COMMUNITY HEALTH SYSTEMS INC
Form 10-Q
April 29, 2009

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended March 31, 2009

Commission file number 001-15925

COMMUNITY HEALTH SYSTEMS, INC.
(Exact name of registrant as specified in its charter)

Delaware	**13-3893191**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification Number)*
4000 Meridian Boulevard Franklin, Tennessee	**37067**
(Address of principal executive offices)	*(Zip Code)*

(Registrant s telephone number)
615-465-7000

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 þ No o

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

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. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicated by check mark whether the registrant is a shell company (as defined in Rule 126-2 of the Exchange Act). Yes o No þ

As of April 20, 2009, there were outstanding 92,479,260 shares of the Registrant s Common Stock, $.01 par value.

Community Health Systems, Inc.
Form 10-Q
For the Three Months Ended March 31, 2009

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PART I FINANCIAL INFORMATION
Item 1. ***Financial Statements***

COMMUNITY HEALTH SYSTEMS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)
(Unaudited)

	March 31, 2009	December 31, 2008
ASSETS		
Current assets		
Cash and cash equivalents	$ 532,132	$ 220,655
Patient accounts receivable, net of allowance for doubtful accounts of $1,194,834 and $1,102,900 at March 31, 2009 and December 31, 2008, respectively	1,643,919	1,613,959
Supplies	275,380	272,937
Prepaid income taxes		92,710
Deferred income taxes	91,875	91,875
Prepaid expenses and taxes	88,717	72,900
Other current assets	195,113	240,014
Total current assets	2,827,136	2,605,050
Property and equipment	7,191,931	7,082,930
Less accumulated depreciation and amortization	(1,323,638)	(1,213,871)
Property and equipment, net	5,868,293	5,869,059
Goodwill	4,173,408	4,166,091
Other assets, net	1,045,529	1,178,054
Total assets	$ 13,914,366	$ 13,818,254
LIABILITIES AND EQUITY		
Current liabilities		
Current maturities of long-term debt	$ 32,672	$ 29,462
Accounts payable	465,393	529,429
Current income taxes payable	17,668	
Deferred income taxes	6,740	6,740
Accrued interest	83,103	152,228

Accrued liabilities	797,432	816,111
Total current liabilities	1,403,008	1,533,970
Long-term debt	9,074,952	8,937,984
Deferred income taxes	461,098	460,793
Other long-term liabilities	890,237	887,445
Total liabilities	11,829,295	11,820,192
Redeemable noncontrolling interests in equity of consolidated subsidiaries	306,942	298,763
EQUITY		
Community Health Systems, Inc. stockholders equity		
Preferred stock, $.01 par value per share, 100,000,000 shares authorized; none issued		
Common stock, $.01 par value per share, 300,000,000 shares authorized; 93,454,809 shares issued and 92,479,260 shares outstanding at March 31, 2009, and 92,483,166 shares issued and 91,507,617 shares outstanding at December 31, 2008	934	925
Additional paid-in capital	1,153,498	1,151,119
Treasury stock, at cost, 975,549 shares at March 31, 2009 and December 31, 2008	(6,678)	(6,678)
Accumulated other comprehensive loss	(283,475)	(295,575)
Retained earnings	835,164	776,249
Total Community Health Systems, Inc. stockholders equity	1,699,443	1,626,040
Noncontrolling interests in equity of consolidated subsidiaries	78,686	73,259
Total equity	1,778,129	1,699,299
Total liabilities and equity	$ 13,914,366	$ 13,818,254

See accompanying notes to the condensed consolidated financial statements.

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COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except share and per share data)
(Unaudited)

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
Net operating revenues	$ 2,892,390	$ 2,688,924
Operating costs and expenses:		
Salaries and benefits	1,164,144	1,076,301
Provision for bad debts	335,451	289,702
Supplies	402,454	380,676
Other operating expenses	539,724	518,966
Rent	59,943	58,663
Depreciation and amortization	135,532	121,270
Total operating costs and expenses	2,637,248	2,445,578
Income from operations	255,142	243,346
Interest expense, net	163,810	164,527
(Gain) loss from early extinguishment of debt	(2,412)	1,328
Equity in earnings of unconsolidated affiliates	(12,919)	(12,884)
Income from continuing operations before income taxes	106,663	90,375
Provision for income taxes	35,532	31,256
Income from continuing operations	71,131	59,119
Discontinued operations, net of taxes:		
Income from operations of hospitals sold and hospitals held for sale	2,175	
(Loss) gain on sale of hospitals, net	(405)	9,617
Income from discontinued operations	1,770	9,617
Net income	72,901	68,736
Less: Net income attributable to noncontrolling interests	13,986	8,609
Net income attributable to Community Health Systems, Inc.	$ 58,915	$ 60,127
Income from continuing operations attributable to Community Health Systems, Inc. common stockholders per share:		
Basic	$ 0.63	$ 0.53
Diluted	$ 0.63	$ 0.52

Discontinued operations attributable to Community Health Systems, Inc. common stockholders per share:				
Basic	$	0.02	$	0.11
Diluted	$	0.02	$	0.11
Net income attributable to Community Health Systems, Inc. common stockholders per share:				
Basic	$	0.65	$	0.64
Diluted	$	0.65	$	0.63
Weighted-average number of shares outstanding:				
Basic		90,604,767		94,107,532
Diluted		90,885,140		95,006,721

See accompanying notes to the condensed consolidated financial statements.

