

DAVITA INC.  
Form 10-Q  
May 03, 2018

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, 2018

Commission File Number: 1-14106

DAVITA INC.  
Delaware 51-0354549  
(State of incorporation) (I.R.S. Employer Identification No.)  
2000 16th Street  
Denver, CO 80202  
Telephone number (303) 405-2100

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of April 30, 2018, the number of shares of the Registrant's common stock outstanding was approximately 174.5 million shares.



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Note: Items 3, 4 and 5 of Part II are omitted because they are not applicable.

DAVITA INC.  
CONSOLIDATED STATEMENTS OF INCOME  
(unaudited)  
(dollars in thousands, except per share data)

	Three months ended	
	March 31,	
	2018	2017
Dialysis and related lab patient service revenues	\$2,591,074	\$2,422,786
Provision for uncollectible accounts	25,545	(107,058 )
Net dialysis and related lab patient service revenues	2,616,619	2,315,728
Other revenues	232,825	315,523
Total revenues	2,849,444	2,631,251
Operating expenses and charges:		
Patient care costs and other costs	2,035,585	1,852,045
General and administrative	266,529	262,895
Depreciation and amortization	142,799	132,884
Equity investment income	(155 )	(677 )
Provision for uncollectible accounts	(6,000 )	1,910
Investment and other asset impairments	—	15,168
Goodwill impairment charges	—	24,198
Gain on changes in ownership interests	—	(6,273 )
Gain on settlement, net	—	(526,827 )
Total operating expenses and charges	2,438,758	1,755,323
Operating income	410,686	875,928
Debt expense	(113,516 )	(104,397 )
Other income, net	4,582	3,986
Income from continuing operations before income taxes	301,752	775,517
Income tax expense	70,737	281,665
Net income from continuing operations	231,015	493,852
Net (loss) income from discontinued operations, net of tax	(5,786 )	6,433
Net income	225,229	500,285
Less: Net income attributable to noncontrolling interests	(46,543 )	(52,588 )
Net income attributable to DaVita Inc.	\$178,686	\$447,697
Earnings per share:		
Basic net income from continuing operations per share attributable to DaVita Inc.	\$1.07	\$2.29
Basic net income per share attributable to DaVita Inc.	\$1.00	\$2.33
Diluted net income from continuing operations per share attributable to DaVita Inc.	\$1.05	\$2.26
Diluted net income per share attributable to DaVita Inc.	\$0.98	\$2.29
Weighted average shares for earnings per share:		
Basic	178,957,865	192,376,735
Diluted	181,834,547	195,281,014
Amounts attributable to DaVita Inc.:		
Net income from continuing operations	\$191,015	\$440,905
Net (loss) income from discontinued operations	(12,329 )	6,792
Net income attributable to DaVita Inc.	\$178,686	\$447,697

See notes to condensed consolidated financial statements.



DAVITA INC.  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(unaudited)  
(dollars in thousands)

	Three months ended March 31,	
	2018	2017
Net income	\$225,229	\$500,285
Other comprehensive income, net of tax:		
Unrealized gains (losses) on interest rate cap agreements:		
Unrealized gains (losses) on interest rate cap agreements	1,050	(3,188 )
Reclassifications of net realized losses on interest rate cap agreements into net income	1,537	1,265
Unrealized gains on investments:		
Unrealized gains on investments	—	1,557
Reclassification of net investment realized gains into net income	—	(140 )
Unrealized gains on foreign currency translation:		
Foreign currency translation adjustments	19,881	13,261
Other comprehensive income	22,468	12,755
Total comprehensive income	247,697	513,040
Less: Comprehensive income attributable to noncontrolling interests	(46,543 )	(52,586 )
Comprehensive income attributable to DaVita Inc.	\$201,154	\$460,454

See notes to condensed consolidated financial statements.

## DAVITA INC.

## CONSOLIDATED BALANCE SHEETS

(unaudited)

(dollars in thousands, except per share data)

	March 31, 2018	December 31, 2017
<b>ASSETS</b>		
Cash and cash equivalents	\$ 358,874	\$ 508,234
Restricted cash and equivalents	88,744	10,686
Short-term investments	4,602	32,830
Accounts receivable, net	1,830,590	1,714,750
Inventories	125,555	181,799
Other receivables	415,914	372,919
Income tax receivable	18,660	49,440
Prepaid and other current assets	106,351	112,058
Current assets held for sale	5,724,265	5,761,642
Total current assets	8,673,555	8,744,358
Property and equipment, net of accumulated depreciation of \$3,230,717 and \$3,103,662	3,185,223	3,149,213
Intangible assets, net of accumulated amortization of \$360,828 and \$356,774	113,366	113,827
Equity method and other investments	245,564	245,534
Long-term investments	34,344	37,695
Other long-term assets	51,728	47,287
Goodwill	6,638,592	6,610,279
	\$ 18,942,372	\$ 18,948,193
<b>LIABILITIES AND EQUITY</b>		
Accounts payable	\$ 437,733	\$ 509,116
Other liabilities	544,846	552,662
Accrued compensation and benefits	526,183	616,116
Current portion of long-term debt	184,136	178,213
Current liabilities held for sale	1,254,625	1,185,070
Total current liabilities	2,947,523	3,041,177
Long-term debt	9,279,885	9,158,018
Other long-term liabilities	391,156	365,325
Deferred income taxes	507,226	486,247
Total liabilities	13,125,790	13,050,767
Commitments and contingencies:		
Noncontrolling interests subject to put provisions	1,034,501	1,011,360
Equity:		
Preferred stock (\$0.001 par value, 5,000,000 shares authorized; none issued)		
Common stock (\$0.001 par value, 450,000,000 shares authorized; 182,660,712 and 182,462,278 shares issued and 178,463,408 and 182,462,278 shares outstanding, respectively)	183	182
Additional paid-in capital	1,030,772	1,042,899
Retained earnings	3,820,767	3,633,713
Treasury stock (4,197,304 and zero shares, respectively)	(298,377)	—
Accumulated other comprehensive income	27,335	13,235
Total DaVita Inc. shareholders' equity	4,580,680	4,690,029
Noncontrolling interests not subject to put provisions	201,401	196,037
Total equity	4,782,081	4,886,066

\$18,942,372 \$18,948,193

See notes to condensed consolidated financial statements.

