

March 21, 2014

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Scott Jackson
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Re: Indication of Interest in St. Francis Medical Center

Dear Mr. Ligibel and Mr. Jackson,

Dignity Health is pleased to have received the Confidential Information Memorandum concerning Daughters of Charity Health System (DCHS) and submits this non-binding Indication of Interest related to the assets of St. Francis Medical Center (SFMC) for your consideration.

Based on our review of the Confidential Information Memorandum, Dignity Health found that DCHS and SFMC's Mission, Vision and Values closely align with those of Dignity Health. For this reason and our belief that Dignity Health can effectively honor and continue SFMC's storied tradition of compassion and excellence in Catholic healthcare in the Southeast Los Angeles community, Dignity Health proposes the acquisition of substantially all of SFMC's assets in the manner described in this non-binding Indication of Interest.

Please do not hesitate to contact us should you have any questions or wish to discuss in detail any aspect of our Indication of Interest.

Respectfully,


Michael Blaszyk
Sr. EVP & Chief Financial Officer

EXECUTIVE SUMMARY

Dignity Health is a California nonprofit public benefit corporation headquartered in San Francisco, California. Today, Dignity Health is the fifth largest health care system in the nation providing care in 16 states and is highly concentrated in California with 32 acute facilities in operation across the state.

Dignity Health understands that DCHS is engaged in a process to identify a preferred “counterparty” that meets a number of established objectives, chief among them the continuation and improvement of health care services for the communities served by DCHS. Dignity Health is interested in acquiring the assets of SFMC to continue SFMC’s mission of providing compassionate and high quality healthcare in the Southeast Los Angeles community. Our organizations share a common vision and culture that will serve as a strong platform for the proposed partnership. To that end, Dignity Health is committed to the following:

- 1. Commitment and Ability to Meet All Transaction Objectives:** Dignity Health is committed to meeting all of the transaction objectives as outlined by DCHS and provides this Indication of Interest addressing each of these objectives for review and comment by the leadership of DCHS and SFMC.
- 2. Ability to Position SFMC for Population Health Management and Other Aspects Of Health Care Reform:** In this Indication of Interest, Dignity Health outlines examples of population health management models that the organization has implemented. Dignity Health would work with SFMC’s leadership and physicians to evaluate the best collaborative model(s) to pursue in the geography. Further, SFMC and its affiliated physicians would be invited to participate in Dignity Health’s Southern California Integrated Care Network, a clinical integration organization established in 2011 with active chapters in the Ventura and Inland Empire service areas.
- 3. Acceptability to Key Stakeholders:** Dignity Health is willing to discuss any aspect of its Indication of Interest with DCHS, SFMC and its Sponsors, and is open to modifying the proposal based on the dialogue with these key stakeholders.
- 4. Commitment to Improve Patient Care and Access in the Service Area:** Dignity Health would commit to maintain an acute facility with emergency and obstetrics services to assure access to key services for the communities served by SFMC, and would implement its care management, performance improvement, patient experience and other initiatives to enhance the quality of patient care delivered at SFMC.
- 5. Successful History of Operating Healthcare Facilities/Systems in California:** Since its founding as Catholic Healthcare West in 1986, Dignity Health has been and continues to be a significant provider of hospital and other health care services, and is currently the largest hospital provider in the State of California.
- 6. Demonstrated Ability to Consummate a Transaction in California:** Dignity Health has consummated numerous transactions within and outside of the State of California, and has a keen understanding of the effort involved in doing so.

Dignity Health seeks to work collaboratively with the leadership of DCHS and SFMC to best meet their stated objectives and welcomes ongoing dialogue around all parts of the proposal.

Dignity Health will need to conduct substantial additional due diligence prior to completing a transaction. As such, this Indication of Interest includes a high level list of those categories of information, data, documents, and inspections, surveys or review that will be required in connection with our review.

Dignity Health’s Executive Leadership fully supports this Indication of Interest; however, any transaction will also be subject to the approval of Dignity Health’s Board of Directors as well as federal and state regulatory approvals.

