

UNIVERSAL HEALTH SERVICES INC

Form 10-Q

November 07, 2014

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

(MARK ONE)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended September 30, 2014**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission file number 1-10765**

**UNIVERSAL HEALTH SERVICES, INC.**

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

**DELAWARE**  
**(State or other jurisdiction of**  
**incorporation or organization)**

**23-2077891**  
**(I.R.S. Employer**  
**Identification No.)**

**UNIVERSAL CORPORATE CENTER**  
**367 SOUTH GULPH ROAD**  
**KING OF PRUSSIA, PENNSYLVANIA 19406**  
**(Address of principal executive offices) (Zip Code)**

**Registrant's telephone number, including area code (610) 768-3300**

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 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 website, 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

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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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. Common shares outstanding, as of October 31, 2014:

Class A	6,595,708
Class B	91,681,078
Class C	664,000
Class D	29,181

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In this Report on Form 10-Q for the quarterly period ended September 30, 2014, we, us, our UHS and the Company refer to Universal Health Services, Inc. and its subsidiaries. UHS is a registered trademark of UHS of Delaware, Inc., the management company for, and a wholly-owned subsidiary of Universal Health Services, Inc. Universal Health Services, Inc. is a holding company and operates through its subsidiaries including its management company, UHS of Delaware, Inc. All healthcare and management operations are conducted by subsidiaries of Universal Health Services, Inc. To the extent any reference to UHS or UHS facilities in this report including letters, narratives or other forms contained herein relates to our healthcare or management operations it is referring to Universal Health Services, Inc.'s subsidiaries including UHS of Delaware, Inc. Further, the terms we, us, our or the Company in such context similar refer to the operations of Universal Health Services Inc.'s subsidiaries including UHS of Delaware, Inc. Any reference to employees or employment contained herein refers to employment with or employees of the subsidiaries of Universal Health Services, Inc. including UHS of Delaware, Inc.



Table of Contents**PART I. FINANCIAL INFORMATION****UNIVERSAL HEALTH SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

(amounts in thousands, except per share amounts)

(unaudited)

	<b>Three months ended</b>		<b>Nine months ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Net revenues before provision for doubtful accounts	\$ 2,175,554	\$ 2,134,740	\$ 6,499,680	\$ 6,294,750
Less: Provision for doubtful accounts	157,796	318,371	541,935	811,774
Net revenues	2,017,758	1,816,369	5,957,745	5,482,976
Operating charges:				
Salaries, wages and benefits	953,583	903,212	2,850,868	2,702,842
Other operating expenses	512,794	393,549	1,323,274	1,100,118
Supplies expense	222,708	206,995	662,280	613,981
Depreciation and amortization	93,456	86,971	277,506	248,465
Lease and rental expense	23,860	23,904	70,656	72,651
Electronic health records incentive income	(1,425)	(23,148)	(4,029)	(27,943)
Costs related to extinguishment of debt	36,171	0	36,171	0
	1,841,147	1,591,483	5,216,726	4,710,114
Income from operations	176,611	224,886	741,019	772,862
Interest expense, net	32,133	32,314	102,413	110,488
Income before income taxes	144,478	192,572	638,606	662,374
Provision for income taxes	48,440	69,473	224,102	241,537
Net income	96,038	123,099	414,504	420,837
Less: Income attributable to noncontrolling interests	13,241	8,512	41,958	34,625
Net income attributable to UHS	\$ 82,797	\$ 114,587	\$ 372,546	\$ 386,212
Basic earnings per share attributable to UHS	\$ 0.84	\$ 1.17	\$ 3.77	\$ 3.94

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Diluted earnings per share attributable to UHS	\$ 0.82	\$ 1.15	\$ 3.71	\$ 3.89
Weighted average number of common shares - basic	99,052	98,151	98,832	97,965
Add: Other share equivalents	1,981	1,436	1,643	1,158
Weighted average number of common shares and equivalents - diluted	101,033	99,587	100,475	99,123

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents**UNIVERSAL HEALTH SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(amounts in thousands, unaudited)

	<b>Three months ended</b>		<b>Nine months ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Net income	\$ 96,038	\$ 123,099	\$ 414,504	\$ 420,837
Other comprehensive income (loss):				
Unrealized derivative gains on cash flow hedges	4,712	3,054	12,922	12,871
Amortization of terminated hedge	(84)	(84)	(252)	(252)
Currency translation adjustment	(2,506)	0	(2,506)	0
Other comprehensive income before tax	2,122	2,970	10,164	12,619
Income tax expense related to items of other comprehensive income	1,620	1,120	4,685	4,758
Total other comprehensive income, net of tax	502	1,850	5,479	7,861
Comprehensive income	96,540	124,949	419,983	428,698
Less: Comprehensive income attributable to noncontrolling interests	13,241	8,512	41,958	34,625
Comprehensive income attributable to UHS	\$ 83,299	\$ 116,437	\$ 378,025	\$ 394,073

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****UNIVERSAL HEALTH SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(amounts in thousands, unaudited)

	<b>September 30, 2014</b>	<b>December 31, 2013</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 39,711	\$ 17,238
Accounts receivable, net	1,239,478	1,116,961
Supplies	104,390	101,781
Deferred income taxes	95,204	119,903
Other current assets	143,311	76,446
Total current assets	1,622,094	1,432,329
Property and equipment	6,105,090	5,691,902
Less: accumulated depreciation	(2,456,116)	(2,249,733)
	3,648,974	3,442,169
Other assets:		
Goodwill	3,296,358	3,049,016
Deferred charges	41,910	57,881
Other	352,256	330,328
	\$ 8,961,592	\$ 8,311,723
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Current maturities of long-term debt	\$ 81,477	\$ 99,312
Accounts payable and accrued liabilities	1,083,987	953,449
Federal and state taxes	0	7,127
Total current liabilities	1,165,464	1,059,888
Other noncurrent liabilities	280,797	284,589
Long-term debt	3,373,341	3,209,762
Deferred income taxes	253,191	239,148
Redeemable noncontrolling interests	231,473	218,107
Equity:		
UHS common stockholders' equity	3,603,204	3,249,979

Noncontrolling interest	54,122	50,250
Total equity	3,657,326	3,300,229
	\$ 8,961,592	\$ 8,311,723

The accompanying notes are an integral part of these consolidated financial statements.