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DAVITA INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(unaudited)  
(dollars in thousands)

	Three months ended March 31,	
	2018	2017
Cash flows from operating activities:		
Net income	\$ 225,229	\$ 500,285
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	142,799	190,206
Impairment charges	—	39,366
Stock-based compensation expense	9,685	9,601
Deferred income taxes	43,617	20,091
Equity investment income, net	3,564	1,423
Other non-cash charges, net	9,959	9,464
Changes in operating assets and liabilities, net of effect of acquisitions and divestitures:		
Accounts receivable	(63,701 )	16,168
Inventories	57,621	(8,909 )
Other receivables and other current assets	(34,120 )	(84,511 )
Other long-term assets	2,054	(2,310 )
Accounts payable	(62,830 )	(26,214 )
Accrued compensation and benefits	(62,550 )	(62,825 )
Other current liabilities	49,379	(9,633 )
Income taxes	30,772	258,490
Other long-term liabilities	11,061	14,479
Net cash provided by operating activities	362,539	865,171
Cash flows from investing activities:		
Additions of property and equipment	(232,443 )	(214,535 )
Acquisitions	(16,582 )	(77,236 )
Proceeds from asset and business sales	18,535	46,612
Purchase of investments available for sale	(2,646 )	(2,358 )
Purchase of investments held-to-maturity	(3,586 )	(121,645 )
Proceeds from sale of investments available for sale	5,151	4,025
Proceeds from investments held-to-maturity	31,454	116,285
Purchase of equity investments	(2,476 )	(1,135 )
Distributions received on equity investments	2,465	—
Net cash used in investing activities	(200,128 )	(249,987 )

DAVITA INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS - (continued)  
(unaudited)  
(dollars in thousands)

	Three months ended March 31,	
	2018	2017
Cash flows from financing activities:		
Borrowings	13,306,898	12,803,015
Payments on long-term debt and other financing costs	(13,202,225)	(12,839,156)
Purchase of treasury stock	(290,377)	—
Stock award exercises and other share issuances, net	(1,185)	3,330
Distributions to noncontrolling interests	(45,467)	(43,316)
Contributions from noncontrolling interests	12,009	17,989
Purchases of noncontrolling interests	(2,200)	(799)
Net cash used in financing activities	(222,547)	(58,937)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	6,668	2,820
Net (decrease) increase in cash, cash equivalents and restricted cash	(53,468)	559,067
Less: Net increase in cash, cash equivalents and restricted cash from discontinued operations	17,834	24,493
Net (decrease) increase in cash, cash equivalents and restricted cash from continuing operations	(71,302)	534,574
Cash, cash equivalents and restricted cash of continuing operations at beginning of the year	518,920	683,463
Cash, cash equivalents and restricted cash of continuing operations at end of the period	\$447,618	\$1,218,037

See notes to condensed consolidated financial statements.

DAVITA INC.  
CONSOLIDATED STATEMENTS OF EQUITY  
(unaudited)  
(dollars and shares in thousands)

	Non-controlling interests subject to put provisions	DaVita Inc. Shareholders' Equity							Accumulated other comprehensive (loss) Total income	Non-controlling interests not subject to put provisions
		Common stock		Additional paid-in capital	Retained earnings	Treasury stock				
		Shares	Amount			Shares	Amount			
December 31, 2016	\$973,258	194,554	\$195	\$1,027,182	\$3,710,313	—	\$—	\$(89,643)	\$4,648,047	\$20
Comprehensive income:										
Net income	103,641				663,618				663,618	63,2
Other comprehensive income								102,878	102,878	(2
Stock purchase shares issued		360		22,131					22,131	
Stock unit shares issued		117		(101 )					(101 )	)
Stock-settled SAR shares issued		398		—					—	
Stock-settled stock-based compensation expense				34,981					34,981	
Changes in noncontrolling interest from:										
Distributions	(128,853 )									(82,
Contributions	52,911									21,6
Acquisitions and divestitures	43,799			(823 )					(823 )	(5,7
Partial purchases	(397 )			(2,752 )					(2,752 )	(2,2
Fair value remeasurements	(32,999 )			32,999					32,999	
Purchase of treasury stock						(12,967)	(810,949 )		(810,949 )	)
Retirement of treasury stock		(12,967 )	(13 )	(70,718 )	(740,218 )	12,967	810,949		—	
Balance at December 31, 2017	\$1,011,360	182,462	\$182	\$1,042,899	\$3,633,713	—	\$—	\$13,235	\$4,690,029	\$19

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Cumulative effect of change in accounting principle					8,368			(8,368 )	—	
Comprehensive income:										
Net income	24,107				178,686				178,686	22,4
Other comprehensive income								22,468	22,468	
Stock unit shares issued	4									
Stock-settled SAR shares issued	195	1		(4,887 )					(4,886 )	
Stock-settled stock-based compensation expense				9,682					9,682	
Changes in noncontrolling interest from:										
Distributions	(26,166 )									(19,
Contributions	9,508									2,50
Acquisitions and divestitures	688			76					76	(66
Partial purchases				(1,994 )					(1,994 )	(206
Fair value remeasurements	15,004			(15,004 )					(15,004 )	
Purchase of treasury stock							(4,197 )	(298,377 )	(298,377 )	
Balance at March 31, 2018	\$1,034,501	182,661	\$183	\$1,030,772	\$3,820,767	(4,197 )	\$(298,377)	\$27,335	\$4,580,680	\$20

See notes to condensed consolidated financial statements

DAVITA INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

(dollars and shares in thousands, except per share data)

Unless otherwise indicated in this Quarterly Report on Form 10-Q "the Company", "we", "us", "our" and similar terms refer to DaVita Inc. and its consolidated subsidiaries.

1. Condensed consolidated interim financial statements

The condensed consolidated interim financial statements included in this report are prepared by the Company without audit. In the opinion of management, all adjustments necessary for a fair presentation of the results of operations are reflected in these condensed consolidated interim financial statements. All significant intercompany accounts and transactions have been eliminated. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. The most significant estimates and assumptions underlying these financial statements and accompanying notes generally involve revenue recognition and accounts receivable, contingencies, impairments of goodwill and investments, accounting for income taxes, long-term variable compensation accruals, consolidation of variable interest entities and certain fair value estimates. The results of operations for the three months ended March 31, 2018 are not necessarily indicative of the operating results for the full year. The condensed consolidated interim financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017. Prior year balances and amounts have been reclassified to conform to the current year presentation. The Company has evaluated subsequent events through the date these condensed consolidated financial statements were issued and has included all necessary adjustments and disclosures.

2. Revenue recognition

On January 1, 2018, the Company adopted Financial Accounting Standards Board (FASB) Accounting Standards Codification Topic 606 Revenue from Contracts with Customers (Topic 606) using the cumulative effect method for those contracts that were not substantially completed as of January 1, 2018. Results for reporting periods beginning on and after January 1, 2018 are presented under Topic 606, while prior period amounts continue to be presented in accordance with the Company's historical accounting under Revenue Recognition (Topic 605).

The adoption of this new standard primarily changed the Company's presentation of revenues, provision for uncollectible accounts and allowance for doubtful accounts. Topic 606 requires revenue to be recognized based on the Company's estimate of the transaction price the Company expects to collect as a result of satisfying its performance obligations. Accordingly, for performance obligations satisfied after the adoption of Topic 606, the Company no longer separately presents a provision for uncollectible accounts on the consolidated income statement and no longer presents the related allowance for doubtful accounts on the consolidated balance sheet.

However, as a result of the Company's election to apply Topic 606 only to contracts not substantially completed as of January 1, 2018, the Company continues to maintain an allowance for doubtful accounts related to performance obligations satisfied prior to the adoption of Topic 606. Changes to this allowance for doubtful accounts, other than write-offs of uncollectible accounts, are recorded through the provision for uncollectible accounts on the consolidated income statement in accordance with Topic 605.

