

COMMUNITY HEALTH SYSTEMS INC  
Form 10-Q  
April 30, 2013  
Table of Contents

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**Form 10-Q**

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2013

Commission file number 001-15925

**COMMUNITY HEALTH SYSTEMS, INC.**

*(Exact name of registrant as specified in its charter)*

**Delaware**

*(State or other jurisdiction of*

*incorporation or organization)*

**4000 Meridian Boulevard  
Franklin, Tennessee**

*(Address of principal executive offices)*

**13-3893191**

*(I.R.S. Employer*

*Identification Number)*

**37067**

*(Zip Code)*

**615-465-7000**

*(Registrant's telephone number)*

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject

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to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of April 23, 2013, there were outstanding 94,258,327 shares of the Registrant's Common Stock, \$0.01 par value.

**Table of Contents**

**Community Health Systems, Inc.**

**Form 10-Q**

**For the Three Months Ended March 31, 2013**

|                 |                                     |                                     |
|-----------------|-------------------------------------|-------------------------------------|
| <b>Part I.</b>  | <b><u>Financial Information</u></b> | <b>Page</b>                         |
|                 | <b>Item 1.</b>                      | <b><u>Financial Statements:</u></b> |
|                 |                                     |                                     |
|                 |                                     | 2                                   |
|                 |                                     | 3                                   |
|                 |                                     | 4                                   |
|                 |                                     | 5                                   |
|                 |                                     | 6                                   |
|                 | <b>Item 2.</b>                      | 40                                  |
|                 | <b>Item 3.</b>                      | 59                                  |
|                 | <b>Item 4.</b>                      | 59                                  |
| <b>Part II.</b> | <b><u>Other Information</u></b>     |                                     |
|                 | <b>Item 1.</b>                      | 60                                  |
|                 | <b>Item 1A.</b>                     | 63                                  |
|                 | <b>Item 2.</b>                      | 64                                  |
|                 | <b>Item 3.</b>                      | 64                                  |
|                 | <b>Item 4.</b>                      | 64                                  |

|                                 |                          |    |
|---------------------------------|--------------------------|----|
| <b>Item 5.</b>                  | <u>Other Information</u> | 64 |
| <b>Item 6.</b>                  | <u>Exhibits</u>          | 65 |
| <b><u>Signatures</u></b>        |                          | 66 |
| <b><u>Index to Exhibits</u></b> |                          | 67 |

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS***(In thousands, except share data)**(Unaudited)*

|  | March 31, 2013 | December 31, 2012 |
|--|----------------|-------------------|
| <b>ASSETS</b>  |                |                   |
| <i>Current assets</i>  |                |                   |
| Cash and cash equivalents  | \$ 285,048     | \$ 387,813        |
| Patient accounts receivable, net of allowance for doubtful accounts of \$2,258,229 and \$2,201,875 at March 31, 2013 and December 31, 2012, respectively | 2,215,198      | 2,067,379         |
| Supplies   | 371,055        | 368,172           |
| Prepaid income taxes   | -              | 49,888            |
| Deferred income taxes  | 117,045        | 117,045           |
| Prepaid expenses and taxes   | 142,366        | 126,561           |
| Other current assets   | 288,071        | 302,284           |
| Total current assets   | 3,418,783      | 3,419,142         |
| <i>Property and equipment</i>  |                |                   |
| Less accumulated depreciation and amortization   | (3,121,782)    | (2,993,535)       |
| Property and equipment, net  | 7,095,134      | 7,151,873         |
| <i>Goodwill</i>  |                |                   |
|  | 4,408,362      | 4,408,138         |
| <i>Other assets, net</i>   |                |                   |
|  | 1,674,923      | 1,627,182         |
| Total assets   | \$ 16,597,202  | \$ 16,606,335     |
| <b>LIABILITIES AND EQUITY</b>  |                |                   |
| <i>Current liabilities</i>   |                |                   |
| Current maturities of long-term debt   | \$ 113,801     | \$ 89,911         |
| Accounts payable   | 741,175        | 825,914           |
| Income tax payable   | 5,924          | -                 |
| Accrued interest   | 109,939        | 110,702           |
| Accrued liabilities  | 1,038,081      | 1,116,693         |
| Total current liabilities  | 2,008,920      | 2,143,220         |
| <i>Long-term debt</i>  |                |                   |
|  | 9,424,383      | 9,451,394         |
| <i>Deferred income taxes</i>   |                |                   |
|  | 808,489        | 808,489           |
| <i>Other long-term liabilities</i>   |                |                   |
|  | 1,039,365      | 1,039,045         |

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|   |               |               |
|---|---------------|---------------|
| <i>Total liabilities</i>  | 13,281,157    | 13,442,148    |
| <i>Redeemable noncontrolling interests in equity of consolidated subsidiaries</i>   | 375,506       | 367,666       |
| <b>EQUITY</b>   |               |               |
| <i>Community Health Systems, Inc. stockholders' equity</i>  |               |               |
| Preferred stock, \$.01 par value per share, 100,000,000 shares authorized; none issued  | -             | -             |
| Common stock, \$.01 par value per share, 300,000,000 shares authorized; 95,042,056 shares issued and 94,066,507 shares outstanding at March 31, 2013, and 92,925,715 shares issued and 91,950,166 shares outstanding at December 31, 2012 | 950           | 929           |
| Additional paid-in capital  | 1,187,535     | 1,138,274     |
| Treasury stock, at cost, 975,549 shares at March 31, 2013 and December 31, 2012   | (6,678)       | (6,678)       |
| Accumulated other comprehensive loss  | (126,998)     | (145,310)     |
| Retained earnings   | 1,823,166     | 1,743,992     |
| <br>  |               |               |
| Total Community Health Systems, Inc. stockholders' equity   | 2,877,975     | 2,731,207     |
| <i>Noncontrolling interests in equity of consolidated subsidiaries</i>  | 62,564        | 65,314        |
| <br>  |               |               |
| <i>Total equity</i>   | 2,940,539     | 2,796,521     |
| <br>  |               |               |
| <i>Total liabilities and equity</i>   | \$ 16,597,202 | \$ 16,606,335 |

See accompanying notes to the condensed consolidated financial statements.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME***(In thousands, except share and per share data)**(Unaudited)*

|  | <b>Three Months Ended<br/>March 31,</b> |              |
|--|---|--------------|
|  | <b>2013</b>                             | <b>2012</b>  |
| Operating revenues (net of contractual allowances and discounts)   | \$ 3,799,864                            | \$ 3,783,491 |
| Provision for bad debts  | 488,114                                 | 486,456      |
| <i>Net operating revenues</i>  | 3,311,750                               | 3,297,035    |
| <i>Operating costs and expenses:</i>   |   |              |
| Salaries and benefits  | 1,577,148                               | 1,524,975    |
| Supplies   | 497,841                                 | 498,579      |
| Other operating expenses   | 707,974                                 | 708,943      |
| Electronic health records incentive reimbursement  | (20,916)                                | (26,168)     |
| Rent   | 71,554                                  | 67,224       |
| Depreciation and amortization  | 192,158                                 | 174,354      |
| Total operating costs and expenses   | 3,025,759                               | 2,947,907    |
| <i>Income from operations</i>  | 285,991                                 | 349,128      |
| <i>Interest expense, net</i>   | 156,350                                 | 152,175      |
| <i>Loss from early extinguishment of debt</i>  | 1,295                                   | 63,429       |
| <i>Equity in earnings of unconsolidated affiliates</i>   | (15,680)                                | (12,013)     |
| <i>Income from continuing operations before income taxes</i>   | 144,026                                 | 145,537      |
| <i>Provision for income taxes</i>  | 47,703                                  | 45,819       |
| <i>Income from continuing operations</i>   | 96,323                                  | 99,718       |
| <i>Discontinued operations, net of taxes:</i>  |   |              |
| Loss from operations of entities sold  | -                                       | (466)        |
| <i>Loss from discontinued operations, net of taxes</i>   | -                                       | (466)        |
| <i>Net income</i>  | 96,323                                  | 99,252       |
| Less: Net income attributable to noncontrolling interests  | 17,149                                  | 23,778       |
| Net income attributable to Community Health Systems, Inc. stockholders                                     | \$ 79,174                               | \$ 75,474    |
| <i>Basic earnings (loss) per share attributable to Community Health Systems, Inc. common stockholders:</i> |   |              |
| Continuing operations  | \$ 0.87                                 | \$ 0.86      |
| Discontinued operations  | -                                       | (0.01)       |

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|            |    |      |    |      |
|------------|----|------|----|------|
| Net income | \$ | 0.87 | \$ | 0.85 |
|------------|----|------|----|------|

*Diluted earnings (loss) per share attributable to Community Health Systems, Inc. common stockholders(1):*

|                         |    |      |    |        |
|-------------------------|----|------|----|--------|
| Continuing operations   | \$ | 0.86 | \$ | 0.85   |
| Discontinued operations |    | -    |    | (0.01) |

|            |    |      |    |      |
|------------|----|------|----|------|
| Net income | \$ | 0.86 | \$ | 0.85 |
|------------|----|------|----|------|

*Weighted-average number of shares outstanding:*

|       |  |            |  |            |
|-------|--|------------|--|------------|
| Basic |  | 91,002,615 |  | 88,674,779 |
|-------|--|------------|--|------------|

|         |  |            |  |            |
|---------|--|------------|--|------------|
| Diluted |  | 91,998,993 |  | 88,852,704 |
|---------|--|------------|--|------------|

(1) Total per share amounts may not add due to rounding.

See accompanying notes to the condensed consolidated financial statements.



**Table of Contents**

**COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

*(In thousands)*

*(Unaudited)*

|  | <b>Three Months Ended<br/>March 31,</b> |             |
|--|---|-------------|
|  | <b>2013</b>                             | <b>2012</b> |
| Net income   | \$ 96,323                               | \$ 99,252   |
| Other comprehensive income, net of income taxes:                                 |   |             |
| Net change in fair value of interest rate swaps                                  | 15,770                                  | 10,536      |
| Net change in fair value of available-for-sale securities                        | 1,809                                   | 2,667       |
| Amortization and recognition of unrecognized pension cost components             | 733                                     | 1,140       |
| Other comprehensive income   | 18,312                                  | 14,343      |
| Comprehensive income   | 114,635                                 | 113,595     |
| Less: Comprehensive income attributable to noncontrolling interests              | 17,149                                  | 23,778      |
| Comprehensive income attributable to Community Health Systems, Inc. stockholders | \$ 97,486                               | \$ 89,817   |

See accompanying notes to the condensed consolidated financial statements.

**Table of Contents**

**COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

*(In thousands)*

*(Unaudited)*

|   | <b>Three Months Ended</b> |             |
|---|---------------------------|-------------|
|   | <b>March 31,</b>          |             |
|   | <b>2013</b>               | <b>2012</b> |
| <i>Cash flows from operating activities</i>   |                           |             |
| Net income  | \$ 96,323                 | \$ 99,252   |
| Adjustments to reconcile net income to net cash provided by operating activities:             |                           |             |
| Depreciation and amortization   | 192,158                   | 174,354     |
| Stock-based compensation expense  | 9,958                     | 10,495      |
| Loss from early extinguishment of debt  | 1,295                     | 63,429      |
| Excess tax benefit relating to stock-based compensation                                       | (5,358)                   | (1,004)     |
| Other non-cash expenses, net  | 5,269                     | 2,569       |
| Changes in operating assets and liabilities, net of effects of acquisitions and divestitures: |                           |             |
| Patient accounts receivable   | (147,805)                 | (163,484)   |
| Supplies, prepaid expenses and other current assets   | (1,752)                   | (125,111)   |
| Accounts payable, accrued liabilities and income taxes  | (97,678)                  | 96,109      |
| Other   | 4,744                     | 30,701      |
| Net cash provided by operating activities   | 57,154                    | 187,310     |
| <i>Cash flows from investing activities</i>   |                           |             |
| Acquisitions of facilities and other related equipment  | (4,750)                   | (248,436)   |
| Purchases of property and equipment   | (112,859)                 | (184,903)   |
| Proceeds from sale of property and equipment  | 714                       | 748         |
| Increase in other investments   | (69,483)                  | (67,708)    |
| Net cash used in investing activities   | (186,378)                 | (500,299)   |
| <i>Cash flows from financing activities</i>   |                           |             |
| Proceeds from exercise of stock options   | 73,429                    | 308         |
| Repurchase of restricted stock shares for payroll tax withholding requirements                | (14,478)                  | (9,032)     |
| Stock buy-back  | (18,726)                  | -           |
| Deferred financing costs  | (878)                     | (24,787)    |
| Excess tax benefit relating to stock-based compensation                                       | 5,358                     | 1,004       |
| Redemption of noncontrolling investments in joint ventures                                    | (436)                     | (31,096)    |
| Distributions to noncontrolling investors in joint ventures                                   | (15,291)                  | (27,038)    |
| Borrowings under credit agreements  | 100,893                   | 2,704,337   |
| Issuance of long-term debt  | -                         | 1,025,000   |
| Proceeds from receivables facility  | 300,000                   | 300,000     |
| Repayments of long-term indebtedness  | (403,412)                 | (3,626,274) |
| Net cash provided by financing activities   | 26,459                    | 312,422     |

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|  |    |           |    |         |
|--|----|-----------|----|---------|
| <i>Net change in cash and cash equivalents</i>           |    | (102,765) |    | (567)   |
| <i>Cash and cash equivalents at beginning of period</i>  |    | 387,813   |    | 129,865 |
| <i>Cash and cash equivalents at end of period</i>        | \$ | 285,048   | \$ | 129,298 |
| <i>Supplemental disclosure of cash flow information:</i> |    |           |    |         |
| Interest payments  | \$ | 149,735   | \$ | 161,140 |
| Income tax refunds received, net                         | \$ | (448)     | \$ | (61)    |

See accompanying notes to the condensed consolidated financial statements.

**Table of Contents**

**COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES**

The unaudited condensed consolidated financial statements of Community Health Systems, Inc. and its subsidiaries (the Company) as of March 31, 2013 and December 31, 2012 and for the three-month periods ended March 31, 2013 and March 31, 2012, have been prepared in accordance with accounting principles generally accepted in the United States of America ( U.S. GAAP ). In the opinion of management, such information contains all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the results for such periods. All intercompany transactions and balances have been eliminated. The results of operations for the three months ended March 31, 2013, are not necessarily indicative of the results to be expected for the full fiscal year ending December 31, 2013. Certain information and disclosures normally included in the notes to consolidated financial statements have been condensed or omitted as permitted by the rules and regulations of the Securities and Exchange Commission (the SEC ). The Company believes the disclosures are adequate to make the information presented not misleading. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2012, contained in the Company's Annual Report on Form 10-K.

Noncontrolling interests in less-than-wholly-owned consolidated subsidiaries of the parent are presented as a component of total equity on the condensed consolidated balance sheets to distinguish between the interests of the parent company and the interests of the noncontrolling owners. Noncontrolling interests that are redeemable or may become redeemable at a fixed or determinable price at the option of the holder or upon the occurrence of an event outside of the control of the Company are presented in mezzanine equity on the condensed consolidated balance sheets.

Throughout these notes to the condensed consolidated financial statements, Community Health Systems, Inc. (the Parent ), and its consolidated subsidiaries are referred to on a collective basis as the Company. This drafting style is not meant to indicate that the publicly-traded Parent or any subsidiary of the Parent owns or operates any asset, business, or property. The hospitals, operations and businesses described in this filing are owned and operated, and management services provided, by distinct and indirect subsidiaries of Community Health Systems, Inc.

*Allowance for Doubtful Accounts.* Accounts receivable are reduced by an allowance for amounts that could become uncollectible in the future. Substantially all of the Company's receivables are related to providing healthcare services to its hospitals' patients.

The Company estimates the allowance for doubtful accounts by reserving a percentage of all self-pay accounts receivable without regard to aging category, based on collection history, adjusted for expected recoveries and, if present, anticipated changes in trends. For all other non-self-pay payor categories, the Company reserves 100% of all accounts aging over 365 days from the date of discharge. The percentage used to reserve for all self-pay accounts is based on the Company's collection history. The Company collects substantially all of its third-party insured receivables, which include receivables from governmental agencies.

Collections are impacted by the economic ability of patients to pay and the effectiveness of the Company's collection efforts. Significant changes in payor mix, business office operations, economic conditions or trends in federal and state governmental healthcare coverage could affect the Company's collection of accounts receivable and the estimates of the collectability of future accounts receivable. The process of estimating the allowance for doubtful accounts requires the Company to estimate the collectability of self-pay accounts receivable, which is primarily based on its collection history, adjusted for expected recoveries and, if available, anticipated changes in collection trends. The Company also continually reviews its overall reserve adequacy by monitoring historical cash collections as a percentage of trailing net revenue less provision for bad debts, as well as by analyzing current period net revenue and admissions by payor classification, aged accounts receivable by payor, days revenue outstanding, and the impact of recent acquisitions and dispositions.

Operating revenues, net of contractual allowances and discounts (but before the provision for bad debts), recognized during the three months ended March 31, 2013 and 2012, were as follows (in thousands):

**Three Months Ended  
March 31,**

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|   | <b>2013</b>         | <b>2012</b>         |
|---|---------------------|---------------------|
| Medicare                                  | \$ 992,893          | \$ 1,064,157        |
| Medicaid                                  | 332,349             | 315,092             |
| Managed Care and other third-party payors | 1,965,858           | 1,906,487           |
| Self-pay                                  | 508,764             | 497,755             |
| <b>Total</b>                              | <b>\$ 3,799,864</b> | <b>\$ 3,783,491</b> |

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

*Electronic Health Records Incentive Reimbursement.* The American Recovery and Reinvestment Act of 2009 included provisions for implementing health information technology under the Health Information Technology for Economic and Clinical Health Act ( HITECH ). These provisions were designed to increase the use of electronic health records ( EHR ) technology and establish the requirements for a Medicare and Medicaid incentive payments program beginning in 2011 for eligible hospitals and providers that adopt and meaningfully use certified EHR technology. Eligibility for annual Medicare incentive payments is dependent on providers demonstrating meaningful use of EHR technology in each period over a four-year period. Initial Medicaid incentive payments are available to providers that adopt, implement or upgrade certified EHR technology; but providers must demonstrate meaningful use of such technology in subsequent years to qualify for additional incentive payments. Medicaid EHR incentive payments are fully funded by the federal government and administered by the states; however, the states are not required to offer EHR incentive payments to providers.

The Company recognized approximately \$20.9 million and \$26.2 million during the three months ended March 31, 2013 and 2012, respectively, of incentive reimbursement for HITECH incentives from Medicare and Medicaid related to certain of the Company's hospitals and for certain of the Company's employed physicians that have demonstrated meaningful use of certified EHR technology or have completed attestations to their adoption or implementation of certified EHR technology. These incentive reimbursements are presented as a reduction of operating costs and expenses on the condensed consolidated statements of income. The Company received cash related to the incentive reimbursement for HITECH incentives of approximately \$45.1 million and \$5.8 million for the three months ended March 31, 2013 and 2012, respectively, of which \$19.9 million and \$1.0 million was recorded as deferred revenue as all criteria for gain recognition had not been met, for the three months ended March 31, 2013 and 2012, respectively.

*Reimbursement Settlement.* Included in net operating revenues for the three months ended March 31, 2012 on a non-same store basis is approximately \$101.8 million of net operating revenues from an industry-wide settlement with the United States Department of Health and Human Services and Centers for Medicare and Medicaid Services, based on a claim that acute-care hospitals in the U.S. were underpaid from the Medicare inpatient prospective payment system in federal fiscal years 1999 through 2011. The underpayments resulted from calculations related to the rural floor budget neutrality adjustments implemented in connection with the Balanced Budget Act of 1997. Also included in net operating revenues for the three months ended March 31, 2012 is an unfavorable adjustment of approximately \$21.0 million related to the revised Supplemental Security Income ratios issued for federal fiscal years 2006 through 2009 utilized for calculating Medicare Disproportionate Share Hospital reimbursements.

**2. ACCOUNTING FOR STOCK-BASED COMPENSATION**

Stock-based compensation awards are granted under the Community Health Systems, Inc. Amended and Restated 2000 Stock Option and Award Plan, amended and restated as of March 20, 2013 (the 2000 Plan ), and the Community Health Systems, Inc. 2009 Stock Option and Award Plan, amended and restated as of March 20, 2013 (the 2009 Plan ).

The 2000 Plan allows for the grant of incentive stock options intended to qualify under Section 422 of the Internal Revenue Code (the IRC ), as well as stock options which do not so qualify, stock appreciation rights, restricted stock, restricted stock units, performance-based shares or units and other share awards. Prior to being amended in 2009, the 2000 Plan also allowed for the grant of phantom stock. Persons eligible to receive grants under the 2000 Plan include the Company's directors, officers, employees and consultants. To date, all options granted under the 2000 Plan have been nonqualified stock options for tax purposes. Generally, vesting of these granted options occurs in one-third increments on each of the first three anniversaries of the award date. Options granted prior to 2005 have a 10-year contractual term, options granted in 2005 through 2007 have an eight-year contractual term and options granted in 2008 or later have a 10-year contractual term. As of March 31, 2013, 814,471 shares of unissued common stock were reserved for future grants under the 2000 Plan. Contingent upon the approval by the Company's stockholders of the March 20, 2013 amendment and restatement of the 2009 Plan, no further shares will be awarded under the 2000 plan.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

The 2009 Plan provides for the grant of incentive stock options intended to qualify under Section 422 of the IRC and for the grant of stock options which do not so qualify, stock appreciation rights, restricted stock, restricted stock units, performance-based shares or units and other share awards. Persons eligible to receive grants under the 2009 Plan include the Company's directors, officers, employees and consultants. To date, all options granted under the 2009 Plan have been nonqualified stock options for tax purposes. Generally, vesting of these granted options occurs in one-third increments on each of the first three anniversaries of the award date. Options granted in 2011 or later have a 10-year contractual term. As of March 31, 2013, 3,342,567 shares of unissued common stock were reserved for future grants under the 2009 Plan, assuming the Company's stockholders approve the March 20, 2013 amendment and restatement of the 2009 Plan, which will add 3,000,000 additional shares for future grants.

The exercise price of all options granted is equal to the fair value of the Company's common stock on the option grant date.

The following table reflects the impact of total compensation expense related to stock-based equity plans on the reported operating results for the respective periods (in thousands):

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2013</b>                             | <b>2012</b> |
| Effect on income from continuing operations before income taxes | \$ (9,958)                              | \$ (10,495) |
| Effect on net income  | \$ (6,254)                              | \$ (6,664)  |

At March 31, 2013, \$57.1 million of unrecognized stock-based compensation expense was expected to be recognized over a weighted-average period of 26 months. Of that amount, \$5.3 million related to outstanding unvested stock options was expected to be recognized over a weighted-average period of 15 months and \$51.8 million related to outstanding unvested restricted stock and restricted stock units was expected to be recognized over a weighted-average period of 27 months. There were no modifications to awards during the three months ended March 31, 2013.

The fair value of stock options granted was estimated using the Black Scholes option pricing model with the following assumptions during the three-months ended March 31, 2013 and 2012:

|                         | <b>Three Months Ended<br/>March 31,</b> |             |
|-------------------------|---|-------------|
|                         | <b>2013 (1)</b>                         | <b>2012</b> |
| Expected volatility     | -                                       | 57.7 %      |
| Expected dividends      | -                                       | -           |
| Expected term           | -                                       | 4.1 years   |
| Risk-free interest rate | -                                       | 0.7 %       |

(1) No stock options were granted during the three months ended March 31, 2013.

In determining the expected term, the Company examined concentrations of option holdings and historical patterns of option exercises and forfeitures, as well as forward-looking factors, in an effort to determine if there were any discernible employee populations. From this analysis, the Company identified two primary employee populations, one consisting of certain senior executives and the other one consisting of

substantially all other recipients.

The expected volatility rate was estimated based on historical volatility. In determining expected volatility, the Company also reviewed the market-based implied volatility of actively traded options of its common stock and determined that historical volatility utilized to estimate the expected volatility rate did not differ significantly from the implied volatility.

The expected term computation is based on historical exercise and cancellation patterns and forward-looking factors, where present, for each population identified. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of the grant. The pre-vesting forfeiture rate is based on historical rates and forward-looking factors for each population identified. The Company adjusts the estimated forfeiture rate to its actual experience.



**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

Options outstanding and exercisable under the 2000 Plan and the 2009 Plan as of March 31, 2013, and changes during the three-month period following December 31, 2012, were as follows (in thousands, except share and per share data):

|                                  | Shares      | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | Aggregate Intrinsic Value as of March 31, 2013 |
|----------------------------------|-------------|---------------------------------|---|--|
| Outstanding at December 31, 2012 | 7,104,113   | \$ 34.25                        |   |  |
| Granted                          | -           | -                               |   |  |
| Exercised                        | (2,248,891) | 32.53                           |   |  |
| Forfeited and cancelled          | (20,010)    | 35.93                           |   |  |
| Outstanding at March 31, 2013    | 4,835,212   | 34.98                           | 4.6 years                                   | \$ 60,000                                      |
| Exercisable at March 31, 2013    | 4,166,134   | \$ 35.67                        | 4.0 years                                   | \$ 48,825                                      |

The weighted-average grant date fair value of stock options granted during the three months ended March 31, 2012 was \$9.15. No stock options were granted during the three months ended March 31, 2013. The aggregate intrinsic value (the number of in-the-money stock options multiplied by the difference between the Company's closing stock price on the last trading day of the reporting period (\$47.39) and the exercise price of the respective stock options) in the table above represents the amount that would have been received by the option holders had all option holders exercised their options on March 31, 2013. This amount changes based on the market value of the Company's common stock. The aggregate intrinsic value of options exercised during the three months ended March 31, 2013 and 2012 was \$19.3 million and \$0.1 million, respectively. The aggregate intrinsic value of options vested and expected to vest approximates that of the outstanding options.

The Company has also awarded restricted stock under the 2000 Plan and the 2009 Plan to its directors and employees of certain subsidiaries. The restrictions on these shares generally lapse in one-third increments on each of the first three anniversaries of the award date. Certain of the restricted stock awards granted to the Company's senior executives contain a performance objective that must be met in addition to any vesting requirements. If the performance objective is not attained, the awards will be forfeited in their entirety. Once the performance objective has been attained, restrictions will lapse in one-third increments on each of the first three anniversaries of the award date. Notwithstanding the above-mentioned performance objectives and vesting requirements, the restrictions will lapse earlier in the event of death, disability or termination of employment by the Company for any reason other than for cause of the holder of the restricted stock, or change in control of the Company. Restricted stock awards subject to performance standards are not considered outstanding for purposes of determining earnings per share until the performance objectives have been satisfied.

Restricted stock outstanding under the 2000 Plan and the 2009 Plan as of March 31, 2013, and changes during the three-month period following December 31, 2012, were as follows:

|                               | Shares    | Weighted-Average Grant Date Fair Value |
|-------------------------------|-----------|--|
| Unvested at December 31, 2012 | 1,744,564 | \$ 30.50                               |
| Granted                       | 786,588   | 41.49                                  |
| Vested                        | (913,970) | 32.38                                  |

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Forfeited

-

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Unvested at March 31, 2013

1,617,182

34.79

Table of Contents

## COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED

Restricted stock units ( RSUs ) have been granted to the Company's outside directors under the 2000 Plan and the 2009 Plan. On February 23, 2011, each of the Company's outside directors received a grant under the 2009 Plan of 3,688 RSUs. On February 16, 2012, each of the Company's outside directors received a grant under the 2009 Plan of 6,645 RSUs. On February 27, 2013, each of the Company's outside directors received a grant under the 2009 Plan of 3,596 RSUs. Vesting of these shares of RSUs occurs in one-third increments on each of the first three anniversaries of the award date.