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COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
Cash flows from operating activities		
Net income attributable to Community Health Systems, Inc.	$ 58,915	$ 60,127
Adjustments to reconcile net income attributable to Community Health Systems, Inc. to net cash provided by operating activities:		
Depreciation and amortization	135,894	122,478
Net income attributable to noncontrolling interests	13,986	8,609
Stock-based compensation expense	12,286	13,246
(Gain) loss on sale of hospitals and partnership interest, net	405	(12,885)
Excess tax benefits relating to stock-based compensation		947
(Gain) loss on early extinguishment of debt	(2,412)	1,328
Other non-cash expenses, net	(4,489)	1,442
Changes in operating assets and liabilities, net of effects of acquisitions and divestitures:		
Patient accounts receivable	(18,013)	(100,057)
Supplies, prepaid expenses and other current assets	(7,592)	(26,584)
Accounts payable, accrued liabilities and income taxes	68,170	(81,965)
Other	2,277	68,447
Net cash provided by operating activities	259,427	55,133
Cash flows from investing activities		
Acquisitions of facilities and other related equipment	(17,053)	(1,705)
Purchases of property and equipment	(136,021)	(141,693)
Proceeds from disposition of hospitals and other ancillary operations	89,909	365,680
Proceeds from sale of property and equipment	326	13,717
Increase in other non-operating assets	(36,344)	(98,182)
Net cash (used in) provided by investing activities	(99,183)	137,817
Cash flows from financing activities		
Proceeds from exercise of stock options		94
Excess tax benefits relating to stock-based compensation		(947)
Deferred financing costs	(57)	(2,232)
Proceeds from noncontrolling investors in joint ventures	21,922	12,881
Redemption of noncontrolling investments in joint ventures	(167)	
Distributions to noncontrolling investors in joint ventures	(6,595)	(7,524)
Borrowings under credit agreement	200,000	25,000
Repayments of long-term indebtedness	(63,870)	(188,743)

Net cash provided by (used in) financing activities	151,233	(161,471)
Net change in cash and cash equivalents	311,477	31,479
Cash and cash equivalents at beginning of period	220,655	132,874
Cash and cash equivalents at end of period	$ 532,132	$ 164,353

See accompanying notes to the condensed consolidated financial statements.

COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. BASIS OF PRESENTATION

The unaudited condensed consolidated financial statements of Community Health Systems, Inc. and its subsidiaries (the Company) as of March 31, 2009 and December 31, 2008 and for the three-month periods ended March 31, 2009 and March 31, 2008, have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). In the opinion of management, such information contains all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the results for such periods. All intercompany transactions and balances have been eliminated. The results of operations for the three months ended March 31, 2009, are not necessarily indicative of the results to be expected for the full fiscal year ending December 31, 2009. Certain information and disclosures normally included in the notes to consolidated financial statements have been condensed or omitted as permitted by the rules and regulations of the Securities and Exchange Commission (SEC). The Company believes the disclosures are adequate to make the information presented not misleading. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2008, contained in the Company s Annual Report on Form 10-K.

On January 1, 2009, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 160, Noncontrolling Interests in Consolidated Financial Statements an Amendment of ARB No. 51 (SFAS No. 160), which addresses the accounting and reporting framework for noncontrolling ownership interests in consolidated subsidiaries of the parent. SFAS No. 160 also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent company and the interests of the noncontrolling owners. These disclosure requirements require that minority interests be renamed noncontrolling interests and that noncontrolling ownership interests be presented separately within equity in the condensed consolidated financial statements. Revenues, expenses and income from continuing operations from less-than-wholly-owned subsidiaries are presented on the condensed consolidated statements of income at the consolidated amounts, with a consolidated net income measure that presents separately the amounts attributable to both the controlling and noncontrolling interests for all periods presented. Noncontrolling ownership interests that are redeemable or may become redeemable at a fixed or determinable price at the option of the holder or upon the occurrence of an event outside of the control of the company continue to be presented in mezzanine equity in accordance with Emerging Issues Task Force Topic D-98, Classification and Measurement of Redeemable Securities. SFAS No. 160 requires retrospective adoption of the presentation and disclosure requirements for all periods presented. Therefore, the condensed consolidated financial statements as of December 31, 2008 and for the three months ended March 31, 2008 reflect the provisions of SFAS No. 160 as if it was effective for those periods. Other than these changes in financial statement presentation, the adoption of SFAS No. 160 did not have a material impact on the condensed consolidated financial statements.

