BEFORE THE INSURANCE DEPARTMENT
OF THE
COMMONWEALTH OF PENNSYLVANIA

Statement Regarding the Acquisition of Control of or Merger with
Domestic Insurers:

Highmark Inc.; First Priority Life Insurance Company; Inc.;
Gateway Health Plan, Inc.; Highmark Casualty Insurance Company;
Highmark Senior Resources Inc.; HM Casualty Insurance Company;
HM Health Insurance Company, d/b/a Highmark Health Insurance Company;
HM Life Insurance Company; HMO of Northeastern Pennsylvania, Inc.,
d/b/a First Priority Health; Inter-County Health Plan, Inc.;
Inter-County Hospitalization Plan, Inc.; Keystone Health Plan West, Inc.;
United Concordia Companies, Inc.; United Concordia Dental Plans of Pennsylvania, Inc ;
United Concordia Life and Health Insurance Company

By UPE, a Pennsylvania nonprofit corporation

SUPPLEMENTAL RESPONSE TO PID INFORMATION REQUEST 4.3.13.1
FROM THE
PENNSYLVANIA INSURANCE DEPARTMENT

REQUEST 4.3.13.1:

Discuss any changes in credit rating or outlook for Highmark, any Highmark Affiliate, WPAHS and/or WPAHS Affiliate related to the Transaction.

RESPONSE:

See attached.

West Penn Allegheny Health System
30 Isabella St., Suite 300
Pittsburgh, PA 15212

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Allegheny County Hospital Development Authority, Pennsylvania
West Penn Allegheny Health System; System

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WPAHS-000065

Allegheny County Hospital Development Authority, Pennsylvania
West Penn Allegheny Health System; System

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Allegheny Cnty Hosp Dev Auth, Pennsylvania		
West Penn Allegheny Hlth Sys, Pennsylvania		
Allegheny Cnty Hosp Dev Auth (West Penn Allegheny Health System)		
Long Term Rating	B+/Developing	Affirmed

Rationale

Standard & Poor's Ratings Services has affirmed its 'B+' long-term rating on $737 million series 2007A fixed-rate bonds issued by the Allegheny County Hospital Development Authority for West Penn Allegheny Health System (WPAHS). The outlook remains developing until the affiliation agreement with Highmark Inc. receives all necessary regulatory approvals, at which time we will likely change the outlook to positive.

Effective Nov. 1, 2011, WPAHS and Highmark Inc. (A/Stable) — the dominant insurer in the western Pennsylvania market -- signed an agreement to form a provider subsidiary anchored by WPAHS, which will operate, along with Highmark Inc., under a single-parent corporation. The agreement is subject to regulatory approvals with final approvals not likely until next year. Concurrent with the signing, Highmark transferred $100 million to WPAHS, which it will account for in fiscal year 2012 as a $50 million unrestricted payment and a $50 million unsecured loan. This is in addition to a $50 million unrestricted payment from Highmark received in fiscal year 2011. WPAHS will use the funds to support its operating losses, develop and expand clinical programs, and make necessary capital investments as it transitions to a new integrated delivery model with Highmark.

The 'B+' rating reflects our opinion of WPAHS':

- Deep speculative-grade financial profile stemming from years of management and operational turmoil and from significant competition in the greater Pittsburgh market from University of Pittsburgh Medical Center (UPMC);
- Substantial pension and debt obligations;
- Continuing revenue and volume declines;
- Losses from employed physicians; and
- Relatively weak demographic profile of WPAHS' service area.

Positive rating factors that support the current rating include WPAHS':

- Increased financial cushion provided by the transfer of $150 million to WPAHS from Highmark with further transfers anticipated in the future;
- Potential benefits from its newly formed relationship with Highmark, which could result in additional business to WPAHS and subsequently improve its financial profile; and
- Critical mass of inpatient admissions, which other local providers cannot easily accommodate, making WPAHS vital to the market as a whole.

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WPAHS-000066

Securing the series 2007A bonds is a mortgage and gross revenue pledge of the obligated group, which includes all but a few smaller subsidiaries in the system. If the affiliation agreement is signed, a new parent corporation will effectively assume control of WPAHS through reserve powers although the parent corporation will not assume WPAHS' debt or pension obligations. WPAHS is not a party to any swaps at this time and the majority of the system's debt is fixed rate. All references in this report to unrestricted cash and investments or unrestricted reserves exclude WPAHS' trustee-held series 2007A project funds, which totaled $27 million as of June 30, 2010. All 2011 figures are unaudited.