RSUs outstanding under the 2000 Plan and the 2009 Plan as of March 31, 2013, and changes during the three-month period following December 31, 2012, were as follows:

|                               | Shares   |    | Weighted-<br>Average Grant<br>Date Fair Value |
|-------------------------------|----------|----|---|
| Unvested at December 31, 2012 | 62,886   | \$ | 26.72   |
| RSUs Granted                  | 21,576   |    | 41.71   |
| Vested                        | (28,926) |    | 29.04   |
| Forfeited                     | -        |    | -   |
| Unvested at March 31, 2013    | 55,536   |    | 31.33   |

Under the Directors' Fees Deferral Plan, the Company's outside directors may elect to receive share equivalent units in lieu of cash for their directors' fees. These share equivalent units are held in the plan until the director electing to receive the share equivalent units retires or otherwise terminates his/her directorship with the Company. Share equivalent units are converted to shares of common stock of the Company at the time of distribution based on the closing market price of the Company's common stock on that date. The following table represents the amount of directors' fees which were deferred during each of the respective periods, and the number of share equivalent units into which such directors' fees would have converted had each of the directors who had deferred such fees retired or terminated his/her directorship with the Company as of the end of the respective periods (in thousands, except share equivalent units):

|   | Three Months Ended<br>March 31, |       |
|---|---------------------------------|-------|
|   | 2013                            | 2012  |
| Directors' fees earned and deferred into plan | \$ 33                           | \$ 28 |
| Share equivalent units                        | 686                             | 1,237 |

At March 31, 2013, a total of 28,755 share equivalent units were deferred in the plan with an aggregate fair value of \$1.4 million, based on the closing market price of the Company's common stock at March 31, 2013 of \$47.39.

**3. COST OF REVENUE**

Substantially all of the Company's operating costs and expenses are cost of revenue items. Operating costs that could be classified as general and administrative by the Company would include the Company's corporate office costs at its Franklin, Tennessee office, which were \$45.4 million and \$47.6 million for the three months ended March 31, 2013 and 2012, respectively. Included in these amounts is stock-based compensation expense of \$10.0 million and \$10.5 million for the three months ended March 31, 2013 and 2012, respectively.

**4. USE OF ESTIMATES**

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements. Actual results could differ from these estimates under different assumptions or conditions.

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**Table of Contents**

**COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

**5. ACQUISITIONS AND DIVESTITURES**

*Acquisitions*

The Company accounts for all transactions that represent business combinations using the acquisition method of accounting, where 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 the Company obtains control in the acquiree. Such fair values that are not finalized for reporting periods following the acquisition date are estimated and recorded as provisional amounts. Adjustments to these provisional amounts during the measurement period (defined as the date through which all information required to identify and measure the consideration transferred, the assets acquired, the liabilities assumed and any noncontrolling interests has been obtained, limited to one year from the acquisition date) are recorded as of the date of acquisition. Any material impact to comparative information for periods after acquisition, but before the period in which adjustments are identified, is reflected in those prior periods as if the adjustments were considered as of the acquisition date. Goodwill is determined as the excess of the fair value of the consideration conveyed in the acquisition over the fair value of the net assets acquired.

Effective July 1, 2012, one or more subsidiaries of the Company completed the acquisition of Memorial Health Systems in York, Pennsylvania. This healthcare system includes Memorial Hospital (100 licensed beds), the Surgical Center of York, and other outpatient and ancillary services. As part of this purchase agreement, the Company has agreed to spend at least \$75.0 million to build a replacement hospital within five years of the closing date. The total cash consideration paid for fixed assets and working capital was approximately \$45.0 million and \$2.6 million, respectively, with additional consideration of \$12.5 million assumed in liabilities, for a total consideration of \$60.1 million. Based upon the Company's preliminary purchase price allocation relating to this acquisition as of March 31, 2013, approximately \$10.3 million of goodwill has been recorded. The preliminary allocation of the purchase price has been determined by the Company based on available information and is subject to settling amounts related to purchased working capital and final appraisals of tangible and intangible assets. Adjustments to the purchase price allocation are not expected to be material.

Effective March 5, 2012, one or more subsidiaries of the Company completed a merger with Diagnostic Clinic of Longview, P.A., which is a multi-specialty clinic serving residents of Longview, Texas and surrounding East Texas communities. This merger was accounted for as a purchase business combination. The total cash consideration paid for the business, including net working capital, was approximately \$52.3 million, with additional consideration of \$6.9 million assumed in liabilities, for a total consideration of \$59.2 million. Based upon the Company's final purchase price allocation relating to this acquisition, approximately \$41.8 million of goodwill has been recorded.

Effective March 1, 2012, one or more subsidiaries of the Company completed the acquisition of MetroSouth Medical Center (330 licensed beds) located in Blue Island, Illinois. The total cash consideration paid for fixed assets was approximately \$39.3 million with additional consideration of \$5.8 million assumed in liabilities as well as a credit applied at closing of \$0.9 million for negative acquired working capital, for a total consideration of \$44.2 million. Based upon the Company's preliminary purchase price allocation relating to this acquisition as of March 31, 2013, no goodwill has been recorded. The preliminary allocation of the purchase price has been determined by the Company based on available information and is subject to settling amounts related to purchased working capital and final appraisals of tangible and intangible assets. Adjustments to the purchase price allocation are not expected to be material.

Effective January 1, 2012, one or more subsidiaries of the Company completed the acquisition of Moses Taylor Healthcare System based in Scranton, Pennsylvania, which is a healthcare system comprised of two acute care hospitals and other healthcare providers. This healthcare system includes Moses Taylor Hospital (217 licensed beds) located in Scranton, Pennsylvania, and Mid-Valley Hospital (25 licensed beds) located in Peckville, Pennsylvania. The total cash consideration paid for fixed assets and working capital was approximately \$151.1 million and \$13.1 million, respectively, with additional consideration of \$9.4 million assumed in liabilities, for a total consideration of \$173.6 million. Based upon the Company's final purchase price allocation relating to this acquisition, approximately \$54.6 million of goodwill has been recorded.

Additionally, during the three months ended March 31, 2013, the Company paid approximately \$1.4 million to acquire the operating assets and related businesses of certain physician practices, clinics and other ancillary businesses that operate within the communities served by its hospitals. In connection with these acquisitions, the Company allocated approximately \$0.5 million of the consideration paid to property and equipment, \$0.4 million to net working capital, and the remainder, approximately \$0.5 million consisting of intangible assets that do not qualify for separate recognition, was allocated to goodwill. These acquisition transactions were accounted for as purchase business combinations.



**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

Approximately \$0.6 million and \$4.3 million of acquisition costs related to prospective and closed acquisitions were expensed during the three months ended March 31, 2013 and 2012, respectively, and are included in other operating expenses on the condensed consolidated statements of income.

**6. INCOME TAXES**

The total amount of unrecognized benefit that would affect the effective tax rate, if recognized, was approximately \$0.9 million as of March 31, 2013. A total of approximately \$0.5 million of interest and penalties is included in the amount of the liability for uncertain tax positions at March 31, 2013. It is the Company's policy to recognize interest and penalties related to unrecognized benefits in its condensed consolidated statements of income as income tax expense.

The Company, or one of its subsidiaries, files income tax returns in the United States federal jurisdiction and various state jurisdictions. The Company has extended the federal statute of limitations for Triad Hospitals, Inc. (Triad) for the tax periods ended December 31, 1999, December 31, 2000, April 30, 2001, June 30, 2001, December 31, 2001, December 31, 2002, December 31, 2003 and December 31, 2004. The Internal Revenue Service (the IRS) has concluded its examination of the federal tax return of Triad for the tax periods ended December 31, 2004, December 31, 2005, December 31, 2006 and July 25, 2007. With few exceptions, the Company is no longer subject to state income tax examinations for years prior to 2009 and federal income tax examinations with respect to Community Health Systems, Inc. federal returns for years prior to 2007. The Company's federal income tax returns for the 2007, 2008, 2009 and 2010 tax years are currently under examination by the IRS. The Company anticipates reaching a resolution on the 2007 and 2008 year examinations within the next six months. The Company believes the results of these examinations will not be material to its consolidated results of operations or consolidated financial position.

Cash paid for income taxes, net of refunds received, resulted in a cash refund of \$0.5 million and \$0.1 million during the three months ended March 31, 2013 and 2012, respectively.

**7. GOODWILL AND OTHER INTANGIBLE ASSETS**

The changes in the carrying amount of goodwill for the three months ended March 31, 2013 are as follows (in thousands):

|   |    |           |
|---|----|-----------|
| Balance as of December 31, 2012   | \$ | 4,408,138 |
| Goodwill acquired as part of acquisitions during 2013   |    | 520       |
| Consideration and purchase price allocation adjustments for prior year's acquisitions and other adjustments |    | (296)     |
| Balance as of March 31, 2013  | \$ | 4,408,362 |

Goodwill is allocated to each identified reporting unit, which is defined as an operating segment or one level below the operating segment (referred to as a component of the entity). Management has determined that the Company's operating segments and hospital management services operations meet the criteria to be classified as reporting units. At March 31, 2013, the hospital operations reporting unit, the home care agency operations reporting unit, and the hospital management services reporting unit had approximately \$4.3 billion, \$40.5 million and \$33.3 million, respectively, of goodwill.

Goodwill is evaluated for impairment at the same time every year and when an event occurs or circumstances change that, more likely than not, reduce the fair value of the reporting unit below its carrying value. There is a two-step method for determining goodwill impairment. Step one is to compare the fair value of the reporting unit with the unit's carrying amount, including goodwill. If this test indicates the fair value is less than the carrying value, then step two is required to compare the implied fair value of the reporting unit's goodwill with the carrying value of the

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reporting unit's goodwill. The Company performed its last annual goodwill evaluation during the fourth quarter of 2012. No impairment was indicated by this evaluation. The next annual goodwill evaluation will be performed during the fourth quarter of 2013.



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**Table of Contents**

**COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

The Company estimates the fair value of the related reporting units using both a discounted cash flow model as well as an EBITDA multiple model. The cash flow forecasts are adjusted by an appropriate discount rate based on the Company's estimate of a market participant's weighted-average cost of capital. These models are both based on the Company's best estimate of future revenues and operating costs and are reconciled to the Company's consolidated market capitalization, with consideration of the amount a potential acquirer would be required to pay, in the form of a control premium, in order to gain sufficient ownership to set policies, direct operations and control management decisions.

Approximately \$0.3 million of intangible assets other than goodwill were acquired during the three months ended March 31, 2013. The gross carrying amount of the Company's other intangible assets subject to amortization was \$60.6 million at March 31, 2013 and \$61.9 million at December 31, 2012, and the net carrying amount was \$25.1 million at March 31, 2013 and \$26.3 million at December 31, 2012. The carrying amount of the Company's other intangible assets not subject to amortization was \$48.1 million at March 31, 2013 and \$48.1 million at December 31, 2012. Other intangible assets are included in other assets, net on the Company's consolidated balance sheets. Substantially all of the Company's intangible assets are contract-based intangible assets related to operating licenses, management contracts, or non-compete agreements entered into in connection with prior acquisitions.

The weighted-average amortization period for the intangible assets subject to amortization is approximately eight years. There are no expected residual values related to these intangible assets. Amortization expense on these intangible assets was \$1.4 million and \$1.6 million during the three months ended March 31, 2013 and 2012, respectively. Amortization expense on intangible assets is estimated to be \$4.5 million for the remainder of 2013, \$4.1 million in 2014, \$3.2 million in 2015, \$2.4 million in 2016, \$2.2 million in 2017, \$2.0 million in 2018 and \$6.7 million thereafter.

The gross carrying amount of capitalized software for internal use was approximately \$740.7 million and \$654.4 million at March 31, 2013 and December 31, 2012, respectively, and the net carrying amount considering accumulated amortization was approximately \$411.2 million and \$354.4 million at March 31, 2013 and December 31, 2012, respectively. The estimated amortization period for capitalized internal-use software is generally three years, except for capitalized costs related to significant system conversions, which is generally eight to ten years. There is no expected residual value for capitalized internal-use software. At March 31, 2013, there was approximately \$138.1 million of capitalized costs for internal-use software that is currently in the development stage and will begin amortization once the software project is complete and ready for its intended use. Amortization expense on capitalized internal-use software was \$30.5 million and \$19.7 million during the three months ended March 31, 2013 and 2012, respectively. Amortization expense on capitalized internal-use software is estimated to be \$82.2 million for the remainder of 2013, \$104.4 million in 2014, \$99.6 million in 2015, \$33.0 million in 2016, \$27.3 million in 2017, \$21.1 million in 2018 and \$43.6 million thereafter.

Table of Contents

## COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED

**8. EARNINGS PER SHARE**

The following table sets forth the components of the numerator and denominator for the computation of basic and diluted earnings per share for income from continuing operations, discontinued operations and net income attributable to Community Health Systems, Inc. common stockholders (in thousands, except share data):

|  | <b>Three Months Ended<br/>March 31,</b> |             |
|--|---|-------------|
|  | <b>2013</b>                             | <b>2012</b> |
| <b>Numerator:</b>  |   |             |
| Income from continuing operations, net of taxes  | \$ 96,323                               | \$ 99,718   |
| Less: Income from continuing operations attributable to noncontrolling interests, net of taxes                         | 17,149                                  | 23,778      |
| Income from continuing operations attributable to Community Health Systems, Inc. common stockholders basic and diluted | \$ 79,174                               | \$ 75,940   |
| Loss from discontinued operations, net of taxes  | \$ -                                    | \$ (466)    |
| Less: Loss from discontinued operations attributable to noncontrolling interests, net of taxes                         | -                                       | -           |
| Loss from discontinued operations attributable to Community Health Systems, Inc. common stockholders basic and diluted | \$ -                                    | \$ (466)    |
| <b>Denominator:</b>  |   |             |
| Weighted-average number of shares outstanding basic  | 91,002,615                              | 88,674,779  |
| Effect of dilutive securities:   |   |             |
| Restricted stock awards  | 281,447                                 | 21,233      |
| Employee stock options   | 705,189                                 | 147,440     |
| Other equity-based awards  | 9,742                                   | 9,252       |
| Weighted-average number of shares outstanding diluted  | 91,998,993                              | 88,852,704  |

|  | <b>Three Months Ended<br/>March 31,</b> |             |
|--|---|-------------|
|  | <b>2013</b>                             | <b>2012</b> |
| <b>Dilutive securities outstanding not included in the computation of earnings per share because their effect is antidilutive:</b> |   |             |
| Employee stock options and restricted stock awards   | -                                       | 6,869,031   |

**9. STOCKHOLDERS EQUITY**

Authorized capital shares of the Company include 400,000,000 shares of capital stock consisting of 300,000,000 shares of common stock and 100,000,000 shares of preferred stock. Each of the aforementioned classes of capital stock has a par value of \$0.01 per share. Shares of preferred stock, none of which were outstanding as of March 31, 2013, may be issued in one or more series having such rights, preferences and other provisions as determined by the Board of Directors without approval by the holders of common stock.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

On December 14, 2011, the Company adopted a new open market repurchase program for up to 4,000,000 shares of the Company's common stock, not to exceed \$100 million in repurchases. The new repurchase program will conclude at the earliest of three years from the commencement date, when the maximum number of shares has been repurchased, or when the maximum dollar amount of repurchases has been expended. During the three months ended March 31, 2013, the Company repurchased and retired 523,023 shares at a weighted-average price of \$35.76 per share, which is the cumulative number of shares repurchased and retired under this program. No shares were repurchased under this program during the three months ended March 31, 2012.

Historically, the Company has not paid any cash dividends. In December 2012, the Company declared and paid a special dividend of \$0.25 per share to holders of its common stock at the close of business as of December 17, 2012, which totaled approximately \$23.0 million. In the foreseeable future, the Company does not anticipate the payment of any other cash dividends. The Company's Credit Facility limits the Company's ability to pay dividends and/or repurchase stock to an amount not to exceed \$150 million in the aggregate plus the aggregate amount of proceeds from the exercise of stock options. The indentures governing the 8% Senior Notes due 2019 and the 7<sup>1</sup>/<sub>8</sub>% Senior Notes due 2020 (collectively, the Senior Notes) and the 5% Senior Secured Notes due 2018 also limit the Company's ability to pay dividends and/or repurchase stock. As of March 31, 2013, under the most restrictive test under these agreements, the Company has approximately \$233.1 million remaining available with which to pay permitted dividends and/or repurchase shares of stock or its Senior Notes.

The following schedule presents the reconciliation of the carrying amount of total equity, equity attributable to the Company, and equity attributable to the noncontrolling interests for the three-month period ended March 31, 2013 (in thousands):

**Community Health Systems, Inc. Stockholders**

|   | <b>Redeemable<br/>Noncontrolling<br/>Interest</b> | <b>Common<br/>Stock</b> | <b>Additional<br/>Paid-In<br/>Capital</b> | <b>Treasury<br/>Stock</b> | <b>Accumulated<br/>Other<br/>Comprehensive<br/>Income (Loss)</b> | <b>Retained<br/>Earnings</b> | <b>Noncontrolling<br/>Interest</b> | <b>Total<br/>Stockholders<br/>Equity</b> |
|---|---|-------------------------|---|---------------------------|--|------------------------------|------------------------------------|--|
| <b>Balance,<br/>December 31,<br/>2012</b>                       | \$ 367,666  | \$ 929                  | \$ 1,138,274                              | \$ (6,678)                | \$ (145,310)   | \$ 1,743,992                 | \$ 65,314                          | \$ 2,796,521                             |
| Comprehensive income  | 11,746  | -                       | -   | -                         | 18,312   | 79,174                       | 5,403                              | 102,889                                  |
| Distributions to noncontrolling interests, net of contributions | (9,455)   | -                       | -   | -                         | -  | -                            | (5,837)                            | (5,837)                                  |
| Purchase of subsidiary shares from noncontrolling interests     | (291)   | -                       | (146)                                     | -                         | -  | -                            | 1                                  | (145)                                    |
| Other reclassifications of noncontrolling interests             | 2,317   | -                       | -   | -                         | -  | -                            | (2,317)                            | (2,317)                                  |

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|   |                   |               |                     |                   |                     |                     |                  |                     |
|---|-------------------|---------------|---------------------|-------------------|---------------------|---------------------|------------------|---------------------|
| Adjustment to redemption value of redeemable noncontrolling interests     | 3,523             | -             | (3,523)             | -                 | -                   | -                   | -                | (3,523)             |
| Repurchases of common stock   | -                 | (5)           | (18,726)            | -                 | -                   | -                   | -                | (18,731)            |
| Issuance of common stock in connection with the exercise of stock options | -                 | 22            | 73,429              | -                 | -                   | -                   | -                | 73,451              |
| Cancellation of restricted stock for tax withholdings on vested shares    | -                 | (4)           | (14,478)            | -                 | -                   | -                   | -                | (14,482)            |
| Excess tax benefit from exercise of stock options                         | -                 | -             | 2,747               | -                 | -                   | -                   | -                | 2,747               |
| Share-based compensation  | -                 | 8             | 9,958               | -                 | -                   | -                   | -                | 9,966               |
| <b>Balance, March 31, 2013</b>  | <b>\$ 375,506</b> | <b>\$ 950</b> | <b>\$ 1,187,535</b> | <b>\$ (6,678)</b> | <b>\$ (126,998)</b> | <b>\$ 1,823,166</b> | <b>\$ 62,564</b> | <b>\$ 2,940,539</b> |

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

The following schedule discloses the effects of changes in the Company's ownership interest in its less-than-wholly-owned subsidiaries on Community Health Systems, Inc. stockholders' equity (in thousands):

|   | <b>Three Months Ended<br/>March 31, 2013</b> |        |
|---|--|--------|
| Net income attributable to Community Health Systems, Inc. stockholders  | \$   | 79,174 |
| Transfers to the noncontrolling interests:  |  |        |
| Net decrease in Community Health Systems, Inc. paid-in capital for purchase of subsidiary partnership interests   |  | (146)  |
| Net transfers to the noncontrolling interests   |  | (146)  |
| Change to Community Health Systems, Inc. stockholders' equity from net income attributable to Community Health Systems, Inc. stockholders and transfers to noncontrolling interests | \$   | 79,028 |

**10. EQUITY INVESTMENTS**

As of March 31, 2013, the Company owned equity interests of 27.5% in four hospitals in Las Vegas, Nevada, and 26.1% in one hospital in Las Vegas, Nevada, in which Universal Health Systems, Inc. owns the majority interest, and an equity interest of 38.0% in three hospitals in Macon, Georgia, in which HCA Inc. owns the majority interest.

Summarized combined financial information for these unconsolidated entities in which the Company owns an equity interest is as follows (in thousands):

|  | <b>Three Months Ended<br/>March 31,</b> |             |         |
|--|---|-------------|---------|
|  | <b>2013</b>                             | <b>2012</b> |         |
| Revenues                                       | \$ 315,396                              | \$          | 317,317 |
| Operating costs and expenses                   | 283,365                                 |             | 277,256 |
| Income from continuing operations before taxes | 32,008                                  |             | 40,035  |

The summarized financial information was derived from the unaudited financial information provided to the Company by those unconsolidated entities.

The Company's investment in all of its unconsolidated affiliates was \$438.2 million and \$432.1 million at March 31, 2013 and December 31, 2012, respectively, and is included in other assets, net in the accompanying condensed consolidated balance sheets. Included in the Company's results of operations is the Company's equity in pre-tax earnings from all of its investments in unconsolidated affiliates, which was \$15.7 million and \$12.0 million for the three months ended March 31, 2013 and 2012, respectively.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****11. LONG-TERM DEBT**

Long-term debt consists of the following (in thousands):

|   | March 31, 2013      | December 31, 2012   |
|---|---------------------|---------------------|
| Credit Facility:  |                     |                     |
| Term loan A   | \$ 712,500          | \$ 712,500          |
| Term loan B   | 3,412,584           | 3,619,062           |
| Revolving credit loans  | -                   | -                   |
| 8% Senior Notes due 2019                                      | 2,022,228           | 2,022,829           |
| 7 <sup>1</sup> / <sub>8</sub> % Senior Notes due 2020         | 1,200,000           | 1,200,000           |
| 5 <sup>1</sup> / <sub>8</sub> % Senior Secured Notes due 2018 | 1,600,000           | 1,600,000           |
| Receivables Facility  | 500,000             | 300,000             |
| Capital lease obligations                                     | 47,037              | 47,951              |
| Other   | 43,835              | 38,963              |
| <b>Total debt</b>   | <b>9,538,184</b>    | <b>9,541,305</b>    |
| Less current maturities                                       | (113,801)           | (89,911)            |
| <b>Total long-term debt</b>                                   | <b>\$ 9,424,383</b> | <b>\$ 9,451,394</b> |

**Credit Facility**

The Company's wholly-owned subsidiary CHS/Community Health Systems, Inc. (CHS) has obtained senior secured financing under a credit facility (the Credit Facility) with a syndicate of financial institutions led by Credit Suisse, as administrative agent and collateral agent. The Credit Facility includes a \$750 million revolving credit facility for working capital and general corporate purposes. The revolving credit facility also includes a subfacility for letters of credit and a swingline subfacility. The Credit Facility requires quarterly amortization payments of each term loan B facility equal to 0.25% of the outstanding amount of such term loans. On November 5, 2010, CHS entered into an amendment and restatement of the Credit Facility. The amendment extended by two and a half years, until January 25, 2017, the maturity date of \$1.5 billion of the existing term loans under the Credit Facility and increased the pricing on these term loans to LIBOR plus 350 basis points. The amendment also increased CHS' ability to issue additional indebtedness under the uncommitted incremental facility to \$1.0 billion from \$600 million, permitted CHS to issue term loan A loans under the incremental facility, and provided up to \$2.0 billion of borrowing capacity from receivable transactions, an increase of \$0.5 billion, of which \$1.7 billion would be required to be used for repayment of existing term loans. On February 2, 2012, CHS completed a second amendment and restatement of the Credit Facility to extend an additional \$1.6 billion of the term loans due 2014 under the Credit Facility to match the maturity date and interest rate margins of the term loans due January 25, 2017.

On August 3, 2012, CHS entered into Amendment No. 1 to the Credit Facility to provide increased flexibility for refinancing and repayment of the term loans due 2014 and amend certain other terms. On August 17, 2012, the Company made a prepayment of \$1.6 billion on the term loans due July 25, 2014, utilizing the proceeds from the issuance of \$1.6 billion of 5 <sup>1</sup>/<sub>8</sub>% Senior Secured Notes due 2018. On August 22, 2012, CHS entered into a loan modification agreement with respect to the Credit Facility to extend approximately \$340 million of the term loans due 2014 to match the maturity date and interest rate margins of the term loans due January 25, 2017.

On November 27, 2012, CHS entered into Amendment No. 2 to the Credit Facility to provide increased flexibility for the Company to make investments and restricted payments, incur debt related to acquisitions, amend certain other terms of the Credit Facility, including the maximum leverage ratio and interest coverage ratio financial coverage levels, and add a one year 1% prepayment premium payable in connection with a repricing of the term loans due in 2017. The extended term loans are subject to customary acceleration events and earlier maturity if the repayment, extension or refinancing with longer maturity on substantially all of the outstanding term loans maturing July 25, 2014 does not occur by April 15, 2015. During the three months ended March 31, 2013, the Company paid down \$206.5 million of the term loans due 2014.

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The July 25, 2014 maturity date of the balance of the remaining non-extended term loans at March 31, 2013 of approximately \$59.6 million remains unchanged.



**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

Effective March 6, 2012, the Company obtained a new \$750 million senior secured revolving credit facility (the Replacement Revolver Facility) and a new \$750 million incremental term loan A facility (the Incremental Term Loan) subject to the terms and conditions set forth in the Credit Facility. The Replacement Revolver Facility replaced in full the existing revolving credit facility under the Credit Facility. The net proceeds of the Incremental Term Loan were used to repay the same amount of the existing term loans under the Credit Facility. Both the Replacement Revolver Facility and the Incremental Term Loan have a maturity date of October 25, 2016, subject to customary acceleration events and to earlier maturity if the repayment, extension or refinancing with longer maturity debt of substantially all of the Company's then outstanding term loans maturing July 25, 2014 and the now fully redeemed 8<sup>7</sup>/<sub>8</sub>% Senior Notes does not occur by April 25, 2014. The pricing on each of the Replacement Revolver Facility and the Incremental Term Loan is initially LIBOR plus a margin of 250 basis points, subject to adjustment based on the Company's leverage ratio. The Incremental Term Loan amortizes at 5% in year one, 10% in years two and three, 15% in year four and 60% in year five.

The term loan facility must be prepaid in an amount equal to (1) 100% of the net cash proceeds of certain asset sales and dispositions by the Company and its subsidiaries, subject to certain exceptions and reinvestment rights, (2) 100% of the net cash proceeds of issuances of certain debt obligations or receivables-based financing by the Company and its subsidiaries, subject to certain exceptions, and (3) 50%, subject to reduction to a lower percentage based on the Company's leverage ratio (as defined in the Credit Facility generally as the ratio of total debt on the date of determination to the Company's EBITDA, as defined, for the four quarters most recently ended prior to such date), of excess cash flow (as defined) for any year, commencing in 2008, subject to certain exceptions. Voluntary prepayments and commitment reductions are permitted in whole or in part, without any premium or penalty, subject to minimum prepayment or reduction requirements.

The obligor under the Credit Facility is CHS. All of the obligations under the Credit Facility are unconditionally guaranteed by the Company and certain of its existing and subsequently acquired or organized domestic subsidiaries. All obligations under the Credit Facility and the related guarantees are secured by a perfected first priority lien or security interest in substantially all of the assets of the Company, CHS and each subsidiary guarantor, including equity interests held by the Company, CHS or any subsidiary guarantor, but excluding, among others, the equity interests of non-significant subsidiaries, syndication subsidiaries, securitization subsidiaries and joint venture subsidiaries.