The Company's allowance for doubtful accounts related to performance obligations satisfied prior to the adoption of Topic 606 was \$162,516 and \$218,399 as of March 31, 2018 and December 31, 2017, respectively.

There are significant risks associated with estimating revenue, which generally take several years to resolve. These estimates are subject to ongoing insurance coverage changes, geographic coverage differences, differing interpretations of contract coverage and other payor issues, as well as patient issues including determining applicable primary and secondary coverage, changes in patient coverage and coordination of benefits. As these estimates are refined over time, both positive and negative adjustments to revenue are recognized in the current period. As a result of changes in these estimates, additional revenue was recognized during the three months ended March 31, 2018

associated with performance obligations satisfied in years prior to the adoption of Topic 606 of \$67,410, which includes a benefit of \$24,000 from electing to apply Topic 606 only to contracts not substantially completed as of January 1, 2018.

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DAVITA INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

The following table summarizes the Company's segment revenues by primary payor source:

	For the three months ended			March 31, 2017 <sup>(1)</sup>		
	March 31, 2018			March 31, 2017 <sup>(1)</sup>		
	U.S. dialysis and related lab services	Other - Ancillary services and strategic initiatives	Consolidated	U.S. dialysis and related lab services	Other - Ancillary services and strategic initiatives	Consolidated
Patient service revenues:						
Medicare and Medicare Advantage	\$1,485,192	\$—	\$1,485,192	\$1,272,595	\$—	\$1,272,595
Medicaid and Managed Medicaid	157,496	—	157,496	144,585	—	144,585
Other government	107,119	82,537	189,656	91,993	47,761	139,754
Commercial	782,979	19,718	802,697	756,710	13,883	770,593
Other revenues:						
Medicare and Medicare Advantage	—	142,758	142,758	—	225,203	225,203
Medicaid and Managed Medicaid	—	15,791	15,791	—	18,595	18,595
Commercial	—	40,420	40,420	—	25,207	25,207
Other <sup>(2)</sup>	5,114	38,941	44,055	5,311	47,576	52,887
Eliminations of intersegment revenues	(18,422 )	(10,199 )	(28,621 )	(11,799 )	(6,369 )	(18,168 )
Total	\$2,519,478	\$329,966	\$2,849,444	\$2,259,395	\$371,856	\$2,631,251

As noted above, prior period amounts have not been adjusted under the cumulative effect method. The Company's (1) dialysis and related lab services revenues for the three months ended March 31, 2017 has been presented net of the provision for uncollectible accounts of \$107,058 in this table to conform to the current period presentation.

(2) Other consists of management fees and revenue from the Company's ancillary services and strategic initiatives.

Dialysis and related lab patient service revenues

Dialysis and related lab services patient service revenues are recognized in the period services are provided. Revenues consist primarily of payments from Medicare, Medicaid and commercial health plans for dialysis and related lab services provided to patients. A usual and customary fee schedule is maintained for the Company's dialysis treatments and related lab patient services; however, actual collectible revenue is normally recognized at a discount from the fee schedule.

Revenues associated with Medicare and Medicaid programs are estimated based on: (a) the payment rates that are established by statute or regulation for the portion of payment rates paid by the government payor (e.g., 80% for Medicare patients) and (b) for the portion not paid by the primary government payor, estimates of the amounts ultimately collectible from other government programs paying secondary coverage (e.g., Medicaid secondary coverage), the patient's commercial health plan secondary coverage, or the patient. The Company's reimbursements from Medicare are subject to certain variations under Medicare's single bundled payment rate system, whereby reimbursements can be adjusted for certain patient characteristics and other factors. The Company's revenue recognition is estimated based on its judgment regarding its ability to collect, which depends upon its ability to effectively capture, document and bill for Medicare's base payment rate as well as these other variable factors. Under Medicare's bundled payment rate system, services covered by Medicare are subject to estimating risk, whereby reimbursements from Medicare can vary significantly depending upon certain patient characteristics and other variable factors. Even with the bundled payment rate system, Medicare payments for bad debt claims as established by

cost reports require evidence of collection efforts. As a result, billing and collection of Medicare bad debt claims can be delayed significantly and final payment is subject to audit.

Medicaid payments, when Medicaid coverage is secondary, can also be difficult to estimate. For many states, Medicaid payment terms and methods differ from Medicare, and may prevent accurate estimation of individual payment amounts prior to billing.



DAVITA INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

Revenues associated with commercial health plans are estimated based on contractual terms for the patients under healthcare plans with which the Company has formal agreements, non-contracted health plan coverage terms if known, estimated secondary collections, historical collection experience, historical trends of refunds and payor payment adjustments (retractions), inefficiencies in the Company's billing and collection processes that can result in denied claims for payments, and regulatory compliance matters.

Commercial revenue recognition also involves significant estimating risks. With many larger, commercial insurers the Company has several different contracts and payment arrangements, and these contracts often include only a subset of the Company's centers. It is often not possible to determine which contract, if any, should be applied prior to billing. In addition, for services provided by non-contracted centers, final collection may require specific negotiation of a payment amount, typically at a significant discount from the Company's usual and customary rates.

Other revenues

Other revenues consist of the revenues associated with the ancillary services and strategic initiatives, management and administrative support services that are provided to outpatient dialysis centers that the Company does not own or in which the Company owns a noncontrolling interest, and administrative and management support services to certain other non-dialysis joint ventures in which the Company owns a noncontrolling interest. Revenues associated with pharmacy services are estimated as prescriptions are filled and shipped to patients. Revenues associated with dialysis management services, disease management services, medical consulting services, clinical research programs, physician services, end stage renal disease (ESRD) seamless care organizations, and comprehensive care are estimated in the period services are provided. Revenues associated with direct primary care are estimated over the membership period.

3. Earnings per share

Basic earnings per share is calculated by dividing net income attributable to the Company, adjusted for any change in noncontrolling interests redemption rights in excess of fair value, by the weighted average number of common shares, net of shares held in escrow that under certain circumstances may be returned to the Company.

Diluted earnings per share includes the dilutive effect of outstanding stock-settled stock appreciation rights (SSARs) and unvested stock units (under the treasury stock method) as well as shares held in escrow that the Company expects will remain outstanding.

## DAVITA INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

The reconciliations of the numerators and denominators used to calculate basic and diluted earnings per share were as follows:

	Three months ended March 31,	
	2018	2017
Numerators:		
Net income from continuing operations attributable to DaVita Inc.	\$ 191,015	\$ 440,905
Net (loss) income from discontinued operations attributable to DaVita Inc.	(12,329 )	6,792
Net income attributable to DaVita Inc. for basic earnings per share calculation	\$ 178,686	\$ 447,697
Basic:		
Weighted average shares outstanding during the period	181,152	194,571
Contingently returnable shares held in escrow for the DaVita HealthCare Partners merger	(2,194 )	(2,194 )
Weighted average shares for basic earnings per share calculation	178,958	192,377
Basic net income from continuing operations per share attributable to DaVita Inc.		
	\$ 1.07	\$ 2.29
Basic net (loss) income from discontinued operations per share attributable to DaVita Inc.		
	(0.07 )	0.04
Basic net income per share attributable to DaVita Inc.		
	\$ 1.00	\$ 2.33
Diluted:		
Weighted average shares outstanding during the period	181,152	194,571
Assumed incremental shares from stock plans	683	710
Weighted average shares for diluted earnings per share calculation	181,835	195,281
Diluted net income from continuing operations per share attributable to DaVita Inc.		
	\$ 1.05	\$ 2.26
Diluted net (loss) income from discontinued operations per share attributable to DaVita Inc.		
	(0.07 )	0.03
Diluted net income per share attributable to DaVita Inc.		
	\$ 0.98	\$ 2.29
Anti-dilutive stock-settled awards excluded from calculation <sup>(1)</sup>		
	3,453	3,427

(1) Shares associated with stock-settled stock appreciation rights excluded from the diluted denominator calculation because they are antidilutive under the treasury stock method.