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**UNIVERSAL HEALTH SERVICES, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(amounts in thousands, unaudited)

	Nine months ended September 30,	
	2014	2013
<b>Cash Flows from Operating Activities:</b>		
Net income	\$ 414,504	\$ 420,837
<i>Adjustments to reconcile net income to net cash provided by operating activities:</i>		
Depreciation & amortization	277,506	248,648
Stock-based compensation expense	22,713	20,072
Gains on sales of assets and businesses, net of losses	(7,837)	(2,973)
Write-off of deferred financing costs related to extinguishment of debt	19,730	0
<i>Changes in assets &amp; liabilities, net of effects from acquisitions and dispositions:</i>		
Accounts receivable	(98,193)	(99,261)
Accrued interest	6,547	10,376
Accrued and deferred income taxes	(18,392)	5,109
Other working capital accounts	59,613	10,313
Other assets and deferred charges	15,868	13,425
Other	(7,000)	5,792
Accrued insurance expense, net of commercial premiums paid	57,729	(1,406)
Payments made in settlement of self-insurance claims	(53,234)	(55,009)
Net cash provided by operating activities	689,554	575,923
<b>Cash Flows from Investing Activities:</b>		
Property and equipment additions, net of disposals	(309,361)	(279,751)
Proceeds received from sale of assets and businesses	15,178	37,118
Cash paid/reserved related to acquisition of property and businesses	(402,405)	(1,320)
Costs incurred for purchase and implementation of electronic health records application	(11,204)	(42,353)
Net cash used in investing activities	(707,792)	(286,306)
<b>Cash Flows from Financing Activities:</b>		
Reduction of long-term debt	(842,543)	(234,231)
Additional borrowings	969,800	1,500
Financing costs	(13,413)	0
Repurchase of common shares	(63,292)	(22,186)
Dividends paid	(19,794)	(14,706)
Issuance of common stock	4,907	4,096
Excess income tax benefits related to stock-based compensation	30,242	15,809
Profit distributions to noncontrolling interests	(25,074)	(51,248)

Net cash provided by (used in) financing activities	40,833	(300,966)
Effect of exchange rate changes on cash and cash equivalents	(122)	0
Increase (decrease) in cash and cash equivalents	22,473	(11,349)
Cash and cash equivalents, beginning of period	17,238	23,471
Cash and cash equivalents, end of period	\$ 39,711	\$ 12,122

**Supplemental Disclosures of Cash Flow Information:**

Interest paid, including early redemption premium and original issue discount write-off in 2014	\$ 98,670	\$ 88,430
Income taxes paid, net of refunds	\$ 212,148	\$ 218,290

The accompanying notes are an integral part of these consolidated financial statements.

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**UNIVERSAL HEALTH SERVICES, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(1) General**

This Quarterly Report on Form 10-Q is for the quarterly period ended September 30, 2014. In this Quarterly Report, we, us, our UHS and the Company refer to Universal Health Services, Inc. and its subsidiaries.

The condensed consolidated financial statements include the accounts of our majority-owned subsidiaries and partnerships and limited liability companies controlled by us, or our subsidiaries, as managing general partner or managing member. The condensed consolidated financial statements included herein have been prepared by us, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission ( SEC ) and reflect all adjustments (consisting only of normal recurring adjustments) which, in our opinion, are necessary to fairly state results for the interim periods. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations, although we believe that the accompanying disclosures are adequate to make the information presented not misleading. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements, significant accounting policies and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2013.

**(2) Relationship with Universal Health Realty Income Trust and Related Party Transactions**

***Relationship with Universal Health Realty Income Trust:***

At September 30, 2014, we held approximately 6.1% of the outstanding shares of Universal Health Realty Income Trust (the Trust ). We serve as Advisor to the Trust under an annually renewable advisory agreement pursuant to the terms of which we conduct the Trust 's day-to-day affairs, provide administrative services and present investment opportunities. In addition, certain of our officers and directors are also officers and/or directors of the Trust. Management believes that it has the ability to exercise significant influence over the Trust, therefore we account for our investment in the Trust using the equity method of accounting. We earned an advisory fee from the Trust, which is included in net revenues in the accompanying condensed consolidated statements of income, of approximately \$700,000 and \$600,000 during the three-month periods ended September 30, 2014 and 2013, respectively, and approximately \$1.9 million and \$1.8 million during the nine-month periods ended September 30, 2014 and 2013, respectively.

Our pre-tax share of income from the Trust was \$1.7 million and \$86,000 during the three-month periods ended September 30, 2014 and 2013, respectively, and \$2.1 million and \$599,000 for the nine-month periods ended September 30, 2014 and 2013, respectively. Included in our share of the Trust 's income for the three and nine-month periods ended September 30, 2014, was approximately \$1.6 million related to our share of an aggregate gain on fair value recognition recorded by the Trust during the third quarter of 2014 in connection with its purchases of third-party minority ownership interests in various limited liability companies in which the Trust formerly held noncontrolling majority ownership interests (the Trust now owns 100% of each of these entities).

The carrying value of our investment in the Trust was approximately \$9 million and \$8 million at September 30, 2014 and December 31, 2013, respectively, and is included in other assets in the accompanying condensed consolidated balance sheets. The market value of this investment, based on the closing price of the Trust 's stock on the respective dates, was approximately \$33 million at September 30, 2014 and \$32 million at December 31, 2013.

Total rent expense under the operating leases on the hospital facilities with the Trust was approximately \$4.0 million during each of the three-month periods ended September 30, 2014 and 2013, and approximately \$12.0 million for each of the nine-month periods ended September 30, 2014 and 2013. In addition, certain of our subsidiaries are tenants in several medical office buildings owned by limited liability companies in which the Trust holds either 100% ownership interests or non-controlling majority ownership interests.

During the third quarter of 2014, we provided notification to the Trust that, upon the December, 2014 expiration of the current lease term on The Bridgeway, we intend to exercise our option to purchase the real property of the facility. We anticipate that the purchase of The Bridgeway's real property (a 103-bed behavioral health facility located in North Little Rock, Arkansas) will occur on December 31, 2014. Pursuant to the terms of the lease, we and the Trust are both required to obtain appraisals of the property to determine its fair market value. Based upon the preliminary property appraisals obtained by each party, we estimate that the purchase price of The Bridgeway's real property will approximate \$17.0 million to \$17.5 million.

In addition, we are currently negotiating with the Trust regarding the Trust's potential ownership of the real property of two free-standing emergency departments located in Texas which are currently under construction by us and scheduled to be completed during the first quarter of 2015. Since these potential transactions are contingent upon the completion and execution of acquisition and lease agreements (subsidiaries of ours are expected to operate the facilities), we can provide no assurance that these transactions will ultimately occur. Should they occur, pursuant to the terms of the acquisition and lease agreements as currently contemplated, we estimate that the aggregate construction cost/sales proceeds of these facilities will approximate \$12.5 million to \$13.0 million, and the aggregate rent expense paid to the Trust at the commencement of the leases will approximate \$850,000 to \$900,000 annually.

