Annual Disclosure Report

For the Two Months Ended June 30, 2016

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Annual Disclosure Report for June 30, 2016

VANDERBILT UNIVERSITY MEDICAL CENTER

NOTICE
relating to:

THE HEALTH AND EDUCATIONAL FACILITIES BOARD OF THE METROPOLITAN GOVERNMENT OF NASHVILLE AND DAVIDSON COUNTY, TENNESSEE REVENUE BONDS (VANDERBILT UNIVERSITY MEDICAL CENTER) SERIES 2016A

THE HEALTH AND EDUCATIONAL FACILITIES BOARD OF THE METROPOLITAN GOVERNMENT OF NASHVILLE AND DAVIDSON COUNTY, TENNESSEE TAXABLE REVENUE BONDS (VANDERBILT UNIVERSITY MEDICAL CENTER) SERIES 2016B

THE HEALTH AND EDUCATIONAL FACILITIES BOARD OF THE METROPOLITAN GOVERNMENT OF NASHVILLE AND DAVIDSON COUNTY, TENNESSEE TAXABLE REVENUE BONDS (VANDERBILT UNIVERSITY MEDICAL CENTER) SERIES 2016C (R-FLOATS)

THE HEALTH AND EDUCATIONAL FACILITIES BOARD OF THE METROPOLITAN GOVERNMENT OF NASHVILLE AND DAVIDSON COUNTY, TENNESSEE TAXABLE REVENUE NOTE (VANDERBILT UNIVERSITY MEDICAL CENTER) SERIES 2016D

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CUSIP Nos: **592041WC7, 592041WD5, 592041WE3, 592041WF0, 592041WG8, 592041WH6, 592041WJ2, 592041RU3, 592041RV1, 592041SF5, 592041SG3, 592041XB8, 592041XC6**

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ATTENTION

This document is marked with a dated date of June 30, 2016 and reflects information only as of that dated date. Readers are cautioned not to assume that any information has been updated beyond the dated date except as to any portion of the document that expressly states that it constitutes an update concerning specific recent events occurring after the dated date of the document. Any information contained in the portion of the document indicated to concern recent events speaks only as of its date. We expressly disclaim any duty to provide an update of any information contained in this document.

The information contained in this document may include "forward looking statements" by using forward-looking words such as "may," "will," "should," "expects," "believes," "anticipates," "estimates," or others. You are cautioned that forward-looking statements are subject to a variety of uncertainties that could cause actual results to differ from the projected results. Those risks and uncertainties include general economic and business conditions, receipt of funding grants, and various other factors which are beyond our control.

Because we cannot predict all factors that may affect future decisions, actions, events, or financial circumstances, what actually happens may be different from what we include in forward-looking statements.

ORGANIZATION

Vanderbilt University Medical Center ("VUMC") is a Tennessee not-for-profit corporation incorporated in March of 2015 for the purpose of operating an academic medical center and a comprehensive research, teaching, and patient care health system in the state of Tennessee (the "Medical Center"). Until April 29, 2016, the Medical Center operated as a unit within Vanderbilt University ("the University" or "VU"), as a part of the University's administrative structure, with the same governing board, legal, financial and other shared services.

VUMC began operations effective April 30, 2016 following the closing of the sale of the Medical Center by the University on April 29, 2016 (the "Acquisition"). VUMC owns and operates the three hospitals primarily located on the main campus of the University in Nashville, TN.: Vanderbilt University Adult Hospital ("VUAH"), Monroe Carell Junior Children's Hospital at Vanderbilt ("MCJCH") and Vanderbilt Psychiatric Hospital ("VPH"). In addition, VUMC partially owns Vanderbilt Stallworth Rehabilitation Hospital ("VSRH"), also located on the main campus of the University, through a joint venture with HealthSouth Corp. in which VUMC holds a 50% interest. Vanderbilt Health Services, LLC, ("VHS") is currently a participant in the VSRH joint venture. VUAH, the Children's Hospital and VPH are licensed for 1,025 beds and VSRH is licensed for 80 beds.

VUMC consists of two major operating divisions and an administrative overhead division. The operating divisions include the Clinical Enterprise and Academic Enterprise divisions. The administrative overhead division is referred to as Medical Center Administration ("MCA").

The Clinical Enterprise division includes the professional clinical practice revenues and related expenses of the Vanderbilt Medical Group ("VMG"), and technical revenues and associated expenses for operation of VUMC's hospitals and clinic facilities, including VUAH, MCJCH and VPH. The Clinical Enterprise also includes VHS.

> VUAH is a quaternary care teaching hospital licensed for 670 acute care and specialty beds. VUAH, a Level I trauma center, provides advanced patient care, and serves as a key site for medical education and clinical research conducted by physician faculty. VUAH includes a comprehensive burn center, the Vanderbilt Transplant Center, the Vanderbilt Heart and Vascular Institute, and Vanderbilt Ingram Cancer Center.
>
> MCJCH is a pediatric quaternary care teaching hospital licensed for 171 acute and specialty beds, and 96 Neonatal Intensive Care beds. MCJCH is the region's only full-service pediatric hospital, with over 300 pediatric subspecialties. MCJCH serves as a site for medical education and clinical research conducted by pediatric physician faculty, houses the only Level IV neonatal intensive care center within the state of Tennessee, and is a regional referral center for extracorporeal membrane oxygenation (heart and lung failure).
>
> VPH is a psychiatric hospital licensed for 88 beds, and provides both inpatient and outpatient partial hospitalization psychiatric services to both adult and adolescent patients.
>
> VMG is the practice group of physicians and advanced practice nurses employed by VUMC who perform billable professional medical services. The VMG is not a separate legal entity. The VMG has a governing board which consists of the VUMC clinical service chiefs, who also serve clinical department chairs. Under the oversight of VUMC executive leadership, the VMG sets professional practice standards, bylaws, policies, and procedures for the administration of a group practice. VUMC bills for services rendered by the VMG clinicians

in both inpatient and outpatient locations. Collected fees derive a component of each VMG clinician's compensation.

The VMG includes nationally recognized physicians whose expertise spans the spectrum from primary care to the most specialized quaternary discipline. The entire clinical faculty is "board certified" or eligible for board certification. All staff members are re-credentialed every two years by the National Committee for Quality Assurance standards. All specialties and subspecialties currently recognized by the various national specialty boards are represented on the clinical faculty.

VHS serves as a holding company for 13 health care related subsidiaries and joint ventures owned with various entities, including, but not limited to, VSRH and the Vanderbilt Health Affiliated Network ("VHAN"). VHS operations primarily consist of community physician practices, imaging services, outpatient surgery centers, radiation oncology centers, a home health care agency, a home infusion and respiratory service, an affiliated health network, and a rehabilitation hospital. These subsidiaries include clinics managed in multiple outpatient locations throughout middle Tennessee.

The Academic Enterprise division includes all clinically-related research, research-support activities and faculty endeavors supporting post-graduate training programs. A significant funding source for VUMC's research has historically been the federal government. Federal funding is received from the Department of Health and Human Services', the National Institutes of Health, the Department of Defense, NASA, and other federal agencies. Sponsored research awards, including multiple-year grants and contracts from government sources, foundations, associations, and corporations signify future research commitments. In addition, core activities supporting research including advanced computing and grant administration are included in this division.

As mentioned above and throughout this document, VUMC acquired the Medical Center and it operations from the University in the Acquisition. For the purpose of funding the Acquisition, VUMC entered into certain debt agreements. Certain of these debt agreements contain certain required disclosures which outline annual and quarterly reporting requirements. In addition, certain of these debt agreements require notices of the occurrence of significant events which include but are not limited to delinquencies, bond calls, rating changes, bankruptcies and mergers or acquisitions.

The VUMC fiscal year end is June 30. Given that April 29, 2016 was the effective date of the Acquisition of the Medical Center from the University, the first year of operations includes only two months of activity.

SUMMARY OF OPERATING AND UTILIZATION DATA

Licensed Beds

VUMC's facilities have 1,025 licensed and fully staffed beds approved for operation with 65 operating rooms, primarily located at VUAH, MCJCH and VPH. A fourth hospital, VSRH, is operated within a separate joint venture entity, which is currently owned 50% by VUMC. Counting VSRH beds, managed beds at Williamson County (Tennessee) Medical Center Inpatient Children's Unit and operated observation beds and bassinet beds, total beds as of June 30, 2016 equates to 1,202.

VUMC Beds (Licensed, Observation, JV, Manage)

Licensed Beds	Available Beds
Licensed-Bed Category Type	
Adult Medical Surgical	606
Adult Obstetric	50
Adult Clinical Research Center	14
Pediatric Medical/Surgical	129
Pediatric Neonatal Intensive Care	96
Pediatric Intensive Care	42
Psychiatric Care	88
Total Licensed Beds as of June 30, 2016	1,025
Observation, JV and Managed Beds and Bassinets	
Current Observation Beds	61
Current Bassinets	20
Stallworth Rehabilitation Hospital Beds (JV) (1)	80
MCJCH at Williamson Medical Center Inpatient and Observation Unit (Managed) (2)	16
Total Observation, JV and Managed Beds and Bassinets as of June 30, 2016	177
Total Licensed, Observation, JV and Managed Beds and Bassinets as of June 30, 2016	1,202

(1) Represents 80 beds in joint venture with VSRH.
(2) Represents 12 licensed beds and four observation beds managed by VUMC with Williamson County Medical Center, Franklin, TN.

VUMC Research Revenue

VUMC receives revenues from research grants which are both federally and non-federally sponsored. The Department of Health and Human Services, the National Institutes of Health, the Department of Defense, NASA, and other federal agencies supported over 70% of the research expenditures conducted by VUMC. The breakdown of direct research revenues for the two months ended June 30, 2016 is as follows *($ in thousands)*:

Source		
Federal	$	37,059
Non-Federal		13,022
Total	$	50,081

Capital Cash Flows

Capital expenditures included primarily construction in progress and internal use software costs from inception through June 30, 2016:

($ in millions)	
Capital Expenditures	$22.6

Utilization

VUMC's overall functional occupancy rate was 93.8% during the two months ended June 30, 2016 (including observation patients in inpatient beds). The average number of inpatients in the hospital at midnight census was 872 at June 30, 2016. Thus, VUMC has continued to operate at or above the theoretical optimal occupancy of 85% when total utilization of capacity is measured. These inpatient utilization rates yielded discharges of 10,035.

Utilization Statistics Of The Hospitals And Clinics
For The Two Months Ended 6-30-16

Licensed beds (1)	1,025
Hospital inpatient days (2)	53,161
Hospital discharges	10,035
Average length of stay in days (2)	5.3
Average occupancy level (licensed beds) (2)	85.0%
Surgical operations (3)	9,854
Ambulatory visits (4)	362,890
Emergency visits	19,134

(1) Excludes nursery bassinets.
(2) Includes nursery and psychiatric hospital; does not include the observation patients.
(3) Excludes surgical operations performed by VUMC-employed physicians at separate surgery centers that are partially owned by a VUMC subsidiary.
(4) Includes visits related to VHS joint ventures.

