospital's relatively high Medicaid patient volume, the Hospital received additional reimbursement of approximately $13,430,000 in both 2007 and 2006 in the form of critical hospital adjustment payments ("CHAP"), safety net access payments ("SNAP") and tertiary payments, the majority of which is provided by the Illinois Medicaid program. The Hospital also receives disproportionate share and Medicaid High Volume Adjustment amounts as a daily add-on for Medicaid patients.

Managed care organizations: The Corporation has also entered into reimbursement agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment under these agreements includes discounts from established charges and prospectively determined per diem rates.

Provider tax assessment program: The Hospital is part of the State of Illinois' hospital tax assessment program which is administered by the Illinois Department of Public Aid. During fiscal year 2007, the program was renewed for the period July 2005 through June 30, 2008. Under this program, the Hospital is to receive annually approximately $12,596,000 from the State and pay annually a provider tax assessment approximating $6,040,000. At June 30, 2007, the Hospital had a receivable of $12,596,005 and a liability of $6,039,734 recorded related to this program. For the year ended June 30, 2007, the Hospital has recorded $25,192,010 in assessment revenue and $12,079,468 in provider tax expense. The State of Illinois has significantly delayed certain payments related to this program as well as collection of the related assessment tax. Although payment cannot be assured, Hospital management believes that the assessment program's obligations will be fulfilled in the next fiscal year. However, the timing of these payments is uncertain.

Note 3. Concentrations of Credit Risk

The Corporation grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at June 30, 2007 and 2006 was as follows:

	2007	2006
Medicare	20%	21%
Medicaid	35	30
Managed care	26	30
Other third-party payors	4	4
Self-pay	15	15
	100%	100%

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Note 4. Community Commitment and Charity Care

Although reimbursement for services rendered is critical to the operation of the Corporation, it is the Corporation's health care mission to serve the community by treating patients in immediate need of medical services without regard for their ability to pay for such services. The Corporation maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy, as well as the estimated cost of services and supplies. The estimated difference between the services provided to Medicaid patients and the reimbursement from the state for this patient care is also monitored.

During the years ended June 30, 2007 and 2006, the following levels of charity care were provided:

	2007	2006
Charges forgone for charity based on established rates	$ 8,799,417	$ 9,273,912
Estimated excess of cost over reimbursement for Medicaid patients	$ 6,247,097	$ 5,621,989

Note 5. Investments and Assets Limited as to Use, Short-Term Investments, and Other Investments

The composition of investments and assets limited as to use, short-term investments, and other investments, which are recorded at fair value based on quoted market values, is as follows as of June 30:

	2007	2006
Cash and cash equivalents	$ 15,315,882	$ 16,876,349
Certificates of deposit	3,536,734	1,934,999
Marketable equity securities	630,524	282,842
U.S. government money market funds	-	300,501
Accrued interest receivable	-	10,003
	$ 19,483,140	$ 19,404,694

Investment return for investments and assets whose use is limited, short-term investments, and other investments for the years ended June 30, 2007 and 2006 is as follows:

	2007	2006
Interest and dividend income	$ 1,057,432	$ 757,905
Other changes in unrestricted net assets - change in unrealized gains and losses on investments	$ 52,007	$ (2,543)

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

Note 6. Investment in Affiliate

The following is a summary of financial information relating to Mercy Heart and Vascular, LLC, the Corporation's investment in joint venture as of June 30:

	2007	2006
Assets	$ 879,735	$ -
Total equity	879,735	-
Revenue	1,005,710	-
Net income	724,344	-

Note 7. Sale-Leaseback Transaction

On April 15, 2005, the Corporation sold land for $7,000,000 and concurrently entered into an agreement to lease the property back at $10 per year through April 2009. The Corporation has an option to repurchase the property within the lease term. Because the Corporation has an option to repurchase the property, the sale did not qualify for sale-leaseback accounting and, thus, was accounted for as a financing transaction under FASB Statement No. 98, *Sale-Leaseback Accounting*. Therefore, the net proceeds from the sale have been recorded as a financing obligation. Payments under the lease are treated as interest expense with an appropriate per annum inflation based on the consumer price index (2.7% and 4.3% at June 30, 2007 and 2006, respectively) and a reduction (or increase, if applicable) of the financing obligation. A sale will be recognized when the Corporation's option to repurchase expires. The land involved in this transaction has a cost basis of approximately $2,983,000 and is included in land and land improvements on the balance sheet.

As required by the related agreement, the Corporation had $717,662 at June 30, 2006 held in escrow related to the sale-leaseback of the land to be used to pay for costs related to the remediation of environmental issues for this property, if necessary. This amount is included with investments and assets limited as to use – externally designated under lease agreement on the consolidated balance sheet. During 2007, the remaining funds in the escrow account were released to the Corporation as all required remediation was completed.

Note 8. Notes Payable, Long-Term Debt and Subsequent Event

During 2003, the Corporation issued an uncollateralized demand note payable to the Sisters of Mercy in the amount of $2,075,000. This note was issued to provide additional working capital to the Corporation. The note was non-interest bearing. The note was forgiven in its entirety in June 2006. The $2,075,000 was recognized as a transfer of net assets (forgiveness of note payable) on the consolidated statement of operations and changes in net assets.

Note 8. Notes Payable, Long-Term Debt and Subsequent Event (Continued)

Long-term debt is summarized as follows at June 30:

	2007	2006
General Electric Capital Corporation, $2,150,000 note bearing interest at 5.5%, payable in monthly installments of $29,982, with final installment due January 1, 2008	$ 180,920	$ 563,892
JPMorgan Chase Bank:		
$12,000,000 promissory note, bearing interest at the prime rate minus 0.75%, interest payable quarterly, principal due October 15, 2008*	12,000,000	12,000,000
$8,000,000 promissory note, bearing interest at the prime rate minus 0.75%, payable in quarterly installments of $100,000 plus interest, with a final payment due October 15, 2008*	7,200,000	7,600,000
$5,000,000 promissory note, bearing interest at the prime rate minus 0.75%, interest payable quarterly, principal due October 15, 2008*	5,000,000	5,000,000
Capital Source Finance, $20,000,000 revolving line of credit, bearing interest at an annual rate equal to the 30-day LIBOR rate plus 3.5%, expires October 15, 2008*	12,413,018	12,113,062
One-time overadvance on Capital Source Finance, $20,000,000 revolving line of credit, bearing interest at an annual rate equal to the 30-day LIBOR rate plus 4.5%, payable in monthly installments of $139,698 plus interest, with final installment due September 30, 2007	333,333	558,784
	37,127,271	37,835,738
Less:		
Current portion	(914,253)	(6,522,676)
	$ 36,213,018	$ 31,313,062

*Subsequent to year end, the debt agreements were amended to extend the due dates from April 15, 2008 to October 15, 2008. The debt is shown in accordance with the new terms.

At June 30, 2007, the prime rate was 8.25% and the 30-day LIBOR rate was 5.31%.

The terms of the loan agreements with JP Morgan Chase Bank require that the Corporation maintain a total of $12,000,000, plus accrued interest, in pledged accounts with a bank. At June 30, 2007 and 2006, the Corporation held approximately $12,041,000 in these pledged accounts.

At June 30, 2007 and 2006, the $8,000,000 note was secured by a guarantee by the Sisters of Mercy and the $5,000,000 note is secured by a mortgage on the Corporation's property. The Corporation's accounts receivable and certain other assets are pledged as collateral under the revolving line of credit.

The loan agreements on the notes contain various covenants including those relating to limitations on incurring additional debt and disposing of property. In addition, the revolving credit and security agreement contains covenants including those relating to financial performance, insurance coverage and timely submission of specified financial reports.

Note 8. Notes Payable, Long-Term Debt and Subsequent Event (Continued)

Future maturities of long-term debt are as follows:

Year Ending June 30:	Long-Term Debt
2008	$ 914,253
2009	36,213,018
	$ 37,127,271

Note 9. Lease Obligations

Rental expense for all operating leases totaled approximately $3,452,000 and $2,860,000 in 2007 and 2006, respectively. Future minimum lease payments under the noncancellable leases and related maintenance agreements are as follows:

Year Ended June 30:	
2008	$ 2,228,224
2009	1,789,297
2010	1,124,015
2011	858,058
2012	782,155
Thereafter	397,676
	$ 7,179,425

Note 10. Retirement Plan

The Hospital sponsored a noncontributory, defined-benefit pension plan, which covered substantially all of the Hospital's full-time employees. Benefits were based on years of service and the employee's compensation during the last five years of employment. The Hospital's funding policy was to contribute such amounts as are necessary to provide for benefits attributed to service to date and those expected to be earned in the future. Effective June 30, 2003, the plan was amended to freeze all benefit accruals. As a result, a curtailment benefit was recorded by the Hospital.

Effective June 30, 2004, the plan was amended to allow the sponsor to terminate the plan and settle pension obligations with all plan participants. The plan amendment accelerated the distribution of benefits earned. Effective July 1, 2004, the plan was amended to cease commencing distributions, eliminate the annuity forms of distribution, revise the allocation formula upon plan termination, revise the provision related to payment in the event a participant or beneficiary is determined to be incompetent, and provide that the plan be terminated effective July 1, 2004. As of June 30, 2006, substantially all plan assets were distributed.

Note 10. Retirement Plan (Continued)

The following table sets forth the plan's funded status and amounts recognized in the accompanying consolidated balance sheets at June 30, 2006:

Change in benefit obligation:	
Benefit obligation at beginning of year	$ 19,837,865
Service cost	-
Interest cost	228,838
Plan amendments	-
Effect of curtailment	-
Actuarial losses	-
Benefits paid	(19,152,047)
Benefit obligation at end of year	$ 914,656
Change in plan assets:	
Fair value of plan assets at beginning of year	$ 19,837,865
Actual return on plan assets	228,838
Employer contributions	-
Benefit paid	(19,152,047)
Fair value of plan assets at end of year	$ 914,656
Funded status of the plan	$ -
Unrecognized prior service cost	-
Unrecognized net actuarial gain	-
Accrued benefit cost, before additional minimum liability	-
Adjustment for additional minimum liability	-
Accrued benefit cost, after additional minimum liability	$ -
Assumptions:	
Discount rate	6.00%
Expected return on plan assets	N/A
Rate of compensation increase	N/A

Due to the distribution of plan assets, the plan's remaining assets are allocated to fixed income investments as of June 30, 2006.

Effective July 1, 2004, the Corporation put in place a defined-contribution pension plan, which covers substantially all of the Corporation's full-time employees. The Corporation's matching contributions are 50% of the amount contributed by participants, up to a maximum of 6% of the participant's compensation. For the years ended June 30, 2007 and 2006, total expense associated with this plan amounted to approximately $1,261,000 and $1,015,000, respectively.

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Note 11. Professional and General Liability Insurance

The actuarially determined professional liability in the accompanying consolidated balance sheets reflects management's assessment of claims applicable to all self-insured periods. Accrued professional liability losses have been discounted at 6% at both June 30, 2007 and 2006 and are based on a confidence level of approximately 60%. An accrual for possible losses attributable to incidents that may have occurred, but that have not been identified under the incident reporting system is included in this liability. If accrued professional liability losses had not been discounted, the estimated liability would be approximately $3,131,000 and $4,031,000 higher than the amounts recorded in the consolidated balance sheets as of June 30, 2007 and 2006, respectively.

The Corporation's 2006 insurance expense was reduced by approximately $7,400,000 due to a change in the estimated professional liability accrual as a result of several factors, including revision of the confidence level used to estimate expected losses from 75% to 60% and favorable loss claim experience. In addition, the Corporation received a prior year premium refund during 2006 in the amount of $1,300,000. This refund resulted in an additional reduction of 2006 insurance expense.

Note 12. Transactions with Related Parties

The following related party transactions have been entered into:

a. As of June 30, 2005, the Corporation had a note payable to the Sisters of Mercy outstanding in the amount of $2,075,000 which was forgiven in June 2006.

b. The Hospital bills and collects monies for services rendered to the Diagnostic and Treatment (D&T) Center's patients. In addition, the Hospital charges the D&T Center certain indirect costs of providing administrative, financial, and clinical services. These charges totaled approximately $413,000 in both 2007 and 2006.

c. The operations of the D&T Center are dependent on the continued financial and operating support of the Hospital. Under the terms of the Hospital's management agreement with the D&T Center, the Hospital has agreed to provide the necessary financial and operating support to the D&T Center for future periods.

Note 13. Functional Expenses

The Corporation provides general health care services to residents within Chicago and the surrounding area and supports medical education programs. The Corporation's expenses related to providing these services are as follows for the years ended June 30:

	2007	2006
Health care services	$ 106,316,115	$ 97,313,451
Medical education	7,985,947	7,520,184
Fund-raising	641,593	515,996
General and administrative	91,602,867	69,634,145
	$ 206,546,522	$ 174,983,776

Certain amounts have been allocated between health care services, medical education, and general and administrative services.

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Note 14. Commitments and Contingencies

Litigation: The Corporation is a defendant in various lawsuits arising in the ordinary course of business. Although the outcome of the lawsuits cannot be determined with certainty, management believes the ultimate disposition of such matters will not have a material effect on the Corporation's financial statements.

Regulatory investigation: The U.S. Department of Justice, other federal agencies and the Illinois Department of Public Aid routinely conduct regulatory investigations and compliance audits of health care providers. The Corporation is subject to these regulatory efforts. Management is currently unaware of any regulatory matters which may have a material effect on the Corporation's financial position or results from operation.

Claim settlement: In 2006, the Corporation settled a lawsuit for the amount of $3,300,000. Of this amount, $1,300,000 was paid on the settlement date (September 1, 2005). The remaining $2,000,000 is to be paid in three equal annual installments on August 1 of 2006, 2007 and 2008. The Corporation intends to fund the settlement with cash from operations. At June 30, 2007 and 2006, the settlement amount included in professional liability on the consolidated balance sheet was approximately $1,333,300 and $2,000,000, respectively.

Land sale: In 2004, the Corporation entered into an agreement with a developer to sell the property east of Prairie Avenue for a floor price of $8,250,000. The Hospital will receive additional proceeds based on the actual number of housing units sold. Total sale proceeds are estimated to be $10.4 million. Two closings were completed in 2006 and an additional two closings were completed in 2007. Sales proceeds received in 2007 and 2006 were approximately $3,246,000 and $944,000, respectively. During 2007 and 2006, the Corporation recognized a gain on the sale of this property of approximately $2,918,000 and $848,000, respectively.

Electronic medical records system implementation: In March 2007, the Corporation entered into an agreement with Cerner Corporation to purchase equipment and certain sub-licensed software licenses for an Electronic Medical Records System. Total cost of the system is estimated to be $5 million. As of June 30, 2007, $400,000 has been paid toward the system. The Corporation intends to fund the remaining cost with cash from operations. The system is expected to be implemented during fiscal year 2008.