## 4. Restricted cash and equivalents

The Company had restricted cash and cash equivalents of \$88,744 and \$10,686 at March 31, 2018 and December 31, 2017, respectively. Approximately \$78,320 of the balance at March 31, 2018 represents restricted cash equivalents held in trust to satisfy insurer and state regulatory requirements related to the Company's self-insurance for professional and general liability and workers' compensation risks administered by wholly-owned captive insurance entities. Prior to the first quarter of 2018, these requirements were satisfied by a letter of credit rather than restricted cash held in trust. The remaining restricted cash and equivalents held at March 31, 2018 and December 31, 2017 primarily represent cash pledged to third parties in connection with two of the Company's ancillary and strategic initiatives businesses.

## 5. Short-term and long-term investments

Effective January 1, 2018, the Company adopted ASU No. 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The amendments in this ASU revise accounting related to (i) the classification and measurement of investments in equity securities and (ii) the presentation of certain fair value changes for financial liabilities at fair value. The Company also adopted ASU

2018-03 which provides related technical corrections and improvements. The principal effect of ASUs 2016-01 and 2018-03 on the Company's consolidated financial statements is that, prior to adoption of ASU 2016-01, changes in the fair values of investments in equity securities with readily determinable fair values or redemption values were recognized in other comprehensive income until realized, while under ASU 2016-01 all changes in the fair values of these equity securities are recognized in current earnings. The adoption of these ASUs did not have a material impact on these condensed consolidated financial statements.

DAVITA INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

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(dollars and shares in thousands, except per share data)

Effective January 1, 2018, the Company recognized a cumulative effect of change in accounting principle upon adoption of ASUs 2016-01 and 2018-03, in conjunction with ASU 2018-02, the effect of which was to decrease accumulated other comprehensive income, and to increase retained earnings, by \$5,662 in after-tax unrealized gains accumulated in other comprehensive income through December 31, 2017 from equity securities classified as available-for-sale investments prior to adoption of ASU 2016-01.

From January 1, 2018, equity securities that have readily determinable fair values or redemption values are recorded at estimated fair value with changes in their value recognized in current earnings. The Company classifies its debt securities as held-to-maturity and records them at amortized cost based on its intentions and strategy concerning those investments.

The Company classifies these debt and equity investments as "Short-term investments" or "Long-term investments" on its consolidated balance sheet, as applicable, based on the characteristics of the financial instrument or the Company's intentions or expectations for the investment.

The Company's investments in these short-term and long-term debt and equity investments consist of the following:

	March 31, 2018			December 31, 2017		
	Debt securities	Equity securities	Total	Debt securities	Equity securities	Total
Certificates of deposit and other time deposits	\$3,402	\$—	\$3,402	\$31,630	\$—	\$31,630
Investments in mutual funds and common stock	—	35,544	35,544	—	38,895	38,895
	\$3,402	\$35,544	\$38,946	\$31,630	\$38,895	\$70,525
Short-term investments	\$3,402	\$1,200	\$4,602	\$31,630	\$1,200	\$32,830
Long-term investments	—	34,344	34,344	—	37,695	37,695
	\$3,402	\$35,544	\$38,946	\$31,630	\$38,895	\$70,525

Debt securities: The Company's short-term debt investments are principally comprised of bank certificates of deposit with contractual maturities longer than three months but shorter than one year. These debt securities are accounted for as held to maturity and recorded at amortized cost, which approximates their fair values at March 31, 2018 and December 31, 2017.

Equity securities: The Company's equity investments in mutual funds and common stock are held within a trust to fund existing obligations associated with several of the Company's non-qualified deferred compensation plans. During the three months ended March 31, 2018, the Company recognized pre-tax net gains of \$86 in the income statement associated with changes in the fair value of these equity securities, comprised of pre-tax realized gains of \$3,746 and a net decrease in unrealized gains of \$3,660. During the three months ended March 31, 2017, the Company recognized pre-tax realized gains on the sale or redemption of equity securities of \$229, or \$140 after-tax, which was previously recorded in other comprehensive income.

#### 6. Equity method and other investments

Equity investments in nonconsolidated investees over which the Company maintains significant influence, but which do not have readily determinable fair values, are carried on the equity method.

As described in Note 5 to these condensed consolidated financial statements, effective January 1, 2018, the Company adopted ASU 2016-01 and related ASU 2018-03 concerning recognition and measurement of financial assets and financial liabilities. In adopting this new guidance, the Company has made an accounting policy election to adopt an adjusted cost method measurement alternative for investments in equity securities without readily determinable fair values.

Specifically, under this measurement alternative, unless elected otherwise for a particular investment, the Company initially records equity investments that qualify for the measurement alternative at cost but remeasures them to fair

value through earnings when there is an observable transaction involving the same or a similar investment with the same issuer or upon an impairment.

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## DAVITA INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

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(dollars and shares in thousands, except per share data)

The Company maintains equity method and minor adjusted cost method investments in the private securities of certain other healthcare and healthcare-related businesses. The Company classifies these investments as "Equity method and other investments" on its consolidated balance sheet.

Total equity method and other investments in nonconsolidated businesses were \$245,564 and \$245,534 at March 31, 2018 and December 31, 2017, respectively. During the three months ended March 31, 2018 and 2017, the Company recognized equity investment income of \$155 and \$677, respectively, from equity method investments in nonconsolidated businesses.

The Company's largest equity method investment is its ownership interest in DaVita Care Pte. Ltd. (the APAC JV), which was carried at \$160,535 and \$160,481 at March 31, 2018 and December 31, 2017, respectively. The Company recognized a non-cash other-than-temporary impairment on this investment of \$280,066 in the fourth quarter of 2017. As of March 31, 2018 and December 31, 2017, the Company holds a 60% voting interest and a 73.3% current economic interest in the APAC JV. Based on the governance structure and voting rights established for the APAC JV at its formation on August 1, 2016, certain key decisions affecting the joint venture's operations are not subject to the unilateral discretion of the Company, but rather are shared with the other noncontrolling investors. These other noncontrolling investors currently collectively hold a 40% voting interest and a 26.7% economic interest in the APAC JV, and their economic interests are expected to increase to match their voting interests in the joint venture as they make additional subscribed capital contributions through August 1, 2019.

The total carrying amount of equity investments carried under the adjusted cost method measurement alternative at March 31, 2018 was \$5,386. Through March 31, 2018, there have been no meaningful impairments or other downward or upward valuation adjustments recognized on these investments.