VUMC Inpatient Acuity

Across all inpatients, VUMC's inpatient acuity is measured by case mix index ("*CMI*"). VUMC's total CMI and CMI for Medicare patients for the two months ended June 30, 2016 are presented below.

Case Mix Index for the Two Month Period Ended June 30, 2016	
Total CMI	2.20
Medicare CMI	2.33

During the two months ended June 30, 2016, ambulatory visits at the Medical Center totaled 328,683, which excludes visits related to VHS joint ventures. While the majority of the VMG adult and children's ambulatory practice is located in VUAH on the main campus, VUMC health care services are offered outside the main campus, with approximately 47% of outpatient visits at off-campus locations during this same time period.

VUMC Payor Mix

The Medical Center has historically received payment on behalf of most of its patients from a number of third parties, including Blue Cross and other private insurers, the federal government through Medicare, and the federal and state governments through Medicaid. TennCare, the State's managed care plan operating under Section 1115 Medicaid demonstration waiver from the federal government, provides the majority of Medicaid revenues. The remaining Medicaid revenues are from Medicaid patients who live outside of the State. Blue Cross, one of the Medical Center's largest payors represented 23% of total gross patient service revenue for the two months ended June 30, 2016.

The revenues attributable to Blue Cross are in the commercial/managed care category in the following table, which sets forth the sources of gross amounts of patient service revenue as well as gross amounts of patient service revenue net of contractual allowances for the two months ended June 30, 2016.

Payor Mix	**Gross**	**Net**
Commercial/Managed Care (1)	45.7%	60.6%
Medicare/Managed Medicare	30.0%	22.9%
Tenncare/Medicaid	20.0%	12.9%
Uninsured (self-pay)	4.3%	3.6%
Total	100.0%	100.0%

(1) Commercial includes commercial indemnity and other patient service programs provided under contractual arrangement

VUMC's major commercial managed care contracts are multi-year agreements, typically three to four years with automatic annual escalators. Commercial contracts reimburse the facility on case rates with stop loss provisions for inpatient medical/surgical services and fee schedules for outpatient services. VPH is reimbursed on per diems. VUMC has no agreements based on full risk or capitation reimbursement. Three major commercial contracts utilize performance on quality metrics as a basis for a portion of the annual escalators. One existing Medical Center commercial contract has two episode-based payment bundles effective July 1, 2015, with upside risk only. Over 78% of VUMC's payments for healthcare services are covered under rates contracted through fiscal year ended June 30, 2018.

The following table details payments received from VUMC's largest commercial contracts as a percentage of total net patient revenue for the two months ended June 30, 2016, as well as the respective contract renewal date.

Commercial Contract Payments as a Percentage of Total Net Patient Revenue

Commercial Contract	Total Payments (1)	Termination Dates
Aetna	6.2%	12/31/2018
BlueCross	27.9%	12/31/2019
CIGNA	6.4%	9/30/2018 (2)
Humana	0.7%	11/1/2018
United	5.4%	12/31/2016
Total as a % of total net patient revenue	46.6%	

(1) Includes global and professional billing payments.
(2) If not renegotiated, contract automatically renews indefinitely.
Note: Does not include behavioral or dental service contracts.

Medicare Advantage contracts represent approximately $21 million in net revenue or 6.1% of total net revenue for the two months ended June 30, 2016 and have termination dates ranging from December 31, 2016 to March 31, 2017.

SUMMARY OF FINANCIAL DATA

Cash and Investments

The VUMC Board of Directors (the "Board") approves the primary investment policy, while the Board's Executive Committee is responsible for appointing and removing investment managers, monitoring asset allocation within the policy guidelines, and other ongoing oversight of the investment portfolio. VUMC utilizes external investment consultants to provide professional investment analysis and guidance and to assist in evaluating the performance of the fund managers. As the risk profile of VUMC matures, VUMC management anticipates undertaking modest additional risk, through asset allocation adjustments, in order to improve long-term investment returns. The table below summarizes VUMC's investment allocation as of June 30, 2016 including working capital.

Summary of Cash and Investments Asset Allocation
(as of Fiscal Year Ended June 30, 2016)

	Working Capital	Unrestricted and Restricted Investments	Self-Insurance Trust	Total
Cash & Cash Equivalents	100%	1%	0%	76%
Short-Term Investments	0%	0%	0%	0%
Equity Investments	0%	41%	55%	11%
Hedged Equity Investments	0%	8%	7%	2%
Fixed Income Investments	0%	13%	26%	4%
Hedged Debt Investments	0%	0%	4%	0%
Other Marketable Alternatives (1)	0%	9%	8%	2%
Non-Marketable Investments	0%	0%	0%	0%
Restricted Cash & Cash Equivalents	0%	14%	0%	2%
Bonds in Workers Comp Account	0%	8%	0%	1%
Split Interest Trusts	0%	6%	0%	1%
Total	100%	100%	100%	100%

(1) Includes REITs and commodities.

The following table sets forth VUMC's unrestricted cash and investments and days cash on hand as of June 30, 2016. This financial information is provided for informational purposes only and is not necessarily, and should not be assumed to be, an indication of the results that will be achieved in the future.

Summary of Unrestricted Cash and Investments

($ in thousands)	
Cash and cash equivalents[(1)]	$ 603,084
Less: restricted cash and cash equivalents included above	(10,048)
Total unrestricted cash and cash equivalents	593,036
Unrestricted investments[(2)]	80,235
Total unrestricted cash and investments	$ 673,271
Average daily operating expenses[(3)]	$ 9,468
Days cash on hand[(4)]	71.1

(1) Cash and cash equivalents as reported on audited balance sheet.

(2) Unrestricted investments are comprised of board designated quasi-endowment funds.

(3) Average daily operating expenses include all VUMC financial flows to the University excluding principal payments on the Subordinated Promissory Note payable to VU.

(4) Unrestricted cash and investments divided by average daily operating expenses (excluding depreciation and amortization) for the two months then ended.

Debt Service Coverage

The following table sets forth, for the two months ended June 30, 2016, VUMC's income available for debt service, and indicates the extent to which such income available for debt service would provide coverage for maximum annual and annual debt service on all long-term debt.

(in thousands)	Actual	Annualized
Excess of revenues over expenses	$ 26,999	$ 161,994
Less: Unrealized gains on investments	(2,222)	(13,332)
Plus: Unrealized loss on interest rate swap	9,568	57,408
Plus: Depreciation and amortization	14,280	85,680
Plus: Interest	9,343	56,058
Income available to pay debt service	$ 57,968	$ 347,808
Maximum annual debt service		$ 74,942
Maximum annual debt service coverage(1)		4.6x
Annual debt service (Scheduled)		$ 52,124
Annual debt service Coverage (Scheduled)(2)		6.7x

(1) Maximum annual debt service coverage consists of estimated annualized income available to pay debt service divided by maximum annual debt service.
(2) Annual debt service coverage consists of estimated annualized income available to pay debt service divided by annual debt service.

Capitalization

The following table provides VUMC's capitalization ratios as of and for the two months ended June 30, 2016 on an annualized basis:

Capitalization Ratios

		($ in thousands)
Long Term Debt [1]	$	1,191,897
Unrestricted Net Assets		509,421
Total Capitalization	$	1,701,318
Ratio of Long-Term Debt to Capitalization (%)		70.1%
EBIDA (annualized)	$	303,732
Ratio Debt to Total EBIDA [2]		3.9x
Total Unrestricted Cash and Investments	$	673,271
Ratio Unrestricted Cash and Investments to Debt (%) [3]		56.5%

(1) Total outstanding long term debt, including current maturities, excluding the Subordinate Promissory Note from VU.
(2) Total outstanding long term debt divided by total EBIDA, which includes realized gains from sale of assets incurred in the normal course of operations, investment income (realized and unrealized), unrealized gains and losses from interest rate swap, unrestricted gifts or restricted gifts released from restrictions (spent on the purpose), and equity earnings in unconsolidated organizations.
(3) Unrestricted cash and investments divided by Long-Term Debt, which includes unrestricted cash and cash equivalents and unrestricted investments.

Interest Rate Exchange Agreements

VUMC uses an interest rate exchange agreement as part of its debt portfolio management strategy. These agreements do not include collateral pledging requirements. Mandatory termination provisions on each agreement are shown below with information regarding the current interest rate exchange agreement is as follows: *($ in thousands)*

Description	Notional Amount	Rate Paid	Rate Received	Maturity	Fair Value
Fixed-payer interest rate agreement[1]	$ 750,000	4.1190%	68% LIBOR	5/1/2040	$ 44,732
Fixed-payer interest rate agreement[2]	$ 750,000	4.1790%	68% LIBOR	5/1/2040	44,804
					$ 89,536

(1) Includes a mandatory termination provision on April 29, 2021
(2) Includes a mandatory termination provision on April 29, 2023

Existing Lease Agreements

VUMC leases certain property and equipment under agreements having lease terms ranging from two to twenty years. VUMC classifies these leases as operating leases. Information regarding these leases and future minimum rentals on non-cancelable operating leases as of June 30, 2016 is included in the audited balance sheet section of this report.

CONSOLIDATED STATEMENT OF OPERATIONS
FROM INCEPTION THROUGH THE TWO MONTHS ENDED JUNE 30, 2016 (UNAUDITED)

The consolidated statement of revenues and expenses from inception through the two months ended June 30, 2016 is as follows:

	(in thousands)
Operating Revenue	
Net patient service revenue, net of provision for bad debts	$ 534,934
Academic and research revenue	61,567
Other operating revenue	27,921
Total operating revenue	624,422
Operating Expenses	
Salaries, wages and benefits	312,929
Supplies and drugs	116,214
Facilities and equipment	45,365
Purchased services and other expense	93,703
Depreciation and amortization expense	14,280
Interest	9,343
Total operating expenses	591,834
Income from operations	32,588
Nonoperating Revenue & Expenses	
Income from investments	1,997
Gift income	1,215
Earnings of unconsolidated organizations	767
Unrealized loss from interest rate swap	(9,568)
Total nonoperating revenue & expenses	(5,589)
Excess of revenues over expenses	$ 26,999

MANAGEMENT DISCUSSION AND ANALYSIS

Income from operations and excess of revenues over expenses were $32.6 million and $27.0 million, respectively, for the two months ended June 30, 2016. Additionally, earnings before interest, depreciation and amortization ("EBIDA"), as defined above, totaled $50.6 million for the same period.

Revenues

Operating revenues totaled approximately $624.4 million for the two months ended June 30, 2016. Net patient service revenue, net of bad debts totaled $534.9 million representing 85.7% of operating revenue. VUMC inpatient discharges exceeded 10,000 for the two month period ended June 30, 2016. Over the same period, surgical cases (inpatient and outpatient) were 3,831 and 6,023, respectively. VUMC's inpatient acuity, measured by case mix index ("*CMI*") for Medicare patients and in total was 2.33 and 2.20, respectively, in the two months ended June 30, 2016. During the two months ended June 30, 2016, ambulatory visits at the VUMC totaled 362,890, including visits from VHS joint ventures.