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

2. ACCOUNTING FOR STOCK-BASED COMPENSATION

Stock-based compensation awards are granted under the Community Health Systems, Inc. Amended and Restated 2000 Stock Option and Award Plan (the 2000 Plan). The 2000 Plan allows for the grant of incentive stock options intended to qualify under Section 422 of the Internal Revenue Code, as well as stock options which do not so qualify, stock appreciation rights, restricted stock, performance units and performance shares, phantom stock awards and share awards. Persons eligible to receive grants under the 2000 Plan include the Company s directors, officers, employees and consultants. To date, all options granted under the 2000 Plan have been nonqualified

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COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

stock options for tax purposes. Generally, vesting of these granted options occurs in one-third increments on each of the first three anniversaries of the award date. Options granted prior to 2005 have a 10 year contractual term, options granted in 2005 through 2007 have an eight year contractual term and options granted in 2008 and 2009 have a 10 year contractual term. The exercise price of all options granted under the 2000 Plan is equal to the fair value of the Company s common stock on the option grant date. As of March 31, 2009, 571,750 shares of unissued common stock remain reserved for future grants under the 2000 Plan.

The following table reflects the impact of total compensation expense related to stock-based equity plans under SFAS No. 123(R), on the reported operating results for the respective periods (in thousands, except per share data):

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
Effect on income from continuing operations before income taxes	$ (12,286)	$ (13,246)
Effect on net income	$ (7,464)	$ (8,047)
Effect on net income attributable to Community Health Systems, Inc. common stockholders per share-diluted	$ (0.08)	$ (0.08)

At March 31, 2009, $70.6 million of unrecognized stock-based compensation expense is expected to be recognized over a weighted-average period of 23.9 months. Of that amount, $23.2 million relates to outstanding unvested stock options expected to be recognized over a weighted-average period of 22.2 months and $47.4 million relates to outstanding unvested restricted stock and phantom shares expected to be recognized over a weighted-average period of 24.7 months.

The fair value of stock options was estimated using the Black Scholes option pricing model with the following weighted-average assumptions during the three months ended March 31, 2009 and 2008:

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
Expected volatility	40.1%	24.1%
Expected dividends	0	0
Expected term	4 years	4 years
Risk-free interest rate	1.63%	2.57%

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

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

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

COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Options outstanding and exercisable under the 2000 Plan as of March 31, 2009, and changes during the three months then ended were as follows (in thousands, except share and per share data):

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in Years)	Aggregate Intrinsic Value as of March 31, 2009
Outstanding at December 31, 2008	8,764,084	$ 30.97		
Granted	1,160,000	18.18		
Exercised				
Forfeited and cancelled	(63,165)	31.78		
Outstanding at March 31, 2009	9,860,919	$ 29.45	5.7 years	$ 660
Exercisable at March 31, 2009	6,072,813	$ 28.73	4.9 years	$ 646

The weighted-average grant date fair value of stock options granted during the three months ended March 31, 2009 and 2008, was $6.06 and $7.55, respectively. The aggregate intrinsic value (the number of in-the-money stock options multiplied by the difference between the Company s closing stock price on the last trading day of the reporting period ($15.34) and the exercise price of the respective stock options) in the table above represents the amount that would have been received by the option holders had all option holders exercised their options on March 31, 2009. This amount changes based on the market value of the Company s common stock. No stock options were exercised during the three months ended March 31, 2009. The aggregate intrinsic value of options exercised during the three months ended March 31, 2008 was $0.1 million. The aggregate intrinsic value of options vested and expected to vest approximates that of the outstanding options.

The Company has also awarded restricted stock under the 2000 Plan to its directors and employees. The restrictions on these shares generally lapse in one-third increments on each of the first three anniversaries of the award date, except for restricted stock granted on July 25, 2007, for which restrictions lapse equally on the first two anniversaries of the award date. Certain of the restricted stock awards granted to the Company s senior executives contain a performance objective that must be met in addition to any vesting requirements. If the performance objective is not attained, the awards will be forfeited in their entirety. Once the performance objective has been attained, restrictions will lapse in one-third increments on each of the first three anniversaries of the award date with the exception of the July 25, 2007 restricted stock awards, which have no additional time vesting restrictions once the performance restrictions are met. Notwithstanding the above-mentioned performance objectives and vesting requirements, the restrictions will lapse earlier in the event of death, disability, termination of employment of the holder of the restricted stock by the Company for any reason other than for cause, or change in control of the Company. Restricted stock awards subject to performance standards are not considered outstanding for purposes of determining earnings per share until the performance objectives have been satisfied.