## 7. Goodwill

Changes in goodwill by reportable segment were as follows:

	U.S. dialysis and related lab services	Other-ancillary services and strategic initiatives	Consolidated total
Balance at January 1, 2017	\$ 5,691,587	\$ 323,788	\$ 6,015,375
Acquisitions	485,434	131,598	617,032
Divestitures	(32,260)	(126)	(32,386)
Goodwill impairment charges	—	(36,196)	(36,196)
Foreign currency and other adjustments	—	46,454	46,454
Balance at December 31, 2017	\$ 6,144,761	\$ 465,518	\$ 6,610,279
Acquisitions	2,137	13,905	16,042
Foreign currency and other adjustments	—	12,271	12,271
Balance at March 31, 2018	\$ 6,146,898	\$ 491,694	\$ 6,638,592

Balance at March 31, 2018:

Goodwill	\$ 6,146,898	\$ 562,214	\$ 6,709,112
Accumulated impairment charges	—	(70,520)	(70,520)
	\$ 6,146,898	\$ 491,694	\$ 6,638,592

The Company elected to early adopt ASU No. 2017-04, Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment, effective January 1, 2017. The amendments in this ASU simplify the test for goodwill impairment by eliminating the second step in the assessment. All goodwill impairment tests performed during 2017 and 2018 have been performed under this new guidance.

Each of the Company's operating segments described in Note 19 to these condensed consolidated financial statements represents an individual reporting unit for goodwill impairment testing purposes, except that each sovereign jurisdiction within the Company's international operating segments is considered a separate reporting unit.

DAVITA INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

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Within the U.S. dialysis and related lab services operating segment, the Company considers each of its dialysis centers to constitute an individual business for which discrete financial information is available. However, since these dialysis centers have similar operating and economic characteristics, and the allocation of resources and significant investment decisions concerning these businesses are highly centralized and the benefits broadly distributed, the Company has aggregated these centers and deemed them to constitute a single reporting unit.

The Company has applied a similar aggregation to the vascular access service centers in its vascular access reporting unit, to the physician practices in its physician services and direct primary care reporting units, and to the dialysis centers within each international reporting unit. For the Company's other operating segments, discrete business components below the operating segment level constitute individual reporting units.

During the three months ended March 31, 2018, the Company did not recognize any goodwill impairment charges.

During the three months ended March 31, 2017, the Company recognized a goodwill impairment charge of \$24,198 at the Company's vascular access reporting unit. This charge resulted primarily from changes in the Company's outlook as the Company's partners and operators continued to evaluate potential changes in operations, including termination of their management services agreements and center closures, as a result of recent changes in Medicare reimbursement. There is no goodwill remaining at the Company's vascular access reporting unit.

For the reporting units considered at risk as of December 31, 2017 listed in the table below, there have been no major changes in the business, prospects, or expected future results of these reporting units from their latest assessment date through March 31, 2018. Based on the most recent assessments, the Company determined that reductions in reimbursement rates, changes in actual or expected growth rates, or other significant adverse changes in expected future cash flows or valuation assumptions could result in goodwill impairment charges in the future for the following reporting units, which remain at risk of goodwill impairment as of March 31, 2018:

Reporting unit	Goodwill		Sensitivities		
	balance as of March 31, 2018	Carrying amount coverage <sup>(1)</sup>	Operating income <sup>(2)</sup>	Discount rate <sup>(3)</sup>	
Kidney Care Germany	\$337,619	13.7 %	(1.6)%	(11.1 )%	
Kidney Care Portugal	\$48,066	16.9 %	(1.9)%	(6.0 )%	
Kidney Care Poland	\$47,669	11.8 %	(1.9)%	(6.0 )%	

(1) Excess of estimated fair value of the reporting unit over its carrying amount as of the latest assessment date.

(2) Potential impact on estimated fair value of a sustained, long-term reduction of 3% in operating income as of the latest assessment date.

(3) Potential impact on estimated fair value of an increase in discount rates of 100 basis points as of the latest assessment date.

Except as described above, none of the Company's various other reporting units were considered at risk of significant goodwill impairment as of March 31, 2018. Since the dates of the Company's last annual goodwill impairment tests, there have been certain developments, events, changes in operating performance and other changes in key circumstances that have affected the Company's businesses. However, these changes did not cause management to believe it is more likely than not that the fair value of any of the Company's reporting units would be less than their respective carrying amounts as of March 31, 2018.

8. Income taxes



As of March 31, 2018, the Company's total liability for unrecognized tax benefits relating to tax positions that do not meet the more-likely-than-not threshold was \$33,880, all of which would impact the Company's effective tax rate if recognized. This balance represents an increase of \$1,104 from the December 31, 2017 balance of \$32,776. The Company recognizes accrued interest and penalties related to unrecognized tax benefits in its income tax expense. At March 31, 2018 and December 31, 2017, the Company had approximately \$3,971 and \$4,195, respectively, accrued for interest and penalties related to unrecognized tax benefits, net of federal tax benefits.

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The Company performed a provisional analysis of the Tax Cuts and Jobs Act of 2017 (2017 Tax Act) and recorded a reasonable estimate of its effect for the year ended December 31, 2017. The Company is in the process of completing its analysis with respect to the 2017 Tax Act and will record any adjustments to its estimate on or before December 22, 2018, with any adjustments to be recorded to income tax expense in the period when the adjustments are determined. As of March 31, 2018, the Company has not made any material adjustments to the December 31, 2017 estimates. The 2018 effective tax rate reduction is primarily due to the impact of the 2017 Tax Act which reduced the federal tax rate from 35% to 21%.

## 9. Long-term debt

Long-term debt was comprised of the following:

	March 31, 2018	December 31, 2017
Senior secured credit facilities:		
Term Loan A	\$750,000	\$775,000
Term Loan A-2	452,000	—
Term Loan B	3,368,750	3,377,500
Revolver	—	300,000
Senior notes	4,500,000	4,500,000
Acquisition obligations and other notes payable	151,167	150,512
Capital lease obligations	304,062	297,170
Total debt principal outstanding	9,525,979	9,400,182
Discount and deferred financing costs	(61,958 )	(63,951 )
	9,464,021	9,336,231
Less current portion	(184,136 )	(178,213 )
	\$9,279,885	\$9,158,018

Scheduled maturities of long-term debt at March 31, 2018 were as follows:

2018 (remainder of the year)	136,885
2019	1,206,668
2020	72,608
2021	3,307,539
2022	1,283,255
2023	32,340
Thereafter	3,486,684

On March 29, 2018, the Company entered into an Increase Joinder No. 1 (Increase Joinder Agreement) under its existing senior secured credit facilities. Pursuant to this Increase Joinder Agreement, the Company entered into an additional \$995,000 Term Loan A-2. The new Term Loan A-2 bears interest at LIBOR plus an interest rate margin of 1.00%. As of March 31, 2018, the Company has initially drawn \$452,000 of the Term Loan A-2, and the Company can draw up to an incremental \$543,000 on Term Loan A-2 through its maturity date in June 2019.