Expenses

Operating expense totaled approximately $591.8 million for the two months ended June 30, 2016 representing 94.8% of total revenue. Salaries, wages and benefits totaled approximately $312.9 million and representing 50.1% of total operating revenue. Supplies and drugs totaled approximately $116.2 million representing 18.6% of total operating revenue. Purchased services totaled approximately $93.7 million representing 15.0% of total operating revenue. The remaining $69.0 million in operating expenses represented facilities and equipment, depreciation and amortization, and interest.

Non-Operating

The Non-Operating loss for the period was primarily driven by a $9.6 million loss related to the interest rate swap mark to market adjustment. This loss was partially offset by investment income (including unrealized), gift income and the results of VUMC's unconsolidated equity method investments.

Balance Sheet / Cash Flow

Cash and cash equivalents totaled approximately $603 million at June 30, 2016. The primary drivers of the increase in cash was the issuance of approximately $1.1 million of debt net of the cost to acquire the assets of the Medical Center of approximately $601 million (a total increase to cash of $529 million), excess revenues over expenses before depreciation and amortization for the two months ended June 30, 2016 of $41.3 million (excess revenue over expense of $27 million plus depreciation and amortization of $14.3 million) and an increase in cash of $105 million related to an increase in accrued compensation. These increases were partially offset by capital expenditures of $22.3 million and investment purchases of $76 million.

CONSOLIDATED STATEMENT OF CHANGES IN NET ASSETS
FROM INCEPTION THROUGH THE TWO MONTHS ENDED JUNE 30, 2016 (UNAUDITED)

The consolidated statement of changes in net assets from inception through the two months ended June 30, 2016 is as follows:

Changes in Unrestricted Net Assets		*(in thousands)*
Excess of Revenue over Expenses	$	26,999
Inherent Contribution		476,895
Total Changes in Unrestricted Net Assets		503,894
Changes in Temporarily Restricted Net Assets		
Inherent Contribution		25,360
Contributions		3,392
Net Assets Released From Restrictions		(1,768)
Total Changes in Temporarily Restricted Net Assets		26,985
Changes in Permanently Restricted Net Assets		
Inherent Contribution		6,761
Appreciation of Permanently Restricted Assets		8
Total Changes in Permanently Restricted Net Assets		6,769
Total Changes in Net Assets	$	537,648

CONSOLIDATED STATEMENT OF CASH FLOWS
FROM INCEPTION THROUGH THE TWO MONTHS ENDED JUNE 30, 2016 (UNAUDITED)

The consolidated statement of cash flows from inception through the two months ended June 30, 2016 is as follows:

Cash flows from operating activites:	*(in thousands)*
Total change in net assets	$ 537,648
Adjustments to reconcile increase in net assets to net cash provided by operating activites:	
Inherent contribution	(509,016)
Provision for bad debts	20,218
Unrealized loss from interest rate swap	9,568
Depreciation and Amortization	14,280
Gain on equity method investee	(767)
Net unrealized gain on investments	(2,230)
Increase (decrease) in cash due to changes in :	
Patient accounts receivable	(7,848)
Other receivables	(54,374)
Inventory	1,760
Prepaid expenses and other assets	(28,177)
Accounts payable and accrued expense	27,701
Bank overdrafts	13,846
Est net receivables and payables - third party	(8,598)
Accrued compensation and benefits	105,670
Other liabilities	7,387
Net cash provided by operating activities:	127,068
Cash flows from investing activities:	
Acquisition of Medical Center, net of cash received	(600,971)
Purchase of property, plant and equipment	(22,551)
Purchase of investments	(76,018)
Net cash used in investing activities	(699,540)
Cash flows from financing activities:	
Principal payments on long-term debt	(833)
Proceeds from the issuance of long-term debt	1,176,389
Net cash provided by financing activities	1,175,556
Net change in cash and cash equivalents	603,084
Cash and cash equivalents at inception	-
Cash and cash equivalents at June 30, 2016	$ 603,084

Vanderbilt University Medical Center
Consolidated Balance Sheet
June 30, 2016

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Independent Auditor's Report

To the Board of Directors of
Vanderbilt University Medical Center

We have audited the accompanying consolidated balance sheet of Vanderbilt University Medical Center (the "Company") as of June 30, 2016.

Management's Responsibility for the Balance Sheet

Management is responsible for the preparation and fair presentation of the consolidated balance sheet in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of a consolidated balance sheet that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the consolidated balance sheet based on our audit. 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 consolidated balance sheet is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated balance sheet. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated balance sheet, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the consolidated balance sheet in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated balance sheet. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the accompanying consolidated balance sheet presents fairly, in all material respects, the financial position of Vanderbilt University Medical Center at June 30, 2016 in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

Nashville, Tennessee
November 4, 2016

PricewaterhouseCoopers LLP, 150 3rd Avenue South, Suite 1400, Nashville, TN 37201
T: (615) 503 2860, F: (615) 503 2870, www.pwc.com/us

Vanderbilt University Medical Center
Consolidated Balance Sheet
June 30, 2016

(in thousands)

Assets		
Current		
Cash and cash equivalents	$	603,084
Patient accounts receivable, net of allowance for bad debts of approximately $20,218		343,241
Estimated receivables under third-party programs		9,123
Current pledge receivable, net		6,070
Grants and contracts receivable, net		60,943
Inventories		61,925
Prepaid expenses		8,553
Other current assets		72,397
Total current assets		1,165,336
Noncurrent investments limited as to use		190,366
Noncurrent pledge receivable, net		7,663
Equity in unconsolidated organizations		19,028
Property, plant, and equipment, net		1,130,116
Other noncurrent assets		6,475
Total assets	$	2,518,984
Liabilities and Net Assets		
Current		
Current installments of long-term debt	$	5,000
Accounts payable and other accrued expenses		215,302
Bank overdrafts		13,846
Estimated payables under third-party programs		30,990
Accrued compensation and benefits		200,110
Current portion of deferred revenue		38,345
Current portion of self-insurance reserves and claims		20,657
Total current liabilities		524,250
Noncurrent portion of deferred revenue		6,268
Noncurrent portion of self-insurance reserves and claims		67,319
Fair value of interest rate exchange agreements		89,536
Long-term debt, net of current installments		1,286,063
Other noncurrent liabilities		2,373
Total liabilities		1,975,809
Net assets		
Unrestricted net assets controlled by Vanderbilt University Medical Center		503,894
Unrestricted net assets related to noncontrolling interests		5,527
Total unrestricted net assets		509,421
Temporarily restricted net assets		26,985
Permanently restricted net assets		6,769
Total net assets		543,175
Total liabilities and net assets	$	2,518,984

The accompanying notes are an integral part of this consolidated balance sheet.

1. Description of Organization

Vanderbilt University Medical Center ("VUMC") is a Tennessee not-for-profit corporation incorporated in March of 2015 for the purpose of operating an academic medical center and a comprehensive research, teaching, and patient care health system in the state of Tennessee (the "Medical Center"). Previously, the Medical Center operated as a unit within Vanderbilt University ("the University" or "VU"), as a part of the University's administrative structure, with the same governing board, legal, financial and other shared services.

VUMC began operations following the closing of the sale of the Medical Center by the University on April 29, 2016. VUMC owns and operates the three hospitals primarily located on the main campus of the University in Nashville, TN.: Vanderbilt University Adult Hospital ("VUAH"), Monroe Carell Junior Children's Hospital at Vanderbilt ("MCJCH") and Vanderbilt Psychiatric Hospital ("VPH"). In addition, VUMC partially owns Vanderbilt Stallworth Rehabilitation Hospital ("*VSRH*"), also located on the main campus of the University, a joint venture with HealthSouth Corp. in which VUMC holds a 50% interest. Vanderbilt Health Services, LLC, (VHS) is currently a participant in the VSRH joint venture. VUAH, the Children's Hospital and VPH are licensed for 1,025 beds and VSRH is licensed for 80 beds.

VUMC consists of two major operating divisions and an administrative overhead division. The operating divisions include the Clinical Enterprise and Academic Enterprise divisions. The administrative overhead division is referred to as Medical Center Administration ("MCA").

The Clinical Enterprise division includes the professional clinical practice revenues and related expenses (the Vanderbilt Medical Group or "VMG"), and technical revenues and associated expenses for operation of VUMC's hospitals and clinic facilities, including VUAH, MCJCH and VPH. The Clinical Enterprise also includes VHS.

VUAH is a quaternary care teaching hospital licensed for 670 acute care and specialty beds. VUAH, a Level I trauma center, provides advanced patient care, and serves as a key site for medical education and clinical research conducted by physician faculty. VUAH includes a comprehensive burn center, the Vanderbilt Transplant Center, the Vanderbilt Heart and Vascular Institute, and Vanderbilt Ingram Cancer Center.

MCJCH is a pediatric quaternary care teaching hospital licensed for 171 acute and specialty beds, and 96 Neonatal Intensive Care beds. MCJCH is the region's only full-service pediatric hospital, with over 300 pediatric subspecialties. MCJCH serves as a site for medical education and clinical research conducted by pediatric physician faculty, houses the only Level IV neonatal intensive care center within the state of Tennessee, and is a regional referral center for extracorporeal membrane oxygenation (heart and lung failure).

VPH is a psychiatric hospital licensed for 88 beds, and provides both inpatient and outpatient partial hospitalization psychiatric services to both adult and adolescent patients.

VMG is the practice group of physicians and advanced practice nurses employed by VUMC who perform billable professional medical services. The VMG is not a separate legal entity. The VMG has a governing board which consists of the VUMC clinical service chiefs, who also serve clinical department chairs. Under the oversight of VUMC executive leadership, the VMG sets professional practice standards, bylaws, policies, and procedures for the administration of a group practice. VUMC bills for services rendered by the VMG clinicians in both inpatient and outpatient locations. Collected fees derive a component of each VMG clinician's compensation.

The VMG includes nationally recognized physicians whose expertise spans the spectrum from primary care to the most specialized quaternary discipline. The entire clinical faculty is “board certified” or eligible for board certification. All staff members are re-credentialed every two years by the National Committee for Quality Assurance standards. All specialties and subspecialties currently recognized by the various national specialty boards are represented on the clinical faculty.

VHS serves as a holding company for 13 health care related subsidiaries and joint ventures owned with various entities, including, but not limited to, VSRH and the Vanderbilt Health Affiliated Network (VHAN). VHS operations primarily consist of community physician practices, imaging services, outpatient surgery centers, radiation oncology centers, a home health care agency, a home infusion and respiratory service, an affiliated health network, and a rehabilitation hospital. These subsidiaries include clinics managed in multiple outpatient locations throughout middle Tennessee.

The Academic Enterprise division includes all clinically-related research, research-support activities and faculty endeavors supporting post-graduate training programs. A significant funding source for VUMC’s research has historically been the federal government. Federal funding is received from the Department of Health and Human Services’, the National Institutes of Health, the Department of Defense, NASA, and other federal agencies. Sponsored research awards, including multiple-year grants and contracts from government sources, foundations, associations, and corporations signify future research commitments. In addition, core activities supporting research including advanced computing and grant administration are included in this division.