The loans under the Credit Facility bear interest on the outstanding unpaid principal amount at a rate equal to an applicable percentage plus, at CHS' option, either (a) an Alternate Base Rate (as defined) determined by reference to the greater of (1) the Prime Rate (as defined) announced by Credit Suisse or (2) the Federal Funds Effective Rate (as defined) plus 0.50% or (3) the adjusted London Interbank Offered Rate (LIBOR) on such day for a three-month interest period commencing on the second business day after such day plus 1%, or (b) a reserve adjusted LIBOR for dollars (Eurodollar rate) (as defined). The applicable percentage for Alternate Base Rate loans is 1.25% for term loans due 2014 and is 2.50% for term loans due 2017. The applicable percentage for Eurodollar rate loans is 2.25% for term loans due 2014 and 3.50% for term loans due 2017. The applicable percentage for revolving loans and the Incremental Term Loan is 1.50% for Alternate Base Rate loans and 2.50% for Eurodollar loans, in each case subject to reduction based on the Company's leverage ratio. Loans under the swingline subfacility bear interest at the rate applicable to Alternate Base Rate loans under the Credit Facility.

CHS has agreed to pay letter of credit fees equal to the applicable percentage then in effect with respect to Eurodollar rate loans under the revolving credit facility times the maximum aggregate amount available to be drawn under all letters of credit outstanding under the subfacility for letters of credit. The issuer of any letter of credit issued under the subfacility for letters of credit will also receive a customary fronting fee and other customary processing charges. CHS is obligated to pay commitment fees of 0.50% per annum (subject to reduction based upon the Company's leverage ratio) on the unused portion of the revolving credit facility. For purposes of this calculation, swingline loans are not treated as usage of the revolving credit facility.

The Credit Facility contains customary representations and warranties, subject to limitations and exceptions, and customary covenants restricting the Company's and its subsidiaries' ability, subject to certain exceptions, to, among other things (1) declare dividends, make distributions or redeem or repurchase capital stock, (2) prepay, redeem or repurchase other debt, (3) incur liens or grant negative pledges, (4) make loans and investments and enter into acquisitions and joint ventures, (5) incur additional indebtedness or provide certain guarantees, (6) make capital expenditures, (7) engage in mergers, acquisitions and asset sales, (8) conduct transactions with affiliates, (9) alter the nature of the Company's businesses, (10) grant certain guarantees with respect to physician practices, (11) engage in sale and leaseback transactions or (12) change the Company's fiscal year. The Company is also required to comply with specified financial covenants (consisting of a leverage ratio and an interest coverage ratio) and various affirmative covenants.



**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

Events of default under the Credit Facility include, but are not limited to, (1) CHS' failure to pay principal, interest, fees or other amounts under the credit agreement when due (taking into account any applicable grace period), (2) any representation or warranty proving to have been materially incorrect when made, (3) covenant defaults subject, with respect to certain covenants, to a grace period, (4) bankruptcy events, (5) a cross default to certain other debt, (6) certain undischarged judgments (not paid within an applicable grace period), (7) a change of control, (8) certain ERISA-related defaults and (9) the invalidity or impairment of specified security interests, guarantees or subordination provisions in favor of the administrative agent or lenders under the Credit Facility.

As of March 31, 2013, the availability for additional borrowings under the Credit Facility was \$750 million pursuant to the Replacement Revolver Facility, of which \$37.8 million was set aside for outstanding letters of credit. CHS has the ability to amend the Credit Facility to provide for one or more tranches of term loans in an aggregate principal amount of \$1.0 billion, which CHS has not yet accessed. As of March 31, 2013, the weighted-average interest rate under the Credit Facility, excluding swaps, was 4.3%.

As of March 31, 2013, the Company had letters of credit issued, primarily in support of potential insurance-related claims and certain bonds, of approximately \$37.8 million.

Subsequent to the issuance of the Company's Quarterly Report on Form 10-Q for the three months ended March 31, 2012, the Company determined that the conversion of the term loans due 2014 to extended term loans resulting from the second amendment and restatement of its Credit Facility on February 2, 2012 should be presented as net financing activities in the condensed consolidated statement of cash flows. Such activities were presented in the previously issued Quarterly Report on Form 10-Q for the three months ended March 31, 2012 as a gross-up of borrowings and repayments of debt in the condensed consolidated statement of cash flows. There was no impact on net cash flows provided by financing activities as previously presented. This correction is reflected in the consolidated statement of cash flows in this Quarterly Report on Form 10-Q. Management does not believe such correction is material to the previously issued condensed consolidated financial statements.

***8 7/8% Senior Notes due 2015***

On July 25, 2007, CHS completed its offering of approximately \$3.0 billion aggregate principal amount of 8 7/8% Senior Notes due 2015 (the 8 7/8% Senior Notes), which were issued in a private placement. The 8 7/8% Senior Notes were to mature on July 15, 2015. The 8 7/8% Senior Notes bore interest at the rate of 8.875% per annum, payable semiannually in arrears on January 15 and July 15, commencing January 15, 2008. Interest on the 8 7/8% Senior Notes accrued from the date of original issuance. Interest was calculated on the basis of a 360-day year comprised of twelve 30-day months.

Pursuant to a registration rights agreement entered into at the time of the issuance of the 8 7/8% Senior Notes, as a result of an exchange offer made by CHS, substantially all of the 8 7/8% Senior Notes issued in July 2007 were exchanged in November 2007 for new notes (the 8 7/8% Exchange Notes) having terms substantially identical in all material respects to the 8 7/8% Senior Notes (except that the 8 7/8% Exchange Notes were issued under a registration statement pursuant to the 1933 Act). References to the 8 7/8% Senior Notes shall also be deemed to include the 8 7/8% Exchange Notes unless the context provides otherwise.

On March 21, 2012, CHS completed the cash tender offer for \$850 million of the then \$1.8 billion aggregate outstanding principal amount of the 8 7/8% Senior Notes.

On July 18, 2012, CHS completed the cash tender offer for \$639.7 million of the then \$934.3 million aggregate outstanding principal amount of the 8 7/8% Senior Notes. On August 17, 2012, pursuant to its redemption option, CHS redeemed the remaining \$294.6 million outstanding principal of the 8 7/8% Senior Notes.

***8% Senior Notes due 2019***

On November 22, 2011, CHS completed its offering of \$1.0 billion aggregate principal amount of 8% Senior Notes due 2019 (the 8% Senior Notes), which were issued in a private placement. The net proceeds from this issuance, together with available cash on hand, were used to finance the purchase of up to \$1.0 billion aggregate principal amount of CHS' then outstanding 8 7/8% Senior Notes and related fees and expenses. On March 21, 2012, CHS completed the secondary offering of \$1.0 billion aggregate principal amount of 8% Senior Notes, which

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were issued in a private placement (at a premium of 102.5%). The net proceeds from this issuance were used to finance the purchase of approximately \$850 million aggregate principal amount of CHS then outstanding 8% Senior Notes, to pay related fees and expenses and for general corporate purposes. The 8% Senior Notes bear interest at 8% per annum, payable semiannually in arrears on May 15 and November 15, commencing May 15, 2012. Interest on the 8% Senior Notes accrues from the date of original issuance. Interest is calculated on the basis of a 360-day year comprised of twelve 30-day months.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

Except as set forth below, CHS is not entitled to redeem the 8% Senior Notes prior to November 15, 2015.

Prior to November 15, 2014, CHS is entitled, at its option, to redeem a portion of the 8% Senior Notes (not to exceed 35% of the outstanding principal amount) at a redemption price equal to 108% of the principal amount of the notes redeemed plus accrued and unpaid interest, with the proceeds from certain public equity offerings. Prior to November 15, 2015, CHS may redeem some or all of the 8% Senior Notes at a redemption price equal to 100% of the principal amount of the notes redeemed plus accrued and unpaid interest, if any, plus a make-whole premium, as described in the 8% Senior Notes indenture. On and after November 15, 2015, CHS is entitled, at its option, to redeem all or a portion of the 8% Senior Notes upon not less than 30 nor more than 60 days' notice, at the following redemption prices (expressed as a percentage of principal amount on the redemption date), plus accrued and unpaid interest, if any, to the redemption date (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date), if redeemed during the 12-month period commencing on November 15 of the years set forth below:

| <b>Period</b>       | <b>Redemption Price</b> |
|---------------------|-------------------------|
| 2015                | 104.000 %               |
| 2016                | 102.000 %               |
| 2017 and thereafter | 100.000 %               |

Pursuant to a registration rights agreement entered into at the time of the issuance of the 8% Senior Notes, as a result of an exchange offer made by CHS, substantially all of the 8% Senior Notes issued in November 2011 and March 2012 were exchanged in May 2012 for new notes (the 8% Exchange Notes) having terms substantially identical in all material respects to the 8% Senior Notes (except that the 8% Exchange Notes were issued under a registration statement pursuant to the 1933 Act). References to the 8% Senior Notes shall also be deemed to include the 8% Exchange Notes unless the context provides otherwise.

***7 1/8% Senior Notes due 2020***

On July 18, 2012, CHS completed an underwritten public offering under its automatic shelf registration filed with the SEC of \$1.2 billion aggregate principal amount of 7 1/8% Senior Notes due 2020 (the 7 1/8% Senior Notes). The net proceeds from this issuance were used to finance the purchase of \$934.3 million aggregate principal amount of CHS' outstanding 8% Senior Notes and related fees and expenses and for general corporate purposes. The 7 1/8% Senior Notes bear interest at 7.125% per annum, payable semiannually in arrears on July 15 and January 15, commencing January 15, 2013. Interest on the 7 1/8% Senior Notes accrues from the date of original issuance. Interest is calculated on the basis of a 360-day year comprised of twelve 30-day months.

Except as set forth below, CHS is not entitled to redeem the 7 1/8% Senior Notes prior to July 15, 2016.

Prior to July 15, 2015, CHS is entitled, at its option, to redeem a portion of the 7 1/8% Senior Notes (not to exceed 35% of the outstanding principal amount) at a redemption price equal to 107.125% of the principal amount of the notes redeemed plus accrued and unpaid interest, with the proceeds from certain public equity offerings. Prior to July 15, 2016, CHS may redeem some or all of the 7 1/8% Senior Notes at a redemption price equal to 100% of the principal amount of the notes redeemed plus accrued and unpaid interest, if any, plus a make-whole premium, as described in the 7 1/8% Senior Notes indenture. On and after July 15, 2016, CHS is entitled, at its option, to redeem all or a portion of the 7 1/8% Senior Notes upon not less than 30 nor more than 60 days' notice, at the following redemption prices (expressed as a percentage of principal amount on the redemption date), plus accrued and unpaid interest, if any, to the redemption date (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date), if redeemed during the 12-month period commencing on July 15 of the years set forth below:

**Period**

|                     | <b>Redemption Price</b> |
|---------------------|-------------------------|
| 2016                | 103.563 %               |
| 2017                | 101.781 %               |
| 2018 and thereafter | 100.000 %               |

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED*****5 1/8% Senior Secured Notes due 2018***

On August 17, 2012, CHS completed an underwritten public offering under its automatic shelf registration filed with the SEC of \$1.6 billion aggregate principal amount of 5 1/8% Senior Secured Notes due 2018 (the "5 1/8% Senior Secured Notes"). The net proceeds from this issuance, together with available cash on hand, were used to finance the prepayment of \$1.6 billion of the outstanding term loans due 2014 under the Credit Facility and related fees and expenses. The 5 1/8% Senior Secured Notes bear interest at 5.125% per annum, payable semiannually in arrears on August 15 and February 15, commencing February 15, 2013. Interest on the 5 1/8% Senior Secured Notes accrues from the date of original issuance. Interest is calculated on the basis of a 360-day year comprised of twelve 30-day months. The 5 1/8% Senior Secured Notes are secured by a first-priority lien subject to a shared lien of equal priority with certain other obligations, including obligations under the Credit Facility, and subject to prior ranking liens permitted by the indenture governing the 5 1/8% Senior Secured Notes on substantially the same assets, subject to certain exceptions, that secure CHS' obligations under the Credit Facility.

Except as set forth below, CHS is not entitled to redeem the 5 1/8% Senior Secured Notes prior to August 15, 2015.

Prior to August 15, 2015, CHS is entitled, at its option, to redeem a portion of the 5 1/8% Senior Notes (not to exceed 35% of the outstanding principal amount) at a redemption price equal to 105.125% of the principal amount of the notes redeemed plus accrued and unpaid interest, with the proceeds from certain public equity offerings. Prior to August 15, 2015, CHS may redeem some or all of the 5 1/8% Senior Secured Notes at a redemption price equal to 100% of the principal amount of the notes redeemed plus accrued and unpaid interest, if any, plus a make-whole premium, as described in the 5 1/8% Senior Secured Notes indenture. On and after August 15, 2015, CHS is entitled, at its option, to redeem all or a portion of the 5 1/8% Senior Notes upon not less than 30 nor more than 60 days' notice, at the following redemption prices (expressed as a percentage of principal amount on the redemption date), plus accrued and unpaid interest, if any, to the redemption date (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date), if redeemed during the 12-month period commencing on August 15 of the years set forth below:

| <b>Period</b>       | <b>Redemption Price</b> |
|---------------------|-------------------------|
| 2015                | 102.563 %               |
| 2016                | 101.281 %               |
| 2017 and thereafter | 100.000 %               |

***Receivables Facility***

On March 21, 2012, CHS and certain of its subsidiaries entered into an accounts receivable loan agreement (the "Receivables Facility") with a group of lenders and banks, Credit Agricole Corporate and Investment Bank, as a managing agent and as the administrative agent, and The Bank of Nova Scotia, as a managing agent. On March 7, 2013, CHS and certain of its subsidiaries amended the Receivables Facility to add an additional managing agent, The Bank of Tokyo-Mitsubishi UFJ, Ltd., to increase the size of the facility from \$300 million to \$500 million and to extend the scheduled termination date. Additional subsidiaries of the Company also agreed to participate in the Receivables Facility as of that date. The existing and future non-self pay patient-related accounts receivable (the "Receivables") for certain of the Company's hospitals serve as collateral for the outstanding borrowings under the Receivables Facility. The interest rate on the borrowings is based on the commercial paper rate plus an applicable interest rate spread. Unless earlier terminated or subsequently extended pursuant to its terms, the Receivables Facility will expire on March 21, 2015, subject to customary termination events that could cause an early termination date. The Company maintains effective control over the Receivables because, pursuant to the terms of the Receivables Facility, the Receivables are sold from certain of the Company's subsidiaries to CHS, which then sells or contributes the Receivables to a special-purpose entity that is wholly-owned by CHS. The wholly-owned special-purpose entity in turn grants security interests in the Receivables in exchange for borrowings obtained from the group of third-party lenders and banks of up to \$500 million outstanding from time to time based on the availability of eligible Receivables and other customary factors. The group of third-party lenders and banks do not have recourse to the Company or its subsidiaries beyond the assets of the wholly-owned special-purpose entity that collateralizes the loan. The Receivables and other assets of the wholly-owned special-purpose entity

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will be available first and foremost to satisfy the claims of the creditors of such entity. The outstanding borrowings pursuant to the Receivables Facility at March 31, 2013 totaled \$500.0 million and are classified as long-term debt on the condensed consolidated balance sheet. At March 31, 2013, the carrying amount of Receivables included in the Receivables Facility totaled approximately \$969.4 million and is included in patient accounts receivable on the condensed consolidated balance sheet.



**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED*****Loss from Early Extinguishment of Debt***

The financing transactions discussed above relating to the repayment of the Company's term loans under the Credit Facility and the  $\frac{8}{8}\%$  Senior Notes due 2015 resulted in a loss from early extinguishment of debt of \$1.3 million and \$63.4 million for the three months ended March 31, 2013 and 2012, respectively, and an after-tax loss of \$0.8 million and \$39.5 million for the years ended March 31, 2013 and 2012, respectively.

***Other Debt***

As of March 31, 2013, other debt consisted primarily of the mortgage obligation on the Company's corporate headquarters and other obligations maturing in various installments through 2020.

To limit the effect of changes in interest rates on a portion of the Company's long-term borrowings, the Company is a party to 21 separate interest swap agreements in effect at March 31, 2013, with an aggregate notional amount of \$2.9 billion. On each of these swaps, the Company receives a variable rate of interest based on the three-month LIBOR in exchange for the payment of a fixed rate of interest. The Company currently pays, on a quarterly basis, a margin above LIBOR of 225 basis points for the outstanding balance of revolver loans and term loans due in 2014, 250 basis points for the Replacement Revolver Facility and the Incremental Term Loan and 350 basis points for term loans due in 2017 under the Credit Facility. See Note 12 for additional information regarding these swaps.

The Company paid interest of \$149.7 million and \$161.1 million on borrowings during the three months ended March 31, 2013 and 2012, respectively.

**12. FAIR VALUE OF FINANCIAL INSTRUMENTS**

The fair value of financial instruments has been estimated by the Company using available market information as of March 31, 2013 and December 31, 2012, and valuation methodologies considered appropriate. The estimates presented are not necessarily indicative of amounts the Company could realize in a current market exchange (in thousands):

|  | March 31, 2013  |                      | December 31, 2012 |                      |
|--|-----------------|----------------------|-------------------|----------------------|
|  | Carrying Amount | Estimated Fair Value | Carrying Amount   | Estimated Fair Value |
| <b>Assets:</b>                         |                 |                      |                   |                      |
| Cash and cash equivalents              | \$ 285,048      | \$ 285,048           | \$ 387,813        | \$ 387,813           |
| Available-for-sale securities          | 59,394          | 59,394               | 56,376            | 56,376               |
| Trading securities                     | 38,932          | 38,932               | 34,696            | 34,696               |
| <b>Liabilities:</b>                    |                 |                      |                   |                      |
| Credit Facility                        | 4,125,084       | 4,153,531            | 4,331,562         | 4,357,910            |
| 8% Senior Notes                        | 2,022,228       | 2,216,980            | 2,022,829         | 2,185,220            |
| 7 $\frac{1}{8}\%$ Senior Notes         | 1,200,000       | 1,306,800            | 1,200,000         | 1,285,848            |
| 5 $\frac{1}{8}\%$ Senior Secured Notes | 1,600,000       | 1,679,040            | 1,600,000         | 1,674,480            |
| Receivables Facility and other debt    | 543,835         | 543,835              | 338,963           | 338,963              |

The estimated fair value is determined using the methodologies discussed below in accordance with accounting standards related to the determination of fair value based on the U.S. GAAP fair value hierarchy as discussed in Note 13. The estimated fair value for financial instruments with a fair value that does not equal its carrying value is considered a Level 1 valuation. The Company utilizes the market approach and obtains indicative pricing from the administrative agent to the Credit Facility to determine fair values, which are validated through publicly available subscription services such as Bloomberg where relevant.

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*Cash and cash equivalents.* The carrying amount approximates fair value due to the short-term maturity of these instruments (less than three months).

*Available-for-sale securities.* Estimated fair value is based on closing price as quoted in public markets.

**Table of Contents**

**COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

*Trading securities.* Estimated fair value is based on closing price as quoted in public markets.

*Credit Facility.* Estimated fair value is based on information from the Company's bankers regarding relevant pricing for trading activity among the Company's lending institutions.

*8% Senior Notes.* Estimated fair value is based on the average bid and ask price as quoted by the bank who served as underwriters in the sale of these notes.

*7<sup>1</sup>/<sub>8</sub>% Senior Notes.* Estimated fair value is based on the average bid and ask price as quoted by the bank who served as underwriters in the sale of these notes.

*5<sup>1</sup>/<sub>8</sub>% Senior Secured Notes.* Estimated fair value is based on the average bid and ask price as quoted by the bank who served as underwriters in the sale of these notes.

*Receivables Facility and other debt.* The carrying amount of the Receivables Facility and all other debt approximates fair value due to the nature of these obligations.

*Interest rate swaps.* The fair value of interest rate swap agreements is the amount at which they could be settled, based on estimates calculated by the Company using a discounted cash flow analysis based on observable market inputs and validated by comparison to estimates obtained from the counterparty. The Company incorporates credit valuation adjustments ( CVAs ) to appropriately reflect both its own nonperformance or credit risk and the respective counterparty's nonperformance or credit risk in the fair value measurements. In adjusting the fair value of its interest rate swap agreements for the effect of nonperformance or credit risk, the Company has considered the impact of any netting features included in the agreements.

The Company assesses the effectiveness of its hedge instruments on a quarterly basis. For the three months ended March 31, 2013 and 2012, the Company completed an assessment of the cash flow hedge instruments and determined the hedges to be highly effective. The Company has also determined that the ineffective portion of the hedges do not have a material effect on the Company's consolidated financial position, operations or cash flows. The counterparties to the interest rate swap agreements expose the Company to credit risk in the event of nonperformance. However, at March 31, 2013, each swap agreement entered into by the Company was in a net liability position so that the Company would be required to make the net settlement payments to the counterparties; the Company does not anticipate nonperformance by those counterparties. The Company does not hold or issue derivative financial instruments for trading purposes.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

Interest rate swaps consisted of the following at March 31, 2013:

| Swap # | Notional Amount<br>(in 000 s) | Fixed Interest Rate | Termination<br>Date | Fair Value of<br>Liability (in 000 s) |
|--------|-------------------------------|---------------------|---------------------|---------------------------------------|
| 1      | \$ 100,000                    | 5.023 %             | May 30, 2013        | \$ 775                                |
| 2      | 300,000                       | 5.242 %             | August 6, 2013      | 5,219                                 |
| 3      | 100,000                       | 5.038 %             | August 30, 2013     | 1,982                                 |
| 4      | 50,000                        | 3.586 %             | October 23, 2013    | 928                                   |
| 5      | 50,000                        | 3.524 %             | October 23, 2013    | 911                                   |
| 6      | 100,000                       | 5.050 %             | November 30, 2013   | 3,168                                 |
| 7      | 200,000                       | 2.070 %             | December 19, 2013   | 2,528                                 |
| 8      | 100,000                       | 5.231 %             | July 25, 2014       | 6,453                                 |
| 9      | 100,000                       | 5.231 %             | July 25, 2014       | 6,453                                 |
| 10     | 200,000                       | 5.160 %             | July 25, 2014       | 12,719                                |
| 11     | 75,000                        | 5.041 %             | July 25, 2014       | 4,651                                 |
| 12     | 125,000                       | 5.022 %             | July 25, 2014       | 7,720                                 |
| 13     | 100,000                       | 2.621 %             | July 25, 2014       | 2,992                                 |
| 14     | 100,000                       | 3.110 %             | July 25, 2014       | 3,640                                 |
| 15     | 100,000                       | 3.258 %             | July 25, 2014       | 3,837                                 |
| 16     | 200,000                       | 2.693 %             | October 26, 2014    | 7,339                                 |
| 17     | 300,000                       | 3.447 %             | August 8, 2016      | 28,680                                |
| 18     | 200,000                       | 3.429 %             | August 19, 2016     | 19,124                                |
| 19     | 100,000                       | 3.401 %             | August 19, 2016     | 9,471                                 |
| 20     | 200,000                       | 3.500 %             | August 30, 2016     | 19,735                                |
| 21     | 100,000                       | 3.005 %             | November 30, 2016   | 8,595                                 |

The Company is exposed to certain risks relating to its ongoing business operations. The risk managed by using derivative instruments is interest rate risk. Interest rate swaps are entered into to manage interest rate fluctuation risk associated with the term loans in the Credit Facility. Companies are required to recognize all derivative instruments as either assets or liabilities at fair value in the condensed consolidated statement of financial position. The Company designates its interest rate swaps as cash flow hedges. For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income ( OCI ) and reclassified into earnings in the same period or periods during which the hedged transactions affect earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

Assuming no change in March 31, 2013 interest rates, approximately \$85.6 million of interest expense resulting from the spread between the fixed and floating rates defined in each interest rate swap agreement will be recognized during the next 12 months. If interest rate swaps do not remain highly effective as a cash flow hedge, the derivatives gains or losses resulting from the change in fair value reported through OCI will be reclassified into earnings.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

The following tabular disclosure provides the amount of pre-tax loss recognized as a component of OCI during the three months ended March 31, 2013 and 2012 (in thousands):

| Derivatives in Cash Flow Hedging | Amount of Pre-Tax Loss Recognized in OCI (Effective Portion) |                                      |             |
|----------------------------------|--|--------------------------------------|-------------|
|                                  | Relationships  | Three Months Ended March 31,<br>2013 | 2012        |
| Interest rate swaps              |  | \$ (2,622)                           | \$ (23,122) |

The following tabular disclosure provides the location of the effective portion of the pre-tax loss reclassified from accumulated other comprehensive loss ( AOCL ) into interest expense on the condensed consolidated statements of income during the three months ended March 31, 2013 and 2012 (in thousands):

| Location of Loss Reclassified from AOCL<br>into Income (Effective Portion) | Amount of Pre-Tax Loss Reclassified from AOCL<br>into Income (Effective Portion) |           |
|--|--|-----------|
|  | Three Months Ended March 31,<br>2013   | 2012      |
| Interest expense, net  | \$ 27,302  | \$ 39,610 |

The fair values of derivative instruments in the condensed consolidated balance sheets as of March 31, 2013 and December 31, 2012 were as follows (in thousands):

|   | Asset Derivatives |            |                   |            | Liability Derivatives       |            |                             |            |
|---|-------------------|------------|-------------------|------------|-----------------------------|------------|-----------------------------|------------|
|   | March 31, 2013    |            | December 31, 2012 |            | March 31, 2013              |            | December 31, 2012           |            |
|   | Balance Sheet     | Fair Value | Balance Sheet     | Fair Value | Balance Sheet               | Fair Value | Balance Sheet               | Fair Value |
|   | Location          |            | Location          |            | Location                    |            | Location                    |            |
| Derivatives designated as hedging instruments | Other assets, net | \$ -       | Other assets, net | \$ -       | Other long-term liabilities | \$ 156,920 | Other long-term liabilities | \$ 181,600 |

**13. FAIR VALUE****Fair Value Hierarchy**

Fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, the Company utilizes the U.S. GAAP fair value hierarchy that distinguishes between market participant assumptions

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based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumption about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

The inputs used to measure fair value are classified into the following fair value hierarchy:

*Level 1:* Quoted market prices in active markets for identical assets or liabilities.

*Level 2:* Observable market-based inputs or unobservable inputs that are corroborated by market data.

*Level 3:* Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities. Level 3 includes values determined using pricing models, discounted cash flow methodologies, or similar techniques reflecting the Company's own assumptions.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

In instances where the determination of the fair value hierarchy measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment of factors specific to the asset or liability.