Contingency: Financial Accounting Standards Board Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations* (FIN 47) clarified when an entity is required to recognize a liability for a conditional asset retirement obligation. The Corporation has a legal obligation to remove hazardous materials from its facilities in the event the facilities are renovated or replaced. Such hazardous materials include asbestos. Management believes there is an indeterminate settlement date for the asset retirement obligations because of the range of time over which the Corporation may settle the obligation is unknown. However, management does not believe that the estimate of the liability related to these asset retirement obligations is a material amount at June 30, 2007 and 2006.

Note 15. Fair Value of Financial Instruments

The following methods and assumptions were used by the Corporation to estimate the fair value of other financial instruments:

The carrying value of cash and cash equivalents, patient accounts receivables due from related party, Medicaid assessment revenue receivable, grant receivable, other current assets, accounts payable, accrued expenses, estimated settlements due to or from third-party payors and Medicaid assessment tax payable are reasonable estimates of their value due to the short-term nature of these financial instruments.

Note 15. Fair Value of Financial Instruments (Continued)

The fair value of investments and assets limited as to use, which are the amounts reported on the balance sheet, is based on quoted market prices.

The fair value of long-term debt is estimated based on interest rates for the same or similar debt offered to the Corporation having the same or similar remaining maturities and collateral requirements. The fair value of the long-term debt approximates the carrying values.

Note 16. Pending Adoptions of New Accounting Principles

In July 2006, the FASB issued Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes – as interpretation of SFAS No. 109, Accounting for Income Taxes. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS, Accounting for Income Taxes. FIN 48 prescribes a comprehensive model for recognizing, measuring, presenting and disclosing in the financial statements tax positions taken or expected to be taken on a tax return. FIN 48 is effective for the Corporation on July 1, 2007. The Corporation is currently evaluating the impact of FIN 48 on its financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. The requirements of SFAS No. 157 are effective for financial statements issued for fiscal years beginning after November 15, 2007. The Corporation is currently evaluating the impact of SFAS No. 157 on its financial statements.

McGladrey & Pullen

Certified Public Accountants

Independent Auditor's Report on the Supplementary Information

To the Board of Directors
Mercy Health System of Chicago
Chicago, Illinois

Our audits were made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The consolidating information is presented for purposes of additional analysis of the basic consolidated financial statements rather than to present the financial position and results of operations of the individual companies. The consolidating information has been subjected to the auditing procedures applied in the audits of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

McGladrey & Pullen, LLP

Chicago, Illinois
October 30, 2007

Mercy Health System of Chicago and Subsidiaries
Consolidating Balance Sheet
June 30, 2007

Assets	Mercy Health System of Chicago	Mercy Hospital and Medical Center	Mercy Health Care Rehabilitation Center	Mercy Services Corporation	Mercy Foundation, Inc.	Eliminations	Consolidated Totals
Current Assets							
Cash and cash equivalents	$ -	$ 6,544,265	$ -	$ 1,000	$ 241,705	$ -	$ 6,786,970
Investments and assets limited as to use							
Internally designated under self-insurance program	-	30,636	-	-	-	-	30,636
Short-term investments	-	71,952	-	-	3,774,140	-	3,846,092
Patient accounts receivable, net of allowance for doubtful accounts	-	33,141,041	-	-	-	-	33,141,041
Interest in net assets of Foundation	-	2,029,273	-	-	-	(2,029,273)	-
Due from related party	681,052	64,958	3,629,125	-	-	(4,375,135)	-
Due from affiliate	-	423,755	-	-	-	-	423,755
Inventories	-	2,153,453	-	-	-	-	2,153,453
Medicaid assessment revenue receivable	-	12,596,005	-	-	-	-	12,596,005
Grant receivable	-	-	-	-	1,000,000	-	1,000,000
Other current assets	-	2,078,124	-	-	53,999	-	2,132,123
Total current assets	681,052	59,133,462	3,629,125	1,000	5,069,844	(6,404,408)	62,110,075
Investments and Assets Limited as to Use, net of amounts required to meet current obligations							
Pledged under debt agreement	-	12,041,020	-	-	-	-	12,041,020
Internally designated under self-insurance program	-	1,933,333	-	-	-	-	1,933,333
Other Investments	-	1,632,059	-	-	-	-	1,632,059
	-	15,606,412	-	-	-	-	15,606,412
Property and Equipment							
Land and land improvements	-	8,486,591	-	-	-	-	8,486,591
Buildings and fixtures	-	109,443,733	-	-	-	-	109,443,733
Equipment	-	120,876,035	-	-	30,447	-	120,906,482
Construction in progress	-	5,103,306	-	-	-	-	5,103,306
	-	243,909,665	-	-	30,447	-	243,940,112
Less accumulated depreciation	-	(186,182,275)	-	-	(27,819)	-	(186,210,094)
	-	57,727,390	-	-	2,628	-	57,730,018
Other Assets							
Deferred financing costs, net	-	207,978	-	-	-	-	207,978
Investment in joint venture and other	-	1,642,065	-	-	81,291	-	1,723,356
	-	1,850,043	-	-	81,291	-	1,931,334
Total assets	$ 681,052	$ 134,317,307	$ 3,629,125	$ 1,000	$ 5,153,763	$ (6,404,408)	$ 137,377,839

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ATTACHMENT FINANCIALS

Liabilities and Net Assets	Mercy Health System of Chicago	Mercy Hospital and Medical Center	Mercy Health Care Rehabilitation Center	Mercy Services Corporation	Mercy Foundation, Inc.	Eliminations	Consolidated Totals
Current Liabilities							
Accounts payable	$ -	$ 15,136,235	$ 128,258	$ -	$ 102,333	$ -	$ 15,366,826
Accrued expenses	-	8,302,998	-	-	297	-	8,303,295
Due to third-party payors	-	573,583	-	-	-	-	573,583
Current portion of long-term debt	-	914,253	-	-	-	-	914,253
Due to related party	-	4,310,177	-	-	64,958	(4,375,135)	-
Medicaid assessment tax payable	-	6,039,734	-	-	-	-	6,039,734
Current portion of professional liability	-	6,037,666	435,000	-	-	-	6,472,666
Current portion of deferred grant revenue	-	125,000	-	-	1,000,000	-	1,125,000
Total current liabilities	-	41,439,646	563,258	-	1,167,588	(4,375,135)	38,795,357
Long-term debt	-	36,213,018	-	-	-	-	36,213,018
Professional Liability, less current portion	-	17,491,667	-	-	-	-	17,491,667
Financing Obligation Arising From Sale-Leaseback Transaction	-	7,537,158	-	-	-	-	7,537,158
Deferred Grant Revenue, less current portion	-	1,821,323	-	-	-	-	1,821,323
Total liabilities	-	104,502,812	563,258	-	1,167,588	(4,375,135)	101,858,523
Net Assets							
Unrestricted	681,052	27,278,732	3,065,867	1,000	1,956,902	-	32,983,553
Temporarily restricted	-	2,223,203	-	-	2,029,273	(2,029,273)	2,223,203
Permanently restricted	-	312,560	-	-	-	-	312,560
Total net assets	681,052	29,814,495	3,065,867	1,000	3,986,175	(2,029,273)	35,519,316
Total liabilities and net assets	$ 681,052	$ 134,317,307	$ 3,629,125	$ 1,000	$ 5,153,763	$ (6,404,408)	$ 137,377,839

ATTACHMENT FINANCIALS

Mercy Health System of Chicago and Subsidiaries
Consolidating Statement of Operations
Year Ended June 30, 2007

	Mercy Health System of Chicago	Mercy Hospital and Medical Center	Mercy Health Care Rehabilitation Center	Mercy Services Corporation	Mercy Foundation, Inc.	Eliminations	Consolidated Totals
Revenue:							
Net patient service revenue	$ -	$ 190,180,524	$ -	$ -	$ -	$ -	$ 190,180,524
Medicaid assessment revenue	-	25,192,010	-	-	-	-	25,192,010
Capitation revenue	-	1,904,432	-	-	-	-	1,904,432
Contributions	-	539,782	-	-	884,657	(430,000)	994,439
Other	-	3,515,005	-	-	-	-	3,515,005
Net assets released from restriction - used for operations	-	220,917	-	-	140,684	-	361,601
	-	221,552,670	-	-	1,025,341	(430,000)	222,148,011
Expenses:							
Salaries and benefits	-	97,309,357	-	-	195,539	-	97,504,896
Supplies	-	29,305,502	-	-	10,351	-	29,315,853
Insurance	-	4,766,676	-	-	-	-	4,766,676
Depreciation and amortization	-	8,274,231	-	-	4,098	-	8,278,329
Provision for uncollectible accounts	-	11,607,707	-	-	23,366	-	11,631,073
Interest	-	2,815,971	-	-	-	-	2,815,971
Professional fees	-	6,295,101	-	-	-	-	6,295,101
Repairs, utilities and rent	-	13,286,725	-	-	33,734	-	13,320,459
Purchased services	-	17,229,098	-	-	-	-	17,229,098
Medicaid assessment tax	-	12,079,468	-	-	-	-	12,079,468
Other	-	2,990,086	-	-	749,512	(430,000)	3,309,598
	-	205,959,922	-	-	1,016,600	(430,000)	206,546,522
Operating income	-	15,592,746	-	-	8,741	-	15,601,489
Nonoperating income:							
Gain on sale of property	-	2,932,909	-	-	-	-	2,932,909
Investment income	570	904,129	-	-	152,733	-	1,057,432
Income from joint venture	-	369,449	-	-	-	-	369,449
Excess of revenue over expenses	570	19,799,235	-	-	161,474	-	19,961,279
Unrestricted net assets:							
Net change in unrealized gains and losses on investments	-	-	-	-	52,007	-	52,007
Increase in unrestricted net assets	$ 570	$ 19,799,235	$ -	$ -	$ 213,481	$ -	$ 20,013,286

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Mercy Health System of Chicago and Subsidiaries

Consolidated Financial Report
June 30, 2006

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McGladrey & Pullen
Certified Public Accountants

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McGladrey & Pullen
Certified Public Accountants

Independent Auditor's Report on the Financial Statements

To the Board of Directors
Mercy Health System of Chicago
Chicago, Illinois

We have audited the accompanying consolidated balance sheets of Mercy Health System of Chicago and Subsidiaries (the "Corporation") as of June 30, 2006 and 2005, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mercy Health System of Chicago and Subsidiaries as of June 30, 2006 and 2005, and the results of their operations and changes in net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 10 to the consolidated financial statements, the Corporation's 2006 insurance expense was reduced by approximately $7,400,000 due to a change in the estimated professional liability accrual as a result of several factors, including favorable loss claim experience and a revision of the confidence level used to estimate expected losses.

McGladrey & Pullen, LLP

Chicago, Illinois
August 29, 2006

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Mercy Health System of Chicago and Subsidiaries

Consolidated Balance Sheets
June 30, 2006 and 2005

	2006	2005
Assets		
Current Assets		
Cash and cash equivalents	$ 7,291,637	$ 7,687,868
Investments and assets limited as to use - internally designated under self-insurance program	127,211	73,220
Short-term investments	1,826,802	1,002,764
Patient accounts receivable, net of allowance for doubtful accounts of $11,362,000 in 2006 and $16,318,000 in 2005	26,568,161	24,094,299
Due from related party	-	234,573
Inventories	2,147,405	1,854,338
Other current assets	1,974,922	2,404,790
Total current assets	39,936,138	37,351,852
Investments and Assets Limited as to Use, net of amounts required to meet current obligations		
Pledged under debt agreement	12,040,542	12,087,649
Externally designated under lease agreement	717,662	800,000
Internally designated under self-insurance program	2,009,888	-
Externally designated under self-insurance program	-	3,812,500
Other Investments	2,682,589	2,449,495
	17,450,681	19,149,644
Property and Equipment		
Land and land improvements	8,753,112	9,316,753
Buildings and fixtures	106,443,732	105,162,988
Equipment	117,627,148	112,839,819
Construction in progress	4,183,699	788,744
	237,007,691	228,108,304
Less accumulated depreciation	(178,250,906)	(170,781,470)
	58,756,785	57,326,834
Other Assets		
Deferred financing costs, net	474,253	479,653
Other noncurrent assets	1,212,436	966,731
	1,686,689	1,446,384
Total assets	$ 117,830,293	$ 115,274,714

See Notes to Consolidated Financial Statements.

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	2006	2005
Liabilities and Net Assets		
Current Liabilities		
Accounts payable	$ 18,195,144	$ 14,135,542
Accrued expenses	8,158,457	9,204,310
Due to third-party payors	6,257,664	5,030,291
Current portion of long-term debt	6,522,676	7,442,634
Note payable	-	2,075,000
Current portion of professional liability	5,580,667	7,423,000
Total current liabilities	44,714,608	45,310,777
Noncurrent Liabilities		
Long-term debt, less current portion	31,313,062	32,815,119
Professional liability, less current portion	17,604,333	20,363,000
Financing obligation arising from sale-leaseback transaction	7,331,968	7,046,641
Deferred grant revenue	1,978,562	2,135,801
Total liabilities	102,942,533	107,671,338
Commitments and Contingencies (Notes 8 and 13)		
Net Assets:		
Unrestricted	12,970,267	5,772,974
Temporarily restricted	1,604,933	1,517,842
Permanently restricted	312,560	312,560
Total net assets	14,887,760	7,603,376
Total liabilities and net assets	$ 117,830,293	$ 115,274,714

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Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets
Years Ended June 30, 2006 and 2005

	2006	2005
Revenue:		
Net patient service revenue	$ 171,780,631	$ 169,628,548
Medicaid hospital assessment revenue	-	11,679,718
Capitation revenue	1,698,339	1,337,213
Contributions	867,944	315,032
Other	3,826,466	4,118,378
Net assets released from restriction - used for operations	328,519	645,537
	178,501,899	187,724,426
Expenses:		
Salaries and benefits	90,200,686	86,613,397
Supplies	25,775,952	25,530,887
Insurance, net (Note 10)	(2,242,683)	5,741,054
Depreciation and amortization	8,373,976	8,419,930
Provision for uncollectible accounts	14,323,749	13,811,990
Interest	2,743,940	3,725,496
Professional fees	5,473,887	5,375,728
Repairs, utilities and rent	11,615,181	10,631,278
Purchased services	14,543,733	13,589,315
Medicaid hospital assessment expense	-	6,779,314
Other	4,175,355	3,783,325
	174,983,776	184,001,714
Operating income	3,518,123	3,722,712
Nonoperating income (expense):		
Gain on sale of property and equipment	848,808	45,324
Investment income	757,905	1,544,392
Loss on advance refunding	-	(978,534)
Other	-	(30,000)
	1,606,713	581,182
Excess of revenue over expenses	$ 5,124,836	$ 4,303,894

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Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets (Continued)
Years Ended June 30, 2006 and 2005

	2006	2005
Unrestricted net assets		
Excess of revenue over expenses	$ 5,124,836	$ 4,303,894
Net change in unrealized gains and losses on investments	(2,543)	-
Forgiveness of note payable	2,075,000	-
Change in minimum pension liability	-	5,503,714
Increase in unrestricted net assets	7,197,293	9,807,608
Temporarily restricted net assets		
Contributions	415,610	669,452
Net assets released from restrictions - used for operations	(328,519)	(645,537)
Increase in temporarily restricted net assets	87,091	23,915
Increase in net assets	7,284,384	9,831,523
Net assets:		
Beginning of year	7,603,376	(2,228,147)
End of year	$ 14,887,760	$ 7,603,376

See Notes to Consolidated Financial Statements.