WPAHS includes four acute-care hospitals at five locations in and around Pittsburgh: Allegheny General Hospital (AGH) and The Western Pennsylvania Hospital (WPH), which are both in Pittsburgh; the Forbes Regional campus of WPH, which is a 318-bed general acute-care hospital in Monroeville to the east where UPMC is also constructing a new hospital expected to open in 2013; Alle-Kiski Medical Center, doing business as Allegheny Valley Hospital, which is a 250-bed acute-care hospital northeast of Pittsburgh in Natrona Heights; and Canonsburg General Hospital, which is a 104-bed acute-care hospital to the southwest of Pittsburgh in Canonsburg. Suburban General Hospital was closed to inpatients in August 2010. WPH's services are currently limited to burn, rehabilitation, obstetrics, and the nursery under the urban consolidation plan approved by prior management; however, Highmark and WPAHS plan to reopen the WPH emergency department and other essential services in 2012. With the expansion of AGH's inpatient capacity earlier this year to accommodate WPH patients, the system now has more capacity than it had one year ago, although its inpatient volumes are down compared with fiscal year 2010 results.

Outlook

The developing outlook reflects our opinion that the rating and outlook could either improve or deteriorate over the next 12 months.

A positive outlook is likely once the parties receive all approvals and Highmark and WPAHS consummate the affiliation agreement. A higher rating is possible, in our view, with both a signed definitive agreement and evidence that Highmark's strategies have resulted in improved finances and stabilized volume at WPAHS. Although Highmark's stated investment in WPAHS is limited to $475 million, Highmark has ample resources to develop non-hospital-based network strategies, which could translate into improved volume, revenue, and profits at WPAHS. More specifically, we could consider a higher rating if cash remains at fiscal year-end 2011 levels and debt service coverage reaches at least 2x.

Credit factors that could result in a downgrade or negative outlook include an inability to get the transaction approved by regulators, continued volume declines, or a failure to show steady improvement toward improved finances throughout fiscal year 2012. More specifically, WPAHS will need to meet its debt service coverage covenant (1.1x) and days' cash-on-hand covenant (35) for fiscal year 2012 or risk a downgrade.

Enterprise Profile:

Economic fundamentals

WPAHS operates in and around the city of Pittsburgh, which is in Allegheny County ('A+'). The area's population trends are weak with Allegheny County's 1.2 million residents and Pittsburgh's 308,000 residents both decreasing by about 5% over the past five years. Of the six counties comprising WPAHS' service area, there were population

declines in four from 2000 through 2010, including declines in the two most populous counties — Allegheny and Westmoreland. However, the population is aging and will likely demand more health care services. There is growth in Washington and Butler counties, as well as pockets of suburban growth where WPAHS is providing or has plans to provide enhanced outpatient and clinical services.

Market position and strategy

The western Pennsylvania market is highly consolidated with one dominant health care system (UPMC; 'A+') and one dominant insurance provider (Highmark), although WPAHS and UPMC Health Plan are also factors in the market. Highmark intends to grow its provider network, using WPAHS as an anchor; however, there are few independent inpatient providers in the greater Pittsburgh market. Therefore, most growth will likely be through outpatient and physician strategies. UPMC currently contracts with Highmark, but has stated that it will not renew that contract, which is set to expire in June 2012. We should know over the next few years how much business Highmark retains despite the potential absence of enrollee access to UPMC facilities and what strategies have been implemented by Highmark, WPAHS, UPMC, UPMC Health Plan, and other new insurers entering the Pittsburgh market.

WPAHS admitted 59,972 inpatients in 2011, which is down 15% from 2010 levels. While some of the decline is economy related, the volume losses also stem from the closure of WPH to certain services. WPAHS' efforts to capture WPH volume at AGH, where new medical and surgical units were opened one month late in February, were not successful, and management indicates that many of the patients went instead to UPMC. While other volume indicators did not decrease as much, births, emergency department visits, and surgeries were all lower in 2011 compared with 2010 results. Management is now focusing its efforts on reopening WPH to more services including an emergency department and a new chief medical officer is working with physicians to rebuild volume.