The following table sets forth, by level within the fair value hierarchy, the financial assets and liabilities recorded at fair value on a recurring basis as of March 31, 2013 and December 31, 2012 (in thousands):

|   | <b>March 31,<br/>2013</b> | <b>Level 1</b>   | <b>Level 2</b>    | <b>Level 3</b> |
|---|---------------------------|------------------|-------------------|----------------|
| Available-for-sale securities               | \$ 59,394                 | \$ 59,394        | \$ -              | \$ -           |
| Trading securities                          | 38,932                    | 38,932           | -                 | -              |
| <b>Total assets</b>                         | <b>\$ 98,326</b>          | <b>\$ 98,326</b> | <b>\$ -</b>       | <b>\$ -</b>    |
| Fair value of interest rate swap agreements | \$ 156,920                | \$ -             | \$ 156,920        | \$ -           |
| <b>Total liabilities</b>                    | <b>\$ 156,920</b>         | <b>\$ -</b>      | <b>\$ 156,920</b> | <b>\$ -</b>    |

|   | <b>December 31,<br/>2012</b> | <b>Level 1</b>   | <b>Level 2</b>    | <b>Level 3</b> |
|---|------------------------------|------------------|-------------------|----------------|
| Available-for-sale securities               | \$ 56,376                    | \$ 56,376        | \$ -              | \$ -           |
| Trading securities                          | 34,696                       | 34,696           | -                 | -              |
| <b>Total assets</b>                         | <b>\$ 91,072</b>             | <b>\$ 91,072</b> | <b>\$ -</b>       | <b>\$ -</b>    |
| Fair value of interest rate swap agreements | \$ 181,600                   | \$ -             | \$ 181,600        | \$ -           |
| <b>Total liabilities</b>                    | <b>\$ 181,600</b>            | <b>\$ -</b>      | <b>\$ 181,600</b> | <b>\$ -</b>    |

Available-for-sale securities and trading securities classified as Level 1 are measured using quoted market prices.

The valuation of the Company's interest rate swap agreements is determined using market valuation techniques, including discounted cash flow analysis on the expected cash flows of each agreement. This analysis reflects the contractual terms of the agreement, including the period to maturity, and uses observable market-based inputs, including forward interest rate curves. The fair value of interest rate swap agreements are determined by netting the discounted future fixed cash payments and the discounted expected variable cash receipts. The variable cash receipts are based on the expectation of future interest rates based on observable market forward interest rate curves and the notional amount being hedged.

The Company incorporates CVAs to appropriately reflect both its own nonperformance or credit risk and the respective counterparty's nonperformance or credit risk in the fair value measurements. In adjusting the fair value of its interest rate swap agreements for the effect of nonperformance or credit risk, the Company has considered the impact of any netting features included in the agreements. The CVA on the Company's interest rate swap agreements at March 31, 2013 resulted in a decrease in the fair value of the related liability of \$2.1 million and an

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after-tax adjustment of \$1.3 million to OCI. The CVA on the Company's interest rate swap agreements at December 31, 2012 resulted in a decrease in the fair value of the related liability of \$3.6 million and an after-tax adjustment of \$2.3 million to OCI.

The majority of the inputs used to value its interest rate swap agreements, including the forward interest rate curves and market perceptions of the Company's credit risk used in the CVAs, are observable inputs available to a market participant. As a result, the Company has determined that the interest rate swap valuations are classified in Level 2 of the fair value hierarchy.



**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****14. OTHER COMPREHENSIVE INCOME**

The following table presents information about items reclassified out of accumulated other comprehensive income (loss) by component for the three months ended March 31, 2013 (in thousands, net of tax):

|  | Change in Fair Value of Interest Rate Swaps | Change in Fair Value of Available for Sale Securities | Change in Unrecognized Pension Cost | Accumulated Other Comprehensive Income (Loss) |
|--|---|---|-------------------------------------|---|
| Balance as of December 31, 2012                                  | \$ (116,382)                                | \$ 4,588  | \$ (33,516)                         | \$ (145,310)                                  |
| Other comprehensive income before reclassifications              | (1,676)                                     | 1,809   | -                                   | 133   |
| Amounts reclassified from accumulated other comprehensive income | 17,446                                      | -   | 733                                 | 18,179  |
| Net current-period other comprehensive income                    | 15,770                                      | 1,809   | 733                                 | 18,312  |
| Balance as of March 31, 2013                                     | \$ (100,612)                                | \$ 6,397  | \$ (32,783)                         | \$ (126,998)                                  |

The following table presents a subtotal for each significant reclassification to net income out of accumulated other comprehensive income (loss) and the line item affected in the condensed consolidated statement of income during the three months ended March 31, 2013 (in thousands):

**For the Three Months Ended March 31, 2013**

| Details about accumulated other comprehensive income (loss) components | Amount reclassified from accumulated other comprehensive loss | Affected line item in the statement where net income is presented |
|--|---|---|
| Gains and losses on cash flow hedges                                   |   |   |
| Interest rate swaps  | \$ (27,302)   | Interest expense, net   |
|  | 9,856   | Tax benefit   |
|  | \$ (17,446)   | Net of tax  |
| Amortization of defined benefit pension items                          |   |   |
| Prior service costs  | \$ (286)  | Salaries and benefits   |
| Actuarial losses   | (880)   | Salaries and benefits   |
|  | (1,166)   | Total before tax  |
|  | 433   | Tax benefit   |
|  | \$ (733)  | Net of tax  |



**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****15. SEGMENT INFORMATION**

Prior to the quarter ended March 31, 2013, the Company operated in three distinct operating segments, represented by hospital operations (which includes its general acute care hospitals and related healthcare entities that provide inpatient and outpatient healthcare services), home care agency operations (which provide in-home outpatient care), and hospital management services (which provides executive management and consulting services to non-affiliated acute care hospitals). During the quarter ended March 31, 2013, the chief operating decision maker stopped receiving discrete financial information for the hospital management services, so it no longer meets the criteria as a separate operating segment. The Company operates in two operating segments, hospital operations and home care agency operations. Financial information for hospital management services is now presented as a component of the hospital operations segment. The financial information from prior years has been revised to reflect the change in the composition of the Company's operating segments. Consistent with 2012, the Company presents two reportable segments, as noted below.

Only the hospital operations segment meets the criteria as a separate reportable segment. The financial information for the home care agency segment does not meet the quantitative thresholds for a separate identifiable reportable segment and is combined into the corporate and all other reportable segment.

The distribution between reportable segments of the Company's net operating revenues and income from continuing operations before income taxes is summarized in the following tables (in thousands):

|  | <b>Three Months Ended<br/>March 31,</b> |              |
|--|---|--------------|
|  | <b>2013</b>                             | <b>2012</b>  |
| Net operating revenues:                                |   |              |
| Hospital operations                                    | \$ 3,265,340                            | \$ 3,250,604 |
| Corporate and all other                                | 46,410                                  | 46,431       |
| Total  | \$ 3,311,750                            | \$ 3,297,035 |
| Income from continuing operations before income taxes: |   |              |
| Hospital operations                                    | \$ 201,382                              | \$ 199,803   |
| Corporate and all other                                | (57,356)                                | (54,266)     |
| Total  | \$ 144,026                              | \$ 145,537   |

**16. CONTINGENCIES**

The Company is a party to various legal proceedings incidental to its business. In the opinion of management, any ultimate liability with respect to these actions will not have a material adverse effect on the Company's consolidated financial position, cash flows or results of operations. With respect to all litigation matters, the Company considers the likelihood of a negative outcome. If the Company determines the likelihood of a negative outcome is probable and the amount of the loss can be reasonably estimated, the Company records an estimated loss for the expected outcome of the litigation and discloses that fact together with the amount accrued, if it was estimable. If the likelihood of a negative outcome is reasonably possible and the Company is able to determine an estimate of the possible loss or a range of loss, the Company discloses that fact together with the estimate of the possible loss or range of loss. However, it is difficult to predict the outcome or estimate a possible loss or range of loss in some instances because litigation is subject to significant uncertainties.

Reasonably Possible Contingencies

For the legal matter below, the Company believes that a negative outcome is reasonably possible, but the Company is unable to determine an estimate of the possible loss or a range of loss.

**Table of Contents**

**COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

*U.S. ex rel. Baker vs. Community Health Systems, Inc. (United States District Court for the District of New Mexico)*

The Company's knowledge of this matter originated in early 2006 with correspondence from the Civil Division of the Department of Justice requesting documents in an investigation it was conducting involving the Company. The inquiry related to the way in which different state Medicaid programs apply to the federal government for matching or supplemental funds that are ultimately used to pay for a small portion of the services provided to Medicaid and indigent patients. These programs are referred to by different names, including intergovernmental payments, upper payment limit programs, and Medicaid disproportionate share hospital payments. For approximately three years, the Company provided the Department of Justice with requested documents, met with its personnel on numerous occasions and otherwise cooperated in its investigation. During the course of the investigation, the Civil Division notified the Company that it believed that the Company and three of its New Mexico hospitals caused the State of New Mexico to submit improper claims for federal funds, in violation of the Federal False Claims Act. This investigation has culminated in the federal government's intervention in the referenced qui tam lawsuit, which alleges that the Company's New Mexico hospitals caused to be filed false claims from the period of August 2000 through June 2011. Two of the parent company's subsidiaries are also defendants in this lawsuit. The Company continues to vigorously defend this action. The current posture of this case is that discovery is closed and both parties' motions for summary judgment are pending. There is currently no hearing date on these motions and no trial date has been set.

**Matters for which an Outcome Cannot be Assessed**

For all of the legal matters below, the Company cannot at this time assess what the outcome may be and is further unable to determine any estimate of loss or range of loss. Because the investigations are at a preliminary stage, there are not sufficient facts available to make these assessments.

*Multi-provider National Department of Justice Investigations*

**Implantable Cardioverter Defibrillators (ICDs)**. The Company was first made aware of this investigation in September 2010, when the Company received a letter from the Civil Division of the United States Department of Justice. The letter advised the Company that an investigation was being conducted to determine whether certain hospitals have improperly submitted claims for payment for ICDs. The period of time covered by the investigation was 2003 to 2010. The Company continues to fully cooperate with the government in this investigation and has provided requested records and documents. On August 30, 2012, the Department of Justice issued a document entitled, "Medical Review Guidelines/Resolution Model," which sets out, for the purposes of this investigation, the patient conditions and criteria for the medical necessity of the implantation of ICDs in Medicare beneficiaries and how the Department of Justice will enforce the repayment obligations of hospitals. The Company is in the process of reviewing its medical records in light of the guidance contained in this document.

*Department of Justice Investigation of Medicare Short-Stay Admissions from Emergency Departments*

In April 2011, the Company received a document subpoena from the United States Department of Health and Human Services (OIG) in connection with an investigation of possible improper claims submitted to Medicare and Medicaid. The subpoena was directed to all of the Company's hospitals and requested documents concerning emergency department processes and procedures, including the hospitals' use of the Pro-MED Clinical Information System, a third-party software system that assists with the management of patient care and provides operational support and data collection for emergency department management. The subpoena also sought information about the Company's relationships with emergency department physicians, including financial arrangements. This investigation is being led by the Department of Justice. The Company is continuing to cooperate with the government with the ongoing document production, as well as conducting a joint medical necessity review of a sampling of medical records at a small number of hospitals. The results of the respective reviews have been exchanged and are undergoing further analysis by the experts.

The following matters, although initiated independently of the Department of Justice's April 2011 subpoena, are factually related in some manner to that subpoena and are grouped here for clarity.

**Texas Attorney General Investigation of Emergency Department Procedures and Billing**. In November 2010, the Company was served with substantially identical Civil Investigative Demands (CIDs) from the Office of Attorney General, State of Texas for all 18 of the Company's

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affiliated Texas hospitals. The subject of the requests appears to concern emergency department procedures and billing. The Company has complied with these requests and provided all documentation and reports requested. The Company continues to cooperate fully with this investigation.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

United States ex rel. and Reuille vs. Community Health Systems Professional Services Corporation and Lutheran Musculoskeletal Center, LLC d/b/a Lutheran Hospital (United States District Court for the Northern District of Indiana, Fort Wayne Division). This lawsuit was originally filed under seal in January 2009. The suit is brought under the False Claims Act and alleges that Lutheran Hospital of Indiana billed the Medicare program for (a) false 23 hour observation after outpatient surgeries and procedures, and (b) intentional assignment of inpatient status to one-day stays for cases that do not meet Medicare criteria for inpatient intensity of service or severity of illness. In December 2010, the government filed a notice that it declined to intervene in this suit. On April 22, 2011, a joint motion was filed by the relator and the Department of Justice to extend the period of time for the relator to serve the Company in the case to allow the government more time to decide if it will intervene in the case. The motion to stay was granted, as have subsequent joint motions, and the stay is currently continued until October 25, 2013. The original motion and subsequent filings gave insight to the fact that there are other qui tam complaints in other jurisdictions and that the government was consolidating its investigations and working cooperatively with other investigative bodies (including the Attorney General of the State of Texas). The government also confirmed that it considers the allegations made in the complaint styled *Tenet Healthcare Corporation vs. Community Health Systems, Inc., et al.* filed in the United States District Court for the Northern District of Texas, Dallas Division on April 11, 2011 to be related to the government's consolidated investigation. The Company is cooperating fully with the government in its investigations.

Shelbyville, Tennessee OIG Subpoena. In May 2011, the Company received a subpoena from the Houston Office of the United States Department of Health and Human Services, OIG, requesting 71 patient medical records from the Company's hospital in Shelbyville, Tennessee. The Company provided the requested records and has met with the government regarding this matter. The Company continues to cooperate fully with this investigation.

SEC Subpoena. In May 2011, the Company received a subpoena from the SEC requesting documents related to or requested in connection with the various inquiries, lawsuits and investigations regarding, generally, emergency room admissions or observation practices at the Company's hospitals. The subpoena also requested documents relied upon by the Company in responding to the Tenet litigation, as well as other communications about the Tenet litigation. As with all government investigations, the Company is cooperating fully with the SEC.

Class Action Shareholder Federal Securities Cases. Three purported class action cases have been filed in the United States District Court for the Middle District of Tennessee; namely, *Norfolk County Retirement System v. Community Health Systems, Inc., et al.*, filed May 9, 2011; *De Zheng v. Community Health Systems, Inc., et al.*, filed May 12, 2011; and *Minneapolis Firefighters Relief Association v. Community Health Systems, Inc., et al.*, filed June 21, 2011. All three seek class certification on behalf of purchasers of the Company's common stock between July 27, 2006 and April 11, 2011 and allege that misleading statements resulted in artificially inflated prices for the Company's common stock. In December 2011, the cases were consolidated for pretrial purposes and NYC Funds and its counsel were selected as lead plaintiffs/lead plaintiffs counsel. The Company's motion to dismiss this case has been fully briefed and is pending before the court. The Company believes this consolidated matter is without merit and will vigorously defend this case.

Shareholder Derivative Actions. Three purported shareholder derivative actions have also been filed in the United States District Court for the Middle District of Tennessee; *Plumbers and Pipefitters Local Union No. 630 Pension Annuity Trust Fund v. Wayne T. Smith, et al.*, filed May 24, 2011; *Roofers Local No. 149 Pension Fund v. Wayne T. Smith, et al.*, filed June 21, 2011; and *Lambert Sweat v. Wayne T. Smith, et al.*, filed October 5, 2011. These three cases allege breach of fiduciary duty arising out of allegedly improper inpatient admission practices, mismanagement, waste and unjust enrichment. These cases have been consolidated into a single, consolidated action. The plaintiffs filed an operative amended derivative complaint in these three consolidated actions on March 15, 2012. The Company's motion to dismiss has been fully briefed and is pending before the court. The Company believes all of these matters are without merit and will vigorously defend them.

The Company incurred the following pre-tax charges in connection with the government investigations and shareholder lawsuits of possible improper claims submitted to Medicare and Medicaid during the three months ending March 31, 2013 and 2012 (in thousands):

| <b>Three Months Ended</b> |             |
|---------------------------|-------------|
| <b>March 31,</b>          |             |
| <b>2013</b>               | <b>2012</b> |

|   |    |       |    |       |
|---|----|-------|----|-------|
| Professional fees and other related costs | \$ | 2,006 | \$ | 1,903 |
|---|----|-------|----|-------|



**Table of Contents**

**COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED**

**Probable Contingencies**

In addition to the cases described above, there are a number of legal matters for which, based on information currently available, the Company believes that a negative outcome is known or is probable. In the aggregate, an estimate of these losses has been accrued in the amount of \$11.6 million and \$22.6 million at March 31, 2013 and December 31, 2012, respectively. Due to the uncertainties and difficulty in predicting the ultimate resolution of these contingencies, the actual amount could differ from the estimated amount; however, the Company does not believe the ultimate outcome of any of these matters would be material.

**17. SUBSEQUENT EVENTS**

The Company evaluated all material events occurring subsequent to the balance sheet date for events requiring disclosure or recognition in the condensed consolidated financial statements.

**18. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION**

The Senior Notes, which are senior unsecured obligations of CHS, and the 5<sup>1</sup>/<sub>8</sub>% Senior Secured Notes are guaranteed on a senior basis by the Company and by certain of its existing and subsequently acquired or organized 100% owned domestic subsidiaries. The Senior Notes and the 5<sup>1</sup>/<sub>8</sub>% Senior Secured Notes are guaranteed on a joint and several basis, with limited exceptions considered customary for such guarantees, including the release of the guarantee when a subsidiary's assets used in operations are sold. The following condensed consolidating financial statements present Community Health Systems, Inc. (as parent guarantor), CHS (as the issuer), the subsidiary guarantors, the subsidiary non-guarantors and eliminations. These condensed consolidating financial statements have been prepared and presented in accordance with SEC Regulation S-X Rule 3-10 Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered.

The accounting policies used in the preparation of this financial information are consistent with those elsewhere in the condensed consolidated financial statements of the Company, except as noted below:

Intercompany receivables and payables are presented gross in the supplemental condensed consolidating balance sheets.

Cash flows from intercompany transactions are presented in cash flows from financing activities, as changes in intercompany balances with affiliates, net.

Income tax expense is allocated from the parent guarantor to the income producing operations (other guarantors and non-guarantors) and the issuer through stockholders' equity. As this approach represents an allocation, the income tax expense allocation is considered non-cash for statement of cash flow purposes.

Interest expense, net has been presented to reflect net interest expense and interest income from outstanding long-term debt and intercompany balances.

The Company's intercompany activity consists primarily of daily cash transfers for purposes of cash management, the allocation of certain expenses and expenditures paid for by the parent on behalf of its subsidiaries, and the push down of investment in its subsidiaries. This activity also includes the intercompany transactions between consolidated entities as part of the Receivables Facility that is further discussed in Note 11. The Company's subsidiaries generally do not purchase services from one another; thus, the intercompany transactions do not represent revenue generating transactions. All intercompany transactions eliminate in consolidation.

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From time to time, the Company sells and/or repurchases noncontrolling interests in consolidated subsidiaries, which may change subsidiaries between guarantors and non-guarantors. Amounts for prior periods are revised to reflect the status of guarantors or non-guarantors as of March 31, 2013.

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****Condensed Consolidating Balance Sheet****March 31, 2013**

|   | <b>Parent<br/>Guarantor</b> | <b>Issuer</b> | <b>Other<br/>Guarantors<br/>(In thousands)</b> | <b>Non -<br/>Guarantors</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|---|-----------------------------|---------------|--|-----------------------------|---------------------|---------------------|
| <b>ASSETS</b>   |                             |               |  |                             |                     |                     |
| Current assets:   |                             |               |  |                             |                     |                     |
| Cash and cash equivalents   | \$ -                        | \$ -          | \$ 163,552                                     | \$ 121,496                  | \$ -                | \$ 285,048          |
| Patient accounts receivable, net of allowance for doubtful accounts | -                           | -             | 783,788  | 1,431,410                   | -                   | 2,215,198           |
| Supplies  | -                           | -             | 257,063  | 113,992                     | -                   | 371,055             |
| Prepaid income taxes  | -                           | -             | -  | -                           | -                   | -                   |
| Deferred income taxes   | 117,045                     | -             | -  | -                           | -                   | 117,045             |
| Prepaid expenses and taxes  | -                           | 65            | 86,017   | 56,284                      | -                   | 142,366             |
| Other current assets  | -                           | -             | 221,807  | 66,264                      | -                   | 288,071             |
| Total current assets  | 117,045                     | 65            | 1,512,227                                      | 1,789,446                   | -                   | 3,418,783           |
| Intercompany receivable   | 511,641                     | 9,593,156     | 4,085,575                                      | 3,440,938                   | (17,631,310)        | -                   |
| Property and equipment, net   | -                           | -             | 4,625,508                                      | 2,469,626                   | -                   | 7,095,134           |
| Goodwill  | -                           | -             | 2,543,898                                      | 1,864,464                   | -                   | 4,408,362           |
| Other assets, net   | -                           | 156,415       | 1,189,267                                      | 798,630                     | (469,389)           | 1,674,923           |
| Net investment in subsidiaries                                      | 3,072,451                   | 8,608,604     | 3,581,210                                      | -                           | (15,262,265)        | -                   |
| Total assets  | \$ 3,701,137                | \$ 18,358,240 | \$ 17,537,685                                  | \$ 10,363,104               | \$ (33,362,964)     | \$ 16,597,202       |
| <b>LIABILITIES AND EQUITY</b>                                       |                             |               |  |                             |                     |                     |
| Current liabilities:  |                             |               |  |                             |                     |                     |
| Current maturities of long-term debt                                | \$ -                        | \$ 94,429     | \$ 16,519                                      | \$ 2,853                    | \$ -                | \$ 113,801          |
| Accounts payable  | -                           | 48            | 504,788  | 236,339                     | -                   | 741,175             |
| Income tax payable  | 5,924                       | -             | -  | -                           | -                   | 5,924               |

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|  |              |               |               |               |                 |               |
|--|--------------|---------------|---------------|---------------|-----------------|---------------|
| Accrued interest   | -            | 109,235       | 294           | 410           | -               | 109,939       |
| Accrued liabilities  | 7,575        | -             | 677,530       | 352,976       | -               | 1,038,081     |
| Total current liabilities  | 13,499       | 203,712       | 1,199,131     | 592,578       | -               | 2,008,920     |
| Long-term debt   | -            | 8,853,561     | 52,372        | 518,450       | -               | 9,424,383     |
| Intercompany payable   | -            | 5,602,211     | 12,137,048    | 7,951,231     | (25,690,490)    | -             |
| Deferred income taxes  | 808,489      | -             | -             | -             | -               | 808,489       |
| Other long-term liabilities  | 1,174        | 626,308       | 680,608       | 200,664       | (469,389)       | 1,039,365     |
| Total liabilities  | 823,162      | 15,285,792    | 14,069,159    | 9,262,923     | (26,159,879)    | 13,281,157    |
| Redeemable noncontrolling interests in equity of consolidated subsidiaries | -            | -             | -             | 375,506       | -               | 375,506       |
| <b>Equity:</b>   |              |               |               |               |                 |               |
| Community Health Systems, Inc. stockholders' equity:                       |              |               |               |               |                 |               |
| Preferred stock  | -            | -             | -             | -             | -               | -             |
| Common stock   | 950          | -             | 1             | 2             | (3)             | 950           |
| Additional paid-in capital   | 1,187,535    | 1,152,914     | 1,259,384     | 530,536       | (2,942,834)     | 1,187,535     |
| Treasury stock, at cost  | (6,678)      | -             | -             | -             | -               | (6,678)       |
| Accumulated other comprehensive (loss) income                              | (126,998)    | (126,998)     | (26,386)      | -             | 153,384         | (126,998)     |
| Retained earnings  | 1,823,166    | 2,046,532     | 2,235,527     | 131,573       | (4,413,632)     | 1,823,166     |
| Total Community Health Systems, Inc. stockholders' equity                  | 2,877,975    | 3,072,448     | 3,468,526     | 662,111       | (7,203,085)     | 2,877,975     |
| Noncontrolling interests in equity of consolidated subsidiaries            | -            | -             | -             | 62,564        | -               | 62,564        |
| Total equity   | 2,877,975    | 3,072,448     | 3,468,526     | 724,675       | (7,203,085)     | 2,940,539     |
| Total liabilities and equity   | \$ 3,701,137 | \$ 18,358,240 | \$ 17,537,685 | \$ 10,363,104 | \$ (33,362,964) | \$ 16,597,202 |

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****Condensed Consolidating Balance Sheet****December 31, 2012**

|   | <b>Parent<br/>Guarantor</b> | <b>Issuer</b> | <b>Other<br/>Guarantors<br/>(In thousands)</b> | <b>Non -<br/>Guarantors</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|---|-----------------------------|---------------|--|-----------------------------|---------------------|---------------------|
| <b>ASSETS</b>   |                             |               |  |                             |                     |                     |
| Current assets:   |                             |               |  |                             |                     |                     |
| Cash and cash equivalents   | \$ -                        | \$ -          | \$ 271,559                                     | \$ 116,254                  | \$ -                | \$ 387,813          |
| Patient accounts receivable, net of allowance for doubtful accounts | -                           | -             | 676,649  | 1,390,730                   | -                   | 2,067,379           |
| Supplies  | -                           | -             | 254,853  | 113,319                     | -                   | 368,172             |
| Prepaid income taxes  | 49,888                      | -             | -  | -                           | -                   | 49,888              |
| Deferred income taxes   | 117,045                     | -             | -  | -                           | -                   | 117,045             |
| Prepaid expenses and taxes  | -                           | 115           | 86,628   | 39,818                      | -                   | 126,561             |
| Other current assets  | -                           | -             | 222,424  | 79,860                      | -                   | 302,284             |
| Total current assets  | 166,933                     | 115           | 1,512,113                                      | 1,739,981                   | -                   | 3,419,142           |
| Intercompany receivable   | 406,534                     | 9,837,904     | 3,723,120                                      | 3,262,823                   | (17,230,381)        | -                   |
| Property and equipment, net   | -                           | -             | 4,660,557                                      | 2,491,316                   | -                   | 7,151,873           |
| Goodwill  | -                           | -             | 2,544,195                                      | 1,863,943                   | -                   | 4,408,138           |
| Other assets, net   | -                           | 165,236       | 1,273,347                                      | 816,373                     | (627,774)           | 1,627,182           |
| Net investment in subsidiaries                                      | 2,974,965                   | 8,686,242     | 3,427,182                                      | -                           | (15,088,389)        | -                   |
| Total assets  | \$ 3,548,432                | \$ 18,689,497 | \$ 17,140,514                                  | \$ 10,174,436               | \$ (32,946,544)     | \$ 16,606,335       |

**LIABILITIES AND EQUITY**

Current liabilities:

|                                      |      |           |           |          |      |           |
|--------------------------------------|------|-----------|-----------|----------|------|-----------|
| Current maturities of long-term debt | \$ - | \$ 75,679 | \$ 11,103 | \$ 3,129 | \$ - | \$ 89,911 |
| Accounts payable                     | -    | 74        | 583,865   | 241,975  | -    | 825,914   |
| Accrued interest                     | -    | 110,091   | 295       | 316      | -    | 110,702   |