The terms “Company”, “VUMC”, “we”, “our” or “us” as used herein and unless otherwise stated or indicated by context, refer to Vanderbilt University Medical Center and its affiliates. The term “facilities” or “hospitals” refer to entities owned and operated by VUMC and its affiliates and the term “employees” refers to employees of VUMC and its affiliates.

2. Summary of Significant Accounting Policies

Basis of Presentation

The consolidated balance sheet of VUMC has been prepared on the accrual basis in accordance with U.S. generally accepted accounting principles (GAAP). Based on the existence or absence of donor-imposed restrictions, VUMC classifies resources into three categories: unrestricted, temporarily restricted, and permanently restricted net assets.

Unrestricted net assets are free of donor-imposed restrictions. This classification includes all revenues, gains and losses not temporarily or permanently restricted by donors. VUMC reports all expenditures in the unrestricted class of net assets, since the use of restricted contributions in accordance with donors’ stipulations results in the release of the restriction.

Temporarily restricted net assets contain donor-imposed stipulations that expire with the passage of time or that can be satisfied by action of VUMC. These net assets may include unconditional pledges, split-interest agreements, interests in trusts held by others, and accumulated appreciation on donor-restricted endowments not yet appropriated by the Board of Directors for distribution.

Permanently restricted net assets are amounts held in perpetuity as requested by donors. These net assets may include unconditional pledges, donor-restricted endowments (at historical value), split-interest agreements, and interests in trusts held by others. Generally, the donors of these assets permit VUMC to use a portion of the income earned on related investments for specific purposes.

Use of Estimates
The preparation of a consolidated balance sheet in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated balance sheet. Actual results ultimately could differ from those estimates.

Principles of Consolidation
The consolidated balance sheet includes the accounts of all entities in which VUMC has a significant financial interest and over which VUMC has control. All significant intercompany accounts between the various entities have been eliminated. Noncontrolling interest in less-than-wholly owned consolidated subsidiaries of VUMC are presented as a component of net assets to distinguish between the interests of VUMC and the interests of the noncontrolling owners.

Cash and Cash Equivalents
Cash and cash equivalents are liquid assets with minimal interest rate risk and maturities of three months or less when purchased. VUMC invests operating assets in a diversified manner. At times, VUMC may have cash and cash equivalents at a financial institution in excess of federally insured limits. VUMC maintains certain cash balances within the noncurrent investments limited as to use caption in the consolidated balance sheet which are not included in the cash and cash equivalents section.

Patient Accounts Receivable, Net
Generally, VUMC provides services to patients in advance of receiving payment and does not require collateral or other security for those services. However, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits payable under patients' health insurance programs, plans or policies (e.g., Medicare, Medicaid, TennCare, Blue Cross, and other commercial third party payors).

Federal healthcare programs such as Medicare, Medicaid, and TennCare (State of Tennessee managed care program for Medicaid-eligible patients) primarily reimburse VUMC for inpatient services based on a set rate per discharge adjusted for acuity of the patient based on the Medicare severity diagnostic related group system (MS-DRG). VUMC receives payment from federal healthcare programs on an outpatient per procedure basis as determined by the ambulatory payment classification system (APC). Benefits assigned to VUMC under patients' insurance policies are paid in accordance with VUMC's contract with the applicable third party payor and related insurance program which includes prospectively determined rates per discharge based on the MS-DRG, discounts from established charges, per diem rates and prospectively determined procedure rates as established in a payor fee schedule. Contractual adjustments are the difference between established charges and the amounts paid by the Federal healthcare program or third party payor.

Patient accounts receivable are reduced by an allowance for bad debts. In evaluating the collectability of accounts receivable, VUMC analyzes its past history and identifies trends for each of its major categories of revenue (technical, professional, and retail pharmacy) to estimate the appropriate allowance for bad debts and related provision. Management regularly reviews data about these major categories of revenue in evaluating the sufficiency of the allowance for bad debts. The allowance is based upon management's judgmental assessment of historical and expected net collections considering business and general economic conditions in its service area, trends in healthcare coverage, and other collection indicators. Throughout the year, management assesses the adequacy of the allowance for uncollectible accounts based upon its review of accounts receivable payor composition and aging, taking into consideration recent write-off experience by payor category, payor agreement rate changes, and other factors. The results of these assessments are used to make modifications to the provision for bad debts and to establish an appropriate allowance for uncollectible accounts receivables. For third-party payors, the provision is determined by analyzing contractually due amounts from payors who are known to be having financial difficulties. For self-pay patients, the provision is based on an analysis of past experience related to patients unable to pay amounts owed. The difference between the standard rate charged (less the negotiated discounted rate) and the amount actually collected (after the reasonable collection efforts have been exhausted) are charged against the allowance for doubtful accounts. VUMC follows established guidelines, CMS regulations, and IRS Reg. §1.501(r)-6 for placing certain past-due patient balances with external collection agencies.

VUMC provides care to patients who meet the criteria under its financial assistance policy for no payment, or at payment amounts less than its established charge rates. VUMC does not report the charges that qualify as charity care as net revenue or net receivables because VUMC does not pursue collection of these amounts.

Estimated Receivables/Estimated Payables Under Third Party Programs
Certain services provided under federal healthcare programs or under VUMC's contracts with third party payors involve calculations of settlements for services in addition to patient payments. Federal health care programs provide cost-based reimbursement for services such as organ transplant acquisition and medical education for which final settlement is determined based on the programs' audits of annual cost reports submitted by VUMC. VUMC reports any differences between estimated year-end settlements and actual final settlements in the year final settlements are known. VUMC recorded all final Medicare settlements determined through June 30, 2010. VUMC expects final settlements relative to periods through June 30, 2012 to be completed during fiscal year 2017 and records provisions in the consolidated balance sheets for the effects of estimated final settlements on open years.

Certain contracts require pay for performance or episode of care settlements whereby VUMC receives additional payment or pays a penalty based on ability to achieve certain clinical measures or manage the cost of care for patients within various thresholds. VUMC estimates and accrues these adjustments in the period the related services are rendered, and adjusts these estimates in future periods as settlements are finalized. The aggregate liability associated with pay for performance and episode of care settlements at June 30, 2016 is less than $1.0 million with ultimate resolution of such financial arrangements not expected to have a material impact on the operating results of VUMC.

VUMC receives periodic interim payments (PIP Payments) bi-weekly from Medicare in lieu of individual payments for patient claims processed by VUMC's fiscal intermediary. PIP Payments received are offset against claims processed on a monthly basis with final settlement of amounts owed for a fiscal year included in the applicable Medicare cost report.

Concentrations of Credit Risk

The Company grants unsecured credit to its patients, most of who reside primarily in Nashville, Tennessee and the surrounding areas of middle Tennessee. In addition, most patients are insured under commercial, Medicare or Tenncare agreements. Medicare, Tenncare and Blue Cross Blue Shield (“BCBS”) represent the only significant concentrations of credit risk from payors. We’ve defined a significant concentration to be those payors representing more than 10% of our total accounts receivable balance, net of allowance for bad debts. Accounts receivable, net of allowance for bad debt, relating to Medicare programs, Tenncare/Medicaid programs and BCBS were approximately $51.2 million, $51.8 million and $76.8 million representing 14.9%, 15.1% and 22.4%, respectively, of consolidated net accounts receivable as of June 30, 2016.

Pledges Receivable, Net

VUMC recognizes unconditional promises to give (pledges) as contribution revenue and a pledge receivable on the consolidated balance sheet upon receipt of a commitment from the donor. VUMC records pledges with payments due in future periods as increases in temporarily restricted or permanently restricted net assets at the estimated present value of future cash flows, net of an allowance for estimated uncollectible promises. VUMC calculates an allowance for uncollectible pledges receivable based upon an analysis of past collection experience and other judgmental factors.

VUMC records pledges with donor-imposed restrictions as unrestricted net assets if VUMC meets the restrictions and receives the contribution in the same reporting period. Otherwise, VUMC records contributions with donor-imposed restrictions as increases in temporarily restricted or permanently restricted net assets, depending upon the nature of the restriction.

After meeting donor stipulations, VUMC releases pledges recorded as temporarily restricted net assets and recognizes these contributions as unrestricted net assets. VUMC releases from restrictions pledges for plant facilities and recognizes these contributions as a change in other unrestricted net assets only after incurring expenses for the applicable plant facilities or when the related asset is placed in service based on donor intent.

In contrast to unconditional promises as described above, VUMC does not record conditional promises (primarily bequest intentions) until the donor contingencies are met.

Grants and Contracts Receivable

VUMC receives research funding (restricted funds) from departments and agencies of the U.S. government, industry and other foundation sponsors. Research grants and contracts receivable include amounts due from these sponsors of externally funded research. These amounts have been billed or are billable to the sponsor. These receivables are reported net of reserves for uncollectible accounts.

Other Current Assets

Other current assets consist primarily of receivables relating to agreements to utilize VUMC employed clinical faculty or other clinical professionals in other local healthcare facilities and other miscellaneous amounts relating to receivables and deposits on various contracts.

Inventories

VUMC reports inventories at the lower of cost or market, with cost being determined on the first-in, first-out method. Inventories consist primarily of medical supplies, implants, and pharmaceuticals.

Investments Limited as to Use
VUMC has investments in hedged equity and hedged debt funds as well as real estate and commodities funds. All investments in these asset classes at June 30, 2016 were in highly liquid mutual fund investment vehicles. VUMC reports investments held at fair value on the balance sheet.

Property, Plant, and Equipment, Net
VUMC records purchases of property, plant, and equipment at cost. VUMC capitalizes interest cost incurred on borrowed funds during the period of construction of capital assets as a component of the cost of acquiring those assets. VUMC capitalizes donated assets at fair value on the date of donation and expenses repairs and maintenance costs as incurred.

Capitalized software for internal use is recorded during the application development stage. These costs include: fees paid to third parties for direct costs of materials and services consumed in developing or obtaining the software; payroll related costs and capitalized interest costs. Costs for training and application maintenance in the post-implementation-operation stage are expensed as incurred.

VUMC computes depreciation using the straight-line method over the estimated useful life of land improvements (3 to 18 years), buildings and leasehold improvements (2 to 37 years) and equipment (1 to 20 years). Equipment costs also include capitalized internal-use software costs, which are expensed over the expected useful life, which is generally 1.5 to 4 years. VUMC assigns useful lives in accordance with American Hospital Association guidelines.

Software for internal use is amortized on a straight line basis over its estimated useful life. In determining the estimated useful life, management considers the effects of: obsolescence, technology, competition, other economic factors and rapid changes that may be occurring in the development of software products, operating systems and computer hardware. Amortization begins once the software project has completed the application development stage regardless of when the software is placed into service.

Impairment of Long-Lived Assets
VUMC reviews long-lived assets, such as property, plant, and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. VUMC measures the recoverability of assets to be held and used by comparing the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, VUMC recognizes an impairment charge to the extent the carrying amount of the asset exceeds its fair value.

Conditional Asset Retirement Costs and Obligations
VUMC accrues for costs related to obligations to perform certain activities in connection with the retirement, disposal, or abandonment of assets. Using site-specific surveys, VUMC identified liabilities of approximately $5.7 million as of June 30, 2016, largely related to asbestos abatement removal. The liability estimate includes an inflation rate of 3% and a discount rate of 4.1%.