1. Description of Potential Acquirer

Overview of Dignity Health

Dignity Health is a California nonprofit public benefit corporation headquartered in San Francisco. Today, Dignity Health is the fifth largest health care system in the nation providing care in 21 states. Dignity Health provides integrated, patient-centered care to more than five million people annually. Our 10,000 affiliated physicians and 56,000 employees deliver excellent, compassionate care through a network of nearly 40 acute care hospitals and more than 250 ancillary care sites, including joint ventures and wholly owned ambulatory surgery centers, imaging centers, urgent care centers, national occupational medicine services, retail clinics, and home care agencies.

Dignity Health's Governance and Leadership Structure

In the evolving healthcare environment, success requires the development of networks and partnerships with a broad variety of organizations, both for profit and not for profit, and Catholic and secular. To best position our organization to thrive, Dignity Health completed a corporate reorganization in 2012 that maintained our Catholic legacy, while providing greater flexibility to enter into partnerships with secular organizations, like SFMC. Our organization changed its name from Catholic Healthcare West to Dignity Health, and converted to a non-Catholic parent organization to own and provide governance to both our Catholic and secular hospitals. The governance board decreased from 22 members to 11, creating a more nimble decision making body. The reorganization enables Dignity Health to more effectively pursue a growth strategy with a variety of different partners and partnership structures.

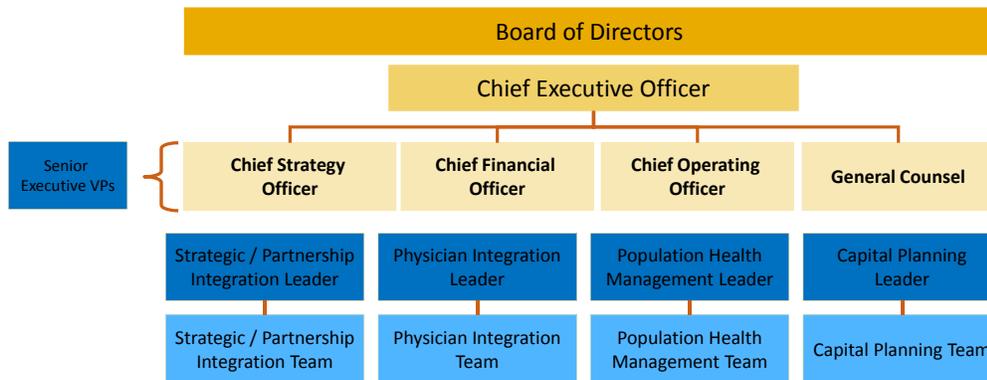
Post reorganization, Dignity Health's Board of Directors (the "Board") is comprised of leaders, as well as the President of Dignity Health, and community members from among the sponsors of our Catholic hospitals, who are independent directors without any other formal relationship to Dignity Health or its affiliates. Dignity Health's Board members are selected based on competencies and are leaders in their respective fields of expertise.

While the Board has delegated certain operational issues to management, the Board is responsible for approving major decisions affecting Dignity Health's health care ministry, such as long-range strategic plans, the allocation of capital, joint ventures and major acquisitions, mergers, and affiliations.

The Dignity Health Board has established separate Hospital Community Boards for the Hospitals and Service Areas where it operates general acute care facilities. The Hospital Community Boards are delegated certain local oversight responsibilities for quality of care and medical staff matters, and also serve as advisory bodies to the Dignity Health Board with respect to strategic business planning for local facilities, local operational issues, and facility level implementation of community benefit programs.

The Executive Leadership Team ("ELT") is charged by the Board of Directors to provide leadership and organizational management in the areas of operations, mission integration, finance and support services, as well as leadership in the strategic direction of the organization.