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|  |                     |                      |                      |                      |                        |                      |
|--|---------------------|----------------------|----------------------|----------------------|------------------------|----------------------|
| Accrued liabilities  | 7,580               | -                    | 748,010              | 361,103              | -                      | 1,116,693            |
| <b>Total current liabilities</b>   | <b>7,580</b>        | <b>185,844</b>       | <b>1,343,273</b>     | <b>606,523</b>       | <b>-</b>               | <b>2,143,220</b>     |
| Long-term debt   | -                   | 9,079,392            | 53,201               | 318,801              | -                      | 9,451,394            |
| Intercompany payable   | -                   | 5,639,928            | 11,693,119           | 7,822,313            | (25,155,360)           | -                    |
| Deferred income taxes  | 808,489             | -                    | -                    | -                    | -                      | 808,489              |
| Other long-term liabilities  | 1,156               | 809,372              | 675,341              | 180,950              | (627,774)              | 1,039,045            |
| <b>Total liabilities</b>   | <b>817,225</b>      | <b>15,714,536</b>    | <b>13,764,934</b>    | <b>8,928,587</b>     | <b>(25,783,134)</b>    | <b>13,442,148</b>    |
| Redeemable noncontrolling interests in equity of consolidated subsidiaries | -                   | -                    | -                    | 367,666              | -                      | 367,666              |
| Equity:  |                     |                      |                      |                      |                        |                      |
| Community Health Systems, Inc. stockholders' equity:                       |                     |                      |                      |                      |                        |                      |
| Preferred stock  | -                   | -                    | -                    | -                    | -                      | -                    |
| Common stock   | 929                 | -                    | 1                    | 2                    | (3)                    | 929                  |
| Additional paid-in capital   | 1,138,274           | 1,176,342            | 1,283,499            | 690,929              | (3,150,770)            | 1,138,274            |
| Treasury stock, at cost  | (6,678)             | -                    | -                    | -                    | -                      | (6,678)              |
| Accumulated other comprehensive (loss) income                              | (145,310)           | (145,310)            | (28,927)             | -                    | 174,237                | (145,310)            |
| Retained earnings  | 1,743,992           | 1,943,929            | 2,121,007            | 121,938              | (4,186,874)            | 1,743,992            |
| <b>Total Community Health Systems, Inc. stockholders' equity</b>           | <b>2,731,207</b>    | <b>2,974,961</b>     | <b>3,375,580</b>     | <b>812,869</b>       | <b>(7,163,410)</b>     | <b>2,731,207</b>     |
| Noncontrolling interests in equity of consolidated subsidiaries            | -                   | -                    | -                    | 65,314               | -                      | 65,314               |
| <b>Total equity</b>  | <b>2,731,207</b>    | <b>2,974,961</b>     | <b>3,375,580</b>     | <b>878,183</b>       | <b>(7,163,410)</b>     | <b>2,796,521</b>     |
| <b>Total liabilities and equity</b>  | <b>\$ 3,548,432</b> | <b>\$ 18,689,497</b> | <b>\$ 17,140,514</b> | <b>\$ 10,174,436</b> | <b>\$ (32,946,544)</b> | <b>\$ 16,606,335</b> |

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****Condensed Consolidating Statement of Income****Three Months Ended March 31, 2013**

|  | <b>Parent<br/>Guarantor</b> | <b>Issuer</b> | <b>Other<br/>Guarantors<br/>(In thousands)</b> | <b>Non -<br/>Guarantors</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|-----------------------------|---------------|--|-----------------------------|---------------------|---------------------|
| Operating revenues (net of contractual allowances and discounts) | \$ -                        | \$ (3,322)    | \$ 2,432,880                                   | \$ 1,370,306                | \$ -                | \$ 3,799,864        |
| Provision for bad debts  | -                           | -             | 338,431  | 149,683                     | -                   | 488,114             |
| Net operating revenues   | -                           | (3,322)       | 2,094,449                                      | 1,220,623                   | -                   | 3,311,750           |
| Operating costs and expenses:                                    |                             |               |  |                             |                     |                     |
| Salaries and benefits  | -                           | -             | 919,268  | 657,880                     | -                   | 1,577,148           |
| Supplies   | -                           | -             | 324,013  | 173,828                     | -                   | 497,841             |
| Other operating expenses   | -                           | 77            | 444,585  | 263,312                     | -                   | 707,974             |
| Electronic health records incentive reimbursement                | -                           | -             | (11,974)                                       | (8,942)                     | -                   | (20,916)            |
| Rent   | -                           | -             | 40,227   | 31,327                      | -                   | 71,554              |
| Depreciation and amortization                                    | -                           | -             | 128,877  | 63,281                      | -                   | 192,158             |
| Total operating costs and expenses                               | -                           | 77            | 1,844,996                                      | 1,180,686                   | -                   | 3,025,759           |
| Income from operations   | -                           | (3,399)       | 249,453  | 39,937                      | -                   | 285,991             |
| Interest expense, net  | -                           | 14,269        | 126,466  | 15,615                      | -                   | 156,350             |
| Loss from early extinguishment of debt                           | -                           | 1,295         | -  | -                           | -                   | 1,295               |
| Equity in earnings of unconsolidated affiliates                  | (79,174)                    | (92,325)      | (18,350)                                       | -                           | 174,169             | (15,680)            |
| Income from continuing operations before income taxes            | 79,174                      | 73,362        | 141,337  | 24,322                      | (174,169)           | 144,026             |
| Provision for (benefit from) income taxes                        | -                           | (5,812)       | 50,931   | 2,584                       | -                   | 47,703              |
| Income from continuing operations                                | 79,174                      | 79,174        | 90,406   | 21,738                      | (174,169)           | 96,323              |
| Discontinued operations, net of taxes:                           |                             |               |  |                             |                     |                     |
| Loss from operations of entities sold                            | -                           | -             | -  | -                           | -                   | -                   |
| Loss from discontinued operations, net of taxes                  | -                           | -             | -  | -                           | -                   | -                   |

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|  |           |           |           |          |              |           |
|--|-----------|-----------|-----------|----------|--------------|-----------|
| Net income   | 79,174    | 79,174    | 90,406    | 21,738   | (174,169)    | 96,323    |
| Less: Net income attributable to noncontrolling interests              | -         | -         | -         | 17,149   | -            | 17,149    |
| Net income attributable to Community Health Systems, Inc. stockholders | \$ 79,174 | \$ 79,174 | \$ 90,406 | \$ 4,589 | \$ (174,169) | \$ 79,174 |



**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****Condensed Consolidating Statement of Income****Three Months Ended March 31, 2012**

|  | <b>Parent<br/>Guarantor</b> | <b>Issuer</b> | <b>Other<br/>Guarantors<br/>(In thousands)</b> | <b>Non -<br/>Guarantors</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|-----------------------------|---------------|--|-----------------------------|---------------------|---------------------|
| Operating revenues (net of contractual allowances and discounts) | \$ -                        | \$ (1,764)    | \$ 2,451,939                                   | \$ 1,333,316                | \$ -                | \$ 3,783,491        |
| Provision for bad debts  | -                           | -             | 349,311  | 137,145                     | -                   | 486,456             |
| Net operating revenues   | -                           | (1,764)       | 2,102,628                                      | 1,196,171                   | -                   | 3,297,035           |
| Operating costs and expenses:                                    |                             |               |  |                             |                     |                     |
| Salaries and benefits  | -                           | -             | 898,591  | 626,384                     | -                   | 1,524,975           |
| Supplies   | -                           | -             | 328,255  | 170,324                     | -                   | 498,579             |
| Other operating expenses   | -                           | 315           | 479,066  | 229,562                     | -                   | 708,943             |
| Electronic health records incentive reimbursement                | -                           | -             | (18,831)                                       | (7,337)                     | -                   | (26,168)            |
| Rent   | -                           | -             | 37,370   | 29,854                      | -                   | 67,224              |
| Depreciation and amortization                                    | -                           | -             | 115,666  | 58,688                      | -                   | 174,354             |
| Total operating costs and expenses                               | -                           | 315           | 1,840,117                                      | 1,107,475                   | -                   | 2,947,907           |
| Income from operations   | -                           | (2,079)       | 262,511  | 88,696                      | -                   | 349,128             |
| Interest expense, net  | -                           | 15,737        | 123,556  | 12,882                      | -                   | 152,175             |
| Loss from early extinguishment of debt                           | -                           | 63,429        | -  | -                           | -                   | 63,429              |
| Equity in earnings of unconsolidated affiliates                  | (75,474)                    | (118,501)     | (41,799)                                       | -                           | 223,761             | (12,013)            |
| Income from continuing operations before income taxes            | 75,474                      | 37,256        | 180,754  | 75,814                      | (223,761)           | 145,537             |
| Provision for (benefit from) income taxes                        | -                           | (38,218)      | 65,252   | 18,785                      | -                   | 45,819              |
| Income from continuing operations                                | 75,474                      | 75,474        | 115,502  | 57,029                      | (223,761)           | 99,718              |
| Discontinued operations, net of taxes:                           |                             |               |  |                             |                     |                     |
| Loss from operations of entities sold                            | -                           | -             | -  | (466)                       | -                   | (466)               |

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|  |           |           |            |           |              |           |
|--|-----------|-----------|------------|-----------|--------------|-----------|
| Loss from discontinued operations,<br>net of taxes                           | -         | -         | -          | (466)     | -            | (466)     |
| Net income   | 75,474    | 75,474    | 115,502    | 56,563    | (223,761)    | 99,252    |
| Less: Net income attributable to<br>noncontrolling interests                 | -         | -         | -          | 23,778    | -            | 23,778    |
| Net income attributable to<br>Community Health Systems, Inc.<br>stockholders | \$ 75,474 | \$ 75,474 | \$ 115,502 | \$ 32,785 | \$ (223,761) | \$ 75,474 |

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****Condensed Consolidating Statement of Comprehensive Income****Three Months Ended March 31, 2013**

|  | <b>Parent<br/>Guarantor</b> | <b>Issuer</b> | <b>Other<br/>Guarantors<br/>(In thousands)</b> | <b>Non -<br/>Guarantors</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|-----------------------------|---------------|--|-----------------------------|---------------------|---------------------|
| Net income   | \$ 79,174                   | \$ 79,174     | \$ 90,406                                      | \$ 21,738                   | \$ (174,169)        | \$ 96,323           |
| Other comprehensive income<br>(loss), net of taxes                                     |                             |               |  |                             |                     |                     |
| Net change in fair value of interest<br>rate swaps                                     | 15,770                      | 15,770        | -  | -                           | (15,770)            | 15,770              |
| Net change in fair value of<br>available-for-sale securities                           | 1,809                       | 1,809         | 1,809  | -                           | (3,618)             | 1,809               |
| Amortization and recognition of<br>unrecognized pension cost<br>components             | 733                         | 733           | 733  | -                           | (1,466)             | 733                 |
| Other comprehensive income (loss)  | 18,312                      | 18,312        | 2,542  | -                           | (20,854)            | 18,312              |
| Comprehensive income   | 97,486                      | 97,486        | 92,948   | 21,738                      | (195,023)           | 114,635             |
| Less: Comprehensive income<br>attributable to noncontrolling<br>interests              | -                           | -             | -  | 17,149                      | -                   | 17,149              |
| Comprehensive income attributable<br>to Community Health Systems, Inc.<br>stockholders | \$ 97,486                   | \$ 97,486     | \$ 92,948                                      | \$ 4,589                    | \$ (195,023)        | \$ 97,486           |

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****Condensed Consolidating Statement of Comprehensive Income****Three Months Ended March 31, 2012**

|  | <b>Parent<br/>Guarantor</b> | <b>Issuer</b> | <b>Other<br/>Guarantors<br/>(In thousands)</b> | <b>Non -<br/>Guarantors</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|-----------------------------|---------------|--|-----------------------------|---------------------|---------------------|
| Net income   | \$ 75,474                   | \$ 75,474     | \$ 115,502                                     | \$ 56,563                   | \$ (223,761)        | \$ 99,252           |
| Other comprehensive income<br>(loss), net of taxes                                     |                             |               |  |                             |                     |                     |
| Net change in fair value of<br>interest rate swaps                                     | 10,536                      | 10,536        | -  | -                           | (10,536)            | 10,536              |
| Net change in fair value of<br>available-for-sale securities                           | 2,667                       | 2,667         | 2,667  | -                           | (5,334)             | 2,667               |
| Amortization and recognition of<br>unrecognized pension cost<br>components             | 1,140                       | 1,140         | 1,140  | -                           | (2,280)             | 1,140               |
| Other comprehensive income<br>(loss)   | 14,343                      | 14,343        | 3,807  | -                           | (18,150)            | 14,343              |
| Comprehensive income   | 89,817                      | 89,817        | 119,309  | 56,563                      | (241,911)           | 113,595             |
| Less: Comprehensive income<br>attributable to noncontrolling<br>interests              | -                           | -             | -  | 23,778                      | -                   | 23,778              |
| Comprehensive income<br>attributable to Community Health<br>Systems, Inc. stockholders | \$ 89,817                   | \$ 89,817     | \$ 119,309                                     | \$ 32,785                   | \$ (241,911)        | \$ 89,817           |

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****Condensed Consolidating Statement of Cash Flows****Three Months Ended March 31, 2013**

|  | <b>Parent<br/>Guarantor</b> | <b>Issuer</b> | <b>Other<br/>Guarantors<br/>(In thousands)</b> | <b>Non -<br/>Guarantors</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|-----------------------------|---------------|--|-----------------------------|---------------------|---------------------|
| Net cash (used in) provided by operating activities                            | \$ (4,881)                  | \$ (12,879)   | \$ 173,042                                     | \$ (98,128)                 | \$ -                | \$ 57,154           |
| Cash flows from investing activities:  |                             |               |  |                             |                     |                     |
| Acquisitions of facilities and other related equipment                         | -                           | -             | (3,656)  | (1,094)                     | -                   | (4,750)             |
| Purchases of property and equipment  | -                           | -             | (94,760)                                       | (18,099)                    | -                   | (112,859)           |
| Proceeds from sale of property and equipment                                   | -                           | -             | 526  | 188                         | -                   | 714                 |
| Increase in other investments  | -                           | -             | (55,469)                                       | (14,014)                    | -                   | (69,483)            |
| Net cash used in investing activities  | -                           | -             | (153,359)                                      | (33,019)                    | -                   | (186,378)           |
| Cash flows from financing activities:  |                             |               |  |                             |                     |                     |
| Proceeds from exercise of stock options  | 73,429                      | -             | -  | -                           | -                   | 73,429              |
| Repurchase of restricted stock shares for payroll tax withholding requirements | (14,478)                    | -             | -  | -                           | -                   | (14,478)            |
| Stock buy-back   | (18,726)                    | -             | -  | -                           | -                   | (18,726)            |
| Deferred financing costs   | -                           | (126)         | -  | (752)                       | -                   | (878)               |
| Excess tax benefit relating to stock-based compensation                        | 5,358                       | -             | -  | -                           | -                   | 5,358               |
| Redemption of noncontrolling investments in joint ventures                     | -                           | -             | -  | (436)                       | -                   | (436)               |
| Distributions to noncontrolling investors in joint ventures                    | -                           | -             | -  | (15,291)                    | -                   | (15,291)            |
| Changes in intercompany balances with affiliates, net                          | (40,702)                    | 219,483       | (132,277)                                      | (46,504)                    | -                   | -                   |
| Borrowings under credit agreement  | -                           | 90,000        | 10,679   | 214                         | -                   | 100,893             |
| Issuance of long-term debt   | -                           | -             | -  | -                           | -                   | -                   |
| Proceeds from receivables facility   | -                           | -             | -  | 300,000                     | -                   | 300,000             |
| Repayments of long-term indebtedness   | -                           | (296,478)     | (6,092)  | (100,842)                   | -                   | (403,412)           |
| Net cash provided by (used in) financing activities                            | 4,881                       | 12,879        | (127,690)                                      | 136,389                     | -                   | 26,459              |

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|  |      |      |            |            |      |            |
|--|------|------|------------|------------|------|------------|
| Net change in cash and cash equivalents          | -    | -    | (108,007)  | 5,242      | -    | (102,765)  |
| Cash and cash equivalents at beginning of period | -    | -    | 271,559    | \$ 116,254 | -    | 387,813    |
| Cash and cash equivalents at end of period       | \$ - | \$ - | \$ 163,552 | \$ 121,496 | \$ - | \$ 285,048 |

**Table of Contents****COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) CONTINUED****Condensed Consolidating Statement of Cash Flows****Three Months Ended March 31, 2012**

|  | <b>Parent<br/>Guarantor</b> | <b>Issuer</b> | <b>Other<br/>Guarantors<br/>(In thousands)</b> | <b>Non -<br/>Guarantors</b> | <b>Eliminations</b> | <b>Consolidated</b> |
|--|-----------------------------|---------------|--|-----------------------------|---------------------|---------------------|
| Net cash (used in) provided by operating activities                            | \$ (1,230)                  | \$ (26,237)   | \$ (67,958)                                    | \$ 282,735                  | \$ -                | \$ 187,310          |
| Cash flows from investing activities:  |                             |               |  |                             |                     |                     |
| Acquisitions of facilities and other related equipment                         | -                           | -             | (242,977)                                      | (5,459)                     | -                   | (248,436)           |
| Purchases of property and equipment  | -                           | -             | (127,673)                                      | (57,230)                    | -                   | (184,903)           |
| Proceeds from sale of property and equipment                                   | -                           | -             | 688  | 60                          | -                   | 748                 |
| Increase in other investments  | -                           | 10,000        | (45,612)                                       | (32,096)                    | -                   | (67,708)            |
| Net cash used in investing activities  | -                           | 10,000        | (415,574)                                      | (94,725)                    | -                   | (500,299)           |
| Cash flows from financing activities:  |                             |               |  |                             |                     |                     |
| Proceeds from exercise of stock options  | 308                         | -             | -  | -                           | -                   | 308                 |
| Repurchase of restricted stock shares for payroll tax withholding requirements | (9,032)                     | -             | -  | -                           | -                   | (9,032)             |
| Stock buy-back   | -                           | -             | -  | -                           | -                   | -                   |
| Deferred financing costs   | -                           | (24,787)      | -  | -                           | -                   | (24,787)            |
| Excess tax benefit relating to stock-based compensation                        | 1,004                       | -             | -  | -                           | -                   | 1,004               |
| Redemption of noncontrolling investments in joint ventures                     | -                           | -             | -  | (31,096)                    | -                   | (31,096)            |
| Distributions to noncontrolling investors in joint ventures                    | -                           | -             | -  | (27,038)                    | -                   | (27,038)            |
| Changes in intercompany balances with affiliates, net                          | 8,950                       | (58,772)      | 469,006  | (419,184)                   | -                   | -                   |
| Borrowings under credit agreements   | -                           | 2,695,000     | 9,337  | -                           | -                   | 2,704,337           |
| Issuance of long-term debt   | -                           | 1,025,000     | -  | -                           | -                   | 1,025,000           |
| Proceeds from receivables facility   | -                           | -             | -  | 300,000                     | -                   | 300,000             |
| Repayments of long-term indebtedness   | -                           | (3,620,204)   | (5,334)  | (736)                       | -                   | (3,626,274)         |
| Net cash provided by (used in) financing activities                            | 1,230                       | 16,237        | 473,009  | (178,054)                   | -                   | 312,422             |

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|  |      |      |          |            |      |            |
|--|------|------|----------|------------|------|------------|
| Net change in cash and cash equivalents          | -    | -    | (10,523) | 9,956      | -    | (567)      |
| Cash and cash equivalents at beginning of period | -    | -    | 14,536   | \$ 115,329 | -    | 129,865    |
| Cash and cash equivalents at end of period       | \$ - | \$ - | \$ 4,013 | \$ 125,285 | \$ - | \$ 129,298 |



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## **Table of Contents**

### **Item 2. *Management's Discussion and Analysis of Financial Condition and Results of Operations***

You should read this discussion together with our unaudited condensed consolidated financial statements and the accompanying notes included herein.

Throughout this Quarterly Report on Form 10-Q, Community Health Systems, Inc., the parent company, and its consolidated subsidiaries are referred to on a collective basis using words like we, our, us and the Company. This drafting style is not meant to indicate that the publicly-traded parent company or any subsidiary of the parent company owns or operates any asset, business, or property. The hospitals, operations and businesses described in this filing are owned and operated, and management services provided, by distinct and indirect subsidiaries of Community Health Systems, Inc.

#### **Executive Overview**

We are one of the largest publicly-traded operators of hospitals in the United States in terms of number of facilities and net operating revenues. We provide healthcare services through the hospitals that we own and operate in non-urban and selected urban markets throughout the United States. We generate revenues by providing a broad range of general and specialized hospital healthcare services and other outpatient services to patients in the communities in which we are located. As of March 31, 2013, we owned or leased 135 hospitals comprised of 131 general acute care hospitals and four stand-alone rehabilitation or psychiatric hospitals. In addition to our hospitals and related businesses, we own and operate home care agencies, located primarily in markets where we also operate a hospital. Also, through our wholly-owned subsidiary, Quorum Health Resources, LLC, or QHR, we provide management and consulting services to non-affiliated general acute care hospitals located throughout the United States. For the hospitals and home care agencies that we own and operate, we are paid for our services by governmental agencies, private insurers and directly by the patients we serve. For our management and consulting services, we are paid by the non-affiliated hospitals utilizing our services.

In March 2013, we announced a new strategic alliance with Cleveland Clinic, one of the nation's leading academic medical centers with a reputation for innovative approaches to patient care and cost reduction. We believe this alliance will enable us to find new and collaborative ways to enhance quality, reduce costs and create greater value for the services provided to our patients. Key components of this alliance include the implementation of Cleveland Clinic quality programs in select markets in which we operate as well as the potential for future joint ventures, clinical research and shared innovations.

Our net operating revenues for the three months ended March 31, 2013 increased to approximately \$3.312 billion, as compared to approximately \$3.297 billion for the three months ended March 31, 2012. Income from continuing operations, before noncontrolling interests, for the three months ended March 31, 2013 decreased 3.4% over the three months ended March 31, 2012 to \$96.3 million compared to \$99.7 million. Included in income from continuing operations for the three months ended March 31, 2012, is a \$42.8 million after-tax benefit from the resolution of an industry-wide governmental settlement and a payment update related to prior periods, an \$8.7 million after-tax charge for certain legal and regulatory matters and a \$39.5 million after-tax loss from the early extinguishment of debt. Total inpatient admissions for the three months ended March 31, 2013 decreased 4.4%, compared to the three months ended March 31, 2012, and adjusted admissions for the three months ended March 31, 2013 decreased 3.5%, compared to the three months ended March 31, 2012. On a same-store basis, admissions decreased 5.9% and adjusted admissions decreased 5.2% compared with the three months ended March 31, 2012.

Self-pay revenues represented approximately 13.4% of our net operating revenues, net of contractual allowances and discounts (but before provision for bad debts), for both of the three-month periods ended March 31, 2013 and 2012. The amount of foregone revenue related to providing charity care services as a percentage of net operating revenues was approximately 5.3% and 4.8% for the three months ended March 31, 2013 and 2012, respectively. Direct and indirect costs incurred by us in providing charity care services were approximately 0.9% of net operating revenues for both of the three-month periods ended March 31, 2013 and 2012.

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**Table of Contents**

The Patient Protection and Affordable Care Act, or PPACA, was signed into law on March 23, 2010. In addition, the Health Care and Education Affordability Reconciliation Act of 2010, or Reconciliation Act, which contains a number of amendments to PPACA, was signed into law on March 30, 2010. These two healthcare acts, referred to collectively as the Reform Legislation, include a mandate that requires substantially all U.S. citizens to maintain medical insurance coverage, which will ultimately increase the number of persons with access to health insurance in the United States. The Reform Legislation, as originally enacted, is expected to expand health insurance coverage through a combination of public program expansion and private sector health insurance reforms. We believe the expansion of private sector and Medicaid coverage will, over time, increase our reimbursement related to providing services to individuals who were previously uninsured, which should reduce our expense from uncollectible accounts receivable. The Reform Legislation also makes a number of other changes to Medicare and Medicaid, such as reductions to the Medicare annual market basket update for federal fiscal years 2010 through 2019, a productivity offset to the Medicare market basket update which began October 1, 2011, and a reduction to the Medicare and Medicaid disproportionate share payments, that could adversely impact the reimbursement received under these programs. The various provisions in the Reform Legislation that directly or indirectly affect reimbursement are scheduled to take effect over a number of years. Over time, we believe the net impact of the overall changes as a result of the Reform Legislation will have a positive effect on our net operating revenues. Other provisions of the Reform Legislation, such as requirements related to employee health insurance coverage, should increase our operating costs.

Also included in the Reform Legislation are provisions aimed at reducing fraud, waste and abuse in the healthcare industry. These provisions allocate significant additional resources to federal enforcement agencies and expand the use of private contractors to recover potentially inappropriate Medicare and Medicaid payments. The Reform Legislation amends several existing federal laws, including the Medicare Anti-Kickback Statute and the False Claims Act, making it easier for government agencies and private plaintiffs to prevail in lawsuits brought against healthcare providers. These amendments also make it easier for potentially severe fines and penalties to be imposed on healthcare providers accused of violating applicable laws and regulations.

On June 28, 2012, the Supreme Court of the United States largely upheld the constitutionality of the Reform Legislation, though it overturned an aspect of the legislation that would have permitted the Federal government to withhold all Medicaid funding from a state if that state did not expand Medicaid coverage to the extent required by the Reform Legislation. The Supreme Court's ruling instead held that only new incremental funding could be withheld from a state in such a situation. As a result, states will face less severe financial consequences if they refuse to expand Medicaid coverage to individuals with incomes below certain thresholds. Since the Supreme Court's ruling, some states have suggested that, for budgetary and other reasons, they would not expand their Medicaid programs. If states refuse to expand their Medicaid programs, the number of uninsured patients at our hospitals will decline by a smaller margin as compared to our expectations when the Reform Legislation was first adopted. In response to the Supreme Court ruling, the previous estimates of the reduction in uninsured individuals as a result of the Reform Legislation have been revised, with approximately 27 million additional individuals expected to have health insurance coverage by 2017. Because of the many variables involved, including clarifications and modifications resulting from the rule-making process, the development of agency guidance and future judicial interpretations, whether and how many states decide to expand or not to expand Medicaid coverage, the number of uninsured who elect to purchase health insurance coverage, and budgetary issues at federal and state levels, we may not be able to realize the positive impact the Reform Legislation may have on our business, results of operations, cash flow, capital resources and liquidity. Furthermore, we cannot predict whether we will be able to modify certain aspects of our operations to offset any potential adverse consequences from the Reform Legislation.

In a number of markets, we have partnered with local physicians in the ownership of our facilities. Such investments have been permitted under an exception to the physician self-referral law, or Stark Law, that allows physicians to invest in an entire hospital (as opposed to individual hospital departments). The Reform Legislation changes the whole hospital exception to the Stark Law. The Reform Legislation permits existing physician investments in a whole hospital to continue under a grandfather clause if the arrangement satisfies certain requirements and restrictions, but physicians are now prohibited, from the time the Reform Legislation became effective, from increasing the aggregate percentage of their ownership in the hospital. The Reform Legislation also restricts the ability of existing physician-owned hospitals to expand the capacity of their facilities.

**Table of Contents**

In addition to the Reform Legislation, the American Recovery and Reinvestment Act of 2009 included provisions for implementing health information technology under the Health Information Technology for Economic and Clinical Health Act, or HITECH. These provisions were designed to increase the use of electronic health records, or EHR, technology and establish the requirements for a Medicare and Medicaid incentive payments program beginning in 2011 for eligible hospitals and providers that adopt and meaningfully use certified EHR technology. These incentive payments are intended to offset a portion of the costs incurred to implement and qualify as a meaningful user of EHR. Rules adopted in July 2010 by the Department of Health and Human Services established an initial set of standards and certification criteria. Our hospital facilities have begun to implement EHR technology on a facility-by-facility basis beginning in 2011. We anticipate recognizing incentive reimbursement related to the Medicare or Medicaid incentives as we are able to implement the certified EHR technology, meet the defined meaningful use criteria, and information from completed cost report periods is available from which to calculate the incentive reimbursement. The timing of recognizing incentive reimbursement will not correlate with the timing of recognizing operating expenses and incurring capital costs in connection with the implementation of EHR technology which may result in material period-to-period changes in our future results of operations. Hospitals that do not qualify as a meaningful user of EHR technology by 2015 are subject to a reduced market basket update to the inpatient prospective payment system standardized amount in 2015 and each subsequent fiscal year. Although we believe that our hospital facilities will be in compliance with the EHR standards by 2015, there can be no assurance that all of our facilities will be in compliance and therefore not subject to the penalty provisions of HITECH. We recognized approximately \$20.9 million and \$26.2 million during the three months ended March 31, 2013 and 2012, respectively, of incentive reimbursement for HITECH incentive reimbursements from Medicare and Medicaid related to certain of our hospitals and for certain of our employed physicians, which are presented as a reduction of operating expenses.