Deferred Revenue
The majority of deferred revenue relates to grants and contracts requiring expenditure for specified activities before VUMC is reimbursed by the grantor for the costs incurred. Documentation showing actual costs expended are included when submitting a monthly or quarterly report for reimbursement. Certain grantors pay in advance of incurring the specified costs. In those cases, the amount received in excess of amounts spent on reimbursable costs is reported as deferred revenue.

Long-Term Debt
VUMC reports long-term debt at carrying value. The carrying value of VUMC's debt is the par amount adjusted for the net unamortized amount of bond premiums and discounts.

Interest Rate Exchange Agreements
VUMC estimates the fair value of interest rate exchange agreements by calculating the present value sum of future net cash settlements that reflect market yields as of the measurement date and estimated amounts that VUMC would pay, or receive, to terminate the contracts as of the report date. VUMC considers current interest rates and creditworthiness of the interest rate exchange counterparties when estimating termination settlements.

Self-Insurance Reserves and Claims
VUMC elects to self-insure a portion of its medical malpractice and professional liability coverage, and its general liability coverage via an irrevocable self-insurance trust. The maximum self-insured retention is $5.5 million per occurrence and $43 million annually up to $105.5 million for fiscal 2016. The self-insurance trust covers medical malpractice, professional, and general liability claims attributable to VUMC. Actuarial firms determine expected losses on an annual basis, at which time VUMC records medical malpractice and professional liability expense within the limits of the program. VUMC obtains excess malpractice, professional, and general liability coverage from commercial insurance carriers on a claims-made basis for claims above the retained amounts.

VUMC also elected to self-insure for employee health and worker's compensation expenses. Actuarial firms determine expected losses on an annual basis. The maximum retention for worker's compensation is $0.8 million per occurrence. There is no stop loss insurance on health plan claims.

Income Taxes
VUMC is a tax-exempt organization as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and is generally exempt from federal income taxes pursuant to Section 501(a) of the Code.

Recent Accounting Pronouncements
In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, which is a principles-based standard on revenue recognition. Companies across all industries will use a five-step model to recognize revenue from customer contracts. The new standard, which replaces nearly all existing United States Generally Accepted Accounting Principles ("US GAAP") revenue recognition guidance, will require significant management judgment in addition to changing the way many companies recognize revenue in their financial statements. The standard is effective for a nonpublic entity that has issued or is a conduit bond obligor for securities that are traded, listed or quoted on an exchange or in an over-the-counter market for annual and interim periods beginning after December 15, 2017. Early adoption is permitted under US GAAP, which allows entities to adopt one year earlier if they choose. VUMC continues to evaluate the effects the adoption of this standard will have on our consolidated financial statements and disclosures.

In April 2015, the FASB issued Accounting Standards Update 2015-03, *Simplifying the Presentation of Debt Issuance Costs* (“ASU 2015-03”), which requires that debt issuance costs be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The guidance in the new standard is limited to the presentation of debt issuance costs. The recognition and measurement guidance for debt issuance costs are not affected by ASU 2015-03. We elected to adopt the new presentation in fiscal 2016.

In May 2015, the FASB issued Accounting Standards Update 2015-07, *Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or its Equivalent)*. ASU 2015-07 removes the requirement to categorize within the fair value hierarchy all investments measured at fair value using the net asset value per share practical expedient. The provisions of ASU 2015-07 are effective for fiscal years beginning after December 15, 2016 (with early adoption permitted) and will require retrospective application to all periods presented. VUMC continues to evaluate the effects the adoption of this standard will have on our consolidated financial statements and disclosures.

In February 2016, the FASB issued Accounting Standards Update 2016-02, *Leases* (“ASU 2016-02”), which requires lessees to recognize assets and liabilities for most leases. ASU 2016-02 is effective for a not-for-profit entity that has issued or is a conduit bond obligor for securities that are traded, listed or quoted on an exchange or in an over-the-counter market for annual periods beginning after December 15, 2018 and interim periods within that fiscal year. Early adoption is permitted. ASU 2016-02’s transition provisions will be applied using a modified retrospective approach at the beginning of the earliest comparative period presented in the financial statements. While we are currently evaluating the provisions of ASU 2016-02 to determine how our financial statements will be affected, we believe the primary effect of adopting the new standard will be to record assets and offsetting obligations for current operating leases.

In August 2016, the FASB issued Accounting Standards Update 2016-14, *Presentation of Financial Statements for Not-For-Profit Entities* (“ASU 2016-14”). NFPs would no longer be required to distinguish between resources with temporary and permanent restrictions on the face of their financial statements, meaning they would present two classes of net assets instead of three. They would be required to present expenses by their natural and functional classification and would be required to provide more quantitative and qualitative information about their liquidity. The guidance is effective for fiscal years beginning after December 15, 2017, and interim periods within fiscal years beginning after December 15, 2018. We continue to evaluate the effects the adoption of this standard will have on our consolidated financial statements and disclosures.

3. Acquisitions

On April 29, 2016, VUMC acquired the assets, liabilities, rights and obligations of the clinical enterprise, post-graduate training programs and clinically-related research of the University owned and operated Medical Center for consideration of $1.23 billion (“the Acquisition”). For the purpose of funding the Acquisition, VUMC entered into certain debt agreements to borrow approximately $1.13 billion of publically and privately placed debt and committed to a $100.0 million subordinate note payable to the University to be paid over twenty years (May 2016 through April 2036). VUMC paid VU cash of $1.13 billion to acquire the Medical Center assets and liabilities which included approximately $529.0 million of cash. The net cash paid of $601.0 million represents the $1.13 billion of cash paid to VU net of the $529.0 million of cash included in the assets acquired. In addition to the cash consideration paid and subordinate note payable, VUMC committed to additional consideration in the form of other payables of approximately $31.7 million; a $12.0 million commitment to fund trans-institutional programs and a $19.7 million memorandum of understanding (“MOU”) to fund certain University capital projects both of which were previously agreed to be funded by the Medical Center. These Medical Center assets and operations were used to form the two major operating divisions of VUMC.

VUMC accounted for the Acquisition using the acquisition method of accounting pursuant to ASC 805-10-05-4 as modified by ASC 958-805-25, whereby the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquired entity are recognized and measured at their fair values on the date VUMC obtained control of the Medical Center. The Acquisition resulted in an inherent contribution from the University totaling approximately $509.0 million. The inherent contribution is a result of the University's interest in the success of VUMC and the shared missions of the two organizations which are memorialized in the agreements discussed within this note. No goodwill was recorded as a result of this transaction.

The table below summarized the allocation of the purchase price (including assumed liabilities) for the Medical Center as of the acquisition date:

(in thousands)

Net cash consideration paid	$ 600,971
Note payable to VU	100,000
Other VU payable	31,700
Total consideration	732,671
Current assets	492,709
Property, plant, and equipment, net	1,121,845
Other noncurrent assets	207,101
Liabilities	(574,466)
Noncontrolling interests	(5,502)
Total identifiable net assets	1,241,687
Total inherent contribution from VU	$ 509,016

The inherent contribution from VU is included in the following fund balances from April 29, 2016, the date of the Acquisition:

(in thousands)

Unrestricted	$ 476,895
Temporarily restricted	25,360
Permanently restricted	6,761
Total inherent contribution from VU	$ 509,016

The assets acquired and liabilities assumed from the Acquisition were detailed in a Master Transfer and Separation Agreement ("MTSA"). In addition to the explanation of the transaction details pertaining to the Medical Center assets and liabilities, the MTSA contains the framework for the ongoing economic relationship between VUMC and the University. The relationship is memorialized in the form of an Academic Affiliation Agreement ("AAA"), a Trademark License Agreement ("TMLA"), a Ground Lease, and a Reciprocal Master Services Agreement ("MSA").

The AAA outlines the ongoing academic, research and clinical affiliation between the University and VUMC for all of the University's degree-granting, certificate and research programs. The AAA allocates responsibility between the University and VUMC for jointly administered academic and residency programs and is an exclusive agreement between VUMC and VU requiring that VUMC be organized, governed and operated in a manner that supports VU's academic and research mission. The agreement provides that VU will be the exclusive academic affiliate of VUMC and VUMC will be the exclusive clinical affiliate of VU. This agreement requires VUMC to pay VU an annualized fee of $70.0 million in equal monthly payments adjusted annually for inflation based upon the Biomedical Research and Development Price Index (BRDPI) in perpetuity pursuant to certain mutually agreed upon termination or default clauses. This agreement also requires the one-time $12.0 million commitment to fund trans-institutional programs with the University, included in the consideration reflected in the above table.

Pursuant to the TMLA, the University grants, subject to certain consents and approvals, a perpetual license to use various University-owned licensed marks in connection with VUMC's fundamental activities after the Acquisition date. The licensed marks, which VUMC will continue to use as the primary brands of VUMC, include virtually all those currently in use by VUMC. This agreement requires VUMC to pay VU a monthly royalty payment equal to 1.0% of all operating revenues (as defined in the TMLA) of VUMC and a percentage of net income (0% in FY 2017, 5% in FY 2018, 10% in FY 2019, and 15% in FY 2020 and beyond) from operations (as defined in the TMLA). In addition, VUMC is required to pay approximately $53.6 million annually. The $53.6 million amount increases 3% annually starting in fiscal year 2017. This agreement is in force in perpetuity pursuant to certain mutually agreed upon termination or default clauses.

The Ground Lease is an agreement between VU and VUMC that allows VUMC to use the land on which its campus and related buildings are located. The initial term of the Ground Lease ends June 30, 2114 with the option to extend the lease for two additional terms of up to fifty to ninety-nine years each with mutual agreement between VU and VUMC. The lease covers approximately 1.7 million square feet or 38.75 acres of space with an annual base rent of $18.0 million payable monthly. VUMC is responsible for all property taxes associated with this lease. This lease is discussed further in Note 16.

The University and VUMC will provide services to one another for agreed-upon consideration subsequent to the Acquisition as outlined in the MSA. VU will provide services to VUMC such as information technology infrastructure support, utilities and law enforcement staffing. VUMC will continue to provide various operational services for the University including student health centers, a psychological counseling center, and animal care. Services under these agreements can be terminated by either party subject to pre-determined cancellation notification periods.

4. Related Parties

On April 29, 2016, VUMC completed the Acquisition. VUMC is now a separately operating 501(c)(3) not-for-profit corporation. VUMC is governed by a separate and autonomous board apart from the governance of VU, where control of the assets necessary to operate VUMC has been transferred from VU to VUMC. VUMC is responsible for its own debt and liabilities, separate and apart from the University. At legal separation, VUMC and VU entered into several agreements that govern the relationship between the two entities moving forward as described in Note 3.

As part of the Acquisition, VUMC pledged $12.0 million to fund trans-institutional programs in accordance with the AAA and $19.7 million to fund certain capital projects previously agreed to by the Medical Center in accordance with the MOU. These amounts are recorded under the accounts payable and accrued expenses caption in the consolidated balance sheet as of June 30, 2016.