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Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Cash Flows
Years Ended June 30, 2006 and 2005

	2006	2005
Cash Flows from Operating Activities		
Increase in net assets	$ 7,284,384	$ 9,831,523
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Net change in unrealized gains and losses on investments	2,543	-
Depreciation	8,115,478	8,162,489
Amortization	258,498	257,441
Provision for uncollectible accounts	14,323,749	13,811,990
Gain on sale of property and equipment	(848,808)	(45,324)
Amortization of deferred revenue	(189,478)	(125,000)
Loss on advance refunding	-	978,534
Interest added to financing obligation arising from sale-leaseback transaction	285,327	46,641
Forgiveness of note payable	(2,075,000)	-
Changes in operating assets and liabilities:		
Accounts receivable	(16,797,611)	(16,523,359)
Accounts payable and accrued expenses	1,400,048	1,624,561
Due to third-party payors	1,227,373	(3,284,525)
Professional liability	(4,601,000)	3,439,000
Pension liability	-	(5,633,240)
Other assets	(108,905)	(1,247,769)
Net cash provided by operating activities	8,276,598	11,292,962
Cash Flows from Investing Activities		
Purchases of property and equipment	(8,148,311)	(7,458,178)
Purchases of investments and assets limited as to use and other investments	(3,123,554)	(16,700,149)
Proceeds from sale of property and equipment	1,065,391	57,659
Proceeds from sale/maturity of investments and assets limited to use	3,941,946	5,132,278
Advance to related party	-	(234,573)
Repayment from related party	234,573	-
Release debt service reserve funds (1992 and 1996 bonds)	-	9,763,743
Net cash (used in) investing activities	(6,029,955)	(9,439,220)
Cash Flows from Financing Activities		
Advance refunding of long-term debt	-	(54,278,138)
Proceeds from issuance of long-term debt	-	40,000,000
Proceeds from sale-leaseback transaction	-	7,000,000
Payments on long-term debt	(2,422,015)	(4,727,757)
Payments on notes payable	-	(542,549)
Payment of deferred financing costs	(253,098)	(576,135)
Proceeds from grant, for property and equipment	32,239	134,329
Net cash (used in) financing activities	(2,642,874)	(12,990,250)
Net (decrease) in cash and cash equivalents	(396,231)	(11,136,508)

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(Continued)

Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Cash Flows (Continued)
Years Ended June 30, 2006 and 2005

	2006	2005
Cash and cash equivalents:		
Beginning	$ 7,687,868	$ 18,824,376
Ending	$ 7,291,637	$ 7,687,868
Supplemental Disclosures of Cash Flow Information		
Cash paid for interest, net of amounts capitalized of $259,000 in 2006 and none in 2005	$ 2,636,915	$ 5,343,427
Supplemental Schedule of Noncash Investing and Financing Activities		
Property and equipment additions included in accounts payable	$ 1,613,701	$ -

See Notes to Consolidated Financial Statements.

Note 1. Nature of Business and Significant Accounting Policies

Organization and nature of business: The accompanying consolidated financial statements represent the accounts of Mercy Health System of Chicago ("Parent") and its subsidiaries (jointly, the "Corporation"). The Corporation is sponsored by the Sisters of Mercy of the Americas, Regional Community of Chicago ("Sisters of Mercy"), a religious institute. Subsidiaries of the Parent include Mercy Health Care Rehabilitation Center ("Center"), Mercy Services Corporation ("MSC"), Mercy Hospital and Medical Center ("Hospital"), and Mercy Foundation, Inc. ("Foundation").

The Hospital is a licensed 479-bed acute care facility with its primary market in the south and southwest side of Chicago, Illinois, and adjacent suburbs. In addition to the main facility, the Hospital has a network of hospital-owned primary care centers, private physician offices, and a number of satellites throughout the City of Chicago.

All of MSC's stock is owned by the Parent. MSC has been inactive since the transfer of its operations to the Hospital.

The Foundation was organized for the purpose of collecting, earning, and receiving funds from public and private sources, accumulating such funds, and making distributions of income to the Parent or related entities properly designated by the Parent.

The Center's assets were sold in December 2001. According to the sale agreement, $300,000 was placed into a trust account to be used to offset Medicare and Medicaid audit adjustments related to periods prior to the sale. Unused funds were released to the Hospital in February 2005. Other than recognizing interest income and expenses related to the release of the trust monies, the Center has been inactive.

A summary of significant accounting policies follows:

Principles of consolidation: The accompanying consolidated financial statements include the Parent, Center, MSC, Hospital and Foundation. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of estimates: The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The use of estimates and assumptions in the preparation of the accompanying financial statements is primarily related to the determination of the net patient accounts receivable and settlements with third-party payors and the accrual for professional liability. Due to uncertainties inherent in the estimation and assumption process, it is at least reasonably possible that changes in these estimates and assumptions in the near-term would be material to the financial statements.

Basis of presentation: The Corporation may classify its net assets into three categories, which are unrestricted, temporarily restricted and permanently restricted.

Unrestricted net assets are reflective of revenues and expenses associated with the principal operating activities of the Corporation and are not subject to donor-imposed stipulations.

Note 1. Nature of Business and Significant Accounting Policies (continued)

Temporarily restricted net assets are subject to donor-imposed stipulations that may or will be met either by actions of the Corporation and/or the passage of time. As of June 30, 2006 and 2005, temporarily restricted net assets were restricted by donors primarily for patient care, community service, education, research, and purchase of equipment. Income earned on donor-restricted marketable securities, unless restricted by donors, is reflected in investment income. When a donor restriction expires, temporarily restricted net assets are classified as unrestricted net assets and reported in the statement of operations and changes in net assets as other revenue.

Permanently restricted net assets have been restricted by donors to be maintained by the Corporation in perpetuity. The income earned on permanently restricted net assets has been restricted by donors to provide care for the poor.

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

Cash and cash equivalents: All investments that are not limited as to use with an original maturity of three months or less at the time of acquisition are reflected as cash equivalents.

Throughout the year, the Corporation may have amounts on deposit with financial institutions in excess of those insured by the FDIC. Management does not believe this presents a significant risk to the Corporation.

Patient accounts receivable, provision for doubtful accounts and due from/to third party-payors: The collection of receivables from third-party payors and patients is the Corporation's primary source of cash for operations and is critical to its operating performance. The primary collection risks relate to uninsured patient accounts and patient accounts for which the primary insurance payor has paid, but patient responsibility amounts (deductibles and co-payments) remain outstanding. Patient receivables, where a third-party payor is responsible for paying the amount, are carried at a net amount determined by the original charge for the service provided, less an estimate made for contractual adjustments or discounts provided to third-party payors.

Patient receivables due directly from the patients are carried at the original charge for the service provided less amounts covered by third-party payors and less an estimated allowance for uncollectible receivables. Management estimates this allowance based on the aging of its accounts receivable and its historical collection experience for each payor type. Recoveries of receivables previously written off are recorded as a reduction of the provision for uncollectible accounts when received.

The past due status of receivables is determined on a case-by-case basis depending on the payor responsible. Interest is generally not charged on past due accounts.

Receivables or payables related to estimated settlements on various payor contracts, primarily Medicare, are reported as amounts due from or to third-party payors. Significant changes in payor mix, business office operations, economic conditions or trends in federal and state governmental health care coverage could affect the Corporation's collection of accounts receivable, cash flows and results of operations.

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Note 1. Nature of Business and Significant Accounting Policies (continued)

Inventories: Inventories are stated at cost (first-in, first-out method).

Investments and assets limited as to use: Investments are recorded at fair value based on quoted market prices. Realized investment income is included in excess of revenue over expenses unless the income or loss is restricted by donor or law. The change in unrealized appreciation in fair value of investments is recognized as a change in net assets.

Investments are regularly evaluated for impairment. The Corporation considers factors affecting the investee, factors affecting the industry the investee operates within, and general debt and equity trends. The Corporation considers the length of time an investment's fair value has been below carrying value, the near-term prospects for recovery to carrying value, and the intent and ability to hold the investment until maturity date or market recovery is realized. If and when a determination is made that a decline in fair value below the cost basis is other than temporary, the related investment is written down to its estimated fair value and included as a realized loss in excess of revenue over expenses.

Assets limited as to use consist of investments set aside by the Board for self-insurance over which the Board retains control and may, at its discretion, subsequently use for other purposes. Assets limited as to use also include investments externally designated under debt and lease agreements and an insurance claim settlement.

Property and equipment: Property and equipment are recorded at cost and depreciated on the straight-line method over their estimated useful lives. The assets' lives are as follows:

Land improvements	5 years
Buildings and fixtures	5 – 40 years
Furniture and equipment	3 – 20 years
Automobiles	3 – 4 years
Leasehold improvements	15 – 20 years

Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

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

Accrued professional liability: The provision for accrued professional liability includes estimates of the ultimate costs for claims incurred but not reported. The provision is actuarially determined. The Corporation is completely self-insured for all claims incurred on and after July 1, 2002.

Note 1. Nature of Business and Significant Accounting Policies (continued)

Deferred financing costs: Costs incurred in connection with the issuance or refinancing of long-term debt are deferred and amortized over the term of the related financing on a method that approximates the effective yield method.

Community commitment: Community commitment includes patient charity care rendered to the community at a reduced rate or at no fee based upon community need or the inability of the individual to pay for services. Because the Corporation does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Net patient service revenue: The Corporation has agreements with third-party payors that provide for payments to the Corporation at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Capitation revenue: The Corporation has agreements with various health maintenance organizations (HMOs) to provide medical services to subscribing participants. Under these agreements, the Corporation receives monthly capitation payments based on the number of each HMO's participants, regardless of services actually performed by the Corporation. In addition, the HMOs make fee-for-service payments to the Corporation for certain covered services based upon discounted fee schedules.

Operating income: The consolidated statements of operations and changes in net assets include operating income. Changes in unrestricted net assets, which are excluded from operating income, include investment income, gains and losses from sales of property and equipment, loss on advance refunding and other income and expense which management views as outside of normal activity.

Results of operations: The consolidated statements of operations and changes in net assets include excess of revenue over expenses that represents the results of operations. Changes in unrestricted net assets that are excluded from excess of revenues over expenses, consistent with industry practice, include the change in net unrealized appreciation in fair value of investments, the change in minimum pension liability and forgiveness of notes payable by related parties.

Income taxes: The Parent, the Hospital, the Center, and the Foundation have received determination letters from the Internal Revenue Service stating that they are exempt from the payment of federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

At June 30, 2006, MSC had approximately $1,566,000 of net operating tax loss carryforwards available for use against future taxable income, which begin to expire in 2007. As a result of the net operating tax loss carryforwards, there is no income tax provision in 2006 and 2005. Due to the uncertain future realization of these loss carryforwards, the related tax assets have been fully reserved by a valuation allowance in the accompanying consolidated balance sheets.

Reclassification: Certain amounts in the 2005 financial statements have been reclassified to conform to the 2006 presentation.

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Note 2. Net Patient Service Revenue

The Corporation has agreements with third-party payors which provide for reimbursement to the Corporation at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Corporation's billings at list price and the amounts reimbursed by Medicare, Medicaid, Blue Cross, and certain other third-party payors, and any differences between estimated third-party reimbursement settlements for prior years and subsequent final settlements. Contractual adjustments under third-party reimbursement programs are accrued on an estimated basis in the period the related services are rendered and are adjusted in future periods as final settlements are determined. A summary of the basis of reimbursement with major third-party payors follows:

Medicare: The Corporation is paid for inpatient acute care and outpatient care services rendered to Medicare program beneficiaries under prospectively determined rates per discharge (Prospective Payment Systems). These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient non-acute services and defined capital and medical education costs related to Medicare beneficiaries are paid based upon either a cost reimbursement method or established fee screens, or a combination thereof. The Corporation's classification of patients under Prospective Payment Systems and the appropriateness of the patient's admissions are subject to validation reviews. The Corporation is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual reimbursement reports by the Corporation and audits by the Medicare fiscal intermediary.

For the years ended June 30, 2006 and 2005, the Corporation recognized approximately $158,854,000 and $153,003,000, respectively, of gross patient service revenues from services provided to Medicare beneficiaries. Changes in Medicare reimbursement as a result of the Centers for Medicare and Medicaid Services' implementation of the provisions of future Medicare legislation may have an adverse effect on the Corporation's net patient service revenue. Fiscal year 2007 represents the first of a three-year phase-in period for implementation of a revised Medicare Diagnosis Related Group (DRG) reimbursement system. This new payment methodology makes meaningful refinements to the current CMS classification system to increase recognition of severity of illness. However, there will be a limited impact on payments in specific DRGs because of the simultaneous implementation of incremental reforms for cost-based and severity-based payments. Management has not determined the reimbursement impact of this change in reimbursement for the Hospital.

Medicaid: The Corporation is reimbursed at prospectively determined rates for each Medicaid inpatient discharge. Outpatient services are reimbursed based on established fee screens. For inpatient acute care services, payment rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. The prospectively determined rates are not subject to retroactive adjustment. As described below, the Corporation also receives incremental Medicaid reimbursement for specific programs and services at the discretion of the State of Illinois Medicaid Program. Medicaid reimbursement may be subject to periodic adjustment, as well as to changes in existing payment levels and rates, based on the amount of funding available to the Medicaid program.

For the years ended June 30, 2006 and 2005, the Corporation recognized approximately $104,234,000 and $97,466,000, respectively, of gross patient service provided to Medicaid patients. Due to the Hospital's relatively high Medicaid patient volume, the Hospital received additional reimbursement of approximately $13,430,000 in both 2006 and 2005 in the form of critical hospital adjustment payments ("CHAP"), safety net access payments ("SNAP") and tertiary payments, the majority of which is provided by the Illinois Medicaid program. The Hospital also receives disproportionate share and Medicaid High Volume Adjustment amounts as a daily add-on for Medicaid patients.