Management

There has been substantial leadership turnover over the past 10 years at WPAHS. As of the signing of the affiliation agreement with Highmark, WPAHS' daily operations are now managed by executives from a turnaround firm, including its CEO, chief operating officer, and chief financial officer positions. Interestingly, Highmark has also hired a former senior UPMC executive to head the new provider subsidiary and oversee network development. We expect that there will be further management changes as Highmark gets more involved in developing its provider network with WPAHS' operations at the core of that strategy.

If the parties receive approval of the affiliation agreement, there will also be changes in the WPAHS board structure. The parent corporation will retain all significant reserve powers including board and management appointments and the ability to approve budgets and capital expenditures. Similarly, the provider board will have significant reserve powers over WPAHS as well. While we plan to continue to rate Highmark and WPAHS separately, if the strategies are successful and WPAHS' financial and operating profile improves, the ratings of the two organizations will likely move much closer together.

Financial Profile:

Operations

WPAHS generated $1.5 billion of net patient service revenue, $1.6 billion of total revenue, and an operating loss of $48 million in 2011. The operating loss was worse than expected, despite $9 million net positive revenue from the Medicaid Modernization Act, and represents the fifth straight year of operating losses. While revenue had been

increasing through 2010, net patient service revenue dropped almost 4% in 2011 largely due to admissions lost from the urban consolidation plan. Net income of almost $10 million in 2011, excludes $27 million of restructuring expense, a $9.6 million gain from the sale of the dialysis business, and a $23.3 million gain from termination of a joint venture with United Healthcare, but includes the $50 million unrestricted payment from Highmark, which was transferred upon execution of the letter of intent. Including $7.5 million of additional debt issued in 2011 but excluding debt service from the $50 million loan from Highmark, we consider maximum annual debt service coverage adequate for the rating level at 1.8x and the debt burden moderate at less than 4%. WPAHS' payor mix is skewed toward Medicare and Medicaid, which accounted for 59% of gross and 47% of net patient service revenue, respectively, in 2011. Management is currently reviewing the 2012 budget in light of the new relationship with Highmark. In addition, a new team in the physician organization is focusing on WPAHS' employed physicians with a goal to reduce the losses substantially.

West Penn Allegheny Health System Financial Statistics

	—Fiscal year ended June 30—			
	2011*	2010	2009	2008
Income statement and cash flow				
Operating revenue ($000s)	1,572,750	1,630,209	1,613,520	1,513,600
Total expenses ($000s)	1,621,093	1,639,721	1,651,991	1,602,447
Operating income ($000s)	(48,343)	(9,512)	(38,471)	(88,847)
Operating margin (%)	(3.1)	(0.6)	(2.4)	(5.9)
Net nonoperating revenues ($000s)	58,109	25,321	19,103	31,067
Excess income ($000s)	9,766	15,809	(19,368)	(57,780)
Excess margin (%)	0.6	1.0	(1.2)	(3.7)
Change in net assets ($000s)	103,204	(114,212)	(132,932)	(101,179)
EBIDA/total revenue (%)	6.6	7.9	5.8	3.2
Cash flow/total liabilities (%)	5.2	6.3	4.1	0.8
Capital expenditures ($000s)	101,771	55,981	46,551	94,017
Debt				
Net available for debt service ($000s)	108,214	130,911	95,162	49,440
Maximum debt service ($000s)	60,345	60,345	60,345	60,345
Maximum debt service coverage (x)	1.8	2.2	1.6	0.8
Maximum debt service-to-total revenue (%)	3.7	3.6	3.7	3.9
Balance sheet				
Unrestricted cash and investments ($000s)	240,933	246,370	194,597	156,012
Restricted cash ($000s)	354,291	356,144	362,312	411,742
Unrestricted days' cash on hand	56	57	45	37
Unrestricted cash/debt (%)	30.4	30.8	23.9	18.9
Cushion ratio (x)	4.0	4.1	3.3	2.7
Net fixed assets ($000s)	369,218	318,837	406,696	426,629
Long-term debt ($000s)	792,492	800,087	813,187	825,766
Unrestricted fund balance ($000s)	(356,631)	(434,997)	(312,416)	(229,793)
Debt/capitalization (%)	181.8	219.1	162.4	138.6
Average age of plant (years)	13.4	10.1	15.7	16.3

*Unaudited results. EBIDA—Earnings before interest, depreciation, and amortization.