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The table below details the renewal options and terms for each of our four hospital facilities leased from the Trust:

<b>Hospital Name</b>	<b>Type of Facility</b>	<b>Annual Minimum Rent</b>	<b>End of Lease Term</b>	<b>Renewal Term (years)</b>
McAllen Medical Center	Acute Care	\$ 5,485,000	December, 2016	15(a)
Wellington Regional Medical Center	Acute Care	\$ 3,030,000	December, 2016	15(b)
Southwest Healthcare System, Inland Valley Campus	Acute Care	\$ 2,648,000	December, 2016	15(b)
The Bridgeway	Behavioral Health	\$ 930,000	December, 2014	10(c)

- (a) We have three 5-year renewal options at existing lease rates (through 2031).
- (b) We have one 5-year renewal option at existing lease rates (through 2021) and two 5-year renewal options at fair market value lease rates (2022 through 2031).
- (c) As discussed above, we have provided notification to the Trust that we intend to purchase the real property of The Bridgeway upon expiration of the current lease term in December, 2014. We had two 5-year renewal options at fair market value lease rates (2015 through 2024) remaining on this property.

**Other Related Party Transactions:**

In December, 2010, our Board of Directors approved the Company's entering into supplemental life insurance plans and agreements on the lives of our chief executive officer and his wife. As a result of these agreements, based on actuarial tables and other assumptions, during the life expectancies of the insureds, we would pay approximately \$25 million in premiums and certain trusts, owned by our chief executive officer, would pay approximately \$8 million in premiums. Based on the projected premiums mentioned above, and assuming the policies remain in effect until the death of the insureds, we will be entitled to receive death benefit proceeds of no less than \$33 million representing the \$25 million of aggregate premiums paid by us as well as the \$8 million of aggregate premiums paid by the trusts. These agreements did not have a material effect on our consolidated financial statements or results of operations during 2013 or the first nine months of 2014.

A member of our Board of Directors and member of the Executive Committee is Of Counsel to Norton Rose Fulbright, one of the law firms used by us as outside counsel. This Board member is also the trustee of certain trusts for the benefit of our Chief Executive Officer ( CEO ) and his family. This law firm also provides personal legal services to our CEO.

**(3) Other Noncurrent liabilities and Redeemable/Noncontrolling Interests**

Other noncurrent liabilities include the long-term portion of our professional and general liability, workers compensation reserves and pension liability.

Outside owners hold noncontrolling, minority ownership interests of: (i) approximately 28% in five acute care facilities currently operating in Las Vegas, Nevada, and a sixth facility currently under construction; (ii) 20% in an acute care facility located in Washington, D.C.; (iii) approximately 11% in an acute care facility located in Laredo, Texas, and; (iv) 20% in a behavioral health care facility located in Philadelphia, Pennsylvania. The redeemable noncontrolling interest balances of \$231 million and \$218 million as of September 30, 2014 and December 31, 2013, respectively, and the noncontrolling interest balances of \$54 million and \$50 million as of September 30, 2014 and

December 31, 2013, respectively, consist primarily of the third-party ownership interests in these hospitals.

In connection with the acute care facilities located in Las Vegas, Nevada, the minority ownership interests of which are reflected as redeemable noncontrolling interests on our Consolidated Balance Sheet, the outside owners have certain put rights, that are currently exercisable, that if exercised, require us to purchase the minority member's interests at fair market value. The put rights are exercisable upon the occurrence of: (i) certain specified financial conditions falling below established thresholds; (ii) breach of the management contract by the managing member (a subsidiary of ours), or; (iii) if the minority member's ownership percentage is reduced to less than certain thresholds. In connection with the behavioral health care facility located in Philadelphia, Pennsylvania, the minority ownership interest of which is also reflected as redeemable noncontrolling interests on our Consolidated Balance Sheet, the outside owner has a put option to put its entire ownership interest to us at any time. If exercised, the put option requires us to purchase the minority member's interest at fair market value. As of September 30, 2014, we believe the fair market value of the minority ownership interests in these facilities, pursuant to the terms of the put options, approximates the book value of the redeemable noncontrolling interests.

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**(4) Long-term debt and cash flow hedges**

***Credit Facilities and Outstanding Debt Securities***

During the third quarter of 2014, we completed the following previously disclosed financing transactions:

On August 7, 2014, we entered into a Fourth Amendment (the *Fourth Amendment*) to our credit agreement dated as of November 15, 2010, as amended on March 15, 2011, September 21, 2012 and May 16, 2013, among UHS, as borrower, the several banks and other financial institutions from time to time parties thereto, as lenders (*Credit Agreement*). The Credit Agreement, as amended, which is scheduled to mature in August, 2019, consists of: (i) an \$800 million revolving credit facility, and; (ii) a \$1.775 billion term loan A facility which combined our previous term loan A and term loan A2 facilities (which were scheduled to mature in 2016);

Repaid \$550 million of outstanding borrowings pursuant to our previous term loan B facility which was scheduled to mature in 2016;

Increased the borrowing capacity on our existing \$275 million accounts receivable securitization program (*Securitization*) to \$360 million effective August 1, 2014. The Securitization, the terms of which remain the same as the previous agreement, as discussed below, is scheduled to mature on October 25, 2016;

Issued \$300 million aggregate principal amount of 3.750% senior secured notes due in 2019 (see below for additional disclosure);

Issued \$300 million aggregate principal amount of 4.750% senior secured notes due in 2022 (see below for additional disclosure);

Redeemed our previously outstanding \$250 million, 7.00% senior unsecured notes due in 2018 on July 31, 2014 for an aggregate price equal to 104.56% of the principal amount.

In connection with these transactions, our results of operations during the three and nine-month periods ended September 30, 2014 included a \$36 million pre-tax charge incurred for the costs related to the extinguishment of debt. This charge consisted of the write-off of deferred charges (\$20 million) and original issue discount on the extinguished debt (\$5 million) as well as the make-whole premium paid (\$11 million) on the early redemption of the \$250 million, 7.00% senior unsecured notes.

Pursuant to the terms of our Credit Agreement and related amendments, as of September 30, 2014, we had:

\$1.775 billion of borrowings outstanding pursuant to our term loan A facility, and;

\$267 million of borrowings outstanding pursuant to our revolving credit facility.

Borrowings under the Credit Agreement bear interest at either (1) the ABR rate which is defined as the rate per annum equal to, at our election: the greatest of (a) the lender's prime rate, (b) the weighted average of the federal funds rate, plus 0.5% and (c) one month LIBOR rate plus 1%, in each case, plus an applicable margin based upon our consolidated leverage ratio at the end of each quarter ranging from 0.50% to 1.25% for revolving credit and term loan-A borrowings, or (2) the one, two, three or six month LIBOR rate (at our election), plus an applicable margin based upon our consolidated leverage ratio at the end of each quarter ranging from 1.50% to 2.25% for revolving credit and term loan-A borrowings. As of September 30, 2014, the applicable margins were 0.50% for ABR-based loans, 1.50% for LIBOR-based loans under the revolving credit and term loan-A facilities.

As of September 30, 2014, we had \$267 million of outstanding borrowings pursuant to the terms of our \$800 million revolving credit facility and we had \$478 million of available borrowing capacity, net of \$35 million of outstanding borrowings pursuant to a short-term, on-demand credit facility and \$20 million of outstanding letters of credit. The revolving credit facility includes a \$125 million sub-limit for letters of credit. The Credit Agreement is secured by certain assets of the Company and our material subsidiaries and guaranteed by our material subsidiaries.