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Note 2. Net Patient Service Revenue (continued)

Blue Cross: The Corporation also participates as a provider of health care services under a reimbursement agreement with Blue Cross. The provisions of this agreement stipulate that services will be reimbursed at a tentative reimbursement rate and that final reimbursement for these services is determined after the submission of an annual cost report by the Corporation and a review by Blue Cross.

Managed Care Organizations: The Corporation has also entered into reimbursement agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment under these agreements includes discounts from established charges and prospectively determined per diem rates.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near-term. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. Net patient service revenue in 2006 decreased by the effect of third-party payor settlements by approximately $2,253,000. During 2005, net patient service revenue was increased by the effect of favorable third-party payor settlements of approximately $1,500,000. At June 30, 2006 the Hospital recorded a liability of approximately $3,500,000 in connection with the Medicare disproportionate share (DSH) settlements related to fiscal years ended June 30, 2006, 2005, and 2004. This liability is an estimate by management of the Hospital of the eventual outcome of a DSH reimbursement matter involving the State of Illinois' reporting of Title 21 days and its impact on DSH reimbursement.

In December 2004, the Federal Centers of Medicare and Medicaid Services (CMS) approved State of Illinois (State) legislation for a Medicaid Hospital Assessment Program (Program) relating to the period May 9, 2004 to June 30, 2005. Under the Program, the Hospital received additional Medicaid reimbursement from the State and paid a related assessment. Total reimbursement revenue recognized by the Hospital related to this Program amounted to $11,679,718 during the Hospital's year ended June 30, 2005. Total assessments incurred by the Hospital related to this program amounted to $6,779,314 during the Hospital's year ended June 30, 2005. The laws and regulations authorizing this Program expired on June 30, 2005. A proposal to continue the Program for three additional years is currently being considered by CMS.

Note 3. Concentrations of Credit Risk

The Corporation grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at June 30, 2006 and 2005 was as follows:

	2006	2005
Medicare	21%	20%
Medicaid	22	29
Managed care	38	30
Other third-party payors	4	5
Self-pay	15	16
	100%	100%

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Note 4. Community Commitment and Charity Care

Although reimbursement for services rendered is critical to the operation of the Corporation, it is the Corporation's health care mission to serve the community by treating patients in immediate need of medical services without regard for their ability to pay for such services. The Corporation maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy, as well as the estimated cost of services and supplies. The estimated difference between the services provided to Medicaid patients and the reimbursement from the state for this patient care is also monitored.

During the years ended June 30, 2006 and 2005, the following levels of charity care were provided:

	2006	2005
Charges forgone for charity based on established rates	$ 9,273,912	$ 7,601,313
Estimated excess of cost over reimbursement for Medicaid patients	$ 5,621,989	$ 6,753,787

Note 5. Investments and Assets Limited as to Use, Short-Term Investments, and Other Investments

The composition of investments and assets limited as to use, short-term investments, and other investments, which are recorded at fair value based on quoted market values, is as follows as of June 30:

	2006	2005
Cash and cash equivalents	$ 16,876,349	$ 19,220,232
Certificates of deposit	1,934,999	916,659
Marketable equity securities	282,842	76,425
U.S. government money market funds	300,501	-
Accrued interest receivable	10,003	12,312
	$ 19,404,694	$ 20,225,628

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Note 5. Investments and Assets Limited as to Use, Short-Term Investments, and Other Investments (continued)

Investment return for investments and assets whose use is limited, short-term investments, and other investments for the years ended June 30, 2006 and 2005 is as follows:

	2006	2005
Interest and dividend income	$ 757,905	$ 506,825
Realized gains on sales of investments, net	-	1,037,567
	$ 757,905	$ 1,544,392
Other changes in unrestricted net assets - change in unrealized gains and losses on investments	$ (2,543)	$ -

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

Note 6. Sale-Leaseback Transaction

On April 15, 2005, the Corporation sold land for $7,000,000 and concurrently entered into an agreement to lease the property back at $10 per year through April 2009. The Corporation has an option to repurchase the property within the lease term. Because the Corporation has an option to repurchase the property, the sale did not qualify for sale-leaseback accounting and, thus, was accounted for as a financing transaction under FASB Statement No. 98, *Sale-Leaseback Accounting*. Therefore, the net proceeds from the sale have been recorded as a financing obligation. Payments under the lease are treated as interest expense with an appropriate per annum inflation based on the consumer price index (4.3% and 2.5% at June 30, 2006 and 2005, respectively) and a reduction (or increase, if applicable) of the financing obligation. A sale will be recognized when the Corporation's option to repurchase expires. The land involved in this transaction has a cost basis of approximately $2,983,000 and is included in land and land improvements on the balance sheet.

As required by the related agreement, the Corporation had $717,662 and $800,000 at June 30, 2006 and 2005, respectively, held in escrow related to the sale-leaseback of the land to be used to pay for costs related to the remediation of environmental issues for this property, if necessary. This amount is included with investments and assets limited as to use – externally designated under lease agreement on the consolidated balance sheet.

Note 7. Notes Payable and Long-Term Debt

During 2003, the Corporation issued an uncollateralized demand note payable to the Sisters of Mercy in the amount of $2,075,000. This note was issued to provide additional working capital to the Corporation. The note was non-interest bearing. The note was forgiven in its entirety in June 2006. The $2,075,000 was recognized as a transfer of net assets (forgiveness of note payable) on the consolidated statement of operations and changes in net assets.

Long-term debt is summarized as follows at June 30:

	2006	2005
General Electric Capital Corporation, $2,150,000 note bearing interest at 5.5%, payable in monthly installments of $29,982, with final installment due January 1, 2007	$ 563,892	$ 909,544
JPMorgan Chase Bank:		
$12,000,000 promissory note, bearing interest at the prime rate minus 0.75%, interest payable quarterly, principal due April 15, 2008	12,000,000	12,000,000
$8,000,000 promissory note, bearing interest at the prime rate minus 0.75%, payable in quarterly installments of $100,000 plus interest, with a final payment due April 15, 2008	7,600,000	8,000,000
$5,000,000 promissory note, bearing interest at the prime rate minus 0.75%, interest payable quarterly, principle originally due April 15, 2006, extended to April 15, 2007	5,000,000	5,000,000
Capital Source Finance, $20,000,000 revolving line of credit, bearing interest at an annual rate equal to the 30-day LIBOR rate plus 3.5%, expires April 15, 2008	12,113,062	11,833,641
One-time overadvance on Capital Source Finance, $20,000,000 revolving line of credit, bearing interest at an annual rate equal to the 30-day LIBOR rate plus 4.5%, payable in monthly installments of $139,698 plus interest, with final installment due October 2006	558,784	2,514,568
	37,835,738	40,257,753
Less:		
Current portion	(6,522,676)	(7,442,634)
	$ 31,313,062	$ 32,815,119

Note 7. Notes Payable and Long-Term Debt (continued)

Principal maturities of long-term debt at June 30, 2006 are as follows:

Year ending June 30,	
2007	$ 6,522,676
2008	31,313,062
	$ 37,835,738

At June 30, 2006, the prime rate was 8.25% and the 30-day LIBOR rate was 5.35%.

On April 15, 2005, the Corporation issued notes payable to JPMorgan Chase Bank in the amounts of $12,000,000, $8,000,000 and $5,000,000 under separate loan agreements. The proceeds were used in connection with the refunding of the Series 1992 and 1996 Revenue Bonds. On April 15, 2005, the Corporation also entered into a Revolving Credit and Security agreement with Capital Source Finance, an asset-based lender. The proceeds of the revolving line were used to refund the Series 1992 and 1996 Revenue Bonds.

Certain proceeds from the issuance of the notes were used to pay the principal and interest outstanding on a portion of the Series 1996 Revenue Bonds on April 15, 2005. Certain proceeds from the issuance of the notes were also placed in an irrevocable escrow account and invested in government securities, which, with interest thereon, were sufficient to pay the principal and interest outstanding on the Series 1992 and 1996 Revenue Bonds in May 2005 and January 2006, respectively. As a result of these transactions the Corporation recognized a $978,534 nonoperating loss on advance refunding.

The terms of the loan agreements require that the Corporation maintain a total of $12,000,000 and $15,812,500, plus accrued interest, in pledged accounts with a bank at June 30, 2006 and 2005, respectively. At June 30, 2006 and 2005, respectively, the Corporation held approximately $12,041,000 and $15,900,000 in these pledged accounts.

At June 30, 2005, one of these secured accounts noted above included $3,812,500 which was externally designated for pending settlement of a liability claim. At June 30, 2005, this amount is included with investments and assets limited as to use on the consolidated balance sheet. During fiscal year 2006, a settlement on the liability claim was agreed to. The total settlement amounted to approximately $3,300,000. The external restriction was removed when the first payment was made by the Corporation in accordance with the settlement agreement. Approximately $1,300,000 was paid on that claim during fiscal year 2006 and approximately $2,000,000 remains internally designated to cover the remaining outstanding liability on that claim at June 30, 2006.

At June 30, 2006 and 2005, the $8,000,000 note is secured by a guarantee by the Sisters of Mercy and the $5,000,000 note is secured by a mortgage on the Corporation's property. The Corporation's accounts receivable and certain other assets are pledged as collateral under the revolving line of credit.

The loan agreements on the notes contain various covenants including those relating to limitations on incurring additional debt and disposing of property. In addition, the revolving credit and security agreement contains covenants including those relating to financial performance, insurance coverage and timely submission of specified financial reports.

Note 8. Lease Obligations

Rental expense for all operating leases totaled approximately $2,860,000 and $2,635,000 in 2006 and 2005, respectively. Future minimum lease payments under the noncancellable leases and related maintenance agreements are as follows:

Year ended June 30:	
2007	$ 2,563,000
2008	2,476,000
2009	1,253,000
2010	540,000
2011	212,000
Thereafter	300,000
	$ 7,344,000

Note 9. Retirement Plan

The Hospital sponsored a noncontributory, defined-benefit pension plan, which covered substantially all of the Hospital's full-time employees. Benefits were based on years of service and the employee's compensation during the last five years of employment. The Hospital's funding policy was to contribute such amounts as are necessary to provide for benefits attributed to service to date and those expected to be earned in the future. Effective June 30, 2003, the plan was amended to freeze all benefit accruals. As a result, a curtailment benefit was recorded by the Hospital.

Effective June 30, 2004, the plan was amended to allow the sponsor to terminate the plan and settle pension obligations with all plan participants. The plan amendment accelerated the distribution of benefits earned. Effective July 1, 2004, the plan was amended to cease commencing distributions, eliminate the annuity forms of distribution, revise the allocation formula upon plan termination, revise the provision related to payment in the event a participant or beneficiary is determined to be incompetent, and provide that the plan be terminated effective July 1, 2004. This amendment resulted in a gain of $6,467,781 during fiscal year 2005. As of June 30, 2006, distribution of plan assets to participants was still in progress.

Note 9. Retirement Plan (continued)

The following table sets forth the plan's funded status and amounts recognized in the accompanying consolidated balance sheets at June 30:

	2006	2005
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 19,837,865	$ 25,204,619
Service cost	-	-
Interest cost	228,838	1,500,299
Plan amendments	-	(6,467,781)
Effect of curtailment	-	-
Actuarial losses	-	-
Benefits paid	(19,152,047)	(399,272)
Benefit obligation at end of year	$ 914,656	$ 19,837,865
Change in plan assets:		
Fair value of plan assets at beginning of year	$ 19,837,865	$ 19,571,379
Actual return on plan assets	228,838	665,758
Employer contributions	-	-
Benefit paid	(19,152,047)	(399,272)
Fair value of plan assets at end of year	$ 914,656	$ 19,837,865
Funded status of the plan	$ -	$ -
Unrecognized prior service cost	-	(6,253,499)
Unrecognized net actuarial gain	-	6,253,499
Accrued benefit cost, before additional minimum liability	-	-
Adjustment for additional minimum liability	-	-
Accrued benefit cost, after additional minimum liability	$ -	$ -
Assumptions:		
Discount rate	6.00%	6.00%
Expected return on plan assets	N/A	5.50%
Rate of compensation increase	N/A	N/A

Due to the distribution of plan assets, the plan's remaining assets are allocated to fixed income investments as of June 30, 2006 and 2005..

Effective July 1, 2004, the Corporation put in place a defined-contribution pension plan, which covers substantially all of the Corporation's full-time employees. The Corporation's matching contributions are 50% of the amount contributed by participants, up to a maximum of 6% of the participant's compensation. For the years ended June 30, 2006 and 2005, total expense associated with this plan amounted to approximately $1,015,000 and $863,000, respectively.

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Note 10. Professional and General Liability Insurance

The actuarially determined professional liability in the accompanying consolidated balance sheets reflects management's assessment of claims applicable to all self-insured periods. Accrued professional liability losses have been discounted at 6% at both June 30, 2006 and 2005. An accrual for possible losses attributable to incidents that may have occurred, but that have not been identified under the incident reporting system is included in this liability. If accrued professional liability losses had not been discounted, the estimated liability would be approximately $4,031,000 and $5,221,000 higher than the amounts recorded in the consolidated balance sheets as of June 30, 2006 and 2005, respectively. The Corporation had investments available for claims settlements of $127,211 and $73,220 as of June 30, 2006 and 2005, respectively.

The Corporation's 2006 insurance expense was reduced by approximately $7,400,000 due to a change in the estimated professional liability accrual as a result of several factors, including revision of the confidence level used to estimate expected losses and favorable loss claim experience. In addition, the Corporation received a prior year premium refund during 2006 in the amount of $1,300,000. This refund resulted in an additional reduction of 2006 insurance expense.

Note 11. Transactions with Related Parties

The following related party transactions have been entered into:

a. As of June 30, 2005, the Corporation had a note payable to the Sisters of Mercy outstanding in the amount of $2,075,000 which was forgiven in June 2006.

b. The Hospital bills and collects monies for services rendered to the Diagnostic and Treatment (D&T) Center's patients. In addition, the Hospital charges the D&T Center certain indirect costs of providing administrative, financial, and clinical services. These charges totaled approximately $413,000 in both 2006 and 2005. At June 30, 2005, the Hospital had amounts due from the D&T Center totaling approximately $235,000 related to these services.

c. The operations of the D&T Center are dependent on the continued financial and operating support of the Hospital. Under the terms of the Hospital's management agreement with the D&T Center, the Hospital has agreed to provide the necessary financial and operating support to the D&T Center for future periods.