During the first three months of 2018, the Company made mandatory principal payments under its senior secured credit facilities totaling \$25,000 on Term Loan A and \$8,750 on Term Loan B.

As of March 31, 2018, the Company maintains several active and forward interest rate cap agreements that have the economic effect of capping the Company's maximum exposure to LIBOR variable interest rate changes on specific portions of the Company's floating rate debt, as described below. The cap agreements are designated as cash flow hedges and, as a result, changes in the fair values of these cap agreements are reported in other comprehensive

income. The amortization of the original cap premium is recognized as a component of debt expense on a straight-line basis over the terms of the cap agreements. The cap agreements do not contain credit-risk contingent features.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

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As of March 31, 2018, the Company maintains several currently effective interest rate cap agreements that were entered into in November 2014 with notional amounts totaling \$3,500,000. These cap agreements became effective September 30, 2016 and have the economic effect of capping the LIBOR variable component of the Company's interest rate at a maximum of 3.50% on an equivalent amount of the Company's debt. These cap agreements expire on June 30, 2018. As of March 31, 2018, these cap agreements had an immaterial fair value. During the three months ended March 31, 2018, the Company recognized debt expense of \$2,070 from these caps. During the three months ended March 31, 2018, the Company recorded an immaterial loss in other comprehensive income due to a decrease in unrealized fair value of these cap agreements.

As of March 31, 2018, the Company also maintains several forward interest rate cap agreements that were entered into in October 2015 with notional amounts totaling \$3,500,000. These forward cap agreements will become effective June 29, 2018 and will have the economic effect of capping the LIBOR variable component of the Company's interest rate at a maximum of 3.50% on an equivalent amount of its debt. These cap agreements expire on June 30, 2020. As of March 31, 2018, the total fair value of these cap agreements was an asset of approximately \$2,446. During the three months ended March 31, 2018, the Company recorded a gain of \$1,414 in other comprehensive income due to an increase in the unrealized fair value of these forward cap agreements.

The following table summarizes the Company's derivative instruments as of March 31, 2018 and December 31, 2017:

	March 31, 2018		December 31, 2017	
Derivatives designated as hedging instruments	Balance sheet location	Fair value	Balance sheet location	Fair value
Interest rate cap agreements	Other long-term assets	\$ 2,446	Other long-term assets	\$ 1,032

The following table summarizes the effects of the Company's interest rate cap agreements for the three months ended March 31, 2018 and 2017:

Derivatives designated as cash flow hedges	Amount of unrecognized gains (losses) in OCI on interest rate cap agreements		Location of losses reclassified from accumulated OCI into income	Amount of losses reclassified from accumulated OCI into income	
	Three months ended March 31,			Three months ended March 31,	
	2018	2017		2018	2017
Interest rate cap agreements	\$ 1,414	\$(5,217)	Debt expense	\$ 2,070	\$ 2,070
Tax (benefit) expense	(364)	2,029	Tax expense	(533)	(805)
Total	\$ 1,050	\$(3,188)		\$ 1,537	\$ 1,265

As of March 31, 2018, the Company's Term Loan B debt bears interest at LIBOR plus an interest rate margin of 2.75%. Term Loan B is subject to interest rate caps if LIBOR should rise above 3.50%. Term Loan A bears interest at LIBOR plus an interest rate margin of 2.00%. The capped portion of Term Loan A is \$131,250 if LIBOR should rise above 3.50%. In addition, the uncapped portion of Term Loan A, which is subject to the variability of LIBOR, is \$618,750. Term Loan A-2 is subject to the variability of LIBOR plus an interest rate margin of 1.00%. Interest rates on the Company's senior notes are fixed by their terms.

The Company's weighted average effective interest rate on the senior secured credit facilities at the end of the quarter was 4.67%, based on the current margins in effect of 2.00% for Term Loan A, 1.00% for Term Loan A-2, and 2.75% for Term Loan B, as of March 31, 2018.

The Company's overall weighted average effective interest rate during the quarter ended March 31, 2018 was 4.87% and as of March 31, 2018 was 4.98%.

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As of March 31, 2018, the Company's interest rates are fixed on approximately 51.34% of its total debt.

As of March 31, 2018, the Company had undrawn revolving credit facilities totaling \$1,000,000, of which approximately \$14,355 was committed for outstanding letters of credit. The remaining amount is unencumbered. The Company

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DAVITA INC.

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(dollars and shares in thousands, except per share data)

also has approximately \$22,351 of additional outstanding letters of credit related to its Kidney Care business and \$211 of committed outstanding letters of credit related to DaVita Medical Group (DMG), which is backed by a certificate of deposit.

#### 10. Contingencies

The majority of the Company's revenues are from government programs and may be subject to adjustment as a result of: (i) examination by government agencies or contractors, for which the resolution of any matters raised may take extended periods of time to finalize; (ii) differing interpretations of government regulations by different Medicare contractors or regulatory authorities; (iii) differing opinions regarding a patient's medical diagnosis or the medical necessity of services provided; and (iv) retroactive applications or interpretations of governmental requirements. In addition, the Company's revenues from commercial payors may be subject to adjustment as a result of potential claims for refunds, as a result of government actions or as a result of other claims by commercial payors.

The Company operates in a highly regulated industry and is a party to various lawsuits, claims, qui tam suits, governmental investigations and audits (including investigations resulting from its obligation to self-report suspected violations of law) and other legal proceedings. The Company records accruals for certain legal proceedings and regulatory matters to the extent that the Company determines an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. As of March 31, 2018 and December 31, 2017, the Company's total recorded accruals, including DMG, with respect to legal proceedings and regulatory matters, net of anticipated third party recoveries, were immaterial. While these accruals reflect the Company's best estimate of the probable loss for those matters as of the dates of those accruals, the recorded amounts may differ materially from the actual amount of the losses for those matters, and any anticipated third party recoveries for any such losses may not ultimately be recoverable. Additionally, in some cases, no estimate of the possible loss or range of loss in excess of amounts accrued, if any, can be made because of the inherently unpredictable nature of legal proceedings and regulatory matters, which also may be impacted by various factors, including that they may involve indeterminate claims for monetary damages or may involve fines, penalties or non-monetary remedies; present novel legal theories or legal uncertainties; involve disputed facts; represent a shift in regulatory policy; are in the early stages of the proceedings; or result in a change of business practices. Further, there may be various levels of judicial review available to the Company in connection with any such proceeding.

The following is a description of certain lawsuits, claims, governmental investigations and audits and other legal proceedings to which the Company is subject.

#### Inquiries by the Federal Government and Certain Related Civil Proceedings

2015 U.S. Office of Inspector General (OIG) Medicare Advantage Civil Investigation: In March 2015, JSA HealthCare Corporation (JSA), a subsidiary of DMG, received a subpoena from the Office of Inspector General (OIG) for the U.S. Department of Health and Human Services (HHS) requesting documents and information for the period from January 1, 2008 through December 31, 2013, for certain MA plans for which JSA provided services. It also requests information regarding JSA's communications about patient diagnoses as they relate to certain MA plans generally, and more specifically as related to two Florida physicians with whom JSA previously contracted. The Company is producing the requested information and is cooperating with the government's investigation.