As a result of our current levels of cash, available borrowing capacity, long-term outlook on our debt repayments, the refinancing of our term loans and our continued projection of our ability to generate cash flows, we do not anticipate a significant impact on our ability to invest the necessary capital in our business over the next twelve months and into the foreseeable future. We believe there continues to be ample opportunity for growth in substantially all of our markets by decreasing the need for patients to travel outside their communities for healthcare services. Furthermore, we continue to benefit from synergies from our acquisitions and will continue to strive to improve operating efficiencies and procedures in order to improve our profitability at all of our hospitals.

**Sources of Revenue**

The following table presents the approximate percentages of operating revenues, net of contractual allowances and discounts (but before provision for bad debts), by payor source for the periods indicated. The data for the periods presented are not strictly comparable due to the effect that hospital acquisitions have had on these statistics.

|   | <b>Three Months Ended</b> |                                 |
|---|---------------------------|---------------------------------|
|   | <b>2013</b>               | <b>March 31,</b><br><b>2012</b> |
| Medicare                                  | 26.1 %                    | 26.6 % (1)                      |
| Medicaid                                  | 8.8                       | 8.5                             |
| Managed Care and other third-party payors | 51.7                      | 51.5                            |
| Self-pay                                  | 13.4                      | 13.4                            |
| Total                                     | <u>100.0 %</u>            | <u>100.0 %</u>                  |

(1) Excludes the \$80.8 million reimbursement settlement and payment update as discussed below.

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**Table of Contents**

As shown above, we receive a substantial portion of our revenues from the Medicare and Medicaid programs. Included in Managed Care and other third-party payors is operating revenues from insurance companies with which we have insurance provider contracts, Medicare managed care, insurance companies for which we do not have insurance provider contracts, workers' compensation carriers and non-patient service revenue, such as rental income and cafeteria sales. In the future, we generally expect revenues received from the Medicare and Medicaid programs to increase due to the general aging of the population. In addition, the Reform Legislation, currently in effect, should increase the number of insured patients, which, in turn, should reduce revenues from self-pay patients and reduce our provision for bad debts. The Reform Legislation, however, imposes significant reductions in amounts the government pays Medicare managed care plans. The trend toward increased enrollment in Medicare managed care may adversely affect our operating revenue growth. Other provisions in the Reform Legislation impose minimum medical-loss ratios and require insurers to meet specific benefit requirements. Furthermore, in the normal course of business, managed care programs, insurance companies and employers actively negotiate the amounts paid to hospitals. There can be no assurance that we will retain our existing reimbursement arrangements or that these third-party payors will not attempt to further reduce the rates they pay for our services.

Net operating revenues include amounts estimated by management to be reimbursable by Medicare and Medicaid under prospective payment systems and provisions of cost-based reimbursement and other payment methods. In addition, we are reimbursed by non-governmental payors using a variety of payment methodologies. Amounts we receive for treatment of patients covered by these programs are generally less than the standard billing rates. We account for the differences between the estimated program reimbursement rates and the standard billing rates as contractual allowance adjustments, which we deduct from gross revenues to arrive at net operating revenues. Final settlements under some of these programs are subject to adjustment based on administrative review and audit by third parties. We account for adjustments to previous program reimbursement estimates as contractual allowance adjustments and report them in the periods that such adjustments become known. During the three months ended March 31, 2012, we recognized a net after-tax benefit of \$42.8 million from the resolution of an industry-wide governmental settlement and a payment update related to prior periods. Other than these items, contractual allowance adjustments related to final settlements and previous program reimbursement estimates impacted net operating revenues and net income by an insignificant amount in both of the three-month periods ended March 31, 2013 and 2012.

The payment rates under the Medicare program for hospital inpatient and outpatient acute care services are based on a prospective payment system, depending upon the diagnosis of a patient's condition. These rates are indexed for inflation annually, although increases have historically been less than actual inflation. On August 31, 2012, CMS issued the final rule to adjust this index by 2.6% for hospital inpatient acute care services that are reimbursed under the prospective payment system. The final rule also made other payment adjustments that, coupled with the 0.7% multifactor productivity reduction and a 0.1% reduction to hospital inpatient rates implemented pursuant to the Reform Legislation, yielded an estimated net 2.3% increase in reimbursement for hospital inpatient acute care services beginning October 1, 2012. Reductions in the rate of increase or overall reductions in Medicare reimbursement may cause a decline in the growth of our net operating revenues.

Currently, several states utilize supplemental reimbursement programs for the purpose of providing reimbursement to providers to offset a portion of the cost of providing care to Medicaid and indigent patients. These programs are designed with input from Centers for Medicare and Medicaid Services, or CMS, and are funded with a combination of state and federal resources, including, in certain instances, fees or taxes levied on the providers. Similar programs are also being considered by other states. After these supplemental programs are signed into law, we recognize revenue and related expenses in the period in which amounts are estimable and collection is reasonably assured. Reimbursement under these programs is reflected in net operating revenues and included as Medicaid revenue in the table above, and fees, taxes or other program related costs are reflected in other operating expenses.

In addition, specified managed care programs, insurance companies and employers are actively negotiating the amounts paid to hospitals. The trend toward increased enrollment in managed care may adversely affect our net operating revenue growth.

**Table of Contents****Results of Operations**

Our hospitals offer a variety of services involving a broad range of inpatient and outpatient medical and surgical services. These include general acute care, emergency room, general and specialty surgery, critical care, internal medicine, obstetrics, diagnostic services, psychiatric and rehabilitation services. The strongest demand for hospital services generally occurs during January through April and the weakest demand for these services occurs during the summer months. Accordingly, eliminating the effect of new acquisitions, our net operating revenues and earnings are historically highest during the first quarter and lowest during the third quarter.

The following tables summarize, for the periods indicated, selected operating data.

|   | <b>Three Months Ended</b> |              |
|---|---------------------------|--------------|
|   | <b>2013</b>               | <b>2012</b>  |
| <b>March 31,</b>  |                           |              |
| <b>(Expressed as a percentage of net operating revenues)</b>                  |                           |              |
| <b>Consolidated:</b>  |                           |              |
| Net operating revenues  | 100.0 %                   | 100.0 %      |
| Operating expenses (a)  | (85.6)                    | (84.1)       |
| Depreciation and amortization   | (5.8)                     | (5.3)        |
| <b>Income from operations</b>   | <b>8.6</b>                | <b>10.6</b>  |
| Interest expense, net   | (4.8)                     | (4.7)        |
| Loss from early extinguishment of debt  | -                         | (1.9)        |
| Equity in earnings of unconsolidated affiliates                               | 0.5                       | 0.4          |
| <b>Income from continuing operations before income taxes</b>                  | <b>4.3</b>                | <b>4.4</b>   |
| Provision for income taxes  | (1.4)                     | (1.4)        |
| <b>Income from continuing operations</b>                                      | <b>2.9</b>                | <b>3.0</b>   |
| Loss from discontinued operations, net of taxes                               | -                         | -            |
| <b>Net income</b>   | <b>2.9</b>                | <b>3.0</b>   |
| Less: Net income attributable to noncontrolling interests                     | (0.5)                     | (0.7)        |
| <b>Net income attributable to Community Health Systems, Inc. stockholders</b> | <b>2.4 %</b>              | <b>2.3 %</b> |

**Table of Contents**

|   | <b>Three Months Ended<br/>March 31, 2013</b> |
|---|--|
| Percentage increase (decrease) from same period prior year:               |  |
| Net operating revenues  | 0.4 %  |
| Admissions  | (4.4)  |
| Adjusted admissions (b)   | (3.5)  |
| Average length of stay  | 2.3  |
| Net income attributable to Community Health Systems, Inc. (c)             | 4.9  |
| Same store percentage increase (decrease) from same period prior year (d) |  |
| Net operating revenues  | 1.4 %  |
| Admissions  | (5.9)  |
| Adjusted admissions (b)   | (5.2)  |

- (a) Operating expenses include salaries and benefits, supplies, other operating expenses, electronic health records incentive reimbursement and rent.
- (b) Adjusted admissions is a general measure of combined inpatient and outpatient volume. We computed adjusted admissions by multiplying admissions by gross patient revenues and then dividing that number by gross inpatient revenues.
- (c) Includes loss from discontinued operations.
- (d) Includes acquired hospitals to the extent we operated them in both years.

**Three Months Ended March 31, 2013 Compared to Three Months Ended March 31, 2012**

Net operating revenues increased \$14.7 million to approximately \$3.312 billion for the three months ended March 31, 2013, from approximately \$3.297 billion for the three months ended March 31, 2012. Included in 2012 net operating revenues on a non-same store basis is approximately \$101.8 million of net operating revenues from an industry-wide settlement with the United States Department of Health and Human Services and CMS, based on a claim that acute-care hospitals in the U.S. were underpaid from the Medicare inpatient prospective payment system in federal fiscal years 1999 through 2011. The underpayments resulted from calculations related to the rural floor budget neutrality adjustments implemented in connection with the Balanced Budget Act of 1997. Also included in 2012 net operating revenues is an unfavorable adjustment of approximately \$21.0 million, related to the revised Supplemental Security Income ratios issued for federal fiscal years 2006 through 2009 utilized for calculating Medicare Disproportionate Share Hospital reimbursements. Excluding the \$80.8 million net effect of these two items on 2012, net operating revenues for the three months ended March 31, 2013 increased \$95.5 million. Growth from hospitals owned throughout both periods contributed \$46.3 million of that increase and \$49.2 million was contributed by hospitals acquired in 2012. On a same-store basis, net operating revenues increased 1.4%. The increased net operating revenues contributed by hospitals that we owned throughout both periods were primarily attributable to favorable changes to payor mix and general rate and reimbursement increases, including revenues from states with provider assessment programs.

On a consolidated basis, inpatient admissions decreased by 4.4% and adjusted admissions decreased by 3.5% during the three months ended March 31, 2013. On a same-store basis, inpatient admissions decreased by 5.9% and adjusted admissions decreased by 5.2% during the three months ended March 31, 2013. This decrease in same-store inpatient admissions was significantly impacted by seasonality factors, including the loss of one day in 2013 as compared to 2012, which was a leap year, as well as additional holidays that fell on weekdays during the first quarter in 2013. The decrease was also reflective of lower admissions from women's services including obstetrics and gynecology, fewer flu and respiratory-related admissions and reductions due to turnover with our employed physicians during the three months ended March 31, 2013, as compared to the three months ended March 31, 2012.

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**Table of Contents**

Operating expenses, excluding depreciation and amortization, as a percentage of net operating revenues, increased from 84.1% for the three months ended March 31, 2012 to 85.6% for the three months ended March 31, 2013. Salaries and benefits, as a percentage of net operating revenues, increased from 46.3% for the three months ended March 31, 2012 to 47.6% for the three months ended March 31, 2013. This increase in salaries and benefits was primarily due to the impact of recent acquisitions. Supplies, as a percentage of net operating revenues, decreased from 15.1% for the three months ended March 31, 2012 to 15.0% for the three months ended March 31, 2013. Other operating expenses, as a percentage of net operating revenues, decreased from 21.5% for the three months ended March 31, 2012 to 21.4% for the three months ended March 31, 2013. Rent, as a percentage of net operating revenues, increased from 2.0% for the three months ended March 31, 2012 to 2.2% for the three months ended March 31, 2013.

Electronic health records incentive reimbursements represent those incentives under the HITECH Act for which the recognition criterion has been met. We have recognized approximately \$20.9 million and \$26.2 million of incentive reimbursements, or 0.6% and 0.8% of net operating revenues, for the three months ended March 31, 2013 and 2012, respectively. We received cash payments of \$45.1 million and \$5.8 million for these incentives, of which \$19.9 million and \$1.0 million was recorded as deferred revenue as all criteria for gain recognition had not been met, during the three months ended March 31, 2013 and 2012, respectively. Operating expenses incurred related to the installation and adoption of electronic health records, including depreciation and amortization, totaled approximately 0.6% of net operating revenues, of which depreciation and amortization represented 0.4% of net operating revenues for the three months ended March 31, 2013. Operating expenses incurred related to the installation and adoption of electronic health records, including depreciation and amortization, totaled approximately 0.4% of net operating revenues, of which depreciation and amortization represented 0.2% of net operating revenues for the three months ended March 31, 2012.

Depreciation and amortization, as a percentage of net operating revenues, increased from 5.3% for the three months ended March 31, 2012 to 5.8% for the three months ended March 31, 2013. This increase was due primarily to depreciation and amortization expense related to electronic health records software and hardware.

Interest expense, net, increased by \$4.2 million from \$152.2 million for the three months ended March 31, 2012, to \$156.4 million for the three months ended March 31, 2013. An increase in our average outstanding debt during 2013, compared to 2012, resulted in an increase in interest expense of \$5.4 million. Additionally, interest expense increased by \$4.1 million as a result of less interest being capitalized during 2013, as compared to 2012, because the prior year period had more major construction projects. These increases were partially offset by a decrease in interest expense of \$1.7 million due to one additional day of interest expense in the prior year period since 2012 was a leap year. Also, a decrease in interest rates during 2013, compared to 2012, resulted in a decrease in interest expense of \$3.6 million.

The loss from early extinguishment of debt of \$1.3 million was recognized during the three months ended March 31, 2013 after the repayment of \$206.5 million of the term loans due 2014. The loss from early extinguishment of debt of \$63.4 million was recognized during the three months ended March 31, 2012 after the purchase and redemption of \$850 million of the 8<sup>7</sup>/<sub>8</sub>% Senior Notes due 2015 and the repayment of existing term loans and revolving credit facility under the Credit Facility as further discussed in Liquidity and Capital Resources.

Equity in earnings of unconsolidated affiliates, as a percentage of net operating revenues, increased from 0.4% for the three months ended March 31, 2012 to 0.5% for the three months ended March 31, 2013.

The net results of the above mentioned changes resulted in income from continuing operations before income taxes decreasing \$1.5 million from \$145.5 million for the three months ended March 31, 2012 to \$144.0 million for the three months ended March 31, 2013.

Provision for income taxes from continuing operations increased from \$45.8 million for the three months ended March 31, 2012 to \$47.7 million for the three months ended March 31, 2013 due to the increase in income from continuing operations before income taxes. Our effective tax rates were 33.1% and 31.5% for the three months ended March 31, 2013 and 2012, respectively. The increase in our effective tax rate is primarily related to an increase in our state effective tax rate.

Income from continuing operations, as a percentage of net operating revenues, decreased from 3.0% for the three months ended March 31, 2012 to 2.9% for the three months ended March 31, 2013.

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**Table of Contents**

Net income, as a percentage of net operating revenues, decreased from 3.0% for the three months ended March 31, 2012 to 2.9% for the three months ended March 31, 2013.

Net income attributable to noncontrolling interests as a percentage of net operating revenues decreased from 0.7% for the three months ended March 31, 2012 to 0.5% for the three months ended March 31, 2013. The decrease in net income attributable to noncontrolling interests is primarily due to lower income from operations from our less than wholly-owned subsidiaries and also the reduction in hospital syndications as a result of the redemption of all of the physician ownership interests at several hospitals during 2012.

Net income attributable to Community Health Systems, Inc. was \$79.2 million for the three months ended March 31, 2013 compared to \$75.5 million for the three months ended March 31, 2012, an increase of 4.9%.

**Liquidity and Capital Resources**

Net cash provided by operating activities decreased \$130.1 million, from approximately \$187.3 million for the three months ended March 31, 2012 to approximately \$57.2 million for the three months ended March 31, 2013. The decrease in cash provided by operating activities is due primarily to a decrease in cash flows from accounts payable, accrued liabilities and income taxes, primarily as a result of the timing of payments of accounts payable and payroll-related accrued liabilities, which decreased cash flows from operating activities by \$193.8 million, a decrease in cash flow from the change in other assets and liabilities of \$26.0 million, a decrease from the change in the non-cash loss from early extinguishment of debt of \$62.1 million, a decrease in net income of \$2.9 million and a decrease in all other non-cash expenses of \$2.2 million. These decreases in cash flows were offset by an increase in cash flows from supplies, prepaid expenses and other current assets of \$123.4 million, primarily from the timing of recognition of the industry-wide governmental settlement in 2012, increase in cash generated from accounts receivable of \$15.7 million, and an increase in depreciation and amortization expense of \$17.8 million. Included in net cash provided by operating activities for the three months ended March 31, 2013 is \$45.1 million of cash received for HITECH incentive reimbursements, compared to \$5.8 million for the three months ended March 31, 2012.

The cash used in investing activities decreased \$313.9 million, from approximately \$500.3 million for the three months ended March 31, 2012 to approximately \$186.4 million for the three months ended March 31, 2013. The decrease in cash used in investing activities was due to a decrease in cash paid for acquisitions of facilities and other related equipment of \$243.7 million, since there were no hospital acquisitions in the current period compared to three hospitals acquired in the first three months of 2012, and a decrease in the cash used for the purchase of property and equipment of \$72 million. These increases in cash outflows were partially offset by an increase in cash used for other investments of \$1.8 million. Included in cash outflows for other investments for the three months ended March 31, 2013 is approximately \$14.2 million of capital expenditures related to the purchase and implementation of certified EHR technology. The remaining cash outflows for other investments consists primarily of purchases and development of other internal-use software and payments made under non-employee physician recruiting agreements of \$55.3 million. We anticipate being able to fund future routine capital expenditures with cash flows generated from operations.

Our net cash provided by financing activities was \$26.5 million for the three months ended March 31, 2013, compared to \$312.4 million for the three months ended March 31, 2012. The decrease in cash provided by financing activities, in comparison to the prior year, is primarily due to a reduction in borrowings under our Credit Facility and the issuance of our 8% Senior Notes in 2012 totaling \$3.6 billion, but was mostly offset by an increase in the repayments of our long-term debt of \$3.2 billion and an increase in proceeds from the exercise of stock options of \$73.1 million.

***Capital Expenditures***

Cash expenditures for purchases of facilities and other related equipment were \$4.8 million for the three months ended March 31, 2013, compared to \$248.4 million for the three months ended March 31, 2012. The expenditures during the three months ended March 31, 2013 were for the purchase of surgery centers and other physician practices. The expenditures during the three months ended March 31, 2012 were for the purchase of two hospitals in Pennsylvania, one hospital in Illinois, a physician practice in Texas, surgery centers and other physician practices and the settlement of working capital items.



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**Table of Contents**

Excluding the cost to construct replacement hospitals, our cash expenditures for routine capital for the three months ended March 31, 2013 totaled \$112.7 million, compared to \$144.4 million for the three months ended March 31, 2012. These capital expenditures related primarily to the purchase of additional equipment, minor renovations and information systems infrastructure. Costs to construct replacement hospitals for the three months ended March 31, 2013 totaled \$0.2 million, compared to \$40.5 million for the three months ended March 31, 2012. The costs to construct replacement hospitals for the three months ended March 31, 2013 represent planning and construction costs for the replacement hospitals discussed below. The costs to construct replacement hospitals for the three months ended March 31, 2012 represent construction and equipment costs primarily for three replacement hospitals opened in 2012 located in Barstow, California; Valparaiso, Indiana; and Siloam Springs, Arkansas.

Pursuant to a hospital purchase agreement in effect as of March 31, 2013, and where final CON approval has been obtained, we have committed to build a replacement facility in York, Pennsylvania by July 2017. Construction costs, including equipment costs, for the York replacement facility is currently estimated to be approximately \$100.0 million. In addition, in October 2008, after the purchase of the noncontrolling owner's interest in our Birmingham, Alabama facility, we initiated the purchase of a site, which includes a partially constructed hospital structure, for a potential replacement to our existing Birmingham facility. In September 2010, we received approval of our request for a certificate of need from the Alabama Certificate of Need Review Board. This CON was challenged in the Alabama state circuit and appellate courts but has recently been upheld, with issuance subject to the final resolution of the appeal process. Our estimated construction costs, including the acquisition of the site and equipment costs, are approximately \$280.0 million for the Birmingham replacement facility.

***Capital Resources***

Net working capital was approximately \$1.4 billion at March 31, 2013, compared to \$1.3 billion at December 31, 2012, an increase of \$133.9 million, primarily the result of an increase in patient accounts receivable, partially offset by decreases in cash, accounts payable and employee compensation liabilities.

We obtained senior secured financing under the Credit Facility with a syndicate of financial institutions led by Credit Suisse, as administrative agent and collateral agent. A \$750 million revolving credit facility was available to us for working capital and general corporate purposes under the Credit Facility. The revolving credit facility also includes a subfacility for letters of credit and a swingline subfacility. The Credit Facility requires quarterly amortization payments of each term loan facility equal to 0.25% of the outstanding amount of the term loans. On November 5, 2010, we entered into an amendment and restatement of our existing Credit Facility. The amendment extended by two and a half years, until January 25, 2017, the maturity date of \$1.5 billion of our existing term loans under the Credit Facility and increased the pricing on these term loans to LIBOR plus 350 basis points. The amendment also increased our ability to issue additional indebtedness under the uncommitted incremental facility to \$1.0 billion from \$600 million, permitted us to issue term loan A loans under the incremental facility and provided up to \$2.0 billion of borrowing capacity from receivable transactions, an increase of \$0.5 billion, of which approximately \$1.7 billion would be required to be used for repayment of our existing term loans. On February 2, 2012, we completed a second amendment and restatement of the Credit Facility to extend an additional \$1.6 billion of our term loans due 2014 under the Credit Facility to match the maturity date and interest rate margins of the term loans due January 25, 2017. On August 3, 2012, we entered into Amendment No. 1 to the Credit Facility to provide increased flexibility for refinancing and repayment of the term loans due 2014 and amend certain other terms. On August 22, 2012, we entered into a loan modification agreement with respect to the Credit Facility to extend approximately \$340 million of the term loans due 2014 to match the maturity date and interest rate margins of the term loans due January 25, 2017. On November 27, 2012, we entered into Amendment No. 2 to the Credit Facility to provide increased flexibility for us to make investments and restricted payments, incur debt related to acquisitions, amend certain other terms of the Credit Facility, including the maximum leverage ratio and interest coverage ratio financial coverage levels, and add a one year 1% prepayment premium payable in connection with a repricing of the term loans due in 2017. The extended term loans are subject to customary acceleration events and earlier maturity if the repayment, extension or refinancing with longer maturity on substantially all of the outstanding term loans maturing July 25, 2014 does not occur by April 15, 2015. During the three months ended March 31, 2013, we paid down \$206.5 million of the term loans due 2014. The July 25, 2014 maturity date of the balance of the remaining non-extended term loans at March 31, 2013 of approximately \$59.6 million remains unchanged.

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**Table of Contents**

Effective March 6, 2012, we obtained a new \$750 million senior secured revolving credit facility, or the Replacement Revolver Facility, and a new \$750 million incremental term loan A facility, or the Incremental Term Loan. The Replacement Revolver Facility replaced in full the existing revolving credit facility under the Credit Facility. The net proceeds of the Incremental Term Loan were used to repay the same amount of the existing term loans under the Credit Facility. Both the Replacement Revolver Facility and the Incremental Term Loan have a maturity date of October 25, 2016, subject to customary acceleration events and to earlier maturity if the repayment, extension or refinancing with longer maturity debt of substantially all of the then outstanding term loans maturing July 25, 2014 and the now fully redeemed  $8\frac{7}{8}\%$  Senior Notes does not occur by April 25, 2014. The pricing on each of the Replacement Revolver Facility and the Incremental Term Loan is initially LIBOR plus a margin of 250 basis points, subject to adjustment based on our leverage ratio. The Incremental Term Loan amortizes at 5% in year one, 10% in years two and three, 15% in year four and 60% in year five.

The term loan facility must be prepaid in an amount equal to (1) 100% of the net cash proceeds of certain asset sales and dispositions by us and our subsidiaries, subject to certain exceptions and reinvestment rights, (2) 100% of the net cash proceeds of issuances of certain debt obligations or receivables-based financing by us and our subsidiaries, subject to certain exceptions, and (3) 50%, subject to reduction to a lower percentage based on our leverage ratio (as defined in the Credit Facility generally as the ratio of total debt on the date of determination to our EBITDA, as defined, for the four quarters most recently ended prior to such date), of excess cash flow (as defined) for any year, commencing in 2008, subject to certain exceptions. Voluntary prepayments and commitment reductions are permitted in whole or in part, without any premium or penalty, subject to minimum prepayment or reduction requirements.

The obligor under the Credit Facility is CHS. All of our obligations under the Credit Facility are unconditionally guaranteed by Community Health Systems, Inc. and certain of its existing and subsequently acquired or organized domestic subsidiaries. All obligations under the Credit Facility and the related guarantees are secured by a perfected first priority lien or security interest in substantially all of the assets of Community Health Systems, Inc., CHS and each subsidiary guarantor, including equity interests held by us or any subsidiary guarantor, but excluding, among others, the equity interests of non-significant subsidiaries, syndication subsidiaries, securitization subsidiaries and joint venture subsidiaries.

The loans under the Credit Facility bear interest on the outstanding unpaid principal amount at a rate equal to an applicable percentage plus, at our option, either (a) an Alternate Base Rate (as defined) determined by reference to the greater of (1) the Prime Rate (as defined) announced by Credit Suisse or (2) the Federal Funds Effective Rate (as defined) plus 0.5% or (3) the adjusted LIBOR rate on such day for a three-month interest period commencing on the second business day after such day plus 1%, or (b) a reserve adjusted LIBOR for dollars (Eurodollar rate) (as defined). The applicable percentage for Alternate Base Rate loans is 1.25% for term loans due 2014 and 2.50% for term loans due 2017. The applicable percentage for Eurodollar rate loans is 2.25% for term loans due 2014 and 3.5% for term loans due 2017. The applicable percentage for revolving loans and Incremental Term Loans is 1.50% for Alternate Base Rate loans and 2.50% for Eurodollar loans, in each case subject to reduction based on our leverage ratio. Loans under the swingline subfacility bear interest at the rate applicable to Alternate Base Rate loans under the Credit Facility.

We have agreed to pay letter of credit fees equal to the applicable percentage then in effect with respect to Eurodollar rate loans under the revolving credit facility times the maximum aggregate amount available to be drawn under all letters of credit outstanding under the subfacility for letters of credit. The issuer of any letter of credit issued under the subfacility for letters of credit will also receive a customary fronting fee and other customary processing charges. We are obligated to pay commitment fees of 0.50% per annum (subject to reduction based upon our leverage ratio), on the unused portion of the revolving credit facility. For purposes of this calculation, swingline loans are not treated as usage of the revolving credit facility.

The Credit Facility contains customary representations and warranties, subject to limitations and exceptions, and customary covenants restricting our and our subsidiaries' ability, subject to certain exception, to, among other things, (1) declare dividends, make distributions or redeem or repurchase capital stock, (2) prepay, redeem or repurchase other debt, (3) incur liens or grant negative pledges, (4) make loans and investments and enter into acquisitions and joint ventures, (5) incur additional indebtedness or provide certain guarantees, (6) make capital expenditures, (7) engage in mergers, acquisitions and asset sales, (8) conduct transactions with affiliates, (9) alter the nature of our businesses, (10) grant certain guarantees with respect to physician practices, (11) engage in sale and leaseback transactions or (12) change our fiscal year. We and our subsidiaries are also required to comply with specified financial covenants (consisting of a leverage ratio and an interest coverage ratio) and various affirmative covenants.

**Table of Contents**

Events of default under the Credit Facility include, but are not limited to, (1) our failure to pay principal, interest, fees or other amounts under the credit agreement when due (taking into account any applicable grace period), (2) any representation or warranty proving to have been materially incorrect when made, (3) covenant defaults subject, with respect to certain covenants, to a grace period, (4) bankruptcy events, (5) a cross default to certain other debt, (6) certain undischarged judgments (not paid within an applicable grace period), (7) a change of control, (8) certain ERISA-related defaults and (9) the invalidity or impairment of specified security interests, guarantees or subordination provisions in favor of the administrative agent or lenders under the Credit Facility.