Note 12. Functional Expenses

The Corporation provides general health care services to residents within Chicago and the surrounding area and supports medical education programs. The Corporation's expenses related to providing these services are as follows for the years ended June 30:

	2006	2005
Health care services	$ 97,313,451	$ 94,746,182
Medical education	7,520,184	7,816,498
Fund-raising	515,996	237,832
General and administrative	69,634,145	81,201,202
	$ 174,983,776	$ 184,001,714

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Certain amounts have been allocated between functional categories.

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Note 13. Commitments, Contingencies and Subsequent Event

Litigation: The Corporation is a defendant in various lawsuits arising in the ordinary course of business. Although the outcome of the lawsuits cannot be determined with certainty, management believes the ultimate disposition of such matters will not have a material effect on the Corporation's financial statements.

Regulatory Investigation: The U.S. Department of Justice, other federal agencies and the Illinois Department of Public Aid routinely conduct regulatory investigations and compliance audits of health care providers. The Corporation is subject to these regulatory efforts. Management is currently unaware of any regulatory matters which may have a material effect on the Corporation's financial position or results from operation.

Claim Settlement: In 2006, the Corporation settled a lawsuit for the amount of $3,300,000. Of this amount, $1,300,000 was paid on the settlement date (September 1, 2005). The remaining $2,000,000 is to be paid in three equal annual installments on August 1 of 2006, 2007 and 2008. The Corporation intends to fund the settlement with cash from operations and the balance is recorded separately as internally designated for liability claims. At June 30, 2005, the settlement amount was included in professional liability on the consolidated balance sheet. At June 30, 2006, the liability was reduced to $2,000,000.

Land Sale: In 2004, the Corporation entered into an agreement with a developer to sell the property east of Prairie Avenue for a floor price of $8,250,000. The Hospital will receive additional proceeds based on the actual number of housing units sold. Total sale proceeds are estimated to be $10.4 million. Two closings were completed in 2006 and a third closing was completed in July 2006. Sale proceeds received in 2006 and subsequent to year-end were $944,000 and $1,710,000, respectively. In 2006, the Corporation recognized a gain on the sale of this property of approximately $848,000. Subsequent to year-end, gains recognized to date are approximately $1,539,000.

Construction Commitment: In 2006, the Corporation entered into an agreement with a contractor for repair and maintenance work on the exterior walls and enclosures of the main hospital building. The total estimated cost of the project was approximately $2.4 million. As of June 30, 2006, the estimated remaining cost of the project was approximately $1.1 million. The project is being funded with cash from operations and is expected to be completed during fiscal year 2007.

Joint Venture: In July 2006, the Corporation entered into an agreement with the cardiology and radiology groups to form a joint venture to purchase a 64 Detector CT Scan. The Hospital will have a 51% ownership of the joint venture.

Contingency: Financial Accounting Standards Board Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations* (FIN 47) clarified when an entity is required to recognize a liability for a conditional asset retirement obligation. The Corporation has a legal obligation to remove hazardous materials from its facilities in the event the facilities are renovated or replaced. Such hazardous materials include asbestos. Management believes there is an indeterminate settlement date for the asset retirement obligations because of the range of time over which the Corporation may settle the obligation is unknown. However, management does not believe that the estimate of the liability related to these asset retirement obligations is a material amount at June 30, 2006.

Note 14. Fair Value of Financial Instruments

The following methods and assumptions were used by the Corporation to estimate the fair value of other financial instruments:

The carrying value of cash and cash equivalents, patient accounts receivables, other assets, accounts payable, accrued expenses and estimated settlements due to or from third-party payors are reasonable estimates of their value due to the short-term nature of these financial instruments.

Note 14. Fair Value of Financial Instruments (Continued)

The fair value of investments and assets limited as to use, which are the amounts reported on the balance sheet, is based on quoted market prices.

The fair value of long-term debt is estimated based on interest rates for the same or similar debt offered to the Corporation having the same or similar remaining maturities and collateral requirements. The fair value of the long-term debt approximates the carrying values.

McGladrey & Pullen
Certified Public Accountants

Independent Auditor's Report on the Supplementary Information

To the Board of Directors
Mercy Health System of Chicago
Chicago, Illinois

Our audits were made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The consolidating information is presented for purposes of additional analysis of the basic consolidated financial statements rather than to present the financial position and results of operations of the individual companies. The consolidating information has been subjected to the auditing procedures applied in the audits of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

McGladrey & Pullen, LLP

Chicago, Illinois
August 29, 2006

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Mercy Health System of Chicago and Subsidiaries
Consolidating Balance Sheet
June 30, 2006

	Mercy Health System of Chicago	Mercy Hospital and Medical Center	Mercy Health Care Rehabilitation Center	Mercy Services Corporation	Mercy Foundation, Inc.	Eliminations	Consolidated Totals
Assets							
Current Assets							
Cash and cash equivalents	$ 30,482	$ 6,934,921	$ -	$ 1,000	$ 325,234	$ -	$ 7,291,637
Investments and assets limited as to use, internally designated under self-insurance program	-	127,211	-	-	-	-	127,211
Short-term investments	-	76,648	-	-	1,750,154		1,826,802
Patient accounts receivable, net of allowance for doubtful accounts	-	26,568,161	-	-	-	-	26,568,161
Interest in net assets of Foundation	-	1,452,414	-	-	-	(1,452,414)	-
Due from related party	650,000	75,119	3,629,125	-	-	(4,354,244)	-
Inventories	-	2,147,405	-	-	-	-	2,147,405
Other assets	-	1,940,515	-	-	34,407	-	1,974,922
Total current assets	680,482	39,322,394	3,629,125	1,000	2,109,795	(5,806,658)	39,936,138
Investments and Assets Limited as to Use, net of amounts required to meet current obligations							
Pledged under debt agreement	-	12,040,542	-	-	-	-	12,040,542
Externally designated under lease agreement	-	717,662	-	-	-	-	717,662
Externally designated under self-insurance program	-	2,009,888	-	-	-	-	2,009,888
Other Investments	-	1,564,402	-	-	1,118,187	-	2,682,589
	-	16,332,494	-	-	1,118,187	-	17,450,681
Property and Equipment							
Land and land improvements	-	8,753,112	-	-	-	-	8,753,112
Buildings and fixtures	-	106,443,732	-	-	-	-	106,443,732
Equipment	-	117,596,701	-	-	30,447	-	117,627,148
Construction in progress	-	4,183,699	-	-	-	-	4,183,699
	-	236,977,244	-	-	30,447	-	237,007,691
Less accumulated deprecation	-	(178,227,185)	-	-	(23,721)	-	(176,250,906)
	-	58,750,059	-	-	6,726	-	58,756,785
Other Assets							
Deferred financing costs, net	-	474,253	-	-	-	-	474,253
Other noncurrent assets	-	1,071,519	-	-	140,917	-	1,212,436
	-	1,545,772	-	-	140,917	-	1,686,689
Total assets	$ 680,482	$ 115,950,719	$ 3,629,125	$ 1,000	$ 3,375,625	$ (5,806,658)	$ 117,830,293

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	Mercy Health System of Chicago	Mercy Hospital and Medical Center	Mercy Health Care Rehabilitation Center	Mercy Services Corporation	Mercy Foundation, Inc.	Eliminations	Consolidated Totals
Liabilities and Net Assets							
Current Liabilities							
Accounts payable	$ -	$ 17,962,512	$ 128,258	$ -	$ 104,374	$ -	$ 18,195,144
Accrued expenses	-	8,158,160	-	-	297	-	8,158,457
Due to third-party payors	-	6,257,664	-	-	-	-	6,257,664
Current portion of long-term debt	-	6,522,676	-	-	-	-	6,522,676
Due to related party	-	4,279,125	-	-	75,119	(4,354,244)	-
Current portion of professional liability	-	5,145,667	435,000	-	-	-	5,580,667
Total current liabilities	-	48,325,804	563,258	-	179,790	(4,354,244)	44,714,608
Long-Term Debt, less current portion	-	31,313,062	-	-	-	-	31,313,062
Professional Liability, less current portion	-	17,604,333	-	-	-	-	17,604,333
Financing Obligation Arising From Sale-Leaseback Transaction	-	7,331,968	-	-	-	-	7,331,968
Deferred Grant Revenue	-	1,978,562	-	-	-	-	1,978,562
Total liabilities	-	106,553,729	563,258	-	179,790	(4,354,244)	102,942,533
Net Assets							
Unrestricted	680,482	7,479,497	3,065,867	1,000	1,743,421	-	12,970,267
Temporarily restricted	-	1,604,933	-	-	1,452,414	(1,452,414)	1,604,933
Permanently restricted	-	312,560	-	-	-	-	312,560
Total net assets	680,482	9,396,990	3,065,867	1,000	3,195,835	(1,452,414)	14,987,760
Total liabilities and net assets	$ 680,482	$ 115,950,719	$ 3,629,125	$ 1,000	$ 3,375,625	$ (5,806,658)	$ 117,830,293

ATTACHMENT FINANCIALS

Mercy Health System of Chicago and Subsidiaries
Consolidating Statement of Operations
Year Ended June 30, 2006

	Mercy Health System of Chicago	Mercy Hospital and Medical Center	Mercy Health Care Rehabilitation Center	Mercy Services Corporation	Mercy Foundation, Inc.	Eliminations	Consolidated Totals
Revenue:							
Net patient service revenue	$ -	$ 171,780,631	$ -	$ -	$ -	$ -	$ 171,780,631
Capitation revenue	-	1,698,339	-	-	-	-	1,698,339
Contributions	-	363,935	-	-	859,009	(355,000)	867,944
Other	-	3,826,199	-	-	267	-	3,826,466
Net assets released from restriction - used for operations	-	105,121	-	-	223,398	-	328,519
	-	177,774,225	-	-	1,082,674	(355,000)	178,501,899
Expenses:							
Salaries and benefits	-	90,021,640	-	-	179,046	-	90,200,686
Supplies	-	25,761,076	-	-	14,876	-	25,775,952
Insurance	-	(2,242,683)	-	-	-	-	(2,242,683)
Depreciation and amortization	-	8,370,394	-	-	3,582	-	8,373,976
Provision for uncollectible accounts	-	14,323,749	-	-	-	-	14,323,749
Interest	-	2,743,940	-	-	-	-	2,743,940
Professional fees	-	5,473,887	-	-	-	-	5,473,887
Repairs, utilities and rent	-	11,579,954	-	-	35,227	-	11,615,181
Purchased services	-	14,541,350	-	-	2,383	-	14,543,733
Other	-	3,894,473	-	-	635,882	(355,000)	4,175,355
	-	174,467,780	-	-	870,996	(355,000)	174,983,776
Income from operations	-	3,306,445	-	-	211,678	-	3,518,123
Nonoperating income:							
Gain on sale of property and equipment	-	848,808	-	-	-	-	848,808
Investment income	342	668,850	-	-	88,713	-	757,905
Excess of revenue over expenses	342	4,824,103	-	-	300,391	-	5,124,836
Unrestricted net assets:							
Net change in unrealized gains and losses on investments	-	-	-	-	(2,543)	-	(2,543)
Forgiveness of note payable	-	2,075,000	-	-	-	-	2,075,000
Increase in unrestricted net assets	$ 342	$ 6,899,103	$ -	$ -	$ 297,848	$ -	$ 7,197,293

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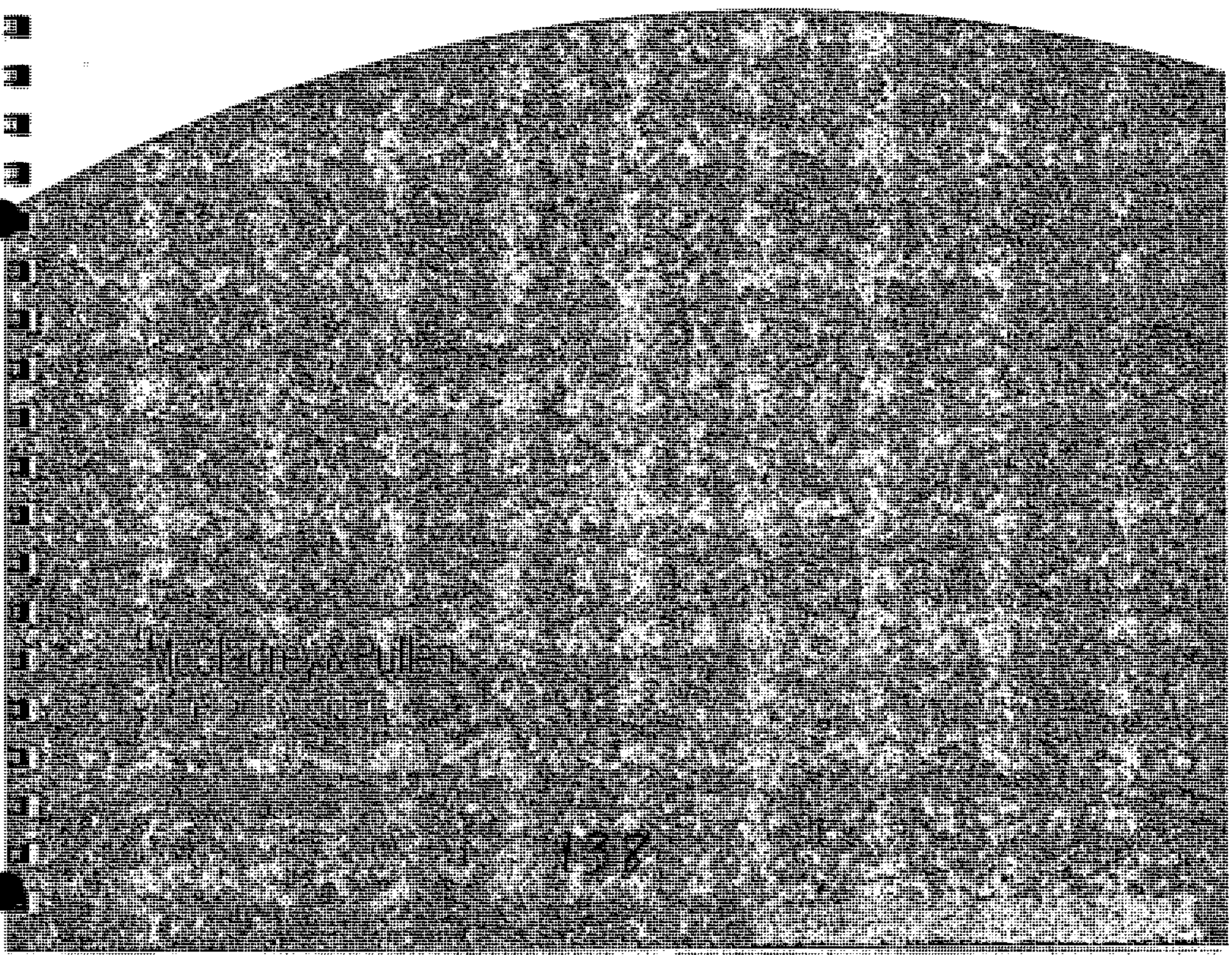
Mercy Health System of Chicago and Subsidiaries