Restricted stock outstanding under the 2000 Plan as of March 31, 2009, and changes during the three months then ended were as follows:

	Shares	Weighted-Average Grant Date Fair Value
Unvested at December 31, 2008	1,684,207	$ 35.57
Granted	1,156,000	18.18
Vested	(621,312)	35.68
Forfeited	(5,667)	33.52
Unvested at March 31, 2009	2,213,228	26.46

COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

On February 25, 2009, each of the Company s outside directors received a grant of shares of phantom stock under the 2000 Plan equal in value to $130,000 divided by the closing price of the Company s common stock on that date ($18.18), or 7,151 shares per director (a total of 42,906 shares of phantom stock). Vesting of these shares of phantom stock occurs in one-third increments on each of the first three anniversaries of the award date. As of March 31, 2009, there were 42,906 shares of phantom stock unvested at a weighted-average grant date fair value of $18.18. No shares of phantom stock were vested or canceled during the three months ended March 31, 2009. Pursuant to a March 24, 2009 amendment to the 2000 Plan, future grants of this type will be denominated as restricted stock unit awards.

Under the Director s Fee Deferral Plan, the Company s outside directors may elect to receive share equivalent units in lieu of cash for their director s fee. These units are held in the plan until the director electing to receive the share equivalent units retires or otherwise terminates his/her directorship with the Company. Share equivalent units are converted to shares of common stock of the Company at the time of distribution. The following table represents the amount of directors fees which were deferred and the equivalent units into which they converted for each of the respective periods (in thousands, except units):

	Three Months Ended March 31,	
	2009	**2008**
Directors fees earned and deferred into plan	$ 20	$ 41
Equivalent units	1,303.781	1,217.605

At March 31, 2009, there was a total of 18,122.783 units deferred in the plan with an aggregate fair value of $0.3 million, based on the closing market price of the Company s common stock on the last trading day of the reporting period of $15.34.

3. COST OF REVENUE

The majority of the Company s operating costs and expenses are cost of revenue items. Operating costs that could be classified as general and administrative by the Company would include the Company s corporate office costs at the Company s Franklin, Tennessee offices, which were $39.2 million and $38.1 million for the three months ended March 31, 2009 and 2008, respectively. Included in these amounts is stock-based compensation expense of $12.3 million and $13.2 million for the three months ended March 31, 2009 and 2008, respectively.

4. USE OF ESTIMATES

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

5. ACQUISITIONS AND DIVESTITURES

In December 2007, the Financial Accounting Standards Board (the FASB) issued SFAS No. 141(R), Business Combinations (SFAS No. 141(R)). SFAS No. 141(R) replaces SFAS No. 141 and addresses the recognition and accounting for identifiable assets acquired, liabilities assumed, and noncontrolling interests in business combinations. This standard will require more assets and liabilities to be recorded at fair value and will require expense recognition (rather than capitalization) of certain pre-acquisition costs. This standard also will require any adjustments to acquired deferred tax assets and liabilities occurring after the related allocation period to be made through earnings. Furthermore, this standard requires this treatment of acquired deferred tax assets and liabilities be applied to acquisitions occurring prior to the effective date of this standard. SFAS No. 141(R) is effective for fiscal years beginning after December 15, 2008 and is required to be adopted prospectively. SFAS No. 141(R) was adopted by the Company on January 1, 2009. Approximately $1.0 million of acquisition

COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

costs related to prospective acquisitions were expensed during the quarter ended March 31, 2009 from the adoption of SFAS No. 141(R). The impact of SFAS No. 141(R) on the Company s consolidated results of operations or consolidated financial position in future periods will be largely dependent on the number of acquisitions pursued by the Company; however, it is not anticipated at this time that such impact will be material.

Triad Acquisition

On July 25, 2007, the Company completed its acquisition of Triad Hospitals, Inc. (Triad). Triad owned and operated 50 hospitals with 49 hospitals located in 17 states in non-urban and middle market communities and one hospital located in the Republic of Ireland. As of March 31, 2009, eight of the hospitals acquired from Triad had been sold and one hospital acquired from Triad remained classified as held for sale. As a result of its acquisition of Triad, the Company also provides management and consulting services on a contract basis to independent hospitals, through its subsidiary, Quorum Health Resources, LLC. The Company acquired Triad for approximately $6.857 billion, including the assumption of $1.686 billion of existing indebtedness.