As of March 31, 2013, the availability for additional borrowings under our Credit Facility was approximately \$750 million pursuant to the revolving credit facility, of which \$37.8 million was set aside for outstanding letters of credit at March 31, 2013. We believe that these funds, along with internally generated cash and continued access to the bank credit and capital markets, will be sufficient to finance future acquisitions, capital expenditures and working capital requirements through the next 12 months and into the foreseeable future.

On March 21, 2012, CHS completed the secondary offering of \$1.0 billion aggregate principal amount of 8% Senior Notes, which were issued in a private placement (at a premium of 102.5%). The net proceeds from this issuance were used to finance the purchase of approximately \$850 million aggregate principal amount of CHS then outstanding  $8\frac{1}{8}\%$  Senior Notes, to pay related fees and expenses and for general corporate purposes. On March 21, 2012, CHS completed the cash tender offer for \$850 million of the then \$1.8 billion aggregate outstanding principal amount of  $8\frac{7}{8}\%$  Senior Notes.

On July 18, 2012, CHS completed an underwritten public offering under our automatic shelf registration filed with the SEC of \$1.2 billion aggregate principal amount of  $7\frac{1}{8}\%$  Senior Notes due 2020. The net proceeds of the offering were used to finance the purchase or redemption of the then outstanding \$934.3 million principal amount plus accrued interest of the  $8\frac{7}{8}\%$  Senior Notes, to pay for consents delivered in connection therewith, to pay related fees and expenses, and for general corporate purposes.

On August 17, 2012, CHS completed an underwritten public offering under our automatic shelf registration filed with the SEC of \$1.6 billion aggregate principal amount of  $5\frac{1}{8}\%$  Senior Secured Notes due 2018. The  $5\frac{1}{8}\%$  Senior Secured Notes are secured by a first-priority lien subject to a shared lien of equal priority with certain other obligations, including obligations under the Credit Facility, and subject to prior ranking liens permitted by the indenture governing the  $5\frac{1}{8}\%$  Senior Secured Notes on substantially the same assets, subject to certain exceptions, that secure CHS obligations under the Credit Facility. The net proceeds of the offering, together with available cash on hand, were used to finance the prepayment of \$1.6 billion of the outstanding term loans due 2014 under the Credit Facility and related fees and expenses.

On March 21, 2012, through certain of its subsidiaries, CHS entered into an accounts receivable loan agreement, or the Receivables Facility, with a group of lenders and banks, Credit Agricole Corporate and Investment Bank, as a managing agent and as the administrative agent, and The Bank of Nova Scotia, as a managing agent. On March 7, 2013, CHS and certain of its subsidiaries amended the Receivables Facility to add an additional managing agent, The Bank of Tokyo-Mitsubishi UFJ, Ltd., to increase the size of the facility from \$300 million to \$500 million and to extend the scheduled termination date. Additional subsidiaries also agreed to participate in the Receivables Facility as of that date. The existing and future non-self pay patient-related accounts receivable, or the Receivables, for certain of our hospitals serve as collateral for the outstanding borrowings under the Receivables Facility. The interest rate on the borrowings is based on the commercial paper rate plus an applicable interest rate spread. Unless earlier terminated or subsequently extended pursuant to its terms, the Receivables Facility will expire on March 21, 2015, subject to customary termination events that could cause an early termination date. We maintain effective control over the Receivables because, pursuant to the terms of the Receivables Facility, the Receivables are sold from certain of our subsidiaries to CHS, and CHS then sells or contributes the Receivables to a special-purpose entity that is wholly-owned by CHS. The wholly-owned special-purpose entity in turn grants security interests in the Receivables in exchange for borrowings obtained from the group of third-party lenders and banks of up to \$500 million outstanding from time to time based on the availability of eligible Receivables and other customary factors. The group of third-party lenders and banks do not have recourse to us or our subsidiaries beyond the assets of the wholly-owned special-purpose entity that collateralizes the loan. The Receivables and other assets of the wholly-owned special-purpose entity will be available first and foremost to satisfy the claims of the creditors of such entity. The outstanding borrowings pursuant to the Receivables Facility at March 31, 2013 totaled \$500.0 million and are classified as long-term debt on the condensed consolidated balance sheet. At March 31, 2013, the carrying amount of Receivables included in the Receivables Facility totaled approximately \$969.4 million and is included in patient accounts receivable on the condensed consolidated balance sheet.

**Table of Contents**

As of March 31, 2013, we are currently a party to the following interest rate swap agreements to limit the effect of changes in interest rates on approximately 63% of our variable rate debt. On each of these swaps, we receive a variable rate of interest based on the three-month LIBOR, in exchange for the payment by us of a fixed rate of interest. We currently pay, on a quarterly basis, a margin above LIBOR of 225 basis points for revolving credit and term loans due 2014, 250 basis points for the Replacement Revolver Facility and the Incremental Term Loan and 350 basis points for term loans due 2017 under the Credit Facility.

| Swap # | Notional Amount<br>(in 000 s) | Fixed Interest Rate | Termination Date  | Fair Value of<br>Liability (in 000 s) |
|--------|-------------------------------|---------------------|-------------------|---------------------------------------|
| 1      | \$ 100,000                    | 5.023 %             | May 30, 2013      | \$ 775                                |
| 2      | 300,000                       | 5.242 %             | August 6, 2013    | 5,219                                 |
| 3      | 100,000                       | 5.038 %             | August 30, 2013   | 1,982                                 |
| 4      | 50,000                        | 3.586 %             | October 23, 2013  | 928                                   |
| 5      | 50,000                        | 3.524 %             | October 23, 2013  | 911                                   |
| 6      | 100,000                       | 5.050 %             | November 30, 2013 | 3,168                                 |
| 7      | 200,000                       | 2.070 %             | December 19, 2013 | 2,528                                 |
| 8      | 100,000                       | 5.231 %             | July 25, 2014     | 6,453                                 |
| 9      | 100,000                       | 5.231 %             | July 25, 2014     | 6,453                                 |
| 10     | 200,000                       | 5.160 %             | July 25, 2014     | 12,719                                |
| 11     | 75,000                        | 5.041 %             | July 25, 2014     | 4,651                                 |
| 12     | 125,000                       | 5.022 %             | July 25, 2014     | 7,720                                 |
| 13     | 100,000                       | 2.621 %             | July 25, 2014     | 2,992                                 |
| 14     | 100,000                       | 3.110 %             | July 25, 2014     | 3,640                                 |
| 15     | 100,000                       | 3.258 %             | July 25, 2014     | 3,837                                 |
| 16     | 200,000                       | 2.693 %             | October 26, 2014  | 7,339                                 |
| 17     | 300,000                       | 3.447 %             | August 8, 2016    | 28,680                                |
| 18     | 200,000                       | 3.429 %             | August 19, 2016   | 19,124                                |
| 19     | 100,000                       | 3.401 %             | August 19, 2016   | 9,471                                 |
| 20     | 200,000                       | 3.500 %             | August 30, 2016   | 19,735                                |
| 21     | 100,000                       | 3.005 %             | November 30, 2016 | 8,595                                 |

The Credit Facility and/or the Notes contain various covenants that limit our ability to take certain actions including; among other things, our ability to:

incur, assume or guarantee additional indebtedness;

issue redeemable stock and preferred stock;

repurchase capital stock;

make restricted payments, including paying dividends and making investments;

redeem debt that is junior in right of payment to the Notes;

create liens without securing the Notes;

sell or otherwise dispose of assets, including capital stock of subsidiaries;

enter into agreements that restrict dividends from subsidiaries;

merge, consolidate, sell or otherwise dispose of substantial portions of our assets;

**Table of Contents**

enter into transactions with affiliates and

guarantee certain obligations.

In addition, our Credit Facility contains restrictive covenants and requires us to maintain specified financial ratios and satisfy other financial condition tests. Our ability to meet these restricted covenants and financial ratios and tests can be affected by events beyond our control, and we cannot assure you that we will meet those tests. A breach of any of these covenants could result in a default under our Credit Facility and/or the Notes. Upon the occurrence of an event of default under our Credit Facility or the Notes, all amounts outstanding under our Credit Facility and the Notes may become immediately due and payable and all commitments under the Credit Facility to extend further credit may be terminated.

We believe that internally generated cash flows, availability for additional borrowings under our Credit Facility of \$750 million (consisting of a \$750 million revolving credit facility, of which \$37.8 million is set aside for outstanding letters of credit at March 31, 2013) and our ability to amend the Credit Facility to provide for one or more tranches of term loans in an aggregate principal amount of \$1.0 billion, and our continued access to the bank credit and capital markets will be sufficient to finance acquisitions, capital expenditures and working capital requirements through the next 12 months. We believe these same sources of cash, borrowings under our Credit Facility as well as access to bank credit and capital markets will be available to us beyond the next 12 months and into the foreseeable future.

On May 24, 2012, we filed a universal automatic shelf registration statement on Form S-3ASR, as amended on June 7, 2012, that will permit us, from time to time, in one or more public offerings, to offer debt securities, common stock, preferred stock, warrants, depositary shares, or any combination of such securities. The shelf registration statement will also permit our subsidiary, CHS, to offer debt securities that would be guaranteed by us, from time to time in one or more public offerings. The terms of any such future offerings would be established at the time of the offering.

The ratio of earnings to fixed charges is a measure of our ability to meet our fixed obligations related to our indebtedness. The following table shows the ratio of earnings to fixed charges for the three months ended March 31, 2013:

|  | <b>Three Months Ended<br/>March 31, 2013</b> |
|--|--|
| Ratio of earnings to fixed charges (1) | 1.79 x                                       |

(1) Fixed charges include interest expensed and capitalized during the year plus an estimate of the interest component of rent expense. There are no shares of preferred stock outstanding. See exhibit 12 filed as part of this Report for the calculation of this ratio.

**Off-balance Sheet Arrangements**

Our consolidated operating results for the three months ended March 31, 2013 and 2012, included \$40.2 million and \$44.2 million, respectively, of net operating revenues and \$0.5 million and \$4.8 million, respectively, of income from continuing operations, generated from four hospitals operated by us under operating lease arrangements at March 31, 2013. In accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP, the respective assets and the future lease obligations under these arrangements are not recorded on our condensed consolidated balance sheet. Lease costs under these arrangements are included in rent expense and totaled approximately \$2.7 million for both of the three-month periods ended March 31, 2013 and 2012, respectively. The current terms of these operating leases expire between May 2015 and June 2022, not including lease extension options. If we allow these leases to expire, we would no longer generate revenues nor incur expenses from these hospitals. The operating lease at our Barstow, California location terminated on November 30, 2012 in conjunction with the opening of the replacement facility that we constructed, which was a requirement of the operating lease agreement.



## **Table of Contents**

In the past, we have utilized operating leases as a financing tool for obtaining the operations of specified hospitals without acquiring, through ownership, the related assets of the hospital and without a significant outlay of cash at the front end of the lease. We utilize the same operating strategies to improve operations at those hospitals held under operating leases as we do at those hospitals that we own. We have not entered into any operating leases for hospital operations since December 2000.

## **Noncontrolling Interests**

We have sold noncontrolling interests in certain of our subsidiaries or acquired subsidiaries with existing noncontrolling interest ownership positions. As of March 31, 2013, we have hospitals in 21 of the markets we serve, with noncontrolling physician ownership interests ranging from less than 1% to 40%, including one hospital that also has a non-profit entity as a partner. In addition, we have three other hospitals with noncontrolling interests owned by non-profit entities. During the three months ended March 31, 2012, one of our subsidiaries purchased the outstanding partnership interests not already owned by us that were held by physician investors in the limited partnership that owns and operates Longview Regional Medical Center in Longview, Texas. The purchase price for these partnership interests was \$28.8 million. After acquiring these partnership interests, one or more of our subsidiaries collectively own 100% of the outstanding equity of the limited partnership that owns and operates this hospital. Redeemable noncontrolling interests in equity of consolidated subsidiaries was \$375.5 million and \$367.7 million as of March 31, 2013 and December 31, 2012, respectively, and noncontrolling interests in equity of consolidated subsidiaries was \$62.6 million and \$65.3 million as of March 31, 2013 and December 31, 2012, respectively, and the amount of net income attributable to noncontrolling interests was \$17.1 million and \$23.8 million for the three months ended March 31, 2013 and 2012, respectively. As a result of the change in the Stark Law whole hospital exception included in the Reform Legislation, we are not permitted to introduce physician ownership at any of our wholly-owned hospital facilities or increase the aggregate percentage of physician ownership in any of our existing hospital joint ventures.

## **Reimbursement, Legislative and Regulatory Changes**

The Reform Legislation was enacted in the context of other ongoing legislative and regulatory efforts, which would reduce or otherwise adversely affect the payments we receive from Medicare and Medicaid. Within the statutory framework of the Medicare and Medicaid programs, including programs currently unaffected by the Reform Legislation, there are substantial areas subject to administrative rulings, interpretations and discretion which may further affect payments made under those programs, and the federal and state governments might, in the future, reduce the funds available under those programs or require more stringent utilization and quality reviews of hospital facilities. Additionally, there may be a continued rise in managed care programs and additional restructuring of the financing and delivery of healthcare in the United States. These events could cause our future financial results to decline. We cannot estimate the impact of Medicare and Medicaid reimbursement changes that have been enacted or are under consideration. We cannot predict whether additional reimbursement reductions will be made or whether any such changes would have a material adverse effect on our business, financial conditions, results of operations, cash flow, capital resources and liquidity.

## **Inflation**

The healthcare industry is labor intensive. Wages and other expenses increase during periods of inflation and when labor shortages occur in the marketplace. In addition, our suppliers pass along rising costs to us in the form of higher prices. We have implemented cost control measures, including our case and resource management program, to curb increases in operating costs and expenses. We have generally offset increases in operating costs by increasing reimbursement for services, expanding services and reducing costs in other areas. However, we cannot predict our ability to cover or offset future cost increases, particularly any increases in our cost of providing health insurance benefits to our employees as a result of the Reform Legislation.

## **Critical Accounting Policies**

The discussion and analysis of our financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our condensed consolidated financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and potentially result in materially different results under different assumptions and conditions. We believe that our critical accounting policies are limited to those described below.





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**Table of Contents*****Third-party Reimbursement***

Net operating revenues include amounts estimated by management to be reimbursable by Medicare and Medicaid under prospective payment systems and provisions of cost-reimbursement and other payment methods. In addition, we are reimbursed by non-governmental payors using a variety of payment methodologies. Amounts we receive for treatment of patients covered by these programs are generally less than the standard billing rates. Contractual allowances are automatically calculated and recorded through our internally developed automated contractual allowance system. Within the automated system, actual Medicare DRG data and payors' historical paid claims data are utilized to calculate the contractual allowances. This data is automatically updated on a monthly basis. All hospital contractual allowance calculations are subjected to monthly review by management to ensure reasonableness and accuracy. We account for the differences between the estimated program reimbursement rates and the standard billing rates as contractual allowance adjustments, which we deduct from gross revenues to arrive at operating revenues (net of contractual allowances and discounts). The process of estimating contractual allowances requires us to estimate the amount expected to be received based on payor contract provisions. The key assumption in this process is the estimated contractual reimbursement percentage, which is based on payor classification and historical paid claims data. Due to the complexities involved in these estimates, actual payments we receive could be different from the amounts we estimate and record. If the actual contractual reimbursement percentage under government programs and managed care contracts differed by 1% at March 31, 2013 from our estimated reimbursement percentage, net income for the three months ended March 31, 2013 would have changed by approximately \$41.0 million, and net accounts receivable at March 31, 2013 would have changed by \$67.0 million. Final settlements under some of these programs are subject to adjustment based on administrative review and audit by third parties. We account for adjustments to previous program reimbursement estimates as contractual allowance adjustments and report them in the periods that such adjustments become known. During the three months ended March 31, 2012, we recognized a net after-tax benefit of \$42.8 million from the resolution of an industry-wide governmental settlement and a payment update related to prior periods. Other than these items, contractual allowance adjustments related to final settlements and previous program reimbursement estimates impacted net operating revenues and net income by an insignificant amount in both of the three-month periods ended March 31, 2013 and 2012.

***Allowance for Doubtful Accounts***

Substantially all of our accounts receivable are related to providing healthcare services to our hospitals' patients. Collection of these accounts receivable is our primary source of cash and is critical to our operating performance. Our primary collection risks relate to uninsured patients and outstanding patient balances for which the primary insurance payor has paid some but not all of the outstanding balance, with the remaining outstanding balance (generally deductibles and co-payments) owed by the patient. At the point of service, for patients required to make a co-payment, we generally collect less than 15% of the related revenue. For all procedures scheduled in advance, our policy is to verify insurance coverage prior to the date of the procedure. Insurance coverage is not verified in advance of procedures for walk-in and emergency room patients.

We estimate the allowance for doubtful accounts by reserving a percentage of all self-pay accounts receivable without regard to aging category, based on collection history, adjusted for expected recoveries and, if present, anticipated changes in trends. For all other non-self-pay payor categories, we reserve 100% of all accounts aging over 365 days from the date of discharge. The percentage used to reserve for all self-pay accounts is based on our collection history. We believe that we collect substantially all of our third-party insured receivables, which include receivables from governmental agencies.

Collections are impacted by the economic ability of patients to pay and the effectiveness of our collection efforts. Significant changes in payor mix, business office operations, economic conditions or trends in federal and state governmental healthcare coverage could affect our collection of accounts receivable. The process of estimating the allowance for doubtful accounts requires us to estimate the collectability of self-pay accounts receivable, which is primarily based on our collection history, adjusted for expected recoveries and, if available, anticipated changes in collection trends. Significant change in payor mix, business office operations, economic conditions, trends in federal and state governmental healthcare coverage or other third-party payors could affect our estimates of accounts receivable collectability. If the actual collection percentage differed by 1% at March 31, 2013 from our estimated collection percentage as a result of a change in expected recoveries, net income for the three months ended March 31, 2013 would have changed by \$24.2 million, and net accounts receivable at March 31, 2013 would have changed by \$39.7 million. We also continually review our overall reserve adequacy by monitoring historical cash collections as a percentage of trailing net revenue less provision for bad debts, as well as by analyzing current period net revenue and admissions by payor classification, aged accounts receivable by payor, days revenue outstanding and the impact of recent acquisitions and dispositions.

**Table of Contents**

Our policy is to write-off gross accounts receivable if the balance is under \$10.00 or when such amounts are placed with outside collection agencies. We believe this policy accurately reflects our ongoing collection efforts and is consistent with industry practices. We had approximately \$2.5 billion and \$2.4 billion at March 31, 2013 and December 31, 2012, respectively, being pursued by various outside collection agencies. We expect to collect less than 3%, net of estimated collection fees, of the amounts being pursued by outside collection agencies. As these amounts have been written-off, they are not included in our gross accounts receivable or our allowance for doubtful accounts. Collections on amounts previously written-off are recognized as a reduction to bad debt expense when received. However, we take into consideration estimated collections of these future amounts written-off in evaluating the reasonableness of our allowance for doubtful accounts.

All of the following information is derived from our hospitals, excluding clinics, unless otherwise noted.

Patient accounts receivable from our hospitals represent approximately 95% of our total consolidated accounts receivable.

Days revenue outstanding was 60 days at March 31, 2013 and 58 days at December 31, 2012. Our target range for days revenue outstanding is from 53 to 63 days.

Total gross accounts receivable (prior to allowance for contractual adjustments and doubtful accounts) was approximately \$10.2 billion as of March 31, 2013 and approximately \$9.6 billion as of December 31, 2012.

The approximate percentage of total gross accounts receivable (prior to allowances for contractual adjustments and doubtful accounts) summarized by payor is as follows:

|                      | March 31, 2013 | December 31, 2012 |
|----------------------|----------------|-------------------|
| Insured receivables  | 62.3 %         | 61.5 %            |
| Self-pay receivables | <u>37.7</u>    | <u>38.5</u>       |
| Total                | <u>100.0 %</u> | <u>100.0 %</u>    |

For the hospital segment, the combined total of the allowance for doubtful accounts for self-pay accounts receivable and related allowances for other self-pay discounts and contractals, as a percentage of gross self-pay receivables, was approximately 84% at both March 31, 2013 and December 31, 2012. If the receivables that have been written-off, but where collections are still being pursued by outside collection agencies, were included in both the allowances and gross self-pay receivables specified above, the percentage of combined allowances to total self-pay receivables would have been approximately 90% at both March 31, 2013 and December 31, 2012.

***Goodwill and Other Intangibles***

Goodwill represents the excess of the fair value of the consideration conveyed in the acquisition over the fair value of net assets acquired. Goodwill is evaluated for impairment at the same time every year and when an event occurs or circumstances change that, more likely than not, reduce the fair value of the reporting unit below its carrying value. There is a two-step method for determining goodwill impairment. Step one is to compare the fair value of the reporting unit with the unit's carrying amount, including goodwill. If this test indicates the fair value is less than the carrying value, then step two is required to compare the implied fair value of the reporting unit's goodwill with the carrying value of the reporting unit's goodwill. We performed our last annual goodwill evaluation during the fourth quarter of 2012. No impairment was indicated by this evaluation. The next annual goodwill evaluation will be performed during the fourth quarter of 2013.

***Impairment or Disposal of Long-Lived Assets***

Whenever events or changes in circumstances indicate that the carrying values of certain long-lived assets may be impaired, we project the undiscounted cash flows expected to be generated by these assets. If the projections indicate that the reported amounts are not expected to be recovered, such amounts are reduced to their estimated fair value based on a quoted market price, if available, or an estimate based on valuation techniques available in the circumstances.



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**Table of Contents*****Professional Liability Claims***

As part of our business of owning and operating hospitals, we are subject to legal actions alleging liability on our part. We accrue for losses resulting from such liability claims, as well as loss adjustment expenses that are out-of-pocket and directly related to such liability claims. These direct out-of-pocket expenses include fees of outside counsel and experts. We do not accrue for costs that are part of our corporate overhead, such as the costs of our in-house legal and risk management departments. The losses resulting from professional liability claims primarily consist of estimates for known claims, as well as estimates for incurred but not reported claims. The estimates are based on specific claim facts, our historical claim reporting and payment patterns, the nature and level of our hospital operations, and actuarially determined projections. The actuarially determined projections are based on our actual claim data, including historic reporting and payment patterns which have been gathered over approximately a 20-year period. As discussed below, since we purchase excess insurance on a claims-made basis that transfers risk to third-party insurers, the liability we accrue does include an amount for the losses covered by our excess insurance. We also record a receivable for the expected reimbursement of losses covered by our excess insurance. Since we believe that the amount and timing of our future claims payments are reliably determinable, we discount the amount we accrue for losses resulting from professional liability claims using the risk-free interest rate corresponding to the timing of our expected payments.

The net present value of the projected payments was discounted using a weighted-average risk-free rate of 1.2%, 1.2% and 1.3% in 2012, 2011 and 2010, respectively. This liability is adjusted for new claims information in the period such information becomes known to us. Professional malpractice expense includes the losses resulting from professional liability claims and loss adjustment expense, as well as paid excess insurance premiums, and is presented within other operating expenses in the accompanying condensed consolidated statements of income.

Our processes for obtaining and analyzing claims and incident data are standardized across all of our hospitals and have been consistent for many years. We monitor the outcomes of the medical care services that we provide and for each reported claim, we obtain various information concerning the facts and circumstances related to that claim. In addition, we routinely monitor current key statistics and volume indicators in our assessment of utilizing historical trends. The average lag period between claim occurrence and payment of a final settlement is between four and five years, although the facts and circumstances of individual claims could result in the timing of such payments being different from this average. Since claims are paid promptly after settlement with the claimant is reached, settled claims represent less than 1.0% of the total liability at the end of any period.

For purposes of estimating our individual claim accruals, we utilize specific claim information, including the nature of the claim, the expected claim amount, the year in which the claim occurred and the laws of the jurisdiction in which the claim occurred. Once the case accruals for known claims are determined, information is stratified by loss layers and retentions, accident years, reported years, geography, and claims relating to the acquired Triad Hospitals, Inc., or Triad, hospitals versus claims relating to our other hospitals. Several actuarial methods are used against this data to produce estimates of ultimate paid losses and reserves for incurred but not reported claims. Each of these methods uses our company-specific historical claims data and other information. This company-specific data includes information regarding our business, including historical paid losses and loss adjustment expenses, historical and current case loss reserves, actual and projected hospital statistical data, a variety of hospital census information, employed physician information, professional liability retentions for each policy year, geographic information and other data.

Based on these analyses, we determine our estimate of the professional liability claims. The determination of management's estimate, including the preparation of the reserve analysis that supports such estimate, involves subjective judgment of management. Changes in reserving data or the trends and factors that influence reserving data may signal fundamental shifts in our future claim development patterns or may simply reflect single-period anomalies. Even if a change reflects a fundamental shift, the full extent of the change may not become evident until years later. Moreover, since our methods and models use different types of data and we select our liability from the results of all of these methods, we typically cannot quantify the precise impact of such factors on our estimates of the liability. Due to our standardized and consistent processes for handling claims and the long history and depth of our company-specific data, our methodologies have produced reliably determinable estimates of ultimate paid losses.

**Table of Contents**

We are primarily self-insured for these claims; however, we obtain excess insurance that transfers the risk of loss to a third-party insurer for claims in excess of our self-insured retentions. Our excess insurance is underwritten on a claims-made basis. For claims reported prior to June 1, 2002, substantially all of our professional and general liability risks were subject to a \$0.5 million per occurrence self-insured retention and for claims reported from June 1, 2002 through June 1, 2003, these self-insured retentions were \$2.0 million per occurrence. Substantially all claims reported after June 1, 2003 and before June 1, 2005 are self-insured up to \$4 million per claim. Substantially all claims reported on or after June 1, 2005 are self-insured up to \$5 million per claim. Management, on occasion, has selectively increased the insured risk at certain hospitals based upon insurance pricing and other factors and may continue that practice in the future. Excess insurance for all hospitals has been purchased through commercial insurance companies and generally covers us for liabilities in excess of the self-insured retentions. The excess coverage consists of multiple layers of insurance, the sum of which totals up to \$95 million per occurrence and in the aggregate for claims reported on or after June 1, 2003, up to \$145 million per occurrence and in the aggregate for claims incurred and reported after January 1, 2008 and up to \$195 million per occurrence and in the aggregate for claims reported after June 1, 2010. For certain policy years, if the first aggregate layer of excess coverage becomes fully utilized, then the self-insured retention could increase to \$10 million per claim for any subsequent claims in that policy year until our total aggregate coverage is met.

Effective January 1, 2008, the former Triad hospitals are insured on a claims-made basis as described above and through commercial insurance companies as described above for substantially all claims occurring on or after January 1, 2002 and reported on or after January 1, 2008. Substantially all losses for the former Triad hospitals in periods prior to May 1, 1999 were insured through a wholly-owned insurance subsidiary of HCA Inc., or HCA, Triad's owner prior to that time, and excess loss policies maintained by HCA. HCA has agreed to indemnify the former Triad hospitals in respect of claims covered by such insurance policies arising prior to May 1, 1999. From May 1, 1999 through December 31, 2006, the former Triad hospitals obtained insurance coverage on a claims incurred basis from HCA's wholly-owned insurance subsidiary with excess coverage obtained from other carriers that is subject to certain deductibles. Effective for claims incurred after December 31, 2006, Triad began insuring its claims from \$1 million to \$5 million through its wholly-owned captive insurance company, replacing the coverage provided by HCA. Substantially all claims occurring during 2007 were self-insured up to \$10 million per claim.

There have been no significant changes in our estimate of the reserve for professional liability claims during the three months ended March 31, 2013.

***Income Taxes***

We must make estimates in recording provision for income taxes, including determination of deferred tax assets and deferred tax liabilities and any valuation allowances that might be required against the deferred tax assets. We believe that future income will enable us to realize certain deferred tax assets, subject to the valuation allowance we have established.