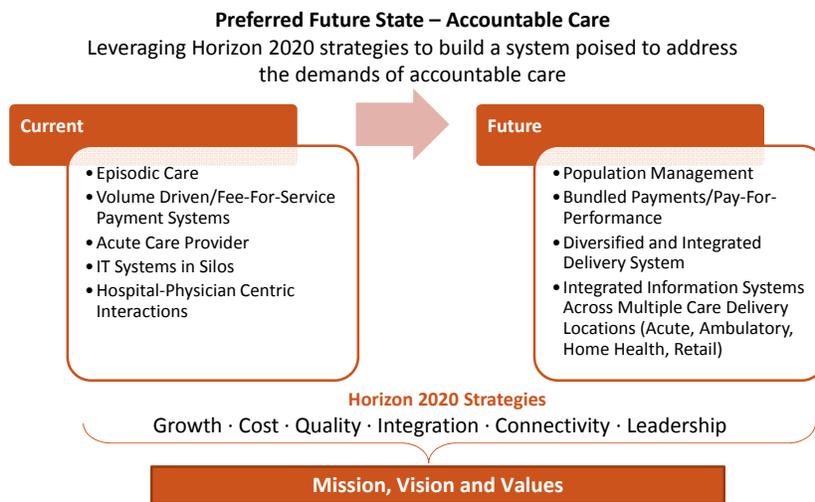
In addition to the expertise of the ELT, Dignity Health has dedicated functional area teams, including physician integration, population health management, capital planning and strategy, structured to best address the opportunities and challenges of the post-reform healthcare landscape.



Dignity Health's Strategic Focus

Horizon 2020 is Dignity Health's integrated strategic, operational, and financial plan—a road-map that will help the organization fulfill its mission over the next ten years— and serves as a framework for service area planning. Dignity Health has positioned the organization through Horizon 2020 to proactively prepare for its strategic future and incorporate its view of the potential impact of health reform.

Dignity Health has developed a range of business models to enable each of its service areas to operationalize the potential opportunities and address future challenges proposed by healthcare reform. Dignity Health anticipates these models will address new payor systems, take full advantage of the new opportunities for greater collaboration with aligned physicians, and build upon Dignity Health's current quality capabilities toward clinical integration, accountable care and population health.



Recognizing the needs of the emerging success model in healthcare, Dignity Health has developed core areas of strategic focus. These areas include quality, cost management, growth, integration, connectivity and leadership. Dignity Health's core areas of strategic focus stem from its Vision Statement and assist Dignity Health in realizing the 10-year goals set forth in Horizon 2020 presented below:

- Deliver the right care at the right place, cost, and time for every patient
- Become America's best health system at which to work and practice

- Become the healthcare system most valued nationally as a leader, partner, and successful model of reform
- Grow presence outside of the acute care model, including ambulatory and post-acute, physician integration and population health management capabilities, among others
- Focus selectively on diversifying the current acute care footprint by expanding into new geographic locations, as well as investing in key existing service areas

Dignity Health is focused on providing significant value through enhanced skill and scale and the sharing of best practices. In particular, some of the commitments and characteristics that differentiate Dignity Health are as follows:

- Commitment to the Communities Served: Dignity Health is committed to improving the overall health of communities it serves through specialized programs and provides significant community benefit through a variety of channels.
- Focus on Local Care Model: Dignity Health is focused on helping hospitals with all aspects of providing sustainable, quality care to its local community.
- Foundation for Growth: Dignity Health is willing to evaluate additional local partnerships towards improving sustainability.
- Partnership Experience: Dignity Health has established and maintained innovative relationships with others that prove its organizational commitment to partnership.
- Enhanced Cost Efficiencies through Scale: As demonstrated in industry studies, greater scale can provide significant operating leverage to lower costs in areas including supply chain, insurance, and back office support. In addition, Dignity Health has a focused LEAN philosophy.
- Employee Engagement: Dignity Health’s leadership and employee development programs attract and retain quality employees and management; peer group interaction and specialty forums enhance idea generation and cross-pollination throughout the organization.
- Brand Position: Dignity Health has embarked upon a major national effort to engage and inspire people to promote acts of human kindness within the health care industry and beyond. “**Hello Humankindness**” is a strategy for returning humanity to health care, and to the world at large. Through this work we are seeking to have a distinct, culturally relevant expression of our mission and values that transcends our current business model. Our promise is clear: to treat our patients and each other with respect, kindness, and the dignity inherent in our name. We believe the “**Hello Humankindness**” strategy touches on what consumers most desire in a health care experience, and what our employees have told us they value most. To deliver on this promise means that Dignity Health can be more trusted, desired, profitable, and enduring.