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WPAHS-000069

Balance sheet:

WPAHS' poor operating performance coupled with ample pension and capital needs have strained its balance sheet for years, although the $150 million cash infusion from Highmark does provide a limited financial cushion. At the end of fiscal year 2011, WPAHS' unrestricted cash and investments totaled $241 million (56 days' cash on hand) including the $50 million payment from Highmark, which it received before year-end and added about 12 days' cash on hand to WPAHS' balances. However, in our opinion, cash as a percent of debt remains extremely light at 30% of WPAHS' $792 million of outstanding long-term debt. Because of the operating losses and substantial pension funding needs, management has had to limit capital investments historically and the average age of plant is relatively high at more than 13 years at the end of 2011. Management has made progress toward pension funding with a $76 million contribution in fiscal year 2011, which brought plan assets to 70% of the projected benefit obligation, up from a low of 61% in 2009. WPAHS allocates its cash and investments conservatively with almost two-thirds invested in cash, cash equivalents, and fixed income. In our opinion, debt as a percent of capitalization remains high at greater than 100% as unrestricted net assets are negative. Management indicates that WPAHS has no future financing plans and the organization still has $27 million from 2007A bond proceeds, which it can spend on various capital needs. We do not expect any material increases in cash and investments during the outlook period.

Related Criteria And Research

USPF Criteria: Not-For-Profit Health Care, June 14, 2007

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FitchRatings

FITCH DOWNGRADES WEST PENN ALLEGHENY HEALTH SYSTEM (PA) BONDS TO 'B+' FROM 'BB-'; OUTLOOK EVOLVING

Fitch Ratings-New York-23 December 2011: As part of its ongoing surveillance effort Fitch Ratings has downgraded to 'B+' from 'BB-' the rating on approximately $757 million series 2007A health system revenue bonds issued by Allegheny County Hospital Development Authority for the benefit of West Penn Allegheny Health System (WPAHS).

The bonds are removed from Rating Watch Evolving and assigned an Evolving Rating Outlook, which indicates that the rating may be raised, lowered or affirmed.

SECURITY

Security is provided via a pledge of gross revenues and a mortgage on the system hospital facilities.

KEY RATING DRIVERS

SIGNIFICANT DETERIORATION IN OPERATING PERFORMANCE: The rating downgrade reflects the significant deterioration in operating performance in fiscal 2011 and first quarter of 2012. The decline in operating performance was primarily driven by a drop in volume and physician losses. Operating losses accelerated in the first quarter of fiscal 2012 with operating loss of $27 million, for a negative 7% operating margin compared to negative 4.8% operating margin for the 2011 fiscal year (unaudited) on operating loss of $75 million (includes $27 million of restructuring expenses and excludes $23 million of non-recurring revenues).

AFFILIATION AGREEMENT WITH HIGHMARK INC.: The Oct. 31, 2011 signing of an Affiliation Agreement (the agreement) with Highmark Inc. (Highmark), in which Highmark commits to provide a total of $475 million to WPAHS over a period of three years, is a positive development and, if fully executed, should be of significant benefit to both parties. The affiliation still requires regulatory approval, which may take 12 months or longer to obtain. The failure to execute the affiliation would likely result in downward pressure on the rating.

INTERIM MANAGEMENT IN PLACE: WPAHS engaged the services of a management company with turnaround experience - Alvarez and Marsall (A&M), and the CEO, CFO, and COO at WPAHS have been replaced with interim cadre provided by A&M. Allegheny General Hospital, the system's flagship, is also headed by an interim CEO. The interim management team is aggressively pursuing cost and revenue initiatives and is implementing plans to reopen West Penn Hospital's emergency department by March 1, 2012.

PHYSICIAN RECRUITMENT AND RETENTION KEY: Fitch sees the ability to retain and recruit physicians as central to the improvement in WPAHS's finances. A 15% decline in discharges in 2011 was to a large degree caused by loss of physicians as the system reorganized and consolidated several of its inpatient services among its urban hospitals.