In addition to the subpoena described above, in June 2015, the Company received a civil subpoena from the OIG covering the period from January 1, 2008 through the present and seeking production of a wide range of documents relating to the Company's and its subsidiaries' (including DMG's and its subsidiary JSA's) provision of services to MA plans and related patient diagnosis coding and risk adjustment submissions and payments. The Company believes that the request is part of a broader industry investigation into MA patient diagnosis coding and risk adjustment practices and potential overpayments by the government. The information requested includes information relating to patient diagnosis coding practices for a number of conditions, including potentially improper historical DMG coding for a

particular condition. With respect to that condition, the guidance related to that coding issue was discontinued following the Company's November 1, 2012 acquisition of HealthCare Partners (now known as the Company's DMG business), and the Company notified Centers for Medicare and Medicaid Services (CMS) in April 2015 of the coding practice and potential overpayments. In that regard, the Company has identified certain additional coding practices which may have been problematic, some of which were the subject of the previously disclosed and dismissed Swoben Private Civil Suit, and is in discussions with the DOJ relating to those practices. The Company is cooperating with the government. In addition, the Company is continuing to review other DMG coding practices to determine whether there were any improper coding issues. In connection with the Company's acquisition of DMG in 2012, the Company

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has certain indemnification rights against the sellers and an escrow was established as security for the indemnification. The Company has submitted an indemnification claim against the sellers secured by the escrow for any and all liabilities incurred relating to these matters and intends to pursue recovery from the escrow. However, the Company can make no assurances that the indemnification and escrow will cover the full amount of the Company's potential losses related to these matters.

**2016 U.S. Attorney Texas Investigation:** In early February 2016, the Company announced that its pharmacy services' wholly-owned subsidiary, DaVita Rx, LLC, (DaVita Rx) received a Civil Investigative Demand (CID) from the U.S. Attorney's Office for the Northern District of Texas. The government is conducting a federal False Claims Act (FCA) investigation concerning allegations that DaVita Rx presented or caused to be presented false claims for payment to the government for prescription medications, as well as into the Company's relationship with pharmaceutical manufacturers. The CID covers the period from January 1, 2006 through the present. In the spring of 2015, the Company initiated an internal compliance review of DaVita Rx during which it identified potential billing and operational issues, including potential write-offs and discounts of patient co-payment obligations, and credits to payors for returns of prescription drugs related to DaVita Rx. The Company notified the government in September 2015 that it was conducting this review of DaVita Rx and began providing regular updates of its review. Upon completion of its review, the Company filed a self-disclosure with the OIG in February 2016 and has been working to address and update the practices it identified in the self-disclosure, some of which overlap with information requested by the U.S. Attorney's Office. The OIG informed the Company in February 2016 that its submission was not accepted. They indicated that the OIG is not expressing an opinion regarding the conduct disclosed or the Company's legal positions. In connection with the Company's ongoing efforts working with the government the Company learned that a qui tam complaint had been filed covering some of the issues in the CID and the Company's self-disclosure. In December 2017, the Company finalized and executed a settlement agreement with the government and relators in the qui tam matter and that included total monetary consideration of \$63,700, as previously announced, of which \$41,500 was an incremental cash payment and \$22,200 was for amounts previously refunded, and all of which was previously accrued. The government's investigation into the Company's relationship with pharmaceutical manufacturers is ongoing and the Company is continuing to cooperate with the government in this investigation.

**2017 U.S. Attorney Massachusetts Investigation:** In January 2017, the Company was served with an administrative subpoena for records by the United States Attorney's Office, District of Massachusetts, relating to an investigation into possible federal health care offenses. The subpoena covers the period from January 1, 2007 through the present, and seeks documents relevant to charitable patient assistance organizations, particularly the American Kidney Fund, including documents related to efforts to provide patients with information concerning the availability of charitable assistance. The Company is cooperating with the government.

**2017 U.S. Attorney Colorado Investigation:** In November 2017, United States Attorney's Office, District of Colorado informed the Company of an investigation it was conducting into possible federal health care offenses involving DaVita Kidney Care, as well as several of the Company's wholly-owned subsidiaries, including DMG, DaVita Rx, DaVita Laboratory Services, Inc. (DaVita Labs), and RMS Lifeline Inc. (Lifeline). There is overlap between the Colorado investigation and the other reported investigations concerning DMG and DaVita Rx. The Company is cooperating with the government.

**2017 U.S. Attorney Florida Investigation:** In November 2017, United States Attorney's Office, Southern District of Florida informed the Company of an investigation it was conducting into possible federal healthcare offenses involving the Company's wholly-owned subsidiary, Lifeline. The Company is cooperating with the government.

**2018 U.S. Attorney Florida Investigation:** In March 2018, DaVita Labs, received two CIDs from the United States Attorney's Office, Middle District of Florida that were identical in nature but directed to the two different labs. According to the face of the CIDs, the U.S. Attorney's Office is conducting an investigation as to whether the



Company's subsidiary submitted claims for blood, urine, and fecal testing, where there were insufficient test validation or stability studies to ensure accurate results, in violation of the False Claims Act. The Company is cooperating with the government.

\* \* \*

Although the Company cannot predict whether or when proceedings might be initiated or when these matters may be resolved (other than as described above), it is not unusual for inquiries such as these to continue for a considerable period of time through the various phases of document and witness requests and on-going discussions with regulators and to develop over the course of time. In addition to the inquiries and proceedings specifically identified above, the Company frequently is subject

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to other inquiries by state or federal government agencies and/or private civil qui tam complaints filed by relators. Negative findings or terms and conditions that the Company might agree to accept as part of a negotiated resolution of pending or future government inquiries or relator proceedings could result in, among other things, substantial financial penalties or awards against the Company, substantial payments made by the Company, harm to the Company's reputation, required changes to the Company's business practices, exclusion from future participation in the Medicare, Medicaid and other federal health care programs and, if criminal proceedings were initiated against the Company, possible criminal penalties, any of which could have a material adverse effect on the Company.

#### Shareholder and Derivative Claims

**Peace Officers' Annuity and Benefit Fund of Georgia Securities Class Action Civil Suit:** On February 1, 2017, the Peace Officers' Annuity and Benefit Fund of Georgia filed a putative federal securities class action complaint in the U.S. District Court for the District of Colorado against the Company and certain executives. The complaint covers the time period of August 2015 to October 2016 and alleges, generally, that the Company and its executives violated federal securities laws concerning the Company's financial results and revenue derived from patients who received charitable premium assistance from an industry-funded non-profit organization. The complaint further alleges that the process by which patients obtained commercial insurance and received charitable premium assistance was improper and "created a false impression of DaVita's business and operational status and future growth prospects." In November 2017, the court appointed the lead plaintiff and an amended complaint was filed on January 12, 2018. On March 27, 2018, the Company and various individual defendants filed a motion to dismiss. The Company disputes these allegations and intends to defend this action accordingly.