Pursuant to the terms of the Fourth Amendment to our Credit Agreement, term loan A quarterly installment payments of approximately: (i) \$11 million are due commencing in the fourth quarter of 2014 and continuing through September, 2016, and; (ii) \$22 million are due from the fourth quarter of 2016 through June, 2019. Prior to commencement of the Fourth Amendment, we made scheduled principal payments of \$36 million on the term loan-A and term loan A2 facilities during the nine-month period ended September 30, 2014 and \$18 million and \$54 million, respectively, during the three and nine-month periods ended September 30, 2013.

As discussed above, on August 1, 2014, our accounts receivable securitization program ( "Securitization" ), with a group of conduit lenders and liquidity banks which is scheduled to mature on October 25, 2016, was amended to increase the borrowing capacity to \$360 million from \$275 million. Substantially all of the patient-related accounts receivable of our acute care hospitals ( "Receivables" ) serve as collateral for the outstanding borrowings. We have accounted for this Securitization as borrowings. We maintain effective control over the Receivables since, pursuant to the terms of the Securitization, the Receivables are sold from certain of our subsidiaries to special purpose entities that are wholly-owned by us. The Receivables, however, are owned by the special purpose entities, can be used only to satisfy the debts of the wholly-owned special purpose entities, and thus are not available to us except through our ownership interest in the special purpose entities. The wholly-owned special purpose entities use the Receivables to collateralize the loans obtained from the group of third-party conduit lenders and liquidity banks. The group of third-party conduit lenders and liquidity banks do not have recourse to us beyond the assets of the wholly-owned special purpose entities that securitize the loans. At September 30, 2014, we had \$333 million of outstanding borrowings and \$27 million of additional capacity pursuant to the terms of our accounts receivable securitization program.

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On August 7, 2014, we issued \$300 million aggregate principal amount of 3.750% Senior Secured Notes due 2019 (the 2019 Notes ) and \$300 million aggregate principal amount of 4.750% Senior Secured Notes due 2022 (the 2022 Notes ), and together with the 2019 Notes, the New Senior Secured Notes ). The New Senior Secured Notes were offered only to qualified institutional buyers under Rule 144A and to non-U.S. persons outside the United States in reliance on Regulation S under the Securities Act of 1933, as amended (the Securities Act ). The New Senior Secured Notes have not been registered under the Securities Act and may not be offered or sold in the United States absent registration or an applicable exemption from registration requirements. Interest is payable on the New Senior Secured Notes on February 1 and August 1 of each year to the holders of record at the close of business on the January 15 and July 15 immediately preceding the related interest payment dates, commencing on February 1, 2015 until the maturity date of August 1, 2019 for the 2019 Notes and August 1, 2022 for the 2022 Notes.

On June 30, 2006, we issued \$250 million of senior secured notes which have a 7.125% coupon rate and mature on June 30, 2016 (the 7.125% Notes ). Interest on the 7.125% Notes is payable semiannually in arrears on June 30th and December 30th of each year. In June, 2008, we issued an additional \$150 million of 7.125% Notes which formed a single series with the original 7.125% Notes issued in June, 2006. Other than their date of issuance and initial price to the public, the terms of the 7.125% Notes issued in June, 2008 are identical to and trade interchangeably with, the 7.125% Notes which were originally issued in June, 2006.

On July 31, 2014, we redeemed the \$250 million, 7.00% senior unsecured notes (the Unsecured Notes ), which were scheduled to mature on October 1, 2018, at a redemption price equal to 104.56% of the principal amount of the Unsecured Notes resulting in a make-whole premium payment of approximately \$11 million. The Unsecured Notes were issued on September 29, 2010 and registered in April, 2011. Interest on the Unsecured Note was payable semiannually in arrears on April 1st and October 1st of each year.

In connection with entering into the previous Credit Agreement on November 15, 2010, and in accordance with the Indenture dated January 20, 2000 governing the rights of our existing notes, we entered into a supplemental indenture pursuant to which our 7.125% Notes (due in 2016) were equally and ratably secured with the lenders under the Credit Agreement with respect to the collateral for so long as the lenders under the Credit Agreement are so secured.

Our Credit Agreement includes a material adverse change clause that must be represented at each draw. The Credit Agreement contains covenants that include a limitation on sales of assets, mergers, change of ownership, liens and indebtedness, transactions with affiliates and dividends; and requires compliance with financial covenants including maximum leverage and minimum interest coverage ratios. We are in compliance with all required covenants as of September 30, 2014.

As of September 30, 2014, the carrying value of our debt was \$3.45 billion and the fair-value of our debt was \$3.49 billion. The fair value of our debt was computed based upon quotes received from financial institutions and we consider these to be level 2 in the fair value hierarchy as outlined in the authoritative guidance for disclosures in connection with debt instruments.

***Cash Flow Hedges:***

We manage our ratio of fixed and floating rate debt with the objective of achieving a mix that management believes is appropriate. To manage this risk in a cost-effective manner, we, from time to time, enter into interest rate swap agreements in which we agree to exchange various combinations of fixed and/or variable interest rates based on agreed upon notional amounts. We account for our derivative and hedging activities using the Financial Accounting Standard Board's ( FASB ) guidance which requires all derivative instruments, including certain derivative instruments embedded in other contracts, to be carried at fair value on the balance sheet. For derivative transactions designated as

hedges, we formally document all relationships between the hedging instrument and the related hedged item, as well as its risk-management objective and strategy for undertaking each hedge transaction.

Derivative instruments designated in a hedge relationship to mitigate exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Cash flow hedges are accounted for by recording the fair value of the derivative instrument on the balance sheet as either an asset or liability, with a corresponding amount recorded in accumulated other comprehensive income ( AOCI ) within shareholders' equity. Amounts are reclassified from AOCI to the income statement in the period or periods the hedged transaction affects earnings. We use interest rate derivatives in our cash flow hedge transactions. Such derivatives are designed to be highly effective in offsetting changes in the cash flows related to the hedged liability. For derivative instruments designated as cash flow hedges, the ineffective portion of the change in expected cash flows of the hedged item are recognized currently in the income statement.

For hedge transactions that do not qualify for the short-cut method, at the hedge's inception and on a regular basis thereafter, a formal assessment is performed to determine whether changes in the fair values or cash flows of the derivative instruments have been highly effective in offsetting changes in cash flows of the hedged items and whether they are expected to be highly effective in the future.