In connection with the consummation of the acquisition of Triad, the Company s wholly-owned subsidiary CHS/Community Health Systems, Inc. (CHS) obtained $7.215 billion of senior secured financing under a new credit facility (the Credit Facility) and issued $3.021 billion aggregate principal amount of 8.875% senior notes due 2015 (the Notes). The Company used the net proceeds of $3.000 billion from the Notes offering and the net proceeds of $6.065 billion of term loans under the Credit Facility to acquire the outstanding shares of Triad, to refinance certain of Triad s indebtedness and the Company s indebtedness, to complete certain related transactions, to pay certain costs and expenses of the transactions and for general corporate uses. This Credit Facility also provides an additional $750 million revolving credit facility and had a $400 million delayed draw term loan facility for future acquisitions, working capital and general corporate purposes. As of December 31, 2007, the $400 million delayed draw term loan was reduced to $300 million at the request of the Company. As of December 31, 2008, $100 million of the delayed draw term loan had been drawn by the Company, reducing the delayed draw term loan availability to $200 million at that date. In January 2009, the Company drew down the remaining $200 million of the delayed draw term loan.

The total cost of the Triad acquisition has been allocated to the assets acquired and liabilities assumed based upon their respective fair values in accordance with SFAS No. 141. The purchase price represented a premium over the fair value of the net tangible and identifiable intangible assets acquired for reasons such as:

- strategically, Triad had operations in five states in which the Company previously had no operations;
- the combined company has smaller concentrations of credit risk through greater geographic diversification;
- many support functions will be centralized; and
- duplicate corporate functions will be eliminated.

The allocation process required the analysis of acquired fixed assets, contracts, contractual commitments, and legal contingencies to identify and record the fair value of all assets acquired and liabilities assumed. The Company completed the allocation of the total cost of the Triad acquisition in the third quarter of 2008 and has made a final analysis and adjustment as of December 31, 2008 to deferred tax accounts based on the final cost allocation, resulting in approximately $2.781 billion of goodwill being recorded with respect to the Triad acquisition.

Other Acquisitions

Effective February 1, 2009, one or more subsidiaries of the Company completed the acquisition of Siloam Springs Memorial Hospital (74 licensed beds), located in Siloam Springs, Arkansas, from the City of Siloam Springs. The total consideration for this hospital consisted of approximately $1.1 million of assumed liabilities. As required by a lease agreement entered into as part of this acquisition, a subsidiary of the Company deposited $1.6 million of cash in an escrow account and agreed to build a replacement facility at this location, with

COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

construction required to commence by February 2011 and be completed by February 2013. If the construction of the replacement facility is not completed within the agreed-upon time frame, the escrow balance will be remitted to the City of Siloam Springs.

Effective November 14, 2008, one or more subsidiaries of the Company acquired from Willamette Community Health Solutions all of its joint venture interest in MWMC Holdings, LLC, which indirectly owns a controlling interest in and operates McKenzie-Willamette Medical Center of Springfield, Oregon. This acquisition resulted from a put right held by Willamette Community Health Solutions in connection with the 2003 transaction establishing the joint venture. The purchase price for this noncontrolling interest was $22.7 million in cash. Physicians affiliated with Oregon Healthcare Resources, Inc. will continue to own a noncontrolling interest in the hospital, with the balance owned by these subsidiaries of the Company.

Effective October 1, 2008, one or more subsidiaries of the Company completed the acquisition of Deaconess Medical Center (388 licensed beds) and Valley Hospital and Medical Center (123 licensed beds) both located in Spokane, Washington, from Empire Health Services. The total consideration for these two hospitals was approximately $185.2 million, of which $149.2 million was paid in cash and $36.0 million was assumed in liabilities. Based upon the Company s preliminary purchase price allocation relating to this acquisition as of March 31, 2009, no goodwill has been recorded. The acquisition transaction was accounted for using the purchase method of accounting. This preliminary allocation of purchase price has been determined by the Company based upon available information and is subject to settling amounts related to purchased working capital and final appraisals of tangible and intangible assets. Adjustments to the purchase price allocation are not expected to be material.

Effective June 30, 2008, one or more subsidiaries of the Company acquired the remaining 35% equity interest in Affinity Health Systems, LLC which indirectly owns and operates Trinity Medical Center (560 licensed beds) in Birmingham, Alabama, from Baptist Health Systems, Inc. of Birmingham, Alabama (Baptist), giving these subsidiaries 100% ownership of that facility. The purchase price for this noncontrolling interest was $51.5 million in cash and the cancellation of a promissory note issued by Baptist to Affinity Health Systems, LLC in the original principal amount of $32.8 million.

Discontinued Operations

Effective March 31, 2009, the Company, through its subsidiaries Triad-Denton Hospital LLC and Triad-Denton Hospital LP, completed the settlement of pending litigation which resulted in the sale of its ownership interest in a partnership, which owned and operated Presbyterian Hospital of Denton (255 licensed beds) in Denton, Texas, to Texas Health Resources for $103.0 million in cash. Also included as part of the settlement, these subsidiaries of the Company transferred certain hospital related assets.