Dignity Health’s Quality Focus

Dignity Health’s approach to quality and management of clinical performance activities to improve clinical outcomes falls along four dimensions: Patient safety, Quality (including evidence-based practices), clinical efficiency, and patient experience. As part of Dignity Health the proposed partnership would have the opportunity to leverage standardized processes, best practices, information systems, and monitoring tools to help drive continuous improvement in quality, safety and patient satisfaction. Examples of Dignity Health’s commitment to improving quality outcomes and patient satisfaction are detailed below.

- Annual establishment of evidence-based metrics using a variety of resources and references including the recommendations of professional societies, the National Hospital Quality Alliance Initiatives, and published literature from peer reviewed journals (incorporating summary of evidence utilizing the evidence reference tool ZYNX®).
- Establishment of facility specific goals, time targets and processes for achieving measurable targeted improvements in key areas, including medical management, and patient safety. Goals are both

department specific (e.g. OB and Emergency Department) and house-wide, and include National Patient Safety Goals, patient satisfaction, medication safety, employee safety, clinical quality such as CMS core measures, and palliative care.

- System-wide, diagnosis-specific initiatives to simultaneously improve quality and reduce cost by reducing variation in clinical practice, implementing evidence-based practice and focusing improvement on key cost drivers. Recent examples include sepsis and venous thrombosis.
- Continual assessment of lessons learned from top performing hospitals and ensures that best demonstrated practices are disseminated within the Dignity Health system regularly, including posting of detailed implementation standards on an internal best practices website.
- Engagement of each facility in a Quality and Care Management Monthly Operating Review (MOR) to assess the performance of each service area, addressing key national measures of the quality of care, HCAHPS measures, and other internal patient satisfaction measures.
- Use of measurementonists to assist in implementation and monitoring the implementation of best practices.
- Provision of video and audio teleconferences, as well as in-person education, with nationally renowned speakers to discuss emerging trends, quality improvement, clinical evidence, best practices and cost improvement, and provide training on improvement processes for best practices so they "stick."
- Performance of mock Joint Commission Surveys, CMS surveys, DPHS surveys and National Patient Safety audits internally to enhance quality results.
- Contracting for criteria and software to offer hospitals significant discounts on criteria, both in the areas of quality and utilization.
- Providing internal training for Medical Necessity Criteria and use of Dignity Health Case Management Call Center for assistance with off-hours review of medical necessity for admission.
- Working closely with medical staff leadership to endorse improvements by presenting to medical staff committee meetings, stressing the relationship between utilization and quality, impacting patient care, improving efficiency of physician time at hospitals and acknowledging physicians who champion improvements.
- Utilization of an on-line system (Avatar) for monitoring and benchmarking satisfaction results, which are updated on a weekly basis to ensure that improvements are distributed to all facilities.
- Use of Studer Group best practice tools to assist in patient satisfaction. Some examples include bedside report, daily rounding, use of white boards in each patient room, discharge phone calls, and the use of "AIDET" as a tool for communication with every patient in every interaction.
- Dignity Health's focus on patient centered care, including the development of patient family councils at each facility to assist the organization in identifying opportunities for improving patient and family satisfaction.

2. Assets to be Acquired

Through a Membership Substitution, Dignity Health would acquire SFMC and replace DCHS as the sole Member of SFMC. Dignity Health intends to continue SFMC as a Catholic Ministry.

3. Treatment of Medical Foundation

Dignity Health believes physician alignment and connectivity is a key element in developing a clinical integration network and aligning physicians. Through a range of physician alignment strategies, Dignity Health has built an existing physician network that is committed to supporting the SFMC operations.

Dignity Health’s first Clinical Integration network was established in Southern California in the Inland Empire Service Area in 2011. Since then, Dignity Health’s Ventura Service Area has joined the network with its own chapter and other physician leaders in the surrounding areas are developing interest in doing the same. While Dignity Health will not be acquiring the assets of the DCHS Medical Foundation, any physicians with specific ties to SFMC will be retained and integrated into the existing Dignity Health physician network.