The fair value of interest rate swap agreements approximates the amount at which they could be settled, based on estimates obtained from the counterparties. We assess the effectiveness of our hedge instruments on a quarterly basis. We performed periodic

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assessments of the cash flow hedge instruments during 2013 and the first nine months of 2014 and determined the hedges to be highly effective. We also determined that any portion of the hedges deemed to be ineffective was de minimis and therefore there was no material effect on our consolidated financial position, operations or cash flows. The counterparties to the interest rate swap agreements expose us to credit risk in the event of nonperformance. However, at September 30, 2014, each swap agreement entered into by us was in a net liability position which would require us to make the net settlement payments to the counterparties. We do not anticipate nonperformance by our counterparties. We do not hold or issue derivative financial instruments for trading purposes.

We entered into six forward starting interest rate swaps in the first quarter of 2011 whereby we pay a fixed rate on a total notional amount of \$425 million and receive three-month LIBOR. Three of these swaps with a total notional amount of \$225 million became effective in March, 2011 and will mature in May, 2015. The average fixed rate payable on these swaps is 1.91%. The three remaining interest rate swaps with total notional amounts of \$100 million, \$25 million and \$75 million became effective in December, 2011 and have/had fixed rates of 2.50%, 1.96% and 1.32%, and maturity dates in December, 2014, December, 2013 and December, 2012, respectively.

During the fourth quarter of 2010, we entered into four forward starting interest rate swaps whereby we pay a fixed rate on a total notional amount of \$600 million and receive three-month LIBOR. Each of the four swaps became effective in December, 2011 and will mature in May, 2015. The average fixed rate payable on these swaps is 2.38%.

We measure our interest rate swaps at fair value on a recurring basis. The fair value of our interest rate swaps is based primarily on quotes from banks. We consider those inputs to be level 2 in the fair value hierarchy as outlined in the authoritative guidance for disclosures in connection with derivative instruments and hedging activities. The fair value of our interest rate swaps was an aggregate gross and net liability of \$11 million at September 30, 2014, which is included in accounts payable and accrued liabilities on the accompanying balance sheet. The fair value of our interest rate swaps was an aggregate gross and net liability of \$24 million at December 31, 2013, of which \$19 million was included in accounts payable and accrued liabilities and \$5 million was included in other noncurrent liabilities on the accompanying balance sheet.

**(5) Commitments and Contingencies***Professional and General Liability and Workers Compensation Liability:*

Effective November, 2010, excluding certain subsidiaries acquired since 2010 as discussed below, our subsidiaries are self-insured for professional and general liability exposure up to \$10 million and \$3 million per occurrence, respectively. Our subsidiaries were provided with several excess policies through commercial insurance carriers which provide for coverage in excess of the applicable per occurrence self-insured retention (either \$3 million or \$10 million) up to \$250 million per occurrence and in the aggregate for claims incurred in 2014 and up to \$200 million per occurrence and in the aggregate for claims incurred from 2011 through 2013. We remain liable for 10% of the claims paid pursuant to the commercially insured coverage in excess of \$10 million up to \$60 million per occurrence and in the aggregate.

Since our acquisition of Psychiatric Solutions, Inc. ( PSI ) in November, 2010, the former PSI subsidiaries are self-insured for professional and general liability exposure up to \$3 million per occurrence. The 9 behavioral health facilities acquired from Ascend Health Corporation ( Ascend ) in October, 2012 have general and professional liability policies through commercial insurance carriers which provide for up to \$10 million of aggregate coverage, subject to a \$100,000 per occurrence deductible. The 18 facilities acquired from Cygnet Health Care Limited ( Cygnet ), consisting of 16 inpatient behavioral health hospitals and 2 nursing homes, have policies through a commercial insurance carrier located in the United Kingdom that provides for £10 million of professional liability coverage and £25 million of

general liability coverage. The facilities acquired from PSI, Ascend and Cygnet, like our other facilities, are also provided excess coverage through commercial insurance carriers for coverage in excess of the underlying commercial policy limitations, as mentioned above.

Our estimated liability for self-insured professional and general liability claims is based on a number of factors including, among other things, the number of asserted claims and reported incidents, estimates of losses for these claims based on recent and historical settlement amounts, estimates of incurred but not reported claims based on historical experience, and estimates of amounts recoverable under our commercial insurance policies. While we continuously monitor these factors, our ultimate liability for professional and general liability claims could change materially from our current estimates due to inherent uncertainties involved in making this estimate. Given our significant self-insured exposure for professional and general liability claims, there can be no assurance that a sharp increase in the number and/or severity of claims asserted against us will not have a material adverse effect on our future results of operations.

During the second quarter of 2013, pursuant to a reserve analysis, we recorded reductions to our professional and general liability self-insurance reserves (relating to years prior to 2013) amounting to \$65 million in the aggregate which is included in our financial results for the nine-month period ended September 30, 2013. The favorable changes in our estimated future claims payments relating to years prior to 2013 were due to: (i) an increased weighting given to company-specific metrics (to 100% from 75%), and decreased general industry metrics (to 0% from 25%), related to projected incidents per exposure, historical claims experience and loss development factors; (ii) historical data which measured the realized favorable impact of medical malpractice tort reform experienced in several

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states in which we operate, and; (iii) a decrease in claims related to certain higher risk specialties (such as obstetrical) due to a continuation of the company-wide patient safety initiative undertaken during the last several years. As the number of our facilities and our patient volumes have increased, thereby providing for a statistically significant data group, and taking into consideration our long-history of company-specific risk management programs and claims experience, our reserve analyses have included a greater emphasis on our historical professional and general liability experience which has developed favorably as compared to general industry trends.

As of September 30, 2014, the total accrual for our professional and general liability claims was \$209 million, of which \$44 million is included in current liabilities. As of December 31, 2013, the total accrual for our professional and general liability claims was \$206 million, of which \$44 million is included in current liabilities.

As of September 30, 2014, the total accrual for our workers' compensation liability claims was \$66 million, of which \$34 million is included in current liabilities. As of December 31, 2013, the total accrual for our workers' compensation liability claims was \$64 million, of which \$34 million is included in current liabilities.

***Property Insurance:***

We have commercial property insurance policies covering catastrophic losses, including windstorm damage, up to a \$1 billion policy limit per occurrence, subject to a \$250,000 deductible for the majority of our properties (the properties acquired from PSI are subject to a \$50,000 deductible). Losses resulting from named windstorms are subject to deductibles between 3% and 5% of the declared total insurable value of the property. In addition, we have commercial property insurance policies covering catastrophic losses resulting from earthquake and flood damage, each subject to aggregated loss limits (as opposed to per occurrence losses). Our earthquake limit is \$250 million, subject to a deductible of \$250,000, except for facilities located within documented fault zones. Earthquake losses that affect facilities located in fault zones within the United States are subject to a \$100 million limit and will have applied deductibles ranging from 1% to 5% of the declared total insurable value of the property. The earthquake limit in Puerto Rico is \$25 million, subject to a \$25,000 deductible. Non-critical flood losses have either a \$250,000 or \$500,000 deductible, based upon the location of the facility. Since certain of our facilities have been designated by our insurer as flood prone, we have elected to purchase policies from The National Flood Insurance Program to cover a substantial portion of the applicable deductible. Property insurance for the facilities acquired from Cygnet are provided on an all risk basis up to a £180 million limit that includes coverage for real and personal property as well as business interruption losses.