MANAGEABLE DEBT LOAD: WPAHS has a conservative debt structure with all fixed-rate debt and maximum annual debt service (MADS) represented a manageable 3.5% of revenues. Debt service coverage by EBITDA was adequate at 1.6 times (x) in fiscal 2011; however, it dropped significantly to 0.2x through the three months ended Sept. 30, 2011 due to the continued deterioration in operations.

VERY THIN LIQUIDITY: Cash and unrestricted investments were at $242.9 million, equal to 58.4 days cash on hand (DCOH), 30.7% cash to debt and 4.4x cushion ratio at 2011 fiscal year end, but declined to $168.6 million at the end of the first quarter of 2012 ended Sept. 30, equating to 40.3 DCOH, 21% cash to debt and 3.1x cushion ratio.

WHAT COULD TRIGGER A RATING ACTION

A return to a Stable Outlook would be dependent on management's ability to stabilize and improve

core operating performance, which would enable the system to rebuild its balance sheet over time and generate sufficient cash flow for much needed capital funding.

Downward rating pressure would occur if there is a further deterioration in financial performance.

CREDIT PROFILE:

AFFILIATION WITH HIGHMARK
On Oct. 31, 2011 the health insurer Highmark Inc. (Highmark) signed an affiliation agreement with WPAHS. The agreement has been formally submitted to the Pennsylvania Department of Insurance for review. Management expects that review may take up to a year or longer. The terms of the Agreement include Highmark's commitment to fund $475 million over a period of three years, with $150 million in unrestricted payments or loans already received ($50 million of which was included in fiscal 2011).

In connection with the Agreement, on Oct.20, 2011, a new non-profit parent company, Ultimate Parent Entity (UPE), was established. UPE became the sole corporate member of a new nonprofit subsidiary, UPE Provider Sub (Provide Sub), which was also established on Oct. 20, 2011. Upon closing of the transaction, Provider Sub will become the sole member of WPAHS. The WPAHS obligated group will stay intact and none of its assets or liabilities are being assumed by Highmark in the proposed transaction.

The goal of the affiliation is to create an integrated health care system using WPAHS facilities and physicians as part of the network. Highmark will also independently pursue investing in expanding the network of outpatient facilities and creating linkages with physicians. The recent announcement that UPMC (rated 'AA-', Stable Outlook by Fitch), WPAHS' primary competitor in the service area, will be terminating its contract with Highmark, should help steer needed volumes to WPAHS facilities, which have been steadily losing market share. As one of the first steps following the affiliation, a decision was made to reopen the West Penn Hospital emergency department, which closed in December of 2010.

Fitch views the affiliation as a positive development, and essential given the acceleration of WPAHS's financial deterioration. The operating loss of $27 million for the first quarter of fiscal 2012 does not reflect the benefit of the $100 million in funding from Highmark which took place on Oct. 31, 2011, nor has the interim management team had sufficient time to produce any material improvement in operations.

The interim A&M management team is developing revised projections for fiscal 2012, which will be available in January 2012. Fitch will closely monitor performance and will assess the turnaround results on a semiannual basis. Failure to produce an improvement in operations in the next 12 months would be viewed negatively.

Headquartered in Pittsburgh, WPAHS is a large, integrated health system now operating five hospitals and other related entities that primarily serve Allegheny County and its five surrounding counties. WPAHS' flagship is the 661-licensed bed Allegheny General Hospital. Total revenues in fiscal 2011 were approximately $1.6 billion. Fiscal 2011 figures are from a draft audit. Disclosure to Fitch and to bondholders has been provided on a quarterly basis and consists of a management discussion and analysis, income statement, balance sheet, cash flow statement, and utilization statistics.

For more detail on WPAHS see Fitch's press releases 'Fitch Places West Penn Allegheny Health system (PA) on Rating Watch Evolving,' dated June 29, 2011 and 'Fitch Affirms West Penn Allegheny Health (PA) at 'BB-'; Maintains Negative Outlook,' dated Jan. 14, 2011, available on the Fitch website at 'www.fitchratings.com'.

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Additional information is available at 'www.fitchratings.com'.The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

Applicable Criteria and Related Research:
--'Revenue-Supported Rating Criteria', dated June 20, 2011.
--'Nonprofit Hospitals and Health Systems Rating Criteria', dated Aug. 12, 2011.