Effective March 1, 2008, one or more subsidiaries of the Company sold Woodland Medical Center (100 licensed beds) located in Cullman, Alabama; Parkway Medical Center (108 licensed beds) located in Decatur, Alabama; Hartselle Medical Center (150 licensed beds) located in Hartselle, Alabama; Jacksonville Medical Center (89 licensed beds) located in Jacksonville, Alabama; National Park Medical Center (166 licensed beds) located in Hot Springs, Arkansas; St. Mary s Regional Medical Center (170 licensed beds) located in Russellville, Arkansas; Mineral Area Regional Medical Center (135 licensed beds) located in Farmington, Missouri; Willamette Valley Medical Center (80 licensed beds) located in McMinnville, Oregon; and White County Community Hospital (60 licensed beds) located in

Sparta, Tennessee, to Capella Healthcare, Inc., headquartered in Franklin, Tennessee. The proceeds from this sale were $315.0 million in cash.

Effective February 21, 2008, one or more subsidiaries of the Company sold THI Ireland Holdings Limited, a private limited company incorporated in the Republic of Ireland, which leased and managed the operations of Beacon Medical Center (122 licensed beds) located in Dublin, Ireland, to Beacon Medical Group Limited, headquartered in Dublin, Ireland. The proceeds from this sale were $1.5 million in cash.

COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Effective February 1, 2008, one or more subsidiaries of the Company sold Russell County Medical Center (78 licensed beds) located in Lebanon, Virginia to Mountain States Health Alliance, headquartered in Johnson City, Tennessee. The proceeds from this sale were $48.6 million in cash.

As of March 31, 2009, the Company had one hospital classified as held for sale.

In connection with the above actions and in accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the Company has classified the results of operations of the above mentioned hospitals as discontinued operations in the accompanying condensed consolidated statements of income.

Net operating revenues and income (loss) on discontinued operations for the respective periods are as follows (in thousands):

	Three Months Ended March 31,	
	2009	**2008**
Net operating revenues	$ 62,386	$ 145,263
Income from operations of hospitals sold and hospitals held for sale before income taxes	3,623	1,173
(Loss) gain on sale of hospitals, net	(644)	17,724
Income from discontinued operations, before taxes	2,979	18,897
Income tax expense	1,209	9,280
Income from discontinued operations, net of tax	$ 1,770	$ 9,617

Interest expense was allocated to discontinued operations based on estimated sale proceeds available for debt repayment.

The assets and liabilities of the hospital held for sale as of March 31, 2009 are included in the accompanying condensed consolidated balance sheet as follows: current assets of $15.7 million, included in other current assets; net property and equipment of $26.5 million and other long-term assets of $1.8 million, included in other assets; and current liabilities of $17.5 million, included in other accrued liabilities.

The assets and liabilities of the hospitals held for sale as of December 31, 2008 are included in the accompanying condensed consolidated balance sheet as follows: current assets of $40.9 million, included in other current assets; net property and equipment of $168.1 million and other long-term assets of $4.8 million, included in other assets; and current liabilities of $106.9 million, included in accrued liabilities.

6. INCOME TAXES

The Company adopted the provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48), on January 1, 2007. The total amount of unrecognized benefit that would affect the effective tax rate, if recognized, is approximately $14.9 million as of March 31, 2009. It is the Company s policy to recognize interest and penalties accrued related to unrecognized benefits in its condensed consolidated statements of income as income tax expense. During the three months ended March 31, 2009, the Company decreased liabilities by approximately $0.1 million and recorded $0.4 million in interest and penalties related to prior state income tax returns through its income tax provision from continuing operations, which are included in its FIN 48 liability at March 31, 2009. A total of approximately $2.1 million of interest and penalties is included in the amount of FIN 48 liability at March 31, 2009.

The Company believes that it is reasonably possible that approximately $4.1 million of its current unrecognized tax benefit may be recognized within the next twelve months as a result of a lapse of the statute of limitations and settlements with taxing authorities.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company, or one of its subsidiaries, files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. The Company has extended the federal statute of limitations for Triad for the tax periods ended December 31, 1999, December 31, 2000, April 30, 2001, June 30, 2001, December 31, 2001, December 31, 2002 and December 31, 2003. In December 2008, the Company was notified by the IRS of its intent to examine the federal tax return of Triad for the tax periods ended December 31, 2005 and ended July 25, 2007. The Company believes the results of this examination will not be material to its consolidated results of operations or consolidated financial position. With few exceptions, the Company is no longer subject to state income tax examinations for years prior to 2004.