***Other***

Our accounts receivable as of September 30, 2014 and December 31, 2013 include amounts due from Illinois of approximately \$33 million and \$49 million, respectively. Collection of the outstanding receivables continues to be delayed due to state budgetary and funding pressures. Approximately \$10 million as of September 30, 2014 and \$28 million as of December 31, 2013, of the receivables due from Illinois were outstanding in excess of 60 days, as of each respective date. In addition, our accounts receivable as of September 30, 2014 and December 31, 2013 includes approximately \$107 million and \$72 million due from Texas in connection with Medicaid supplemental payment programs. The \$107 million due from Texas as of September 30, 2014 consists of \$62 million related to uncompensated care program revenues and \$45 million related to disproportionate share hospital program revenues. Although the accounts receivable due from Illinois and Texas could remain outstanding for the foreseeable future, since we expect to eventually collect all amounts due to us, no related reserves have been established in our consolidated financial statements. However, we can provide no assurance that we will eventually collect all amounts due to us from Illinois and/or Texas. In September, 2014 CMS deferred the federal matching funds on Texas Medicaid uncompensated care payments made to providers in certain counties in Texas. Although we do not believe our

hospitals located in Texas are impacted by this deferral since they are not located in the impacted geographical areas, we can provide no assurance that our hospitals will not be impacted by future deferrals if CMS expands the deferrals to other counties in Texas. Failure to ultimately collect all outstanding amounts due from these states would have an adverse impact on our future consolidated results of operations and cash flows.

As of September 30, 2014 we were party to certain off balance sheet arrangements consisting of standby letters of credit and surety bonds which totaled \$94 million consisting of: (i) \$73 million related to our self-insurance programs, and; (ii) \$21 million of other debt and public utility guarantees.

### ***Legal Proceedings***

We are subject to claims and suits in the ordinary course of business, including those arising from care and treatment afforded by our hospitals and are party to litigation, as outlined below.

#### *Office of Inspector General ( OIG ) and Other Government Investigations*

In September, 2010, we, along with many other companies in the healthcare industry, received a letter from the United States Department of Justice ( DOJ ) advising of a False Claim Act investigation being conducted in connection with the implantation of implantable cardioverter defibrillators ( ICDs ) from 2003 to 2010 at several of our acute care facilities. The DOJ alleges that ICDs were implanted and billed by our facilities in contravention of a National Coverage Determination regarding these devices. We have established a reserve in connection with this matter which did not have a material impact on our consolidated financial statements.

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In February, 2013, the OIG served a subpoena requesting various documents from January, 2008 to the date of the subpoena directed at Universal Health Services, Inc. ( UHS ) concerning it and UHS of Delaware, Inc., and several UHS owned behavioral health facilities including: Keys of Carolina, Old Vineyard Behavioral Health, The Meadows Psychiatric Center, Streamwood Behavioral Health, Hartgrove Hospital, Rock River Academy and Residential Treatment Center, Roxbury Treatment Center, Harbor Point Behavioral Health Center, f/k/a, The Pines Residential Treatment Center, including the Crawford, Brighton and Kempsville campuses, Wekiva Springs Center and River Point Behavioral Health. Prior to receiving this subpoena: (i) the Keys of Carolina and Old Vineyard received notification during the second half of 2012 from the United States Department of Justice of its intent to proceed with an investigation following requests for documents for the period of January, 2007 to the date of the subpoenas from the North Carolina state Attorney General's Office; (ii) Harbor Point Behavioral Health Center received a subpoena in December, 2012 from the Attorney General of the Commonwealth of Virginia requesting various documents from July, 2006 to the date of the subpoena, and; (iii) The Meadows Psychiatric Center received a subpoena from the OIG in February, 2013 requesting certain documents from 2008 to the date of the subpoena. Unrelated to these matters, the Keys of Carolina was closed and the real property was sold in January, 2013. We were advised that a qui tam action had been filed against Roxbury Treatment Center but the government declined to intervene and the case was dismissed.

In April, 2013, the OIG served facility specific subpoenas on Wekiva Springs Center and River Point Behavioral Health requesting various documents from January, 2005 to the date of the subpoenas. In July, 2013, another subpoena was issued to Wekiva Springs Center and River Point Behavioral Health requesting additional records. In October, 2013, we were advised by the DOJ's Criminal Frauds Section that they received a referral from the DOJ Civil Division and opened an investigation of River Point Behavioral Health and Wekiva Springs Center. Subsequent subpoenas have since been issued to River Point Behavioral Health and Wekiva Springs Center requesting additional documentation. In April, 2014, the Centers for Medicare and Medicaid Services ( CMS ) instituted a Medicare payment suspension at River Point Behavioral Health in accordance with federal regulations which implemented provisions of the Affordable Care Act regarding suspension of payments during certain investigations. The Florida Agency for Health Care Administration subsequently issued a Medicaid payment suspension for the facility. River Point Behavioral Health submitted a rebuttal statement disputing the basis of the suspension and requesting revocation of the suspension. In response, CMS has continued the payment suspension. River Point Behavioral Health has provided additional information to CMS in an effort to obtain relief from the payment suspension but the suspension remains in effect. In August 2014, we received notification from CMS that the payment suspension was to be continued for another 180 days. We cannot predict if and/or when the facility's suspended payments will resume. However, if continued for a significant period of time, the payment suspension will likely have a material adverse effect on River Point Behavioral Health's future results of operations and financial condition. The operating results of River Point Behavioral Health did not have a material impact on our consolidated results of operations for the three and nine-month periods ended September 30, 2014 or the year ended December 31, 2013.

In June, 2013, the OIG served a subpoena on Coastal Harbor Health System in Savannah, Georgia requesting documents from January, 2009 to the date of the subpoena.

In February, 2014, we were notified that the investigation conducted by the Criminal Frauds Section had been expanded to include the National Deaf Academy. In March, 2014, a Civil Investigative Demand ( CID ) was served on the National Deaf Academy requesting documents and information from the facility from January 1, 2008 through the date of the CID. We have been advised by the government that the National Deaf Academy has been added to the facilities which are the subject of the coordinated investigation referenced above.

In March, 2014, CIDs were served on Hartgrove Hospital, Rock River Academy and Streamwood Behavioral Health requesting documents and information from those facilities from January 2008 through the date of the CID.

In September, 2014, the DOJ Civil Division advised us that they were expanding their investigation to include four additional facilities and were requesting production of documents from these facilities. These facilities are Arbour-HRI Hospital, Behavioral Hospital of Bellaire, St. Simons by the Sea, and Turning Point Care Center.