For information on Build America Bonds, visit www.fitchratings.com/BABs.

Applicable Criteria and Related Research:
Revenue-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=637130
Nonprofit Hospitals and Health Systems Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=648836

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MOODY'S INVESTORS SERVICE

Rating Update: MOODY'S DOWNGRADES WEST PENN ALLEGHENY HEALTH SYSTEM'S (PA) BOND RATING TO Caa1 FROM B2; OUTLOOK REMAINS NEGATIVE

Global Credit Research - 22 Nov 2011

ACTION AFFECTS $737 MILLION OF OUTSTANDING DEBT

ALLEGHENY COUNTY HOSPITAL DEVELOPMENT AUTHORITY, PA
Hospitals & Health Service Providers
PA

Opinion

NEW YORK, November 22, 2011 --Moody's Investors Service has downgraded the bond rating for West Penn Allegheny Health System (WPAHS) (PA) to Caa1 from B2, affecting $737 million of Series 2007 fixed rate bonds issued through the Allegheny County Hospital Development Authority. The outlook remains negative.

RATINGS RATIONALE

The Caa1 rating and downgrade reflect the severity of the financial status of the system and our belief that, without the financial support of Highmark (Baa2/stable), the system would have been forced to restructure earlier in the year, which without such support, may have resulted in a bond payment default as Moody's has seen in other similar circumstances. While a new affiliation agreement with Highmark has provided significant cash to WPAHS to remain viable, the affiliation may not close until 2013 and, therefore, we are only partly incorporating the benefit of the Highmark affiliation at this time. Without the affiliation agreement and financial support of Highmark, and in the event the agreement is terminated, the rating would be lower.

WPAHS reported a very large $75 million operating loss in fiscal year 2011 (excluding approximately $23 million in a non-recurring positive item included in operating revenue), driven by a significant 15% decline in discharges. Unrestricted cash at fiscal yearend 2011 was only $5 million below the prior fiscal yearend 2010 because of $85 million in several cash infusions; without these payments, cash would have declined by 37%. Continuing a history of management turnover, a new interim management team was recently engaged at WPAHS, but has not yet had time to fully develop revised financial projections. The system's overall strategy in the affiliation with Highmark has changed from one of downsizing to targeted expansion, which creates a high degree of uncertainty and execution and financial risks, although the magnitude of financial risk is difficult to assess at this time without revised financial projections.

CHALLENGES

*Uncertainty related to the viability of a new strategy to expand rather than downsize, given the very recent arrival of a new interim management team and absence of revised financial projections; risks relate to reversing the strategy to regain volumes and investing in recruiting physicians while reducing financial losses

*Very large operating loss in fiscal year 2011 of $75 million (excluding a large non-recurring positive item) and quarterly run rate of over $20 million in operating losses in the latter quarters; revenue declined 3.5% in 2011

*Significant decline in acute discharges of 15% in fiscal year 2011, largely due to the closure and downsizing of services at West Penn Hospital and inability to retain volumes within the system

*Weak unrestricted cash position of 55 days of cash on hand as of fiscal yearend June 30, 2011 (excluding trustee-held project funds), which represented a $5 million decline from fiscal yearend 2010; cash would have declined by $90 million (37%) without $85 million in one-time cash payments (including $50 million from a Highmark unrestricted payment); without further support from Highmark, we expect cash to continue to decline at a fairly rapid rate until operating losses are stemmed

*As of fiscal yearend 2011, underfunded status of pension plan was large at almost $200 million, even though decreasing from $300 million at fiscal yearend 2010; the system made large required pension payments in fiscal year 2011

*Heavy competition from UPMC Health System (Aa3/positive), which is the largest health system in the region and owns a large managed care plan, enabling UPMC to influence health plan membership and volumes

*High leverage relative to operating performance with 51% debt-to-operating revenues and peak debt service coverage under one time in fiscal year 2011 by Moody's calculation

*Challenging demographic service area with declining population trends in the primary service area and an aging patient base

STRENGTHS

*Affiliation agreement with Highmark, executed October 31, 2011, which provides significant financial and management support to the system; as of the execution date, the system received $150 million in unrestricted payments or loans from the insurer

*Favorable debt structure with all fixed rate debt and no interest rate derivatives

*System's prominence as the second largest healthcare system in Pittsburgh with almost 60,000 acute discharges

DETAILED CREDIT DISCUSSION

LEGAL SECURITY: Joint and several obligation of the Obligated Group with mortgage lien on certain real property, including the primary hospital facilities, and gross revenue pledge; debt service reserve fund present; limitations on additional indebtedness and withdrawal from obligated group permitted if a combination of certain coverage and financial ratio tests are met. Days cash on hand covenant liberal with definition including project funds.