Consolidated Financial Report

June 30, 2005



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Contents

McGladrey & Pullen
Certified Public Accountants

Independent Auditor's Report on the Financial Statements

To the Board of Directors
Mercy Health System of Chicago
Chicago, Illinois

We have audited the accompanying consolidated balance sheet of Mercy Health System of Chicago and Subsidiaries (the "Corporation") as of June 30, 2005, and the related consolidated statements of operations and changes in net assets (deficiency) and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit. The consolidated financial statements of Mercy Health System of Chicago and Subsidiaries for the year ended June 30, 2004 were audited by other auditors whose report, dated October 20, 2004, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2005 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mercy Health System of Chicago and Subsidiaries as of June 30, 2005, and the results of their operations, changes in net assets (deficiency), and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Chicago, Illinois
December 2, 2005, except for the last paragraph of Note 7,
as to which the date is January 25, 2006

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Mercy Health System of Chicago and Subsidiaries

Consolidated Balance Sheets
June 30, 2005 and 2004

	2005	2004
Assets		
Current Assets		
Cash and cash equivalents	$ 7,687,868	$ 18,824,376
Investments and assets limited as to use:		
Externally designated under debt agreement	-	2,710,150
Internally designated under self-insurance program	73,220	910,151
Short-term investments	1,002,764	1,311,775
Patient accounts receivable, net of allowances for doubtful accounts of $16,318,000 in 2005 and $16,718,000 in 2004	24,094,299	21,382,930
Due from related party	234,573	-
Inventories	1,854,338	1,775,123
Other current assets	2,404,790	1,194,338
Total current assets	37,351,852	48,108,843
Investments and Assets Limited as to Use		
Pledged under debt agreement	12,087,649	-
Externally designated under debt agreement	-	7,444,884
Externally designated under lease agreement	800,000	-
Internally designated under self-insurance program	-	4,000,000
Externally designated under self-insurance program	3,812,500	-
Other Investments	2,449,495	2,558,374
	19,149,644	14,003,258
Property and Equipment		
Land and land improvements	9,316,753	8,792,213
Buildings and fixtures	105,162,988	101,278,237
Equipment	112,839,819	108,132,944
Construction in progress	788,744	2,961,636
	228,108,304	221,165,030
Less accumulated depreciation	(170,781,470)	(163,076,032)
	57,326,834	58,088,998
Other Assets		
Deferred financing costs, net	479,653	537,167
Other noncurrent assets	966,731	1,008,629
	1,446,384	1,545,796
Total assets	$ 115,274,714	$ 121,746,895

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See Notes to Consolidated Financial Statements.

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	2005	2004
Liabilities and Net Assets (Deficiency)		
Current Liabilities		
Accounts payable	**$ 14,135,542**	$ 11,130,228
Accrued expenses	**9,204,310**	10,585,063
Pension liability	**-**	5,633,240
Due to third-party payors	**5,030,291**	8,314,816
Current portion of long-term debt	**7,442,634**	4,068,651
Notes payable	**2,075,000**	2,617,549
Current portion of professional liability	**7,423,000**	5,803,000
Total current liabilities	**45,310,777**	48,152,547
Noncurrent Liabilities		
Long-term debt, less current portion	**32,815,119**	55,152,023
Professional liability, less current portion	**20,363,000**	18,544,000
Financing obligation arising from sale-leaseback transaction	**7,046,641**	-
Deferred grant revenue	**2,135,801**	2,126,472
Total liabilities	**107,671,338**	123,975,042
Commitments and Contingencies (Note 13)		
Net Assets (Deficiency):		
Unrestricted	**5,810,974**	(3,996,634)
Temporarily restricted	**1,479,842**	1,455,927
Permanently restricted	**312,560**	312,560
Total net assets (deficiency)	**7,603,376**	(2,228,147)
Total liabilities and net assets (deficiency)	**$ 115,274,714**	$ 121,746,895

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ATTACHMENT FINANCIALS

Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Operations and Changes In Net Assets (Deficiency)
Years Ended June 30, 2005 and 2004

	2005	2004
Revenue:		
Net patient service revenue	$ 169,628,548	$ 159,913,124
Medicaid hospital assessment revenue	11,679,718	-
Capitation revenue	1,337,213	1,426,263
Contributions	315,032	173,740
Other	4,118,378	3,698,665
Net assets released from restriction - used for operations	645,537	688,596
	187,724,426	165,900,388
Expenses:		
Salaries and benefits	86,613,397	76,352,023
Supplies	25,530,887	21,727,502
Insurance	5,741,054	3,301,425
Depreciation and amortization	8,419,930	8,604,035
Provision for uncollectible accounts	13,811,990	12,540,073
Interest	3,725,496	3,930,831
Professional fees	5,375,728	5,277,607
Repairs, utilities and rent	10,631,278	9,426,582
Purchased services	13,589,315	13,853,288
Medicaid hospital assessment expense	6,779,314	-
Other	3,783,325	3,276,070
	184,001,714	158,289,436
Operating income	3,722,712	7,610,952
Nonoperating income (expense):		
Gain on sale of property and equipment	45,324	4,339,008
Investment income	1,544,392	210,578
Loss on advance refunding	(978,534)	-
Other	(30,000)	650,000
	581,182	5,199,586
Excess of revenue over expenses	$ 4,303,894	$ 12,810,538

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Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets (Deficiency)(Continued)
Years Ended June 30, 2005 and 2004

	2005	2004
Unrestricted net assets		
Excess of revenue over expenses	$ 4,303,894	$ 12,810,538
Net change in unrealized appreciation in fair value of investments	-	22,027
Change in minimum pension liability	5,503,714	(1,571,622)
Increase in unrestricted net assets	9,807,608	11,260,943
Temporarily restricted net assets		
Contributions	669,452	824,392
Net assets released from restrictions, used for operations	(645,537)	(688,596)
Increase in temporarily restricted net assets	23,915	135,796
Increase in net assets	9,831,523	11,396,739
Net assets (deficiency):		
Beginning of year	(2,228,147)	(13,624,886)
End of year	$ 7,603,376	$ (2,228,147)

See Notes to Consolidated Financial Statements.

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Mercy Health System of Chicago and Subsidiaries

Consolidated Statements of Cash Flows
Years Ended June 30, 2005 and 2004

	2005	2004
Cash Flows from Operating Activities		
Increase in net assets	$ 9,831,523	$ 11,396,739
Adjustments to reconcile increase in unrestricted net assets to net cash provided by operating activities:		
Net change in unrealized appreciation of investments	-	(22,027)
Depreciation and amortization	8,419,930	8,604,035
Provision for bad debts	13,811,990	12,540,073
Gain on sale of property	(45,324)	(4,339,008)
Amortization of deferred revenue	(125,000)	-
Loss on advance refunding	978,534	-
Interest added to financing obligation arising from sale-leaseback transaction	46,641	-
Changes in operating assets and liabilities:		
Accounts receivable	(16,523,359)	(16,095,319)
Accounts payable and accrued expenses	1,624,561	(1,510,909)
Due to third-party payors	(3,284,525)	2,518,817
Professional liability	3,439,000	354,000
Pension liability	(5,633,240)	-
Other assets	(1,247,769)	808,468
Net cash provided by operating activities	11,292,962	14,254,869
Cash Flows from Investing Activities		
Purchases of property and equipment	(7,458,178)	(7,392,981)
Purchases of investments and assets limited as to use and other investments	(16,700,149)	(14,397,482)
Proceeds from sale of property and equipment	57,659	7,987,623
Proceeds from sale/maturity of investments and assets limited to use	5,132,278	12,504,034
Advance to related party	(234,573)	-
Release debt service reserve funds (1992 and 1996 bonds)	9,763,743	-
Net cash (used in) investing activities	(9,439,220)	(1,298,806)
Cash Flows from Financing Activities		
Advance refunding of long-term debt	(54,278,138)	-
Proceeds from issuance of long-term debt	40,000,000	-
Proceeds from sale-leaseback transaction	7,000,000	-
Payments on long-term debt	(4,727,757)	(3,769,802)
Payments on notes payable	(542,549)	(500,000)
Payment of deferred financing costs	(576,135)	-
Proceeds from grant, for property and equipment	134,329	-
Other	-	(149,645)
Net cash (used in) financing activities	(12,990,250)	(4,419,447)
Net (decrease) increase in cash and cash equivalents	(11,136,508)	8,536,616
Cash and cash equivalents:		
Beginning	18,824,376	10,287,760
Ending	$ 7,687,868	$ 18,824,376
Supplemental Disclosures of Cash Flow Information		
Interest paid	$ 5,343,427	$ 4,324,851

See Notes to Consolidated Financial Statements. 145

ATTACHMENT FINANCIALS

Note 1. Nature of Business and Significant Accounting Policies

Organization and nature of business: The accompanying consolidated financial statements represent the accounts of Mercy Health System of Chicago ("Parent") and its subsidiaries (jointly, the "Corporation"). The Corporation is sponsored by the Sisters of Mercy of the Americas, Regional Community of Chicago ("Sisters of Mercy"), a religious institute. Subsidiaries of the Parent include Mercy Health Care Rehabilitation Center ("Center"), Mercy Services Corporation ("MSC"), Mercy Hospital and Medical Center ("Hospital"), and Mercy Foundation, Inc. ("Foundation").

The Hospital is a licensed 479-bed acute care facility with its primary market in the south and southwest side of Chicago, Illinois, and adjacent suburbs. In addition to the main facility, the Hospital has a network of hospital-owned primary care centers, private physician offices, and a number of satellites throughout the City of Chicago.

Prior to the transfer of its operations to the Hospital, effective January 1, 1998, MSC, a taxable organization, operated several businesses, including home health care services for certain contracts, an occupational therapy registry, and a supplier of small medical equipment and supplies. All of MSC's stock is owned by the Parent.

The Foundation was organized for the purpose of collecting, earning, and receiving funds from public and private sources, accumulating such funds, and making distributions of income to the Parent or related entities properly designated by the Parent.

The Center was sold in December 2001. According to the sale agreement, $300,000 was placed into a trust account to be used to offset Medicare and Medicaid audit adjustments related to periods prior to the sale. Unused funds were released to the Hospital in February 2005. Other than recognizing interest income and expenses related to the release of the trust monies, the Center has been inactive.

A summary of significant accounting policies follows:

Principles of consolidation: The accompanying consolidated financial statements include the Parent, Center, MSC, Hospital and Foundation. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of estimates: The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The use of estimates and assumptions in the preparation of the accompanying financial statements is primarily related to the determination of the net patient accounts receivable and settlements with third-party payors and the accrual for professional liability. Due to uncertainties inherent in the estimation and assumption process, it is at least reasonably possible that changes in these estimates and assumptions in the near term would be material to the financial statements.

Basis of presentation: The Corporation may classify its net assets into three categories, which are unrestricted, temporarily restricted and permanently restricted.

Unrestricted net assets are reflective of revenues and expenses associated with the principal operating activities of the Corporation and are not subject to donor-imposed stipulations.

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Note 1. Nature of Business and Significant Accounting Policies (continued)

Temporarily restricted net assets are subject to donor-imposed stipulations that may or will be met either by actions of the Corporation and/or the passage of time. As of June 30, 2005 and 2004, temporarily restricted net assets were restricted by donors primarily for patient care, community service, education, research, and purchase of equipment. Income earned on donor-restricted marketable securities, unless restricted by donors, is reflected in investment income. When a donor restriction expires, temporarily restricted net assets are classified as unrestricted net assets and reported in the statement of operations and changes in net assets as other revenue.

Permanently restricted net assets have been restricted by donors to be maintained by the Corporation in perpetuity. The income earned on permanently restricted net assets has been restricted by donors to provide care for the poor.

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

Cash and cash equivalents: All investments that are not limited as to use with an original maturity of three months or less at the time of acquisition are reflected as cash equivalents.

Throughout the year, the Corporation may have amounts on deposit with financial institutions in excess of those insured by the FDIC. Management does not believe this presents a significant risk to the Corporation.

Patient accounts receivable, provision for doubtful accounts and due from/to third party-payors: The collection of receivables from third-party payors and patients is the Corporation's primary source of cash for operations and is critical to its operating performance. The primary collection risks relate to uninsured patient accounts and patient accounts for which the primary insurance payor has paid, but patient responsibility amounts (deductibles and copayments) remain outstanding. Patient receivables, where a third-party payor is responsible for paying the amount, are carried at a net amount determined by the original charge for the service provided, less an estimate made for contractual adjustments or discounts provided to third-party payors.

Patient receivables due directly from the patients are carried at the original charge for the service provided less amounts covered by third-party payors and less an estimated allowance for uncollectible receivables. Management estimates this allowance based on the aging of its accounts receivable and its historical collection experience for each payor type. Recoveries of receivables previously written off are recorded as a reduction of the provision for uncollectible accounts when received.

The past due status of receivables is determined on a case-by-case basis depending on the payor responsible. Interest is generally not charged on past due accounts.

Receivables or payables related to estimated settlements on various payor contracts, primarily Medicare, are reported as amounts due from or to third-party payors. Significant changes in payor mix, business office operations, economic conditions or trends in federal and state governmental health care coverage could affect the Corporation's collection of accounts receivable, cash flows and results of operations.

Note 1. Nature of Business and Significant Accounting Policies (continued)

Recevables and payables related to the Medicaid Hospital Assessment Program are reported as amounts due from/to third-party payors.

Inventories: Inventories are stated at cost (first-in, first-out method).

Investments and assets limited as to use: Investments whose use is limited are recorded at fair value based on quoted market prices. Realized investment income is included in excess of revenue over expenses unless the income or loss is restricted by donor or law. The change in unrealized appreciation in fair value of investments is recognized as a change in net assets.

Investments are regularly evaluated for impairment. The Corporation considers factors affecting the investee, factors affecting the industry the investee operates within, and general debt and equity trends. The Corporation considers the length of time an investment's fair value has been below carrying value, the near-term prospects for recovery to carrying value, and the intent and ability to hold the investment until maturity date or market recovery is realized. If and when a determination is made that a decline in fair value below the cost basis is other than temporary, the related investment is written down to its estimated fair value and included as a realized loss in excess of revenue over expenses.

Assets limited as to use consist of investments set aside by the Board for self-insurance over which the Board retains control and may, at its discretion, subsequently use for other purposes. Assets limited as to use also include investments externally designated under debt and lease agreements and an insurance claim settlement.