At present, we are uncertain as to the specific focus, scope or extent of the investigations, liability of the facilities and/or potential financial exposure, if any, in connection with these matters.

*Matters Relating to PSI:*

The following matters pertain to PSI or former PSI facilities (owned by subsidiaries of Psychiatric Solutions, Inc.) which were in existence prior to the acquisition of PSI and for which we have assumed the defense as a result of our acquisition which was completed in November, 2010:

*Garden City Employees Retirement System v. Psychiatric Solutions, Inc. ( PSI ), Joey A. Jacobs, Brent Turner and Jack E. Polson:*

This is a shareholder class action lawsuit filed in 2009 in the United States District Court for the Middle District of Tennessee against PSI and certain of its former officers alleging violations of federal securities laws. As we previously disclosed, in September of 2014,

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a \$65 million settlement agreement was reached in connection with this matter. A settlement escrow, pending final court approval, was funded in October of 2014. A pre-tax charge of \$49 million was incurred by us during the first nine months of 2014 in connection with this settlement which is net of approximately \$16 million of commercial insurance recoveries.

*Department of Justice Investigation of Friends Hospital:*

In October, 2010, Friends Hospital in Philadelphia, Pennsylvania, received a subpoena from the DOJ requesting certain documents from the facility. The requested documents have been collected and provided to the DOJ for review and examination. Another subpoena was issued to the facility in July 2011 requesting additional documents, which have been collected and delivered to the DOJ. At present, we are uncertain as to the focus, scope or extent of the investigation, liability of the facility and/or potential financial exposure, if any, in connection with this matter.

*Department of Justice Investigation of Riveredge Hospital:*

In 2008, Riveredge Hospital in Chicago, Illinois received a subpoena from the DOJ requesting certain information from the facility. Additional requests for documents were also received from the DOJ in 2009 and 2010. The requested documents have been provided to the DOJ. At present, we are uncertain as to the focus, scope or extent of the investigation, liability of the facility and/or potential financial exposure, if any, in connection with this matter.

*General:*

The healthcare industry is subject to numerous laws and regulations which include, among other things, matters such as government healthcare participation requirements, various licensure, certifications, and accreditations, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Government action has increased with respect to investigations and/or allegations concerning possible violations of fraud and abuse and false claims statutes and/or regulations by healthcare providers. Currently, and from time to time, some of our facilities are subjected to inquiries and/or actions and receive notices of potential non-compliance of laws and regulations from various federal and state agencies. Providers that are found to have violated these laws and regulations may be excluded from participating in government healthcare programs, subjected to potential licensure, certification, and/or accreditation revocation, subjected to payment suspension, subjected to fines or penalties or required to repay amounts received from the government for previously billed patient services. We monitor all aspects of our business and have developed a comprehensive ethics and compliance program that is designed to meet or exceed applicable federal guidelines and industry standards. Because the law in this area is complex and constantly evolving, governmental investigation or litigation may result in interpretations that are inconsistent with industry practices, including ours. Although we believe our policies, procedures and practices comply with governmental regulations, there is no assurance that we will not be faced with sanctions, fines or penalties in connection with such inquiries or actions, including with respect to the investigations and other matters discussed herein. Even if we were to ultimately prevail, such inquiries and/or actions could have a material adverse effect on us.

The outcome of any current or future litigation or governmental or internal investigations, including the matters described above, cannot be accurately predicted, nor can we predict any resulting penalties, fines or other sanctions that may be imposed at the discretion of federal or state regulatory authorities. We record accruals for such contingencies to the extent that we conclude it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. No estimate of the possible loss or range of loss in excess of amounts accrued, if any, can be made at this time regarding the matters specifically described above because the inherently unpredictable nature of legal proceedings may be exacerbated by various factors, including, but not limited to: (i) the damages sought in the proceedings are unsubstantiated or indeterminate; (ii) discovery is not complete; (iii) the proceeding is in

its early stages; (iv) the matters present legal uncertainties; (v) there are significant facts in dispute; (vi) there are a large number of parties, or; (vii) there is a wide range of potential outcomes. It is possible that the outcome of these matters could have a material adverse impact on our future results of operations, financial position, cash flows and, potentially, our reputation.

In addition, various suits and claims arising against us in the ordinary course of business are pending. In the opinion of management, the outcome of such claims and litigation will not materially affect our consolidated financial position or results of operations.

#### **(6) Segment Reporting**

Our reportable operating segments consist of acute care hospital services and behavioral health care services. The

Other segment column below includes centralized services including information services, purchasing, reimbursement, accounting, taxation, legal, advertising, design and construction and patient accounting as well as the operating results for our other operating entities including outpatient surgery and radiation centers. The chief operating decision making group for our acute care hospital services and behavioral health care services is comprised of the Chief Executive Officer, the President and the Presidents of each operating segment. The Presidents of each operating segment also manage the profitability of each respective segment's various facilities. The operating segments are managed separately because each operating segment represents a business unit that offers different types of healthcare services or operates in different healthcare environments. The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies included in our Annual Report on Form 10-K for the year ended December 31, 2013.

**Table of Contents****Three months ended September 30, 2014**

	<b>Acute Care Hospital Services</b>	<b>Behavioral Health Services</b>	<b>Other</b>	<b>Total Consolidated</b>
	(Amounts in thousands)			
Gross inpatient revenues	\$ 3,616,647	\$ 1,678,222	\$ 0	\$ 5,294,869
Gross outpatient revenues	\$ 2,058,148	\$ 192,032	\$ 8,972	\$ 2,259,152
Total net revenues	\$ 1,038,135	\$ 976,014	\$ 3,609	\$ 2,017,758
Income/(loss) before allocation of corporate overhead and income taxes	\$ 100,388	\$ 228,710	(\$ 184,620)	\$ 144,478
Allocation of corporate overhead	(\$ 44,698)	(\$ 24,750)	\$ 69,448	\$ 0
Income/(loss) after allocation of corporate overhead and before income taxes	\$ 55,690	\$ 203,960	(\$ 115,172)	\$ 144,478
Total assets as of 9/30/14	\$ 3,321,166	\$ 5,429,453	\$ 210,973	\$ 8,961,592

**Nine months ended September 30, 2014**

	<b>Acute Care Hospital Services</b>	<b>Behavioral Health Services</b>	<b>Other</b>	<b>Total Consolidated</b>
	(Amounts in thousands)			
Gross inpatient revenues	\$ 11,217,320	\$ 4,973,633	\$ 0	\$ 16,190,953
Gross outpatient revenues	\$ 6,083,715	\$ 580,627	\$ 25,821	\$ 6,690,163
Total net revenues	\$ 3,033,535	\$ 2,913,819	\$ 10,391	\$ 5,957,745
Income/(loss) before allocation of corporate overhead and income taxes	\$ 330,382	\$ 693,399	(\$ 385,175)	\$ 638,606
Allocation of corporate overhead	(\$ 134,088)	(\$ 74,055)	\$ 208,143	\$ 0
Income/(loss) after allocation of corporate overhead and before income taxes	\$ 196,294	\$ 619,344	(\$ 177,032)	\$ 638,606
Total assets as of 9/30/14	\$ 3,321,166	\$ 5,429,453	\$ 210,973	\$ 8,961,592