INTEREST RATE DERIVATIVES: None

RECENT DEVELOPMENTS/RESULTS

WPAHS signed an affiliation agreement with Highmark on October 31, 2011. On October 20, 2011, a new nonprofit parent company, Ultimate Parent Entity (UPE), was established. UPE became the sole corporate member of a new nonprofit subsidiary, UPE Provider Sub (Provide Sub), which was also established on October 20, 2011. Upon closing of the transaction, Provider Sub will become the sole member of WPAHS. Closing of the transaction is subject to regulatory approvals with a closing date targeted for May 1, 2013. Highmark has committed a total of $475 million in unrestricted payments or loans to WPAHS over a period starting June 2011 to April 2014.

The affiliation with Highmark is positive for WPAHS in the short-term because of the unrestricted payments provided to the healthcare system that we believe prevented a restructuring and possible bond payment default as discussed previously and continue to support the system to date. Over the longer-term, in addition to the unrestricted payments or loans provided to date, the affiliation provides the system with management support and oversight. However, we are only partly incorporating the benefit of the Highmark affiliation into our rating assessment at this time because of the extent and length of the approval process and the dependence WPAHS has on the closing of the affiliation to remain viable.

WPAHS has struggled with management turnover and inconsistent strategies. Very recently, a new interim management team at WPAHS has been retained for the turnaround but has not yet had time to fully develop financial projections for a new strategy.

With the affiliation agreement and new team, the system is reversing strategy to move toward targeted expansion of services, rather than downsizing, which was the prior strategy. Without further details, it is unclear whether this strategy will be successful. Significant challenges include redirecting the system, investing in facilities to accommodate expansion, and recruiting and retaining physicians to regain lost volumes, simultaneously with reducing operating losses. The system is beginning with a revitalization project for West Penn Hospital, which will occur in three phases over the next 18 months to transition the hospital back to a full service community hospital. Initiatives include reopening the emergency department in early 2012 and expanding the hospital's overall capacity to 300-350 private patient rooms. Phase two of the project for West Penn Hospital will involve enhancements to the hospital's women and infants program, including expansion and renovation of its labor and delivery facilities and neonate intensive care unit. Other existing services are expected to grow at this location. Additionally, the system will expand and enhance service capabilities at its other hospitals, including Forbes and Canonsburg, to more effectively compete.

Excluding $23 million of a non-recurring positive item and including restructuring costs, WPAHS had an operating loss of $75 million (-4.8%) in fiscal year 2011, compared with $30 million (-1.8% margin) in fiscal year 2010 (also excluding non-recurring items). Operating cash flow was a weak $23.3 million (1.5%) in fiscal year 2011, compared with $85.2 million (5.2%) in fiscal year 2010. Revenue declined by a large 3.5% in fiscal year 2011 due to significant volume declines. The revenue decline would have been greater without the benefit of revenue from the Medicaid Modernization Act and higher third-party settlements; excluding revenue from MMA, net patient revenue was down 5.8%. Additional MMA income and third-party settlements provided approximately $20 million in incremental income in 2011. A revised fiscal year 2012 budget is not yet available; the system's quarterly run rate in the latter part of fiscal year 2011 was an operating loss exceeding $20 million.

Acute discharges declined 15% in fiscal year 2011 (12% including an increase in observation cases) with quarterly declines from the prior year averaging 17% in the last three quarters. This decline followed a decline of 7.4% in acute discharges in fiscal year 2010. Outpatient surgeries declined 4.6% in fiscal year 2011. The decline is primarily due to the closure and downsizing of services and the inability to retain volumes within the system. Additionally, a weak economy contributed somewhat to softness in volumes in the region. Predicting volumes for the system over the next couple of years is difficult due to a number of factors including the ability to regain volumes with a new strategy and the impact on WPAHS of any disruption in Highmark's contract with UPMC. Since WPAHS's largest insurance contract is with Highmark, any loss in Highmark's market share if UPMC and Highmark do not renew their contract, will be disruptive to patient referrals starting in 2013, pending the outcome of contract discussions between UPMC and Highmark.