The total amount of unrecognized benefit that would impact the effective tax rate, if recognized, was approximately \$0.9 million as of March 31, 2013. A total of approximately \$0.5 million of interest and penalties is included in the amount of liability for uncertain tax positions at March 31, 2013. It is our policy to recognize interest and penalties related to unrecognized benefits in our condensed consolidated statements of income as income tax expense.

It is possible the amount of unrecognized tax benefit could change in the next twelve months as a result of a lapse of the statute of limitations and settlements with taxing authorities; however, we do not anticipate the change will have a material impact on our consolidated results of operations or consolidated financial position.

We, or one or more of our subsidiaries, file income tax returns in the United States federal jurisdiction and various state jurisdictions. We have extended the federal statute of limitations for Triad for the tax periods ended December 31, 1999, December 31, 2000, April 30, 2001, June 30, 2001, December 31, 2001, December 31, 2002, December 31, 2003 and December 31, 2004. The Internal Revenue Service, or IRS, has concluded its examination of the federal tax return of Triad for the tax periods ended December 31, 2004, December 31, 2005, December 31, 2006 and July 25, 2007. With few exceptions, we are no longer subject to state income tax examinations for years prior to 2009 and federal income tax examinations with respect to Community Health Systems, Inc. federal returns for years prior to 2007. Our federal income tax returns for the 2007, 2008, 2009 and 2010 tax years are currently under examination by the IRS. We anticipate reaching a resolution on the 2007 and 2008 year examinations within the next six months. We believe the results of these examinations will not be material to our consolidated results of operations or consolidated financial position.

## **Table of Contents**

### ***Recent Accounting Pronouncements***

In February 2013, the Financial Accounting Standards Board issued Accounting Standards Update, or ASU, 2013-02, which requires additional disclosures on the effect of significant reclassifications out of accumulated other comprehensive income. The ASU requires a company that reports other comprehensive income to present (either on the face of the statement where net income is presented or in the notes) the effects on the line items of net income of significant amounts reclassified out of accumulated other comprehensive income. For other amounts that are not required to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference to other required disclosures that provide additional details about those amounts. This ASU is effective for fiscal years beginning after December 15, 2012, and was adopted by us on January 1, 2013. As it only requires additional disclosure, the adoption of this ASU had no impact our consolidated financial position, results of operations or cash flows.

### **FORWARD-LOOKING STATEMENTS**

Some of the matters discussed in this report include forward-looking statements. Statements that are predictive in nature, that depend upon or refer to future events or conditions or that include words such as expects, anticipates, intends, plans, believes, estimates, thinks, and similar expressions are forward-looking statements. These statements involve known and unknown risks, uncertainties, and other factors that may cause our actual results and performance to be materially different from any future results or performance expressed or implied by these forward-looking statements. These factors include the following:

general economic and business conditions, both nationally and in the regions in which we operate,

implementation and effect of adopted and potential federal and state healthcare legislation,

risks associated with our substantial indebtedness, leverage and debt service obligations,

demographic changes,

changes in, or the failure to comply with, governmental regulations,

potential adverse impact of known and unknown government investigations, audits, and Federal and State False Claims Act litigation and other legal proceedings,

our ability, where appropriate, to enter into and maintain managed care provider arrangements and the terms of these arrangements,

changes in, or the failure to comply with, managed care provider contracts, which could result in, among other things, disputes and changes in reimbursements, both prospectively and retroactively,

changes in inpatient or outpatient Medicare and Medicaid payment levels,

increases in the amount and risk of collectability of patient accounts receivable,

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increases in wages as a result of inflation or competition for highly technical positions and rising supply costs due to market pressure from pharmaceutical companies and new product releases,

liabilities and other claims asserted against us, including self-insured malpractice claims,

competition,

our ability to attract and retain, at reasonable employment costs, qualified personnel, key management, physicians, nurses and other healthcare workers,

trends toward treatment of patients in less acute or specialty healthcare settings, including ambulatory surgery centers or specialty hospitals,

changes in medical or other technology,

changes in U.S. GAAP,

the availability and terms of capital to fund additional acquisitions or replacement facilities,

our ability to successfully acquire additional hospitals or complete divestitures,

our ability to successfully integrate any acquired hospitals or to recognize expected synergies from such acquisitions,



## **Table of Contents**

our ability to obtain adequate levels of general and professional liability insurance and

timeliness of reimbursement payments received under government programs.

Although we believe that these statements are based upon reasonable assumptions, we can give no assurance that our goals will be achieved. Given these uncertainties, prospective investors are cautioned not to place undue reliance on these forward-looking statements. These forward-looking statements are made as of the date of this filing. We assume no obligation to update or revise them or provide reasons why actual results may differ.

### **Item 3. *Quantitative and Qualitative Disclosures about Market Risk***

We are exposed to interest rate changes, primarily as a result of our Credit Facility which bears interest based on floating rates. In order to manage the volatility relating to the market risk, we entered into interest rate swap agreements described under the heading Liquidity and Capital Resources in Item 2. We utilize risk management procedures and controls in executing derivative financial instrument transactions. We do not execute transactions or hold derivative financial instruments for trading purposes. Derivative financial instruments related to interest rate sensitivity of debt obligations are used with the goal of mitigating a portion of the exposure when it is cost effective to do so. As interest rate swap agreements expire throughout the year, we will become more subject to variable interest rates during 2013.

A 1% change in interest rates on variable rate debt in excess of that amount covered by interest rate swaps would have resulted in interest expense fluctuating approximately \$4.2 million and \$3.4 million for the three months ended March 31, 2013 and 2012, respectively.

### **Item 4. *Controls and Procedures***

Our Chief Executive Officer and Chief Financial Officer, with the participation of other members of management, have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended, or the Exchange Act), as of the end of the period covered by this report. Based on such evaluations, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective (at the reasonable assurance level) to ensure that the information required to be included in this report has been recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and to ensure that the information required to be included in this report was accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

There have been no changes in our internal control over financial reporting during the quarter ended March 31, 2013, that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

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## **Table of Contents**

### **PART II OTHER INFORMATION**

#### **Item 1. *Legal Proceedings***

From time to time, we receive various inquiries or subpoenas from state regulators, fiscal intermediaries, the Centers for Medicare and Medicaid Services and the Department of Justice regarding various Medicare and Medicaid issues. In addition to the subpoenas discussed below, we are currently responding to subpoenas and administrative demands concerning certain cardiology procedures, medical records and policies at a New Mexico hospital. In addition, we are subject to other claims and lawsuits arising in the ordinary course of our business. We are not aware of any pending or threatened litigation that is not covered by insurance policies or reserved for in our condensed consolidated financial statements or which we believe would have a material adverse impact on us; however, some pending or threatened proceedings against us may involve potentially substantial amounts as well as the possibility of civil, criminal, or administrative fines, penalties, or other sanctions, which could be material. Settlements of suits involving Medicare and Medicaid issues routinely require both monetary payments as well as corporate integrity agreements. Additionally, qui tam or whistleblower actions initiated under the civil False Claims Act may be pending but placed under seal by the court to comply with the False Claims Act's requirements for filing such suits. Also, from time to time, we detect issues of non-compliance with Federal healthcare laws pertaining to claims submission and reimbursement practices and/or financial relationships with physicians. We avail ourselves of various mechanisms to address potential overpayments arising out of these issues, including repayment of claims, rebilling of claims, and participation in voluntary disclosure protocols offered by the Centers for Medicare and Medicaid Services and the Office of the Inspector General. Participating in voluntary repayments and voluntary disclosure protocols can have the potential for significant settlement obligations or even enforcement action, however, we are not aware of any such exposures that have not been reserved for in our condensed consolidated financial statements or which we believe would have a material adverse impact on us.

#### *U.S. ex rel. Baker vs. Community Health Systems, Inc. (United States District Court for the District of New Mexico)*

Our knowledge of this matter originated in early 2006 with correspondence from the Civil Division of the Department of Justice requesting documents in an investigation it was conducting involving the Company. The inquiry related to the way in which different state Medicaid programs apply to the federal government for matching or supplemental funds that are ultimately used to pay for a small portion of the services provided to Medicaid and indigent patients. These programs are referred to by different names, including intergovernmental payments, upper payment limit programs, and Medicaid disproportionate share hospital payments. For approximately three years, we provided the Department of Justice with requested documents, met with its personnel on numerous occasions and otherwise cooperated in its investigation. During the course of the investigation, the Civil Division notified us that it believed that we and three of our New Mexico hospitals caused the State of New Mexico to submit improper claims for federal funds, in violation of the Federal False Claims Act. This investigation has culminated in the federal government's intervention in the referenced qui tam lawsuit, which alleges that our New Mexico hospitals caused to be filed false claims from the period of August 2000 through June 2011. Two of our parent company's subsidiaries are also defendants in this lawsuit. We continue to vigorously defend this action. The current posture of this case is that discovery is closed and both parties' motions for summary judgment are pending. There is currently no hearing date on these motions and no trial date has been set.

#### *Multi-provider National Department of Justice Investigations*

**Kyphoplasty.** Kyphoplasty is a surgical spine procedure that returns a compromised vertebra (either from trauma or osteoporotic disease process) to its previous height, reducing or eliminating severe pain. We were first made aware of this investigation in June 2008, when two of our hospitals received document request letters from the United States Attorney's Office for the Western District of New York. Subsequently, additional hospitals (a total of five) also received requests for documents and/or medical records. The investigation covers the period of January 1, 2002 through June 9, 2008. This investigation is part of a national investigation and is related to a qui tam settlement between the same United States Attorney's office and the manufacturer and distributor of the Kyphon product, which is used in performing the kyphoplasty procedure. We are cooperating with the investigation and we are continuing to evaluate and discuss this matter with the federal government.

**Implantable Cardioverter Defibrillators (ICDs).** We were first made aware of this investigation in September 2010, when we received a letter from the Civil Division of the United States Department of Justice. The letter advised us that an investigation was being conducted to determine whether certain hospitals have improperly submitted claims for payment for ICDs. The period of time covered by the investigation was 2003 to 2010. We continue to fully cooperate with the government in this investigation and have provided requested records and documents. On August 30, 2012, the Department of Justice issued a document entitled, "Medical Review Guidelines/Resolution Model," which sets out, for the purposes of this investigation, the patient conditions and criteria for the medical necessity of the implantation of ICDs in Medicare beneficiaries and how the Department of Justice will enforce the repayment obligations of hospitals. We are in the process of reviewing our medical records in light of the guidance contained in this document.

#### *Laredo, Texas Department of Justice Investigation*

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In December 2009, we received a document subpoena from the United States Department of Health and Human Services, Office of the Inspector General, or OIG, requesting documents related to our hospital in Laredo, Texas. The categories of documents requested included case management, resource management, admission criteria, patient medical records, coding, billing, compliance, the Joint Commission accreditation, physician documentation, payments to referral sources, transactions involving physicians, disproportionate share hospital status and audits by the hospital's Quality Improvement organization. In January 2010, we received a request for information or assistance from the OIG's Office of Investigation requesting patient medical records from this facility for certain Medicaid patients with extended lengths of stay. We continue to cooperate fully with this investigation.

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## **Table of Contents**

### *Department of Justice Investigation of Medicare Short-Stay Admissions from Emergency Departments*

In April 2011, we received a document subpoena from the United States Department of Health and Human Services, OIG, in connection with an investigation of possible improper claims submitted to Medicare and Medicaid. The subpoena was directed to all of our hospitals and requested documents concerning emergency department processes and procedures, including our hospitals' use of the Pro-MED Clinical Information System, a third-party software system that assists with the management of patient care and provides operational support and data collection for emergency department management. The subpoena also sought information about our relationships with emergency department physicians, including financial arrangements. This investigation is being led by the Department of Justice. We are continuing to cooperate with the government with the ongoing document production, as well as conducting a joint medical necessity review of a sampling of medical records at a small number of hospitals. The results of the respective reviews have been exchanged and are undergoing further analysis by the experts.

The following matters, although initiated independently of the Department of Justice's April 2011 subpoena, are factually related in some manner to that subpoena and are grouped here for clarity.

Texas Attorney General Investigation of Emergency Department Procedures and Billing. In November 2010, we were served with substantially identical Civil Investigative Demands (CIDs) from the Office of Attorney General, State of Texas for all 18 of our affiliated Texas hospitals. The subject of the requests concerns emergency department procedures and billing. We have complied with these requests and provided all documentation and reports requested. We continue to cooperate fully with this investigation.

United States ex rel. and Reuille vs. Community Health Systems Professional Services Corporation and Lutheran Musculoskeletal Center, LLC d/b/a Lutheran Hospital (United States District Court for the Northern District of Indiana, Fort Wayne Division). This lawsuit was originally filed under seal in January 2009. The suit is brought under the False Claims Act and alleges that Lutheran Hospital of Indiana billed the Medicare program for (a) false 23 hour observation after outpatient surgeries and procedures, and (b) intentional assignment of inpatient status to one-day stays for cases that do not meet Medicare criteria for inpatient intensity of service or severity of illness. In December 2010, the government filed a notice that it declined to intervene in this suit. On April 22, 2011, a joint motion was filed by the relator and the Department of Justice to extend the period of time for the relator to serve us in the case to allow the government more time to decide if it will intervene in the case. The motion to stay was granted, as have subsequent joint motions, and the stay is currently continued until October 25, 2013. The original motion and subsequent filings gave insight to the fact that there are other qui tam complaints in other jurisdictions and that the government was consolidating its investigations and working cooperatively with other investigative bodies (including the Attorney General of the State of Texas). The government also confirmed that it considers the allegations made in the complaint styled *Tenet Healthcare Corporation vs. Community Health Systems, Inc., et al.* filed in the United States District Court for the Northern District of Texas, Dallas Division on April 11, 2011 to be related to the government's consolidated investigation. We are cooperating fully with the government in its investigations.

Shelbyville, Tennessee OIG Subpoena. In May 2011, we received a subpoena from the Houston Office of the United States Department of Health and Human Services, OIG, requesting 71 patient medical records from our hospital in Shelbyville, Tennessee. We provided the requested records and have met with the government regarding this matter. We continue to cooperate fully with this investigation.

SEC Subpoena. In May 2011, we received a subpoena from the SEC requesting documents related to or requested in connection with the various inquiries, lawsuits and investigations regarding, generally, emergency room admissions or observation practices at our hospitals. The subpoena also requested documents relied upon by us in responding to the Tenet litigation, as well as other communications about the Tenet litigation. As with all government investigations, we are cooperating fully with the SEC.

Class Action Shareholder Federal Securities Cases. Three purported class action cases have been filed in the United States District Court for the Middle District of Tennessee; namely, *Norfolk County Retirement System v. Community Health Systems, Inc., et al.*, filed May 9, 2011; *De Zheng v. Community Health Systems, Inc., et al.*, filed May 12, 2011; and *Minneapolis Firefighters Relief Association v. Community Health Systems, Inc., et al.*, filed June 21, 2011. All three seek class certification on behalf of purchasers of our common stock between July 27, 2006 and April 11, 2011 and allege that misleading statements resulted in artificially inflated prices for our common stock. In December 2011, the cases were consolidated for pretrial purposes and NYC Funds and its counsel were selected as lead plaintiffs/lead plaintiffs' counsel. Our motion to dismiss this case has been fully briefed and is pending before the court. We believe this consolidated matter is without merit and will vigorously defend this case.

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## **Table of Contents**

**Shareholder Derivative Actions.** Three purported shareholder derivative actions have also been filed in the United States District Court for the Middle District of Tennessee; Plumbers and Pipefitters Local Union No. 630 Pension Annuity Trust Fund v. Wayne T. Smith, et al., filed May 24, 2011; Roofers Local No. 149 Pension Fund v. Wayne T. Smith, et al., filed June 21, 2011; and Lambert Sweat v. Wayne T. Smith, et al., filed October 5, 2011. These three cases allege breach of fiduciary duty arising out of allegedly improper inpatient admission practices, mismanagement, waste and unjust enrichment. These cases have been consolidated into a single, consolidated action. The plaintiffs filed an operative amended derivative complaint in these three consolidated actions on March 15, 2012. Our motion to dismiss has been fully briefed and is pending before the court. We believe all of these matters are without merit and will vigorously defend them.

### *Other Government Investigations*

**Easton, Pennsylvania Urologist.** On June 13, 2011, our hospital in Easton, Pennsylvania received a document subpoena from the Philadelphia office of the United States Department of Justice. The documents requested included medical records for certain urological procedures performed by a non-employed physician who is no longer on the medical staff and other records concerning the hospital's relationship with the physician. Certain procedures performed by the physician had been previously reviewed and appropriate repayments had been made. We are cooperating fully with the government in this investigation.

**Hattiesburg, Mississippi Allegiance Health Management, Inc.** On February 23, 2012, our hospital in Hattiesburg, Mississippi received a document subpoena from the United States Department of Health and Human Services, OIG relating to its relationship with Allegiance Health Management, Inc., or Allegiance, a company that provides intensive outpatient psychiatric, or IOP, services to its patients. The subpoena seeks information concerning the hospital's financial relationship with Allegiance, medical records of patients receiving IOP services, and other documents relating to Allegiance such as agreements, policies and procedures, audits, complaints, budgets, financial analyses and identities of those delivering services. This is our only hospital that received services from this vendor. We are cooperating fully with this investigation.

### *Qui Tam Cases – Government Declined Intervention*

On June 2, 2011, an order was entered unsealing a relator's qui tam complaint in the matter of *U.S. ex rel. Wood M. Deming, MD, individually and on behalf of Regional Cardiology Consultants, PC v. Jackson-Madison County General Hospital, an Affiliate of West Tennessee Healthcare, Regional Hospital of Jackson, a Division of Community Health Systems Professional Services Corporation, James Moss, individually, Timothy Puthoff, individually, Joel Perchik, MD, individually, and Elie H. Korban, MD, individually*. The action is pending in the Western District of Tennessee, Jackson Division. Regional Hospital of Jackson is an affiliated hospital and Mr. Puthoff is a former chief executive officer there. The Order recited that the United States had elected to intervene to a limited degree only concerning the claims against Dr. Korban for false and fraudulent billing for allegedly unnecessary stent procedures and for causing the submission of false claims by the hospitals. On July 28, 2011, we were served by the relator. We believe the claims against our hospital are without merit and we are vigorously defending this case.

On August 8, 2012, an order was entered unsealing a relator's qui tam complaint in the matter of *U.S. and N.M. ex rel. Sally Hansen v. Mimbres Memorial Hospital, et al.* This action is pending in the United States District Court for New Mexico. This case cites alleged quality control failures as violations of the Clinical Laboratory Improvement Amendments of 1988 as the basis for a False Claims Act suit. Both the U.S. government and the New Mexico state government declined to intervene in this case. We filed a motion to dismiss and the relator filed an amended complaint. Both the U.S. government and the New Mexico state government have now declined to intervene on this amended complaint. We believe the claim against our hospital is without merit and we are vigorously defending this case.

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## **Table of Contents**

### *Commercial Litigation and Other Lawsuits*

*Managed Care Solutions, Inc. v. Community Health Systems, Inc. (United States District Court for the Southern District of Florida).* This suit was filed on February 4, 2010. Plaintiff contracted with two affiliated hospitals to provide services collecting receivables from third-party payors. Plaintiff sought to extend the contract to additional facilities at which it never provided any services and claimed \$435 million in damages. A motion for summary judgment was filed on February 17, 2012. On June 4, 2012, the District Court affirmed the recommendation of the Magistrate Judge limiting the Plaintiff's claims to only two hospitals. The Court continued the trial until July 2013. The Magistrate Judge recently recommended denial of our renewed motion for summary judgment and we have filed objections to this report. We will continue to vigorously defend this action.

*Becker v. Community Health Systems, Inc. d/b/a Community Health Systems Professional Services Corporation d/b/a Community Health Systems d/b/a Community Health Systems PSC, Inc. d/b/a Rockwood Clinic P.S. and Rockwood Clinic, P.S. (Superior Court, Spokane, Washington).* This suit was filed on February 29, 2012, by a former chief financial officer at Rockwood Clinic in Spokane, Washington. Becker claims he was wrongfully terminated for allegedly refusing to certify a budget for Rockwood Clinic in 2012. On February 29, 2012, he also filed an administrative complaint with the Department of Labor, Occupational Safety and Health Administration alleging that he is a whistleblower under Sarbanes-Oxley; a response was filed on May 21, 2012. At a hearing on July 27, 2012, the court dismissed Community Health Systems, Inc. from this case and has subsequently certified the case for an interlocutory appeal of the denial to dismiss his employer and the management company. The appellate court has accepted the interlocutory appeal. We are vigorously defending this action.

### **Management of Significant Legal Proceedings**

In accordance with our governance documents, including our Governance Guidelines and the charter of the Audit and Compliance Committee, our management of significant legal proceedings is overseen by the independent members of the Board of Directors and, in particular, the Audit and Compliance Committee. The Audit and Compliance Committee is charged with oversight of compliance, regulatory and litigation matters, and enterprise risk management. Management has been instructed to refer all significant legal proceedings and allegations of financial statement fraud, error, or misstatement to the Audit and Compliance Committee for its oversight and evaluation. Consistent with New York Stock Exchange and Sarbanes-Oxley independence requirements, the Audit and Compliance Committee is comprised entirely of individuals who are independent of Company management, and all three members of the Audit and Compliance Committee are audit committee financial experts as defined in the Exchange Act.

In addition, the Audit and Compliance Committee and the other independent members of the Board of Directors oversee the functions of the voluntary compliance program, including its auditing and monitoring functions and confidential disclosure program. In recent years, the voluntary compliance program has addressed the potential for a variety of billing errors that might be the subject of audits and payment denials by the CMS Recovery Audit Contractors' permanent project, including MS-DRG coding, outpatient hospital and physician coding and billing, and medical necessity for services (including a focus on hospital stays of very short duration). Efforts by management, through the voluntary compliance program, to identify and limit risk from these government audits have included significant policy and guidance revisions, training and education, and auditing.

Since April 2011, our Audit and Compliance Committee and/or Board of Directors has met, on average, monthly to review the status of the lawsuits and investigations relating to allegations of improper billing for inpatient care at our hospitals and to oversee management in connection with our investigation and defense of these matters. At many of those meetings, the independent members of the Board of Directors have met in separate session, first with outside counsel handling the investigations and lawsuits, and then alone, to discuss their duties and oversight of these matters. The independent members of our Board of Directors remain fully engaged in the oversight of these matters.

### **Item 1A. Risk Factors**

There have been no material changes with regard to risk factors previously disclosed in our most recent annual report on Form 10-K.

**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table contains information about our purchases of common stock during the three months ended March 31, 2013.

| Period                                  | Total Number of<br>Shares<br>Purchased | Average Price Paid<br>per<br>Share | Total Number of<br>Shares<br>Purchased as Part of Publicly<br>Announced Plans<br>or<br>Programs(a) | Maximum Number of Shares<br>That May Yet Be<br>Purchased<br>Under the Plans or Programs(a) |
|---|--|------------------------------------|--|--|
| January 1, 2013 -<br>January 31, 2013   | 223,023                                | \$ 30.18                           | 223,023  | 3,776,977  |
| February 1, 2013 -<br>February 28, 2013 | -                                      | -                                  | -  | 3,776,977  |
| March 1, 2013 -<br>March 31, 2013       | 300,000                                | 39.91                              | 300,000  | 3,476,977  |
| Total                                   | 523,023                                | \$ 35.76                           | 523,023  | 3,476,977  |

- (a) On December 14, 2011, we commenced a new open market repurchase program for up to 4,000,000 shares of our common stock, not to exceed \$100 million in repurchases. This program will conclude at the earliest of three years from the commencement date, when the maximum number of shares has been repurchased or when the maximum dollar amount has been expended. During the three months ended March 31, 2013, we repurchased and retired 523,023 shares at a weighted-average price of \$35.76 per share, which is the cumulative number of shares that have been repurchased and retired under this program.

Historically, we have not paid any cash dividends. In December 2012, we declared and paid a special dividend of \$0.25 per share to holders of our common stock at the close of business as of December 17, 2012, which totaled approximately \$23.0 million. In the foreseeable future, we do not anticipate the payment of any other cash dividends. Our Credit Facility limits our ability to pay dividends and/or repurchase stock to an amount not to exceed \$150 million in the aggregate plus the aggregate amount of proceeds from the exercise of stock options. The indentures governing our 8% Senior Notes, our 7<sup>1</sup>/<sub>8</sub>% Senior Notes and our 5<sup>1</sup>/<sub>8</sub>% Senior Secured Notes also limit our ability to pay dividends and/or repurchase stock. As of March 31, 2013, under the most restrictive test under these agreements, we have approximately \$233.1 million available with which to pay permitted dividends and/or repurchase shares of stock or our Notes.

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

None.





**Table of Contents**

**Item 6. Exhibits**

| <b>No.</b> | <b>Description</b>   |
|------------|--|
| 4.1        | Fifth Supplemental Indenture relating to CHS/Community Health Systems, Inc. s 8.000% Senior Notes due 2019, dated as of March 31, 2013, by and among CHS/Community Health Systems, Inc., the guarantors party thereto and Regions Bank, as successor trustee |
| 4.2        | Second Supplemental Indenture relating to CHS/Community Health Systems, Inc. s 7.125% Senior Notes due 2020, dated as of March 31, 2013, by and among CHS/Community Health Systems, Inc., the guarantors party thereto and Regions Bank                      |
| 4.3        | Second Supplemental Indenture relating to CHS/Community Health Systems, Inc. s 5.125% Senior Secured Notes due 2018, dated as of March 31, 2013, by and among CHS/Community Health Systems, Inc., the guarantors party thereto and Regions Bank              |
| 4.4        | Release of Certain Guarantor relating to CHS/Community Health Systems, Inc. s 8.000% Senior Notes due 2019, dated as of March 31, 2013, by and among CHS/Community Health Systems, Inc., the guarantors party thereto and Regions Bank                       |
| 4.5        | Release of Certain Guarantor relating to CHS/Community Health Systems, Inc. s 7.125% Senior Notes due 2020, dated as of March 31, 2013, by and among CHS/Community Health Systems, Inc., the guarantors party thereto and Regions Bank                       |
| 4.6        | Release of Certain Guarantor relating to CHS/Community Health Systems, Inc. s 5.125% Senior Secured Notes due 2018, dated as of March 31, 2013, by and among CHS/Community Health Systems, Inc., the guarantors party thereto and Regions Bank               |
| 12         | Ratio of Earnings to Fixed Charges   |
| 31.1       | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002   |
| 31.2       | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002   |
| 32.1       | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002   |
| 32.2       | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002   |
| 101.INS    | XBRL Instance Document   |
| 101.SCH    | XBRL Taxonomy Extension Schema   |
| 101.CAL    | XBRL Taxonomy Extension Calculation Linkbase   |
| 101.DEF    | XBRL Taxonomy Extension Definition Linkbase  |
| 101.LAB    | XBRL Taxonomy Extension Label Linkbase   |
| 101.PRE    | XBRL Taxonomy Extension Presentation Linkbase  |

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

COMMUNITY HEALTH SYSTEMS, INC.  
(Registrant)

By: /s/ Wayne T. Smith  
Wayne T. Smith  
Chairman of the Board,  
President and Chief Executive Officer  
(principal executive officer)

By: /s/ W. Larry Cash  
W. Larry Cash  
Executive Vice President, Chief Financial  
Officer and Director  
(principal financial officer)

By: /s/ Kevin J. Hammons  
Kevin J. Hammons  
Vice President and Chief Accounting Officer  
(principal accounting officer)

Date: April 30, 2013

**Table of Contents**

**Index to Exhibits**

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