**Three months ended September 30, 2013**

	<b>Acute Care Hospital Services</b>	<b>Behavioral Health Services</b>	<b>Other</b>	<b>Total Consolidated</b>
	(Amounts in thousands)			
Gross inpatient revenues	\$ 3,296,484	\$ 1,567,436	\$ 0	\$ 4,863,920
Gross outpatient revenues	\$ 1,712,290	\$ 179,783	\$ 10,207	\$ 1,902,280
Total net revenues	\$ 899,533	\$ 907,935	\$ 8,901	\$ 1,816,369
Income/(loss) before allocation of corporate overhead and income taxes	\$ 68,266	\$ 211,456	(\$ 87,150)	\$ 192,572
Allocation of corporate overhead	(\$ 46,112)	(\$ 22,265)	\$ 68,377	\$ 0
Income/(loss) after allocation of corporate overhead and before income taxes	\$ 22,154	\$ 189,191	(\$ 18,773)	\$ 192,572
Total assets as of 9/30/13	\$ 3,123,780	\$ 4,926,271	\$ 301,692	\$ 8,351,743



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	<b>Nine months ended September 30, 2013</b>			
	<b>Acute Care Hospital Services</b>	<b>Behavioral Health Services</b>	<b>Other</b>	<b>Total Consolidated</b>
	(Amounts in thousands)			
Gross inpatient revenues	\$ 10,124,908	\$ 4,741,967	\$ 0	\$ 14,866,875
Gross outpatient revenues	\$ 5,072,065	\$ 559,288	\$ 31,680	\$ 5,663,033
Total net revenues	\$ 2,702,913	\$ 2,746,949	\$ 33,114	\$ 5,482,976
Income/(loss) before allocation of corporate overhead and income taxes	\$ 267,285	\$ 672,787	(\$ 277,698)	\$ 662,374
Allocation of corporate overhead	(\$ 138,333)	(\$ 67,093)	\$ 205,426	\$ 0
Income/(loss) after allocation of corporate overhead and before income taxes	\$ 128,952	\$ 605,694	(\$ 72,272)	\$ 662,374
Total assets as of 9/30/13	\$ 3,123,780	\$ 4,926,271	\$ 301,692	\$ 8,351,743

**(7) Earnings Per Share Data ( EPS ) and Stock Based Compensation**

Basic earnings per share are based on the weighted average number of common shares outstanding during the period. Diluted earnings per share are based on the weighted average number of common shares outstanding during the period adjusted to give effect to common stock equivalents.

The following table sets forth the computation of basic and diluted earnings per share for the periods indicated (in thousands, except per share data):

	<b>Three months ended September 30,</b>		<b>Nine months ended September 30,</b>	
	(amounts in thousands)			
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
<b>Basic and Diluted:</b>				
Net income attributable to UHS	\$ 82,797	\$ 114,587	\$ 372,546	\$ 386,212
Less: Net income attributable to unvested restricted share grants	(17)	(43)	(164)	(200)
Net income attributable to UHS basic and diluted	\$ 82,780	\$ 114,544	\$ 372,382	\$ 386,012
Weighted average number of common shares - basic	99,052	98,151	98,832	97,965
Net effect of dilutive stock options and grants based on the treasury stock method	1,981	1,436	1,643	1,158
Weighted average number of common shares and equivalents - diluted	101,033	99,587	100,475	99,123
Earnings per basic share attributable to UHS:	\$ 0.84	\$ 1.17	\$ 3.77	\$ 3.94

Earnings per diluted share attributable to UHS:	\$	0.82	\$	1.15	\$	3.71	\$	3.89
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The Net effect of dilutive stock options and grants based on the treasury stock method , for all periods presented above, excludes certain outstanding stock options applicable to each period since the effect would have been anti-dilutive. There were no significant anti-dilutive stock options during the three and nine months ended September 30, 2014 and 2013. All classes of our common stock have the same dividend rights.

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**Stock-Based Compensation:** During the three-month periods ended September 30, 2014 and 2013, compensation cost of \$7.5 million and \$6.2 million, respectively, was recognized related to outstanding stock options. During the nine-month periods ended September 30, 2014 and 2013, compensation cost of \$21.7 million and \$19.0 million, respectively was recognized related to outstanding stock options. In addition, during the three-month periods ended September 30, 2014 and 2013, compensation cost of approximately \$274,000 and \$307,000, respectively, was recognized related to restricted stock. During the nine-month periods ended September 30, 2014 and 2013, compensation cost of approximately \$921,000 and \$1.0 million, respectively, was recognized related to restricted stock. As of September 30, 2014 there was \$57.4 million of unrecognized compensation cost related to unvested options and restricted stock which is expected to be recognized over the remaining weighted average vesting period of 2.8 years. There were 2,749,150 stock options granted (net of cancellations) during the first nine months of 2014 with a weighted-average grant date fair value of \$17.16 per share.

The expense associated with share-based compensation arrangements is a non-cash charge. In the Consolidated Statements of Cash Flows, share-based compensation expense is an adjustment to reconcile net income to cash provided by operating activities and aggregated to \$22.7 million and \$20.0 million during the nine-month periods ended September 30, 2014 and 2013, respectively. In accordance with ASC 718, excess income tax benefits related to stock based compensation are classified as cash inflows from financing activities on the Consolidated Statement of Cash Flows. Previously for the nine-month period ended September 30, 2013, we included \$15.8 million of excess income tax benefits related to stock based compensation as net cash provided by operating activities as included in the change in accrued and deferred income taxes for that period. In our Consolidated Statements of Cash Flows, as included herein, that amount is reflected as cash inflows from financing activities for the 2013 nine-month period. We assessed this misclassification and concluded that it was not material to our previously issued quarterly Consolidated Statements of Cash Flows. During the first nine months of 2014, we generated \$30.2 million of excess income tax benefits related to stock based compensation which are reflected as cash inflows from financing activities in our Consolidated Statements of Cash Flows.

**(8) Dispositions and acquisitions*****Nine-month periods ended September 30, 2014 and 2013:*****Acquisitions:**

During the first nine months of 2014, we spent \$402 million to: (i) acquire the stock of Cygnet Health Care Limited which consists of 18 facilities located throughout the United Kingdom including 16 inpatient behavioral health hospitals and 2 nursing homes with a total of 734 beds (during the third quarter); (ii) acquire and fund the required capital reserves related to a commercial health insurer headquartered in Reno, Nevada (during the second quarter); (iii) acquire the Psychiatric Institute of Washington ( PIW ), a 124-bed behavioral health care facility and outpatient treatment center located in Washington, D.C. (during the second q