As of June 30, 2016, VUMC has a receivable from VU and a payable to VU in the amount of approximately $21.2 million and $26.2 million, respectively, as of June 30, 2016. The receivable is recorded under the other current assets caption and the payable is recorded under the accounts payable and other accrued expenses caption in the consolidated balance sheet. The receivable from VU consists of approximately $17.3 million associated with the final settlement of the Acquisition and the remaining $3.9 million relates to the MSA for services provided to VU. Conversely, the payable to VU relates entirely to the MSA for services provided to VUMC. In addition, VUMC has a $100 million subordinate promissory note payable to VU as part of the Acquisition.

Intermittently, members of VUMC's Board of Directors or VUMC employees may be directly or indirectly associated with companies engaged in business activities with VUMC. Accordingly, VUMC has a written conflict of interest policy that requires, among other things, that members of the VUMC community (including trustees) may not review, approve, or administratively control contracts or business relationships when (a) the contract or business relationship is between VUMC and a business in which the individual or a family member has a material financial interest or (b) the individual or a family member is an employee of the business and is directly involved with activities pertaining to VUMC.

Furthermore, VUMC's conflict of interest policy extends beyond the foregoing business activities in that disclosure is required for any situation in which an applicable individual's financial, professional, or other personal activities may directly or indirectly affect, or have the appearance of affecting, an individual's professional judgment in exercising any VUMC duty or responsibility, including the conduct or reporting of research.

The policy extends to all members of the VUMC community (including trustees, faculty, and staff and their immediate family members). Each applicable person is required to certify compliance with the conflict of interest policy on an annual basis. This certification includes specifically disclosing whether VUMC conducts business with an entity in which he or she (or an immediate family member) has a material financial interest as well as any other situation that could appear to present a conflict with VUMC's best interests.

When situations exist relative to the conflict of interest policy, VUMC takes active measures to manage appropriately the actual or perceived conflict in the best interests of VUMC, including periodic reporting of the measures taken to the Board of Directors Audit Committee.

5. Patient Accounts Receivable

Accounts receivable as of June 30, 2016 were $343.2 million, net of $20.2 million in allowances for doubtful accounts. The largest component of VUMC's receivables was from third party payors.

As of June 30, 2016, VUMC had receivables, net of related contractual and bad debt allowances from the following payors:

(in thousands)		
Medicare	$	51,238
TennCare/Medicaid		51,769
Blue Cross		76,847
Other commercial carriers		127,828
Patient responsibility		35,559
	$	343,241

6. Reimbursement Under Third-Party Agreements

A summary of estimated third-party settlements by major payor category as of June 30, 2016 follows:

(in thousands)		
Estimated third-party receivables		
Tricare/Champus	$	9,123
Estimated third-party liabilities		
Medicare	$	18,024
Medicaid		12,385
Other		581
	$	30,990

7. Pledge Receivable, net

The pledge receivables net of applied discounts and allowance for uncollectible pledges as of June 30, 2016 were as follows:

(in thousands)		Gross		Discount		Allowance for Uncollectible Pledges		Net
In one year or less	$	6,136	$	(30)	$	(36)	$	6,070
Between one year and five years		7,928		(236)		(29)		7,663
Total pledge receivable, net	$	14,064	$	(266)	$	(65)	$	13,733

VUMC discounts contributions receivable at a rate commensurate with the scheduled timing of receipt. VUMC applied discount rates ranging from 0.5% to 1.5% to amounts outstanding as of June 30, 2016. Our methodology for calculating an allowance for uncollectible promises consists of analyzing write-offs as a percentage of gross pledges receivable along with assessing the age and activity of outstanding pledges.

In addition to pledges reported as pledge receivables, VUMC had cumulative bequest intentions and conditional promises to give of approximately $37.7 million as of June 30, 2016. Due to their conditional nature, VUMC does not recognize intentions to give as assets.

The pledge receivable, net as of June 30, 2016, broken down by net asset class, was as follows:

(in thousands)

Unrestricted	$	194
Temporarily restricted		13,347
Permanently restricted		192
Total pledge receivable, net	$	13,733

8. Grants and Contracts Receivable

VUMC receives research funding from a variety of sources, as described in Note 2. Grants and contracts receivable as of June 30, 2016 is approximately $60.9 million. This receivable is comprised of $33.0 million and $27.9 million of federally and nonfederally funded grants and contracts, respectively.

9. Charity Care Assistance, Community Benefits, and Other Unrecovered Costs

VUMC (including all hospitals, clinics, physician practices, and controlled clinical joint ventures) maintains a policy which sets forth the criteria to provide, without expectation of payment or at a reduced payment rate, health care services to patients who have minimal financial resources to pay for medical care. VUMC does not report these charity care services as revenue. Accordingly, no receivable for charity care services is recorded in this consolidated balance sheet.

VUMC maintains records to identify and monitor the level of charity care it provides, and these records include the amount of gross charges and patient deductibles, co-insurance and co-payments forgone for services furnished under its charity care policy, and the estimated cost of those services. Charity care is determined by utilizing a tiered grid relative to the federal poverty guidelines. VUMC provides additional discounts based on the income level of the patient household using a sliding scale for those patients with a major catastrophic medical event that do not qualify for full charity assistance. VUMC calculates a ratio of total costs to gross charges, and then multiplies the ratio by foregone charity care charges in determining the estimated cost of charity care.

In addition to the charity care services described above, VUMC provides a number of other services to benefit the economically disadvantaged for which we receive little or no payment. TennCare/Medicaid and state indigent programs do not cover the full cost of providing care to beneficiaries of those programs. As a result, in addition to direct charity care costs, VUMC provided services related to TennCare/Medicaid and state indigent programs and was reimbursed substantially below the cost of rendering such services.

VUMC also provides public health education and training for new health professionals and provides, without charge, services to the community at large, together with support groups for many patients with special needs.

10. Investments Limited as to Use

VUMC investments include assets limited as to use, which include assets held in an irrevocable trust related to self-insured malpractice and workers compensation programs, internally-designated assets, donor-designated gifts for capital assets, and split interest trusts of approximately $88.5 million, $79.7 million, $15.7 million, and $6.4 million as of June 30, 2016, respectively.

Investments limited as to use at June 30, 2016 were as follows:

(in thousands)	Market Value	Amortized Cost	Unrealized Gain (Loss)
Cash and cash equivalents	$ 16,378	$ 16,378	$ -
Bonds	9,019	8,991	28
Fixed income mutual funds	35,377	34,842	535
Hedged debt funds	3,200	3,200	-
Equity mutual funds	88,565	90,414	(1,849)
Hedged equity funds	14,740	15,006	(266)
Commodities and managed futures mutual funds	3,305	3,161	144
Real estate mutual funds	13,398	12,386	1,012
Split interest trusts	6,384	5,168	1,216
	$ 190,366	$ 189,546	$ 820

VUMC has elected the fair value option related to investments and reports investments held at fair value on the consolidated balance sheet using the three-level hierarchy. VUMC records purchases and sales of securities on the trade dates, and realized gains and losses are determined based on the average historical cost of the securities sold. VUMC reports net receivables and payables arising from unsettled trades as a component of investments.

VUMC has exposure to a number of risks including liquidity, interest rate, counterparty, basis, regulatory, market, and credit risks for marketable securities. Due to the level of risk exposure, it is possible that near-term valuation changes for investment securities may occur to an extent that could materially affect the amounts reported in VUMC's consolidated balance sheet.

Unless donor-restricted endowment gift agreements require separate investment, VUMC manages all endowment investments as an investment pool.

Cash and cash equivalents are composed primarily of donor-designated gifts to be used for the acquisition or construction of noncurrent assets. In addition, a portion of this balance represents amounts posted as collateral in accordance with regulatory requirements associated with self-insurance and liquid assets associated with internally designated investments.

Bonds consist of $9,000 par value of US Treasury Notes held in a workers compensation account.

Fixed income mutual funds includes investments directed towards capital preservation and predictable yield as well as more opportunistic strategies focused on generating return on price appreciation. These mutual fund investments held in both the self-insurance trust portfolio as well as the long-term portfolio of internally- designated funds and are designed to reflect a highly diversified total return investment strategy.

Hedged equity and debt funds include marketable alternative strategies to diversify risks and reduce volatility in the portfolios. These liquid mutual fund investments include investments in highly diversified long-short equity portfolios as well as long-short credit-oriented portfolios.

Equity mutual funds consist of investment funds globally diversified across public markets including U.S. markets, other developed markets, and emerging and frontier markets.

Commodities funds include public investments such as commodity futures and commodity-related equities. Investments in this asset class included only liquid mutual fund investments.

Real estate mutual funds comprises liquid investments in mutual funds investing in Real Estate Investment Trusts (REITS).

Split interest trusts are Vanderbilt University Medical Center's split interest agreements with donors.

11. Property, Plant, and Equipment, Net

A summary of property, plant, and equipment at June 30, 2016 follows:

(in thousands)

Land and land improvements	$	18,117
Buildings and improvements		863,023
Equipment		164,395
Property, plant, and equipment at cost		1,045,535
Less: Accumulated depreciation		(14,279)
Property, plant, and equipment, net of accumulated depreciation		1,031,256
Construction in progress		98,860
Property, plant, and equipment, net	$	1,130,116

Capitalized software for internal use is included in the equipment caption in the above table. The gross carrying amount of internal use software was approximately $5.8 million, and the net carrying amount considering accumulated amortization was approximately $5.5 million at June 30, 2016. Construction in progress includes $33.4 million of capitalized costs for internal use software at June 30, 2016, of which $20.9 million were incurred during the period beginning April 29, 2016 and ended June 30, 2016. The $20.9 million of capitalized internal use software includes approximately $3.0 million of internal costs. These costs represent amounts accrued in the application development stage of the project and will begin amortization once the software project is complete and ready for its intended use.

As part of the MTSA, VUMC acquired real property not allowed to be repurposed without express consent of VU.

12. Long-Term Debt

Long-term debt consists of bonds and notes payable and certain financing obligations at June 30, 2016 as follows:

(in thousands)	**Fiscal Years to Maturity**	**Fixed Coupon Interest Rate**	**Effective Interest Rate**	**Outstanding Principal**
2016 Series debt				
Fixed-rate Debt				
Series 2016A, Tax-Exempt Revenue Bonds	31	5.00 %	4.30 %	$ 476,930
Series 2016B, Taxable Revenue Bonds	11	4.05 %	4.30 %	300,000
Total fixed-rate debt			4.30 %	776,930
Variable-rate Debt				
Series 2016C, Taxable Revenue Bonds	31		1.90 %	50,000
Series 2016D, Taxable Revenue Notes	6		3.20 %	100,000
Series 2016E, Taxable Term Loan Revenue Note	21		3.00 %	128,070
Series 2016F, Taxable Revenue Bonds	26		3.10 %	75,000
Total variable-rate debt			2.90 %	353,070
Par amount of 2016 Series Debt				1,130,000
Other long-term debt				
Subordinated Promissory Note Payable to VU	20	3.25 %	3.25 %	99,166
Product Financing Arrangement	11		4.10 %	14,977
Subtotal[1]			3.90 %	1,244,143
Net unamortized premium on 2016 Series Debt				59,328
Net unamortized bond issuance costs on 2016 Series Debt				(12,408)
Total long-term debt				1,291,063
Less: Current installments of long-term debt				(5,000)
Long-term debt, net of current installments				$ 1,286,063

[1] The effective interest rate of 3.9% is exclusive of interest rate exchange agreements discussed in Note 13. Inclusive of these agreements, the overall portfolio effective interest rate was 4.3%.