4. Amount and Form of Consideration

Based solely on the financial information supplied to date, Dignity Health proposes that the consideration for the asset acquisition described in this Indication of Interest will be a proposed purchase price of all cash at \$200 million with the agreement that DCHS pays off all outstanding long-term debt – including the current portion of said debt – estimated at approximately \$84.1 million as of December 31, 2013; contributes the unfunded portion of the pension liability that is reported as \$83 million as of December 31, 2013. If direct funding for the pension liabilities is not achievable, then Dignity Health would request a credit against the cash consideration of an equivalent amount as noted above. These amounts are subject to further diligence and confirmation and will be adjusted to actual amounts as of the date of close. Dignity Health will keep all current assets and current liabilities, (excluding cash) as of date of close, and will compensate DCHS for any excess working capital which is estimated at \$41.1 million as of December 31, 2013 (excluding the intercompany due to SFMC) through our Membership Substitution.

As additional consideration, Dignity Health is prepared to enter into a Transition Services Agreement to support any pre or post closing services required to continue the uninterrupted operations of SFMC, including collection of outstanding accounts receivable or other business services.

We have arrived at this valuation through an assumed EBIDA performance projected for FY 14 of approximately \$40 million, inclusive of provider fee.

A key component of Dignity Health’s due diligence process for this transaction will be determining the annual recurring operating revenue and EBIDA generation as well as actual amounts of pension, post-retirement, other contingent and off-balance sheet liabilities in order to finalize the consideration offer.

5. Working Capital Assumption

Dignity Health will acquire SFMC’s net working capital, subject to due diligence. Net working capital is defined as: [current assets less (i) cash and short-term investments and (ii) due from related organizations] minus [current liabilities less (i) current portion of long term debt¹ and (ii) due to related organizations].

6. CBA Agreements and Non-Union Employee Retention

Dignity Health collaborates with the following labor union organizations currently:

SEIU UHW 28 facilities; 13,900 employees	CNA California 27 facilities; 11,000 RNs	AFSCME Sequoia 337 employees
SEIU 121 RN	CNA Las Vegas	SPFPA—St. John’s

¹ Assumed as a part of the overall interest bearing debt.

3 facilities; 1,500 RNs	3 facilities; 1,200 RNs	19 employees
SEIU 1107 3 facilities; 1,300 employees	Teamsters Sierra Nevada 403 employees	IOUE—Bay Area 45 employees

Dignity Health does not contemplate accepting the current DCHS bargaining agreements. Dignity Health is committed to bargaining in good faith regarding a collective bargaining agreement with respect to the represented employees at SFMC.

Dignity Health will offer employment to substantially all of SFMC’s employees with existing seniority and with salary and benefit levels that are reasonably comparable to the levels existing for SFMC’s employees immediately prior to the close, subject to a review during the due diligence process of the market comparability of SFMC’s existing salary, wage and benefit levels, an understanding of SFMC’s benefit plans, a productivity analysis, and a review of SFMC’s service line requirements.

More information is required to compare SFMC’s salaries, wages and benefits with Dignity Health’s salaries, wages and benefits; however, the goal would be to transition to Dignity health’s common salary, wage and benefits structure when feasible following the closing of a transaction.

7. Post-Retirement Obligations

As noted above, as a part of the consideration for the proposed transaction, Dignity Health will transfer funds to DCHS in an amount equal to the current unfunded liability for SFMC’s employees and retirees who participate in the DCHS Retirement Plan (currently estimated to be \$83 million), subject to review of the amount of the unfunded liability and the DCHS Retirement Plan as a part of the due diligence process associated with the proposed transaction. In exchange for the consideration described above, SFMC and Dignity Health will be relieved of any and all further liability or obligations under the DCHS Retirement Plan. Any then existing retirees receiving benefits under the DCHS Retirement Plan will continue to receive distributions of their vested benefits there from. As of the closing date of the proposed transaction, Dignity Health contemplates that SFMC’s employees will become participants in the Dignity Health Retirement Plan.

8. Treatment of Other Agreements

As a part of the transaction and subject to the completion of its due diligence review, Dignity Health will assume substantially all of SFMC’s contracts, agreements and leases related to its hospital operations and those assets to be acquired in the transaction.