Property and equipment: Property and equipment are recorded at cost and depreciated on the straight-line method over their estimated useful lives. The assets' lives are as follows:

Land improvements	5 years
Building and fixtures	5 – 40 years
Furniture and equipment	3 – 20 years
Automobiles	3 – 4 years
Leasehold improvements	15 – 20 years

Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Interest expense capitalized as property and equipment was $160,000 in 2004. There was no interest expense capitalized in 2005.

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

Accrued professional liability: The provision for accrued professional liability includes estimates of the ultimate costs for claims incurred but not reported. The provision is actuarially determined. The Corporation is completely self-insured for all claims incurred on and after July 1, 2002.

Note 1. Nature of Business and Significant Accounting Policies (continued)

Deferred financing costs: Costs incurred in connection with the issuance or refinancing of long-term debt are deferred and amortized over the term of the related financing on a method that approximates the effective yield method.

Community commitment: Community commitment represents patient charity care rendered to the community at a reduced rate or at no fee based upon community need or the inability of the individual to pay for services. Because the Corporation does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Net patient service revenue: The Corporation has agreements with third-party payors that provide for payments to the Corporation at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Capitation revenue: The Corporation has agreements with various health maintenance organizations (HMOs) to provide medical services to subscribing participants. Under these agreements, the Corporation receives monthly capitation payments based on the number of each HMO's participants, regardless of services actually performed by the Corporation. In addition, the HMOs make fee-for-service payments to the Corporation for certain covered services based upon discounted fee schedules.

Operating income: The consolidated statements of operations and changes in net assets (deficiency) include operating income. Changes in unrestricted net assets (deficiency), which are excluded from operating income, include investment income, gains and losses from sales of property and equipment, loss on advance refunding and other income and expense which management views as outside of normal activity.

Results of operations: The consolidated statements of operations and changes in net assets (deficiency) include excess of revenue over expenses that represents the results of operations. Changes in unrestricted net assets (deficiency) that are excluded from excess of revenues over expenses, consistent with industry practice, include the change in net unrealized appreciation in fair value of investments and change in minimum pension liability.

Income taxes: The Parent, the Hospital, the Center, and the Foundation have received determination letters from the Internal Revenue Service stating that they are exempt from the payment of federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

At June 30, 2005, MSC had approximately $1,566,000 of net operating tax loss carryforwards available for use against future taxable income, which begin to expire in 2007. As a result of the net operating tax loss carryforwards, there is no income tax provision in 2005 and 2004. Due to the uncertain future realization of these loss carryforwards, the related tax assets have been fully reserved by a valuation allowance in the accompanying consolidated balance sheets.

Reclassification: Certain amounts in the 2004 financial statements have been reclassified to conform to the 2005 presentation.

Note 2. Net Patient Service Revenue

The Corporation has agreements with third-party payors which provide for reimbursement to the Corporation at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Corporation's billings at list price and the amounts reimbursed by Medicare, Medicaid, Blue Cross, and certain other third-party payors, and any differences between estimated third-party reimbursement settlements for prior years and subsequent final settlements. Contractual adjustments under third-party reimbursement programs are accrued on an estimated basis in the period the related services are rendered and are adjusted in future periods as final settlements are determined. A summary of the basis of reimbursement with major third-party payors follows:

Medicare: The Corporation is paid for inpatient acute care and outpatient care services rendered to Medicare program beneficiaries under prospectively determined rates per discharge (Prospective Payment Systems). These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient nonacute services and defined capital and medical education costs related to Medicare beneficiaries are paid based upon either a cost reimbursement method, established fee screens, or a combination thereof. The Corporation's classification of patients under Prospective Payment Systems and the appropriateness of the patient's admissions are subject to validation reviews. The Corporation is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual reimbursement reports by the Corporation and audits by the Medicare fiscal intermediary.

Medicaid: The Corporation is reimbursed at prospectively determined rates for each Medicaid inpatient discharge. Outpatient services are reimbursed based on established fee screens. For inpatient acute care services, payment rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. The prospectively determined rates are not subject to retroactive adjustment. The Corporation also receives incremental Medicaid reimbursement for specific programs and services at the discretion of the State of Illinois Medicaid Program. Medicaid reimbursement may be subject to periodic adjustment, as well as to changes in existing payment levels and rates, based on the amount of funding available to the Medicaid program.

Blue Cross: The Corporation also participates as a provider of health care services under a reimbursement agreement with Blue Cross. The provisions of this agreement stipulate that services will be reimbursed at a tentative reimbursement rate and that final reimbursement for these services is determined after the submission of an annual cost report by the Corporation and a review by Blue Cross.

Managed Care Organizations: The Corporation has also entered into reimbursement agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment under these agreements includes discounts from established charges and prospectively determined per diem rates.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near-term. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. Net patient service revenue in 2005 and 2004 was increased by the effect of favorable third-party payor settlements of approximately $1,500,000 and $2,500,000, respectively.

Note 2. Net Patient Service Revenue (Continued)

In December 2004, the Federal Centers of Medicare and Medicaid Services (CMS) approved State of Illinois (State) legislation for a Medicaid Hospital Assessment Program (Program) relating to the period May 9, 2004 to June 30, 2005. Under the Program, the Hospital received additional Medicaid reimbursement from the State and paid a related assessment. Total reimbursement revenue recognized by the Hospital related to this Program amounted to $11,679,718 during the Hospital's year ended June 30, 2005. Total assessments incurred by the Hospital related to this program amounted to $6,779,314 during the Hospital's year ended June 30, 2005. The laws and regulations authorizing this Program expired on June 30, 2005.

Note 3. Concentrations of Credit Risk

The Corporation grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at June 30, 2005 and 2004, was as follows:

	2005	2004
Medicare	20%	25%
Medicaid	29	16
Managed care	30	31
Other third-party payors	5	24
Self-pay	16	4
	100%	100%

Note 4. Community Commitment and Charity Care

Although reimbursement for services rendered is critical to the operation of the Corporation, it is the Corporation's health care mission to serve the community by treating patients in immediate need of medical services without regard for their ability to pay for such services. The Corporation maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy, as well as the estimated cost of services and supplies. The estimated difference between the services provided to Medicaid patients and the reimbursement from the state for this patient care is also monitored.

During the years ended June 30, 2005 and 2004, the following levels of charity care were provided:

	2005	2004
Charges forgone for charity based on established rates	$ 7,601,313	$ 8,034,409
Estimated excess of cost over reimbursement for Medicaid patients	6,753,787	4,642,495
	$ 14,355,100	$ 12,676,904

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Note 5. Investments and Assets Limited as to Use, Short-Term Investments, and Other Investments

The composition of investments and assets limited as to use, short-term investments, and other investments, which are recorded at fair value based on quoted market values, is as follows as of June 30:

	2005	2004
Cash and cash equivalents	$ 19,220,232	$ 8,126,820
Certificates of deposit	916,659	628,374
Marketable equity securities	76,425	
U.S. government money market funds	-	10,150,592
Accrued interest receivable	12,312	29,548
	$ 20,225,628	$ 18,935,334

Investment return for investments and assets whose use is limited, short-term investments, and other investments for the years ended June 30, 2005 and 2004, is as follows:

	2005	2004
Interest and dividend income	$ 506,825	$ 210,578
Realized gains on sales of investments, net	1,037,567	-
	$ 1,544,392	$ 210,578
Other changes in unrestricted net assets - change in unrealized appreciation in fair value of investments	$ -	$ 22,027

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

Note 6. Sale-Leaseback Transaction

On April 15, 2005, the Corporation sold land for $7,000,000 and concurrently entered into an agreement to lease the property back at $10 per year through April 2009. The Corporation has an option to repurchase the property within the lease term. Because the Corporation has an option to repurchase the property, the sale did not qualify for sale-leaseback accounting and, thus, was accounted for as a financing transaction under FASB Statement No. 98, *Sale-Leaseback Accounting*. Therefore, the net proceeds from the sale have been recorded as a financing obligation. Payments under the lease are treated as interest expense with an appropriate per annum inflation based on the consumer price index (3.2% during 2005) and a reduction (or increase, if applicable) of the financing obligation. A sale will be recognized when the Corporation's option to repurchase expires. The land involved in this transaction has a cost basis of approximately $2,983,000 and is included in land and land improvements on the balance sheet.

As required by the related agreement, the Corporation has $800,000 held in escrow related to the sale-leaseback of the land to be used for additional environmental costs, if necessary. This amount is included with investments and assets limited as to use – externally designated under lease agreement on the consolidated balance sheet at June 30, 2005.

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Note 7. Notes Payable and Long-Term Debt

During 2003, the Corporation issued an uncollateralized demand note payable to the Sisters of Mercy in the amount of $2,075,000 and a note payable to Resurrection Health Care (an unrelated party) in the amount of $1,000,000. These notes were issued to provide additional working capital to the Corporation. Both notes are non-interest bearing. The outstanding balance on the note to the Sisters of Mercy was $2,075,000 as of June 30, 2005 and 2004. The outstanding balance on the note to Resurrection Health Cere as of June 30, 2004 was $542,549. The note was paid during the year ended June 30, 2005.

Long-term debt is summarized as follows at June 30:

	2005	2004
Illinois Health Facilities Authority Revenue Refunding Bonds, Series 1992, paid during 2005	$ -	$ 41,195,000
Illinois Health Facilities Authority Revenue Refunding Bonds, Series 1996, paid during 2005	-	17,145,000
General Electric Capital Corporation, $2,150,000 note bearing interest at 5.5%, payable in monthly installments of $29,982, with final installment due January 1, 2007	909,544	1,211,577
JPMorgan Chase Bank:		
$12,000,000 promissory note, bearing interest at the prime rate (6.25% at June 30, 2005) minus 0.75%, interest payable quarterly, principal due April 15, 2008	12,000,000	-
$8,000,000 promissory note, bearing interest at the prime rate (6.25% at June 30, 2005) minus 0.75%, payable in quarterly installments of $100,000 plus interest, with a final payment due April 15, 2008	8,000,000	-
$5,000,000 promissory note, bearing interest at the prime rate (6.25% at June 30, 2005) minus 0.75%, interest payable quarterly, principal due April 15, 2006	5,000,000	-
Capital Source Finance, $20,000,000 revolving line of credit, bearing interest at an annual rate of LIBOR (3.39% at June 30, 2005) plus 3.5%, expires April 15, 2008	11,833,641	
One-time overadvance on Capital Source Finance, $20,000,000 revolving line of credit, bearing interest at an annual rate of LIBOR (3.39% at June 30, 2005) plus 4.5%, payable in monthly installments of $139,698 plus interest, with final installment due October 2006	2,514,568	-
Other	-	33,933
	40,257,753	59,551,577
Less unamortized discount	-	(364,836)
	40,257,753	59,186,741
Less:		
Current portion	(7,442,634)	(4,068,651)
	$ 32,815,119	$ 55,118,090

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Note 7. Notes Payable and Long-Term Debt (continued)

Principal maturities of long-term debt at June 30, 2005 are as follows:

Year ending June 30,	
2006	$ 7,442,634
2007	1,807,177
2008	31,007,942
	$ 40,257,753

On April 15, 2005, the Corporation issued notes payable to JPMorgan Chase Bank in the amounts of $12,000,000, $8,000,000 and $5,000,000 under separate loan agreements. The proceeds were used in connection with the refunding of the Series 1992 and 1996 Revenue Bonds. On April 15, 2005, the Corporation also entered into a Revolving Credit and Security agreement with Capital Source Finance, an asset-based lender. The proceeds of the revolving line were used to refund the Series 1992 and 1996 Revenue Bonds.

Certain proceeds from the issuance of the notes were used to pay the principal and interest outstanding on a portion of the Series 1996 Revenue Bonds on April 15, 2005. Certain proceeds from the issuance of the notes were also placed in an irrevocable escrow account and invested in government securities, which, with interest thereon, were sufficient to pay the principal and interest outstanding on the Series 1992 Revenue Bonds on May 16, 2005. Proceeds have also been placed in an irrevocable escrow account and invested in government securities, which, with interest thereon, will be sufficient to pay the principal and interest outstanding on the remainder of the Series 1996 Revenue Bonds on January 1, 2006. At June 30, 2005, $1,667,204 in principal and interest on advance refunded Series 1996 Revenue Bonds, which are considered extinguished and removed from the balance sheet, remain outstanding. As a result of this transaction the Corporation recognized a $978,534 nonoperating loss on advance refunding.

The terms of the new loan agreements require that the Corporation maintain a total of $15,812,500, plus accrued interest, in two secured accounts with a bank. At June 30, 2005, the Corporation held approximately $15,900,000 in these secured accounts. One of the secured accounts, in the amount of $3,812,500, is designated for liability claims. This amount is included with investments and assets limited as to use on the consolidated balance sheet at June 30, 2005. In addition, the $8,000,000 note is secured by a guarantee by the Sisters of Mercy. The $5,000,000 note is secured by a mortgage on the Corporation's property.

The Corporation's accounts receivable, and certain other assets, are pledged as collateral under the revolving line of credit. The amount outstanding under the revolving line of credit at June 30, 2005 is $14,348,209.

The loan agreements on the notes contain various covenants including those relating to limitations on incurring additional debt and disposing of property. In addition, the revolving credit and security agreement contains covenants including those relating to financial performance, insurance coverage and timely submission of specified financial reports. The Corporation was not in compliance with a certain financial covenant required by Capital Source Finance as of and for the year ended June 30, 2005. Effective January 25, 2006, Capital Source Finance waived this covenant violation through November 7, 2005 and amended this certain financial covenant effective November 8, 2005.

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Note 8. Lease Obligations

Rental expense for all operating leases totaled approximately $2,635,000 and $2,253,000 in 2005 and 2004, respectively. Future minimum lease payments under the noncancelable leases and related maintenance agreements are as follows:

Year ended June 30:		
2006	$	2,873,000
2007		2,562,000
2008		2,476,000
2009		1,253,000
2010		540,000
Thereafter		300,000
	$	10,004,000

Note 9. Retirement Plan

The Hospital sponsored a noncontributory, defined-benefit pension plan, which covered substantially all of the Hospital's full-time employees. Benefits were based on years of service and the employee's compensation during the last five years of employment. The Hospital's funding policy was to contribute such amounts as are necessary to provide for benefits attributed to service to date and those expected to be earned in the future. Effective June 30, 2003, the plan was amended to freeze all benefit accruals. As a result, a curtailment benefit was recorded by the Hospital.

Effective June 30, 2004, the plan was amended to allow the sponsor to terminate the plan and settle pension obligations with all plan participants. The plan amendment, which accelerates the distribution of benefits earned, resulted in a gain of $3,295,667. The Hospital will not receive any future benefit from the plan amendment; therefore, the gain was recognized during the year ended June 30, 2004, and is classified as a reduction to salaries and benefits expense in the accompanying consolidated statement of operations and changes in net assets (deficiency). Effective July 1, 2004, the plan was amended to cease commencing distributions, eliminate the annuity forms of distribution, revise the allocation formula upon plan termination, revise the provision related to payment in the event a participant or beneficiary is determined to be incompetent, and provide that the plan be terminated effective July 1, 2004. This amendment resulted in a gain of $6,467,781. The Hospital will record a pension settlement when the plan assets are distributed to participants.