Prior to the adoption of SFAS No. 160 on January 1, 2009, income from noncontrolling interests was deducted from earnings before arriving at income from continuing operations. With the adoption of SFAS No. 160, the income from noncontrolling interests has been reclassified below net income and therefore is no longer deducted in arriving at income from continuing operations. However, the provision for income taxes does not change because those subsidiaries with noncontrolling interests pay no income tax, but distribute taxable income to their respective investors. Accordingly, the Company will not pay tax on the income attributable to the noncontrolling interests. As a result of separately reporting income that is taxed to others, the Company s effective tax rate on continuing operations before income taxes, as reported on the face of the financial statements is 33.3% and 34.6% for the three months ended March 31, 2009 and 2008, respectively. However, the actual effective tax rate that is attributable to the Company s share of income from continuing operations before income taxes (income from continuing operations before income taxes, as presented on the face of the statement of income, less income from continuing operations attributable to noncontrolling interests of $14.1 million and $9.3 million for the three months ended March 31, 2009 and 2008, respectively) is 38.4% for the three months ended March 31, 2009, as compared to 38.5% for the three months ended March 31, 2008. While the adoption of SFAS No. 160 does change the location of the net income attributable to noncontrolling interests on the statement of income, it does not change the income tax from interests owned by the Company.

Cash paid for income taxes, net of refunds received, resulted in a net cash refund of $62.4 million and $2.8 million for the three months ended March 31, 2009 and 2008, respectively.

7. GOODWILL AND OTHER INTANGIBLE ASSETS

The changes in the carrying amount of goodwill for the three months ended March 31, 2009, are as follows (in thousands):

Balance as of December 31, 2008	$ 4,166,091
Goodwill acquired as part of acquisitions during 2009	3,887
Consideration adjustments and finalization of purchase price allocation adjustments for prior year s acquisitions	3,430
Balance as of March 31, 2009	$ 4,173,408

SFAS No. 142 requires that goodwill be allocated to each identified reporting unit, which is defined as an operating segment or one level below the operating segment (referred to as a component of the entity). Management has determined that the Company s operating segments meet the criteria to be classified as reporting units. At March 31, 2009, the hospital operations reporting unit, the home care agencies reporting unit, and the hospital management services reporting unit had $4.106 billion, $34.3 million and $33.3 million, respectively, of goodwill.

SFAS No. 142 requires goodwill to be evaluated for impairment at the same time every year and when an event occurs or circumstances change that, more likely than not, reduce the fair value of the reporting unit below its carrying value. SFAS No. 142 requires a two-step method for determining goodwill impairment. Step one is to compare the fair value of the reporting unit with the unit s carrying amount, including goodwill. If this test indicates the fair value is less than the carrying value, then step two is required to compare the implied fair value of the

COMMUNITY HEALTH SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

reporting unit s goodwill with the carrying value of the reporting unit s goodwill. The Company has selected September 30th as its annual testing date. The Company performed its annual goodwill evaluation as required by SFAS No. 142 as of September 30, 2008. No impairment was indicated by this evaluation.

The Company estimates the fair value of the related reporting units using both a discounted cash flow model, as well as an EBITDA multiple model. These models are both based on the Company s best estimate of future revenues and operating costs and are reconciled to the Company s consolidated market capitalization. The cash flow forecasts are adjusted by an appropriate discount rate based on the Company s weighted-average cost of capital. Historically, the Company s valuation models did not fully capture the fair value of the Company s business as a whole, as they did not consider the increased consideration a potential acquirer would be required to pay, in the form of a control premium, in order to gain sufficient ownership to set policies, direct operations and control management decisions. However, because the Company s models have indicated value significantly in excess of the carrying amount of assets in the Company s reporting units, the additional value from a control premium was not a determining factor in the outcome of step one of the Company s impairment assessment.

As indicated above, in addition to the annual impairment analysis, the Company is required to evaluate goodwill for impairment whenever an event occurs or circumstances change such that it is more likely than not that an impairment may exist. In light of this requirement, the Company has considered whether the decline in the Company s market capitalization between September 30, 2008 and March 31, 2009 has, more likely than not, resulted in the existence of an impairment and concluded that the decline in the Company s market capitalization did not, more likely than not, result in the existence of an impairment. In making this conclusion, the Company gave consideration to the valuation of hospitals in which it sold equity interests during periods subsequent to September 30, 2008, currently proposed hospital equity sale transactions, the proposed purchase price for the acquisition of a health care system which the Company anticipates closing in the quarter ending June 30, 2009, the volatility of the current equity markets, including the increase in our stock price since March 31, 2009 and the average stock price over the trailing three-month, six-month and one-year periods. The Company also considered the fact that the decline in its stock price has not been related to a decline in operating performance and that any near term credit tightening within the financial markets could be overcome by the Company through the substantial amount of cash flows being generated by the Company, as well as the borrowing capacity available through its existing credit facilities. The current turmoil in the financial markets and weakness in macroeconomic conditions globally continue to be challenging and the Company cannot be certain of the duration of these conditions and their potential impact on the Company s stock price performance. If a further decline in the Company s market capitalization and other factors results in the decline in the Company s fair value, it is reasonably likely that a goodwill impairment assessment prior to the next annual review, in the fourth quarter of 2009, would be necessary. If such an assessment is required, an impairment of goodwill may be recognized. A non-cash goodwill impairment charge would have the effect of decreasing the Company s earnings or increasing the Company s losses in the period the impairment is recognized. The amount of such effect on earnings and losses is dependent on the size of the impairment charge. Such a charge, however, would be a non-cash charge and therefore would not impact the Company s compliance with covenants contained in the Credit Facility.