9. Sources of Capital

This is anticipated as an all cash transaction.

10. Anticipated Operating Plan and Capital Commitments

SFMC will be funded for current and future capital needs based on Dignity Health's Capital Budgeting policies as currently applied to all Dignity Health facilities.

11. Community Service and Charity Care

In collaboration with community partners, Dignity Health is moving forward with deliberate strategies that will help bring about the realization of health reform's goals and through focused community benefit programming will be poised to empower people, ensure healthy and safe community environments, promote clinical and community preventive services, and eliminate health disparities. Dignity Health's community benefit and charity care commitment totaled \$907.7 million in fiscal year ended June 30, 2013.

12. Process and Timing

The consummation of the transaction will require the approval of Dignity Health's Board of Directors, which meets 5 times per calendar year, and, if necessary, will call a special meeting to obtain the approval of this transaction. Dignity Health will work with SFMC to obtain all required pre-closing governmental consents or approvals to the proposed transaction, the Hart-Scott-Rodino Act Premerger Notification Program by each completing and filing a "Notification and Report Form for Certain Mergers and Acquisitions" with the Federal Trade Commission and the required consent of the California Attorney General. Dignity Health will pay its costs associated with federal and state regulatory approvals. Dignity Health is committed to proceeding with a timely transition which includes working in good faith to:

- Negotiate and execute a definitive agreement.
- Commit to staffing the transaction with the appropriate internal and external resources
- Perform all required due diligence
- Complete the Hart-Scott-Rodino pre-merger notification process, if necessary, and the CMS and CDPH change of ownership processes. The transaction would close immediately upon receipt of all governmental regulatory approvals.
- Complete and file a Health Impact Report and an application for consent with, and receive the consent of, the California Attorney General to the transaction.

Dignity Health will close the transaction with DCHS and SFMC in a timely manner. After signing a non-binding letter of intent setting forth the principal terms and conditions of the transaction, Dignity Health proposes the following closing timeline:

- Simultaneous due diligence and negotiation of a definitive agreement (Up to 90 days)
- Consent, licensure and change of ownership, and other regulatory approvals (Up to 105 days following execution of definitive agreements)

13. Due Diligence

The key categories that Dignity Health would consider critical for additional due diligence are listed below. Shaded items indicate that some information has already been provided via the confidential information memorandum, although additional information on a more detailed basis in the areas would be required, and items in white either were not provided or require additional information in order for Dignity Health to finalize due diligence and a definitive agreement.

1.	General Information and Organization
2.	Planning and Marketing
3.	Corporate Records
4.	General Government and Regulatory Filings and Correspondence (excluding healthcare matters)
5.	Healthcare Matters (excluding those covered above)
6.	Clinical
7.	Material Agreements and Transactions
8.	Financial/Accounting
9.	Revenue Services
10.	Taxes (“Tax” refers to Income, Sales and Use, Real and Personal Property, Franchise (Net Worth), Gross Receipts)
11.	Treasury Services – Cash, Investments, Financings and Derivatives
12.	Litigation and Other Contingent Liabilities
13.	Insurance
14.	Employment and Benefit Matters
15.	Properties
16.	Information Technology
17.	Physician and Referral Relationships
18.	Hospital Outpatient Services, Clinics and Joint Ventures

A key component of Dignity Health’s due diligence process for this transaction will be determining the annual recurring operating revenue and EBIDA generation as well as actual amounts of pension, post-retirement, other contingent and off-balance sheet liabilities in order to finalize the consideration offer.

14. Specific Contingencies to Closure

See # 12 – Process and Timing.

15. Other Parties

None at this time.

16. Contact Information

The Executive Leadership Team is charged by the Board of Directors to provide leadership and organizational management in the areas of operations, mission integration, finance and support services, as well as leadership in the strategic direction of the organization.

The primary contacts for this partnership development are:

Name	Title	Phone	Email
Michael Blaszyk	Sr. EVP & Chief Financial Officer	415.438.5535	Michael.Blaszyk@dignityhealth.org
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