On April 29, 2016, VUMC issued the Series 2016 A,B,C,D,E, and F bonds (“2016 Series Debt”) and notes aggregating $1.278 billion of proceeds for the purpose of financing the Medical Center Acquisition and paying a portion of the costs of issuance associated with the 2016 Series Debt.

The Series 2016A tax-exempt fixed-rate revenue bonds were issued in the par amount of approximately $476.9 million and include an original issue premium of approximately $59.6 million. The Series 2016A bonds have a final maturity date of July 1, 2046 and can be optionally redeemed at par on or after July 1, 2026. The 2016A bonds were structured as serial bonds with maturites from fiscal 2030 through 2032, as well as three term bonds maturing fiscal 2036 through 2047 which are subject to mandatory sinking fund redemption in lots. The Series 2016A bonds bear interest at 5% per annum, and pay interest semi-annually on July 1st and January 1st.

The Series 2016B taxable fixed-rate revenue bonds were issued in the par amount of $300.0 million bear interest at 4.053% per annum, and have a bullet maturity of July 1, 2026. VUMC is entitled, at its option, to redeem all or a portion of the Series 2016B bonds prior to April 1, 2026 at a make-whole redemption price, as defined in the Series 2016B indenture and official statement.

The Series 2016C taxable variable-rate revenue bonds (R-FLOATs) were issued in the par amount of $50.0 million and bear interest initially at a fixed spread to weekly LIBOR of 1.6% through final maturity of July 1, 2046. The R-FLOATs have an optional tender provision whereby the bondholder can tender the bond to the trustee for purchase in whole or part. The funds for optional redemption are derived solely from remarketing proceeds or funds provided by VUMC, however, VUMC is not required to provide such funds. If the bonds cannot be remarketed at optional redemption they are returned to the bondholder and enter a term out period of twenty-four months. If bonds cannot be successfully remarketed by the end of the 24 month term out period they are subject to mandatory redemption. In addition to optional redemption of all or a portion of the bonds, the Series 2016C bonds are subject to mandatory sinking fund redemption starting on July 1, 2030.

The Series 2016D taxable variable-rate revenue notes (floating rate notes) were issued in the par amount of $100.0 million and bear interest initially at a fixed spread to one month LIBOR of 2.5% through the initial mandatory tender date of July 1, 2021 and final maturity of July 1, 2046. In addition to optional redemption of all or a portion of the bonds beginning six months prior to the mandatory tender date of July 1, 2021, the Series 2016D bonds are subject to mandatory redemption in lots commencing on July 1, 2021, and each July thereafter until final maturity.

The Series 2016E taxable term loan revenue notes were issued in the par amount of approximately $128.1 million and were placed privately with a bank. The notes bear interest in a variable-rate mode at a fixed spread to one month LIBOR of 2.4% through the initial mandatory tender date of July 1, 2022 and final maturity of July 1, 2046. In addition to optional redemption of all or a portion of the notes at anytime, subject to notice, the Series 2016E notes are subject to principal amortization commencing on July 1, 2022, as defined in the Series 2016E loan agreement between VUMC and the lender.

The Series 2016F taxable variable-rate revenue bonds were issued in the par amount of $75.0 million and were placed privately with a bank. The notes bear interest in a variable-rate mode at a fixed spread to one month LIBOR of 2.5% through the initial mandatory tender date of July 1, 2022. The bonds can be optionally redeemed in part or in whole in the current interest mode at par on or after July 1, 2022, at which time the bonds are also subject to mandatory sinking fund redemption until the final maturity date of July 1, 2041.

All of the aforementioned bonds and notes issued by VUMC (2016 Series Debt) on April 29, 2016 (with the exception of the subordinated note payable to Vanderbilt University described below) were issued by the Health and Educational Facilities Board of The Metropolitan Government of Nashville and Davidson County, Tennessee (HEFB). As a conduit issuer, the HEFB loans the debt proceeds to VUMC. Pursuant to loan agreements, VUMC's debt service requirements under these loan agreements coincide with required debt service of the actual HEFB bonds.

Each of the bonds and notes issued by the HEFB on April 29, 2016 were issued as separate obligations under a Master Trust Indenture (MTI) structure dated April 1, 2016. The MTI provides the flexibility for multiple parties to participate in debt issuances as part of an obligated group; presently, VUMC has no other members participating in the obligated group. All debt issued under the MTI are general obligations of the obligated group. Under the provisions of the Leasehold Deed of Trust, Security Agreement, Assignment of Rents and Leases, and Fixture Filing ("the Security Agreement") within the MTI, gross receivables of the obligated group are pledged as collateral. Additionally the Security Agreement established a mortgage lien on: (i) the leasehold interest of the land subject to the Ground Lease; (ii) the buildings, structures, improvements and fixtures now or hereafter located on the land subject to the Ground Lease; and (iii) certain other collateral.

Trust indentures for certain bond issues contain covenants and restrictions, the most material of which include limitations on the issuance of additional debt, maintenance of a specified debt service coverage ratio, and a minimum amount of days cash on hand. VUMC believes it is in compliance with such covenants and restrictions as of June 30, 2016.

On April 29, 2016, VUMC delivered a secured subordinated promissory note in the amount of $100 million to Vanderbilt University for the purpose of financing the Acquisition ("the VU subordinated note"). The note was issued at a fixed rate of 3.25% with monthly principal payments totaling $5 million annually commencing on May 31, 2016 for a period of twenty years ending on April 30, 2036. This note is secured by the gross receivables and mortgaged property described in the Security Agreement subject to the requirements of the 2016 Series Debt and the MTI.

On April 29, 2016, as part of the Acquisition, VUMC assumed a 10 year, unsecured, noninterest bearing product financing arrangement with a vendor for the purchase and implementation of internal use software described in Note 11 ("Product Financing Arrangement"). As part of this agreement, VUMC has committed to an annual payment of $0.5 million payable in monthly installments through November of 2019. These payments will be considered imputed interest expense. During fiscal year 2020, the annual payment increases to $4.9 million payable in monthly installments. These payments are considered principal and imputed interest and continue through fiscal year 2026. At June 30, 2016, the principal balance shown in the below schedule of approximately $15.0 million represents software for which we have taken ownership and incurred implementation services. To determine the obligation, we discounted the future cash outflows relating to this obligation using an estimated effective interest rate of 4.1%. The estimated balance of $15.0 million is reflected in the long-term debt caption of the consolidated balance sheet.

Principal retirements and scheduled sinking fund requirements based on nominal maturity schedules for long-term debt due in subsequent fiscal years ending June 30 are as follows:

(in thousands)	**2016 Series Debt**	**VU Subordinated Note**	**Product Financing Agreement**	**Total Principal Retirements**
2017	$ -	$ 5,000	$ -	$ 5,000
2018	-	5,000	-	5,000
2019	-	5,000	-	5,000
2020	-	5,000	2,544	7,544
2021	-	5,000	4,504	9,504
Thereafter	1,130,000	74,166	7,929	1,212,095
Total long-term debt principal retirements	$ 1,130,000	$ 99,166	$ 14,977	$ 1,244,143

On April 29, 2016 VUMC entered into an agreement with a bank to provide a general use line of credit with a maximum available commitment totaling $100.0 million. The line of credit, which may be drawn upon for general operating purposes, expires on April 28, 2017. Interest on each advance under this line of credit accrues at a rate of 0.75% plus LIBOR, and a commitment fee of 0.20% per annum accrues on any unused portion of the line of credit. No amounts were drawn on this credit facility as of June 30, 2016.

13. Interest Rate Exchange Agreements

On April 29, 2016, the University transferred an interest rate exchange agreement to VUMC with a total notional amount of $150.0 million. VUMC split the transferred notional amount into two agreements with new notional amounts of $75 million each and incorporated these interest rate exchange agreements into its debt portfolio management strategy. Collateral pledging requirements were removed from the novated agreements and mandatory termination provisions were added at that time. The estimated fair value of VUMC’s outstanding interest rate exchange agreements represented a liability of $89.5 million as of June 30, 2016.

The notional amount of VUMC’s outstanding interest rate exchange agreements as of June 30, 2016 totaled $150.0 million with an average rate paid of 4.15% with a maturity date of May 1, 2040. The variable portions of these agreements are equal to 68% of one-month LIBOR rate. Notional amounts of $75.0 million terminate automatically on April 29, 2021 and 2023, at which point the exchange agreements will be settled at fair value.

14. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets as of June 30, 2016 represented donor restricted gifts.

A summary of VUMC's temporarily restricted net assets as of June 30, 2016 is as follows:

(in thousands)		**Total**
Property, plant and equipment	$	15,737
Research and education		11,087
Operations		161
Total temporarily restricted net assets	$	26,985

Permanently restricted net assets as of June 30, 2016 consisted of cash proceeds from life insurance policies totaling approximately $0.6 million and remainder or split-interest trust funds of approximately $6.2 million. These amounts will be invested in our endowment upon death of the donor.

Endowment-related assets include institutional endowments (quasi-endowments). VUMC's endowment does not include gift annuities, interests in trusts held by others, contributions pending donor designation, or contributions receivable.

The Board of Director's interpretation of its fiduciary responsibilities for donor-restricted endowments under the Uniform Prudent Management of Institutional Funds Act (UPMIFA) requirements is to preserve intergenerational equity, barring the existence of any donor-specific provisions. Under this broad guideline, future endowment beneficiaries should receive at least the same level of real economic support as the current generation. The overarching objective is to preserve and enhance the real (inflation-adjusted) purchasing power of the endowment in perpetuity. VUMC invests assets to provide a relatively predictable and stable stream of earnings to meet spending needs and attain long-term return objectives without the assumption of undue risks.

UPMIFA specifies that unless stated otherwise in a gift instrument, donor-restricted assets in an endowment fund are restricted assets until appropriated for expenditure. Barring the existence of specific instructions in gift agreements for donor-restricted endowments, VUMC reports the historical value for such endowments as permanently restricted net assets and the net accumulated appreciation as temporarily restricted net assets. In this context, historical value represents the original value of initial contributions restricted as permanent endowments plus the original value of subsequent contributions and, if applicable, the value of accumulations made in accordance with the direction of specific donor gift agreements.

VUMC may not fully expend Board-appropriated endowment distributions in a particular fiscal year. In some cases, VUMC will approve endowment distributions for reinvestment into the endowment.

15. Fair Value Measurements

Fair value measurements represent the price received to sell an asset or price paid to transfer a liability in an orderly transaction between market participants at the measurement date. GAAP establishes a three-level hierarchy for fair value measurements based on the observable inputs to the valuation of an asset or liability at the measurement date. Inputs to the valuation techniques used are prioritized to measure fair value by giving the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements).