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Note 9. Retirement Plan (continued)

The following table sets forth the plan's funded status and amounts recognized in the accompanying consolidated balance sheets at June 30:

	2005	2004
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 25,204,619	$ 29,851,052
Service cost	-	-
Interest cost	1,500,299	1,699,554
Plan amendments	(6,467,781)	(3,295,667)
Effect of curtailment	-	-
Actuarial losses	-	-
Benefits paid	(399,272)	(3,050,320)
Benefit obligation at end of year	$ 19,837,865	$ 25,204,619
Change in plan assets:		
Fair value of plan assets at beginning of year	$ 19,571,379	$ 21,889,002
Actual return on plan assets	665,758	732,697
Employer contributions	-	-
Benefit paid	(399,272)	(3,050,320)
Fair value of plan assets at end of year	$ 19,837,865	$ 19,571,379
Funded status of the plan	$ -	$ (5,633,240)
Unreconized prior service cost	(6,253,499)	-
Unrecognized net actuarial gain	6,253,499	5,503,714
Accrued benefit cost, before additional minimum liability	-	(129,526)
Adjustment for additional minimum liability	-	(5,503,714)
Accrued benefit cost, after additional minimum liability	$ -	$ (5,633,240)
Assumptions:		
Discount rate	6.00%	6.00%
Expected return on plan assets	5.50%	7.50%
Rate of compensation increase	N/A	N/A

Due to the impending distributions of plan assets, the plan's assets are 100% allocated to fixed income investments as of June 30, 2005 and 2004.

Effective July 1, 2004, the Corporation put in place a noncontributory, defined-contribution pension, which covers substantially all of the Corporation's full-time employees.

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Note 10. Professional and General Liability Insurance

The actuarially determined self-insurance liability in the accompanying consolidated balance sheets reflects management's assessment of claims applicable to all self-insured periods. Accrued malpractice losses have been discounted at 6.0% at June 30, 2005. An accrual for possible losses attributable to incidents that may have occurred, but that have not been identified under the incident reporting system is included in this liability. If accrued malpractice losses had not been discounted, the estimated liability would be approximately $5,221,000 and $4,198,000 higher than the amounts recorded in the consolidated balance sheets as of June 30, 2005 and 2004, respectively. The Corporation had investments available for claims settlements of $73,220 and $4,910,151 as of June 30, 2005 and 2004, respectively.

Note 11. Transactions with Related Parties

The following related party transactions have been entered into:

a. The Hospital and the Center entered into transactions with the Sisters of Mercy and other affiliated corporations under the control of the Sisters of Mercy and participated in trusts sponsored by the Sisters of Mercy to provide for professional liability claims. In addition, as of June 30, 2005 and 2004 the Corporation had a note payable to the Sisters of Mercy outstanding in the amount of $2,075,000.

b. The Hospital bills and collects monies for services rendered to the Diagnostic and Treatment (D&T) Center's patients. In addition, the Hospital charges the D&T Center certain indirect costs of providing administrative, financial, and clinical services. These charges totaled approximately $413,000 in both 2005 and 2004. At June 30, 2005, the Hospital had amounts due from the D&T Center totaling approximately $235,000 related to these services. The Hospital had no amounts due from the D&T Center at June 30, 2004.

c. The operations of the D&T Center are dependent on the continued financial and operating support of the Hospital. Under the terms of the Hospital's management agreement with the D&T Center, the Hospital has agreed to provide the necessary financial and operating support to the D&T Center for future periods.

Note 12. Functional Expenses

The Corporation provides general health care services to residents within Chicago and the surrounding area and supports medical education programs. The Corporation's expenses related to providing these services are as follows for the years ended June 30:

	2005	2004
Health care services	$ 94,746,182	$ 83,882,475
Medical education	7,816,498	7,911,944
Fund-raising	237,832	438,840
General and administrative	81,201,202	66,056,177
	$ 184,001,714	$ 158,289,436

Certain amounts have been allocated between functional categories.

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Note 13. Commitments, Contingencies and Subsequent Event

Medicare Reimbursement: For the years ended June 30, 2005 and 2004, the Corporation recognized approximately $153,003,000 and $158,063,000, respectively, of gross patient service revenues from services provided to Medicare beneficiaries. Changes in Medicare reimbursement as a result of the Centers for Medicare and Medicaid Services' implementation of the provisions of future Medicare legislation may have an adverse effect on the Corporation's net patient service revenue.

Medicaid Reimbursement: For the years ended June 30, 2005 and 2004, the Corporation recognized approximately $97,466,000 and $94,869,000, respectively, of gross patient service provided to Medicaid patients. Due to the Hospital's relatively high Medicaid patient volume, the Hospital receives additional reimbursement of approximately $13,430,000 in 2005 and 2004 in the form of critical hospital adjustment payments ("CHAP"), safety net access payments ("SNAP") and tertiary payments, the majority of which is provided by the Illinois Medicaid program. The Hospital also receives disproportionate share and Medicaid High Volume Adjustment amounts as a daily add on for Medicaid patients. The amount of additional reimbursement from the Illinois Medicaid program which will be made to hospitals in the future is uncertain, and future legislative changes to reimbursements provided to hospitals could have a material adverse effect on the Hospital's operating results.

Medicaid Hospital Assessment Program: The Corporation operations for the year ended June 30, 2005 benefited from Medicaid Hospital Assessment Program (Program) net payments of approximately $4,900,000. A proposal to continue this Program for three additional years is currently being considered by CMS.

Litigation: The Corporation is a defendant in various lawsuits arising in the ordinary course of business. Although the outcome of the lawsuits cannot be determined with certainty, management believes the ultimate disposition of such matters will not have a material effect on the Corporation's financial statements.

Regulatory Investigation: The U.S. Department of Justice, other federal agencies and the Illinois Department of Public Aid routinely conduct regulatory investigations and compliance audits of health care providers. The Corporation is subject to these regulatory efforts. Management is currently unaware of any regulatory matters which may have a material effect on the Corporation's financial position or results from operation.

Claim Settlement: Subsequent to year-end, the Hospital settled a lawsuit for the amount of $3,300,000. Of this amount, $1,300,000 is to be paid upon the settlement date. The remaining $2,000,000 is to be paid in three annual installments of $666,666.66 on August 1 of 2006, 2007 and 2008. The Hospital intends to fund the settlement with cash from operations. At June 30, 2005, the settlement amount was included in professional liability on the consolidated balance sheet.

Note 14. Fair Value of Financial Instruments

The following methods and assumptions were used by the Corporation to estimate the fair value of other financial instruments:

The carrying value of cash and cash equivalents, patient accounts receivables and other assets, accounts payable, accrued expenses and estimated settlements due to or from third-party payors are reasonable estimates of their value due to the short-term nature of these financial instruments.

The fair value of investments and assets limited as to use, which are the amounts reported on the balance sheet, is based on quoted market prices.

The fair value of long-term debt is estimated based on interest rates for the same or similar debt offered to the Corporation having the same or similar remaining maturities and collateral requirements. The fair value of the long-term debt approximates the carrying values.

McGladrey & Pullen
Certified Public Accountants

Independent Auditor's Report on Supplementary Information

To the Board of Directors
Mercy Health System of Chicago
Chicago, Illinois

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

McGladrey & Pullen, LLP

Chicago, Illinois
December 2, 2005, except for the last paragraph of Note 7,
as to which the date is January 25, 2006

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Mercy Health System of Chicago and Subsidiaries
Consolidating Balance Sheet
June 30, 2005

	Mercy Health System of Chicago	Mercy Hospital and Medical Center	Mercy Health Care Rehabilitation Center	Mercy Services Corporation	Mercy Foundation, Inc.	Eliminations	Consolidated Totals
Assets							
Current Assets							
Cash and cash equivalents	$ 30,140	$ 6,687,349	$ -	$ 1,000	$ 969,379	$ -	$ 7,687,868
Investments and assets limited as to use							
Internally designated under self-insurance program	-	73,220	-	-	-	-	73,220
Short-term investments	-	49,781	-	-	952,983	-	1,002,764
Patient accounts receivable, net of allowances for doubtful accounts of $16,318,000	-	24,094,299				-	24,094,299
Interest in net assets of Foundation	-	1,352,527	-	-	-	(1,352,527)	-
Due from related party	650,000	258,901	3,629,125	-	-	(4,303,453)	234,573
Inventories	-	1,854,338	-	-	-	-	1,854,338
Other assets	-	2,359,133	-	-	45,657	-	2,404,790
Total current assets	680,140	36,729,548	3,629,125	1,000	1,968,019	(5,655,980)	37,351,852
Investments and Assets Limited as to Use							
Pledged under debt agreement	-	12,087,649	-	-	-	-	12,087,649
Externally designated under lease agreement	-	800,000	-	-	-	-	800,000
Externally designated under self-insurance program	-	3,812,500	-	-	-	-	3,812,500
Other investments	-	1,552,713	-	-	896,782	-	2,449,495
	-	18,252,862	-	-	896,782	-	19,149,644
Property and Equipment							
Land and land improvements	-	9,316,753	-	-	-	-	9,316,753
Building and fixtures	-	105,162,988	-	-	-	-	105,162,988
Equipment	-	112,813,238	-	-	26,581	-	112,839,819
Construction in progress	-	788,744	-	-	-	-	788,744
	-	228,081,723	-	-	26,581	-	228,108,304
Less accumulated deprecation	-	(170,761,331)	-	-	(20,139)	-	(170,781,470)
	-	57,320,392	-	-	6,442	-	57,326,834
Other Assets							
Deferred financing costs, net	-	479,653	-	-	-	-	479,653
Other noncurrent assets	-	921,731	-	-	45,000	-	966,731
	-	1,401,384	-	-	45,000	-	1,446,384
Total assets	$ 680,140	$ 113,704,186	$ 3,629,125	$ 1,000	$ 2,916,243	$ (5,655,980)	$ 115,274,714

Liabilities and Net Assets (Deficiency)	Mercy Health System of Chicago	Mercy Hospital and Medical Center	Mercy Health Care Rehabilitation Center	Mercy Services Corporation	Mercy Foundation, Inc.	Eliminations	Consolidated Totals
Current Liabilities							
Accounts payable	$ -	$ 13,913,470	$ 128,258	$ -	$ 93,814	$ -	$ 14,135,542
Accrued expenses	-	9,204,310	-	-	-	-	9,204,310
Pension liability	-	-	-	-	-	-	-
Due to third-party payors	-	5,030,291	-	-	-	-	5,030,291
Current portion of long-term debt	-	7,442,634	-	-	-	-	7,442,634
Note payable	-	2,075,000	-	-	-	-	2,075,000
Due to related party	-	4,279,125	-	-	24,328	(4,303,453)	-
Current portion of professional liability	-	6,988,000	435,000	-	-	-	7,423,000
Total current liabilities	-	48,932,830	563,258	-	118,142	(4,303,453)	45,310,777
Long-Term Debt, less current portion	-	32,815,119	-	-	-	-	32,815,119
Professional Liability, less current portion	-	20,363,000	-	-	-	-	20,363,000
Financing Obligation Arising From Sale-Leaseback Transaction	-	7,046,641	-	-	-	-	7,046,641
Deferred Grant Revenue	-	2,135,801	-	-	-	-	2,135,801
Total liabilities	-	111,293,391	563,258	-	118,142	(4,303,453)	107,671,338
Net Assets (Deficiency)							
Unrestricted	680,140	580,393	3,065,867	1,000	1,445,574	38,000	5,810,974
Temporarily restricted	-	1,517,842	-	-	1,352,527	(1,390,527)	1,479,842
Permanently restricted	-	312,560	-	-	-	-	312,560
Total net assets (deficiency)	680,140	2,410,795	3,065,867	1,000	2,798,101	(1,352,527)	7,603,376
Total liabilities and net assets (deficiency)	$ 680,140	$ 113,704,186	$ 3,629,125	$ 1,000	$ 2,916,243	$ (5,655,980)	$ 115,274,714

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Mercy Health System of Chicago and Subsidiaries
Consolidating Statement of Operations
Year Ended June 30, 2005

	Mercy Health System of Chicago	Mercy Hospital and Medical Center	Mercy Health Care Rehabilitation Center	Mercy Foundation, Inc.	Eliminations	Consolidated Totals
Revenue:						
Net patient service revenue	$ -	$ 169,628,548	$ -	$ -	$ -	$ 169,628,548
Medicaid hospital assessment revenue	-	11,679,718	-	-	-	11,679,718
Capitation revenue	-	1,337,213	-	-	-	1,337,213
Contributions	-	213,590	-	371,442	(270,000)	315,032
Other	-	4,117,204	-	1,174	-	4,118,378
Net assets released from restriction - used for operations	-	138,893	-	506,644	-	645,537
	-	187,115,166	-	879,260	(270,000)	187,724,426
Expenses:						
Salaries and benefits	-	86,451,735	-	161,662	-	86,613,397
Supplies	-	25,527,134	-	3,753	-	25,530,887
Insurance	-	5,741,054	-	-	-	5,741,054
Depreciation and amortization	-	8,417,128	-	2,802	-	8,419,930
Provision for uncollectible accounts	-	13,811,990	-	-	-	13,811,990
Interest	-	3,725,496	-	-	-	3,725,496
Professional fees	-	5,375,728	-	-	-	5,375,728
Repairs, utilitites and rent	-	10,595,927	-	35,351	-	10,631,278
Purchased services	-	13,585,570	-	3,745	-	13,589,315
Medicaid hospital assessment expense	-	6,779,314	-	-	-	6,779,314
Other	-	3,553,917	675	498,733	(270,000)	3,783,325
	-	183,564,993	675	706,046	(270,000)	184,001,714
Income (loss) from operations	-	3,550,173	(675)	173,214	-	3,722,712
Nonoperating income (expense):						
Gain on sale of property and equipment	-	45,324	-	-	-	45,324
Investment income	197	1,475,154	2,977	66,064	-	1,544,392
Loss on advance refunding	-	(978,534)	-	-	-	(978,534)
Other	-	(30,000)	-	-	-	(30,000)
Excess of revenue over expenses	197	4,062,117	2,302	239,278	-	4,303,894
Unrestricted net assets:						
Change in minimum pension liability	-	5,503,714	-	-	-	5,503,714
Increase unrealized net assets	$ 197	$ 9,565,831	$ 2,302	$ 239,278	$ -	$ 9,807,608

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ATTACHMENT FINANCIALS