WPAHS's unrestricted cash (excluding project funds) declined modestly to $241 million (55 days cash on hand) at fiscal yearend 2011, compared with $246 million (57 days cash on hand) as of fiscal yearend 2010. The system received $85 million in one-time cash payments in fiscal year 2011, including a $50 million unrestricted payment from Highmark, a $25 million advance from a payer contract and $10 million from the sale of a dialysis center. In fiscal year 2011, the system used approximately $35 million in project funds for capital projects, which helped to maintain cash. Conversely, approximately $45 million in additional pension funding was made on fiscal year 2011. Based on the operating loss run rate in fiscal year 2011, cash will decline further without support from Highmark. Highmark did make a $100 million payment ($50 million unrestricted payment and $50 million loan) on October 31, 2011 as part of the affiliation agreement. The remainder of Highmark's $475 million commitment is expected to be funded between April 2012 and 2014. As of June 30, 2011, according to management, 77% of unrestricted cash and investments were invested in cash and 16% was invested in fixed income.

The system's pension obligation decreased as of fiscal yearend 2011, but remains large and future contributions are uncertain. As of fiscal yearend 2011, the underfunded status of the pension plan was almost $200 million, compared with almost $300 million at the prior fiscal yearend 2010. In fiscal year 2011 the system made about $45 million in contributions to the plan in excess of pension expense. Pension funding in fiscal year 2012 is expected to be close to pension expense, but will be dependent on asset values and other assumptions. WPAHS's pension fund currently has a relatively high allocation to equities, exposing future funding levels to market volatility.

Outlook

Maintenance of the negative outlook reflects the substantial execution and financial risks as the system reverses strategy, and a weak operating performance and cash position that leave little flexibility to absorb any unexpected challenges, such as continued volume declines.

WHAT COULD MAKE THE RATING GO UP

With a negative outlook, a rating upgrade in the near-term is not likely. Long-term, an upgrade would be considered with significant and sustained improvement in operating cash flow for several years, at least stability in volumes, significant growth in unrestricted cash, stability or

growth in medical staff and closing of the Highmark affiliation.

WHAT COULD MAKE THE RATING GO DOWN

Decline in unrestricted cash (excluding project funds), continued large operating losses and volume declines; failure to close the Highmark affiliation

KEY INDICATORS

Assumptions & Adjustments:

-Based on financial statements for West Penn Allegheny Health System

-First number reflects audit year ended June 30, 2010

-Second number reflects draft of audit year ended June 30, 2011 (audit has not yet been signed by auditors)

-Investment returns smoothed at 6% unless otherwise noted

-Non-recurring items adjusted: 2010 - $10.7 million related to a FICA refund added back to expenses; 2011 - $23 million gain from the termination of a joint venture with a payer removed from revenue; restructuring costs reclassified to operating expenses for all periods

*Inpatient acute discharges: 70,790; 69,972

*Total operating revenues: $1.63 billion; $1.57 billion

*Moody's-adjusted net revenue available for debt service: $101.1 million; $38.2 million

*Total debt outstanding: $813 million; $807 million

*Total comprehensive debt: $1,394 million; $1,278 million

*Maximum annual debt service (MADS): $53.9 million; $53.9 million (excluding balloon payments in 2015 and 2016 related to a financing for helicopters, which would increase MADS by approximately $5 million and $3 million, respectively, in these years)

*MADS coverage based on reported investment income: 1.9 times; 0.7 times

*Moody's-adjusted MADS coverage with normalized investment income: 1.9 times; 0.7 times

*Debt-to-cash flow: 13.5 times; over 1,000 times

*Days cash on hand (excluding project funds): 57 days; 55 days

*Cash-to-debt: 30%; 30%

*Cash-to-comprehensive debt: 18%; 19%

*Operating margin: -1.8%; -4.8%

*Operating cash flow margin: 5.2%; 1.5%

RATED DEBT

-Series 2007 fixed rate bonds ($737 million): Caa1

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The principal methodology used in this rating was Not-for-Profit Hospitals and Health Systems published in January 2008. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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