VUMC utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Level 1 Consists of quoted prices (unadjusted) in active markets for identical assets or liabilities that are accessible at the measurement date.

Level 2 Include inputs other than quoted prices included in Level 1 that are either directly or indirectly observable for the assets or liabilities.

Level 3 Are unobservable inputs for the assets or liabilities.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls depends on the lowest level input that is significant to the fair value measurement. VUMC's Treasury Office and a team of external investment managers manage these investments.

The following table summarizes the financial instruments carried on the balance sheet by valuation hierarchy level as of June 30, 2016:

(in thousands)	**Market Value Level 1**	**Market Value Level 2**	**Total Market Value**
Assets			
Cash and cash equivalents	$ 16,378	$ -	$ 16,378
Bonds (US Treasury Notes)	9,019	-	9,019
Fixed income mutual funds	4,926	30,451	35,377
Hedged debt funds	-	3,200	3,200
Equity mutual funds	12,038	76,527	88,565
Hedged equity funds	4,567	10,173	14,740
Commodities and managed futures mutual funds	-	3,305	3,305
Real estate mutual funds	-	13,398	13,398
Split interest trusts	6,384	-	6,384
Total assets reported at fair value	$ 53,312	$ 137,054	$ 190,366
Liabilities			
Interest rate swaps	$ -	$ 89,536	$ 89,536

The recorded amounts for receivables, prepaid expenses, accounts payable, and other accrued expenses and liabilities approximate fair value.

VUMC's long-term debt is reported at carrying value (par) along with the net unamortized amount of premiums. As of June 30, 2016, the carrying value and estimated fair value of long-term debt totaled $1.189 billion and $1.264 billion, respectively. VUMC bases estimated fair value of long-term debt on market conditions prevailing at fiscal year-end reporting dates. Besides potentially volatile market conditions, fair value estimates typically reflect limited secondary market trading. VUMC reports the promissory note payable to VU and the product financing arrangement at carrying value, which approximates fair value for those liabilities.

VUMC employs derivatives, primarily interest rate exchange agreements, to help manage interest rate risks associated with variable-rate debt. In addition to the credit risk of the counterparty owing a balance, VUMC calculates the fair value of interest rate exchange agreements based on the present value sum of future net cash settlements that reflect market yields as of the measurement date.

Parties to interest rate exchange agreements are subject to risk for changes in interest rates as well as risk of credit loss in the event of nonperformance by the counterparty. VUMC deals only with high-quality counterparties that meet rating criteria for financial stability and credit worthiness.

16. Lease Obligations

VUMC leases certain property and equipment. VUMC classifies these leases as operating leases and has lease terms ranging from two to twenty years.

The following is a schedule by fiscal year of future minimum rentals on noncancelable operating leases as of June 30, 2016:

(in thousands)	**Equipment**	**Property**	**Ground Lease**	**Total**
2017	$ 19,373	$ 42,355	$ 18,000	$ 79,728
2018	10,992	41,324	18,000	70,316
2019	6,584	40,282	18,000	64,866
2020	3,753	38,811	18,000	60,564
2021	2,776	30,908	18,000	51,684
Thereafter	-	188,207	1,692,000	1,880,207
Total future minimum rentals	$ 43,478	$ 381,887	$ 1,782,000	$ 2,207,365

VUMC has 106 separate equipment leases for office and medical equipment at various monthly payment terms expiring through fiscal year 2021 with minimum rental payments totaling approximately $43.5 million. The majority of these leases were assumed through the MTSA.

In July 2007, VU entered an agreement to lease approximately 50% of the space in the 850,000 square foot One Hundred Oaks shopping center located approximately five miles from the main campus ("100 Oaks Lease"). VU redeveloped this leased space primarily for medical and office uses. This operating lease commenced during fiscal year 2009 with an initial lease term of twelve years. In October 2014, VU agreed to an amendment which extends the original lease term by an additional fifteen years, with an option to renew the lease further for four additional ten-year periods. As part of the lease agreement, the lessee also has first rights on leasing additional space in the shopping center, and first rights on purchasing if the landlord desires to sell. On April 29, 2016, the 100 Oaks Lease was assigned to VUMC. As a condition of the assignment, amendments to the 100 Oaks lease were added which required VUMC to provide the landlord a $25 million irrevocable standby letter of credit, pay a $13.2 million refinancing penalty payable to the landlord, and pay $7.8 million of the landlord's closing costs, financing fees, and prepayment penalties associated with a refinancing of the landlord's debt. The prepayment penalty and closing costs were recorded as part of the Acquisition. VUMC included minimum property rental payments aggregating approximately $145.6 million related to this space in the above future minimum property rentals.

In July 2015, VU restructured previously existing lease agreements related to approximately 231,000 square feet of office space at 2525 West End Avenue and extended the lease terms for periods ranging from eleven to fifteen years, with options to renew for two additional five-year periods. On April 29, 2016, VU assigned this lease to VUMC. VUMC included minimum property rental payments aggregating approximately $94.5 million related to this space in the above future minimum property rentals.

On April 29, 2016, VUMC and VU entered into certain lease agreements for the use of space in buildings owned by both entities. As of June 30, 2016, VUMC's estimated future minimum property lease payments to VU totaled approximately $43.2 million and estimated future lease receipts from VU totaled approximately $69.9 million.

On April 29, 2016, VUMC entered into a Ground Lease with an initial term of ninety-nine years ending June 30, 2114 with an option to extend for up to two additional terms of fifty to ninety-nine years each upon mutual agreement by VU and VUMC. The initial annual base rent of $18.0 million is payable monthly and CPI adjusted annually. The Ground Lease allows VUMC to use the land on which its campus and related buildings are located. The Ground Lease incorporates approximately 1.7 million square feet or 38.75 acres of space. VUMC is responsible for all property taxes associated with this lease. The Ground Lease payments in the table above represents VUMC's estimate of future minimum payments.

17. Retirement Plans

VUMC's full-time employees participate in a 403(b) defined contribution retirement plan administered by a third-party. For eligible employees with one year of continuous service, these plans require employee matching of employer contributions. The employee immediately vests in these contributions.

VUMC funds the obligations under these plans through monthly transfers to the respective retirement plan administrators with the corresponding expenses recognized in the year incurred.

18. Commitments and Contingencies

Management continues to implement policies, procedures, and a compliance overview organizational structure to enforce and monitor compliance with government statutes and regulations. VUMC's compliance with such laws and regulations is subject to future government review and interpretations, as well as regulatory actions unknown or unasserted at this time.

(A) Litigation. VUMC is a defendant in certain lawsuits alleging medical malpractice and civil action.

One such legal action is a qui tam civil action related to billing and government reimbursement for certain professional health care services provided by VUMC. The lawsuit was unsealed in the fall of 2013, and the government has declined to intervene in the litigation shortly after it was unsealed. The relators have proceeded with the lawsuit, which is currently in the discovery phase. VUMC intends to vigorously defend this matter and believes that the outcome of these actions will not have a material impact on its consolidated financial position. At June 30, 2016, VUMC has accrued an amount to cover estimated exposure as a result of the investigation, which is not material to VUMC's overall financial position.

In February 2015, VUMC received a letter from the Office of Audit Services (OAS) of the Office of Inspector General (OIG) in connection with its nationwide review to determine whether, in certain cases, services were provided to certain Medicare beneficiaries in accordance with national coverage criteria. OAS has issued their final report regarding their audit which contains an overpayment amount. At June 30, 2016, VUMC has accrued an amount sufficient to cover estimated exposure as a result of the investigation, which is not material to VUMC's overall financial position. VUMC is vigorously defending this matter and intends to appeal a number of OAS's findings to Cahaba GBA, VUMC's Medicare administrative contractor.

On August 16, 2016, VUMC received written notice from VU of a third-party claim which may, if determined adversely to VU, require indemnification by VUMC pursuant to the provisions of the Master Transfer and Separation Agreement, dated as of April 29, 2016. That third party claim is a lawsuit (Cassell v. Vanderbilt University, et al., No. 3:16-cv-02086 (U.S.D.C. M.D. TN)) brought by current and former employees of VU which alleges claims relating to administration of the Vanderbilt University Retirement Plan and New Faculty Plan. Due to the early stage of the litigation, it is not possible to assess the likely outcome of the litigation or to estimate the amount of the indemnification obligation which VUMC might have, were the matter decided adversely to VU.

(B) Regulations. VUMC's compliance with regulations and laws is subject to future government reviews and interpretations, as well as regulatory actions unknown at this time. VUMC believes that the liability, if any, from such reviews will not have a significant effect on VUMC's consolidated financial position.

(C) Medical Malpractice Liability Insurance. Refer to Note 19 for further discussion.

(D) Employee Health and Workers Compensation Insurance. Refer to Note 19 for further discussion.

(E) Federal and State Contracts and Other Requirements. Expenditures related to federal and state grants and contracts are subject to adjustment based upon review by the granting agencies. Amounts of expenditures that granting agencies might disallow cannot be determined at this time. These amounts affect government grants and contract revenue as well as facilities and administrative cost recovery. VUMC would not expect these costs to influence the consolidated financial position significantly.

(F) Health Care Services. Refer to Note 6 for further discussion.

(G) HIPAA Compliance. Under the Health Insurance Portability and Accountability Act of 1996 (HIPAA), the federal government has authority to complete fraud and abuse investigations. HIPAA has established substantial fines and penalties for offenders. VUMC maintains policies, procedures, and organizational structures to enforce and monitor compliance with HIPAA, as well as other applicable local, state, and federal statutes and regulations.

(H) Construction. VUMC had contractual commitments under major construction and equipment contracts of approximately $34.1 million as of June 30, 2016. Subsequent to June 30, 2016, VUMC entered into a $79.6 million construction contract related to a four floor vertical expansion of the MCJCH.

(I) Letter of Credit. As a requirement of the assignment of the 100 Oaks Lease described in Note 16, VUMC provided an irrevocable standby letter of credit of $25 million to the landlord of the property dated June 10, 2016.

(J) Other. VUMC has an agreement with a supplier of medical supplies that contains minimum purchase obligations. This obligation requires VUMC to purchase a minimum of approximately $24.7 million for Fiscal 2017, through February 2017.

19. Self–Insurance Reserves and Claims

The consolidated balance sheet includes reserves for malpractice, professional and general liability coverage totaling approximately $88.0 million. Of this amount, approximately $20.7 million is recorded in the current self- insurance reserves and claims caption of the balance sheet and approximately $67.3 million is shown in the noncurrent self-insurance reserves and claims caption. This malpractice, professional and general insurance liability was discounted at a rate of 2.5%.

The consolidated balance sheet includes the actuarial liabilities for employee health and workers' compensation insurance totaling approximately $19.1 million and $7.9 million, respectively. These amounts are recorded in the accrued employee compensation caption.

20. Subsequent Events

Management evaluated events subsequent to June 30, 2016, and through the date on which the financial statements were available for issuance, November 4, 2016. No material subsequent events were identified.