The gross carrying amount of the Company s other intangible assets subject to amortization was $72.1 million at March 31, 2009 and $68.6 million at December 31, 2008, and the net carrying amount was $52.1 million at March 31, 2009 and $54.1 million at December 31, 2008. The carrying amount of the Company s other intangible assets not subject to amortization was $35.9 million and $35.2 million at March 31, 2009 and December 31, 2008, respectively. Other intangible assets are included in other assets, net on the Company s condensed consolidated balance sheets.

Substantially all of the Company s intangible assets are contract-based intangible assets related to operating licenses, management contracts, or non-compete agreements entered into in connection with prior acquisitions.

The weighted-average amortization period for the intangible assets subject to amortization is approximately ten years. There are no expected residual values related to these intangible assets. Amortization expense on these

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

intangible assets during the three months ended March 31, 2009 and 2008 was $3.3 million and $2.4 million, respectively. Amortization expense on intangible assets is estimated to be $8.7 million for the remainder of 2009, $10.3 million in 2010, $7.2 million in 2011, $4.0 million in 2012, $3.6 million in 2013, and $18.3 million in 2014 and thereafter.

8. EARNINGS PER SHARE

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

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
Numerator for basic and diluted earnings per share:		
Income from continuing operations, net of tax	$ 71,131	$ 59,119
Less: Income from continuing operations attributable to noncontrolling interests, net of taxes	(14,131)	(9,292)
Income from continuing operations attributable to Community Health Systems, Inc. common stockholders basic and diluted	$ 57,000	$ 49,827
Income on discontinued operations, net of tax	$ 1,770	$ 9,617
Plus: Loss from discontinued operations attributable to noncontrolling interests, net of taxes	145	683
Income on discontinued operations attributable to Community Health Systems, Inc. common stockholders basic and diluted	$ 1,915	$ 10,300
Denominator:		
Weighted-average number of shares outstanding basic	90,604,767	94,107,532
Effect of dilutive securities:		
Restricted stock awards	38,745	77,299
Employee options	241,628	821,890
Weighted-average number of shares outstanding diluted	90,885,140	95,006,721
Dilutive securities outstanding not included in the computation of earning per share because their effect is antidilutive:		
Employee options	9,524,719	4,361,131

9. STOCKHOLDERS EQUITY

Authorized capital shares of the Company include 400,000,000 shares of capital stock consisting of 300,000,000 shares of common stock and 100,000,000 shares of preferred stock. Each of the aforementioned classes of capital stock has a par value of $0.01 per share. Shares of preferred stock, none of which are outstanding as of March 31, 2009, may be issued in one or more series having such rights, preferences and other provisions as determined by the Board of Directors without approval by the holders of common stock.

On December 13, 2006, the Company commenced an open market repurchase program for up to 5,000,000 shares of the Company s common stock, not to exceed $200 million in repurchases. This program will conclude at the earlier of three years or when the maximum number of shares has been repurchased. During the year ended December 31, 2008, the Company repurchased 4,786,609 shares, which is the cumulative number of

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shares that have been repurchased under this program, at a weighted-average price of $18.80 per share. During the three months ended March 31, 2009, the Company did not repurchase any shares under this program.

The following schedule presents the reconciliation of the carrying amount of total equity, equity attributable to the Company, and equity attributable to the noncontrolling interests as if the provisions of SFAS No. 160 were adopted on the first day of the quarter ended March 31, 2009 (in thousands):

		Community Health Systems, Inc. Stockholders						
	Redeemable Noncontrolling Interests	**Common Stock**	**Additional Paid-in Capital**	**Treasury Stock**	**Accumulated Other Comprehensive Income (Loss)**	**Retained Earnings**	**Noncontrolling Interests**	**Total Stockholders Equity**
Balance, December 31, 2008 (as previously reported)	$	$ 925	$ 1,197,944	$ (6,678)	$ (295,575)	$ 776,249	$	$ 1,672,865
January 1, 2009 adjustment to noncontrolling interests from adoption of SFAS No. 160	298,763		(46,825)				73,259	26,434
Balance, December 31, 2008 (as adjusted)	298,763	925	1,151,119	(6,678)	(295,575)	776,249	73,259	1,699,299
Comprehensive income (loss):								
Net income	9,205					58,915		