**In re DaVita Inc. Stockholder Derivative Litigation:** On August 15, 2017, the U.S. District Court for the District of Delaware consolidated three previously disclosed shareholder derivative lawsuits: the Blackburn Shareholder action filed on February 10, 2017, the Gabilondo Shareholder action filed on May 30, 2017, and the City of Warren Police and Fire Retirement System Shareholder action filed on June 9, 2017. The complaint covers the time period from 2015 to present and alleges, generally, breach of fiduciary duty, unjust enrichment, abuse of control, gross mismanagement, corporate waste, and misrepresentations and/or failures to disclose certain information in violation of the federal securities laws in connection with an alleged practice to direct patients with government-subsidized health insurance into private health insurance plans to maximize the Company's profits. An amended complaint was filed in September 2017, and on December 18, 2017 the Company filed a motion to dismiss and a motion to stay proceedings in the alternative. The plaintiffs filed an opposition to the motion to dismiss on March 9, 2018. The Company disputes these allegations and intends to defend this action accordingly.

#### Other Proceedings

In addition to the foregoing, from time to time the Company is subject to other lawsuits, demands, claims, governmental investigations and audits and legal proceedings that arise due to the nature of its business, including contractual disputes, such as with payors, suppliers and others, employee-related matters and professional and general liability claims. From time to time, the Company also initiates litigation or other legal proceedings as a plaintiff arising out of contracts or other matters.

#### Resolved Matters

**2011 Suit against the U.S. Department of Veterans Affairs:** As previously disclosed, the Company had a pending lawsuit in the U.S. Court of Federal Claims against the federal government which was originally filed in May 2011. The lawsuit related to the U.S. Department of Veterans Affairs (VA) underpayment of dialysis services the Company provided from 2005 through 2011 to veterans pursuant to VA regulations. In the first quarter of 2017, the Company received a payment of \$538,000 related to the settlement with the VA. The Company's consolidated entities recognized a net gain of \$527,000 on this settlement. The Company's nonconsolidated and managed entities recognized a gain of \$9,000, of which the Company's equity investment share was \$3,000. The net effect was a net

increase of \$530,000 to the Company's operating income.

\* \* \*

Other than as described above, the Company cannot predict the ultimate outcomes of the various legal proceedings and regulatory matters to which the Company is or may be subject from time to time, including those described in this Note 10 to these condensed consolidated financial statements, or the timing of their resolution or the ultimate losses or impact of developments in those matters, which could have a material adverse effect on the Company's revenues, earnings and cash flows. Further, any legal proceedings or regulatory matters involving the Company, whether meritorious or not, are time

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consuming, and often require management's attention and result in significant legal expense, and may result in the diversion of significant operational resources, or otherwise harm the Company's business, financial results or reputation.

#### 11. Noncontrolling interests subject to put provisions and other commitments

The Company has potential obligations to purchase the equity interests held by third parties in several of its majority-owned joint ventures and other nonconsolidated entities. These obligations are in the form of put provisions that are exercisable at the third-party owners' discretion within specified periods as outlined in each specific put provision. If these put provisions were exercised, the Company would be required to purchase the third-party owners' equity interests at either the appraised fair market value or a predetermined multiple of earnings or cash flows attributable to the equity interests put to the Company, which is intended to approximate fair value. The methodology the Company uses to estimate the fair values of noncontrolling interests subject to put provisions assumes the higher of either a liquidation value of net assets or an average multiple of earnings, based on historical earnings, patient mix and other performance indicators that can affect future results, as well as other factors. The estimated fair values of noncontrolling interests subject to put provisions are a critical accounting estimate that involves significant judgments and assumptions and may not be indicative of the actual values at which the noncontrolling interests may ultimately be settled, which could vary significantly from the Company's current estimates. The estimated fair values of noncontrolling interests subject to put provisions can fluctuate and the implicit multiple of earnings at which these noncontrolling interests obligations may be settled will vary significantly depending upon market conditions including potential purchasers' access to the capital markets, which can impact the level of competition for dialysis and non-dialysis related businesses, the economic performance of these businesses and the restricted marketability of the third-party owners' equity interests. The amount of noncontrolling interests subject to put provisions that employ a contractually predetermined multiple of earnings rather than fair value are immaterial.

The Company has certain other potential commitments to provide operating capital to a number of dialysis centers that are wholly-owned by third parties or businesses in which the Company maintains a noncontrolling equity interest as well as to physician-owned vascular access clinics or medical practices that the Company operates under management and administrative services agreements of approximately \$5,542.

Certain consolidated joint ventures are originally contractually scheduled to dissolve after terms ranging from 10 to 50 years. While noncontrolling interests in these limited life entities qualify as mandatorily redeemable financial instruments, they are subject to a classification and measurement scope exception from the accounting guidance generally applicable to other mandatorily redeemable financial instruments. Future distributions upon dissolution of these entities would be valued below the related noncontrolling interest carrying balances in the consolidated balance sheet.

#### 12. Long-term incentive compensation

Long-term incentive program (LTIP) compensation includes both stock-based awards (principally stock-settled stock appreciation rights, restricted stock units, and performance stock units) as well as long-term performance-based cash awards. Long-term incentive compensation expense, which was primarily general and administrative in nature, was attributed to the Company's U.S. dialysis and related lab services business, corporate administrative support, and ancillary services and strategic initiatives.

The Company's stock-based compensation awards are measured at their estimated fair values on the date of grant if settled in shares or at their estimated fair values at the end of each reporting period if settled in cash. The value of stock-based awards so measured is recognized as compensation expense on a cumulative straight-line basis over the vesting terms of the awards, adjusted for expected forfeitures.

During the three months ended March 31, 2018, the Company granted 11 stock-settled stock appreciation rights with an aggregate grant-date fair value of \$200 and a weighted-average expected life of approximately 3.7 years and 60

stock units with an aggregate grant-date fair value of \$3,995 and a weighted-average expected life of approximately 1.0 years.

For the three months ended March 31, 2018 and 2017, the Company recognized \$15,215 and \$15,254, respectively, in total LTIP expense, of which \$9,155 and \$8,425, respectively, represented stock-based compensation expense for stock appreciation rights, restricted stock units, and discounted employee stock plan purchases, which are primarily included in general and administrative expense. The estimated tax benefits recorded for stock-based compensation for the three months ended March 31, 2018 and 2017 was \$2,088 and \$2,922, respectively.

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As of March 31, 2018, the Company had \$91,823 of total estimated but unrecognized compensation expense for outstanding LTIP awards, including \$62,013 related to stock-based compensation arrangements under the Company's equity compensation and employee stock purchase plans. The Company expects to recognize the performance-based cash component of these LTIP costs over a weighted average remaining period of 1.1 years and the stock-based component of these LTIP costs over a weighted average remaining period of 1.3 years.

For the three months ended March 31, 2018 and 2017, the Company recognized \$4,895 and \$1,091, respectively, in actual tax benefits upon the exercise of stock awards.

## 13. Share repurchases

During the three months ended March 31, 2018, the Company repurchased a total of 4,197 shares of its common stock for \$298,377 at an average price of \$71.09 per share. The Company also repurchased 4,350 shares of its common stock for \$275,992 at an average price of \$63.44 per share, subsequent to March 31, 2018 through May 2, 2018.

On October 10, 2017, the Company's Board of Directors approved an additional share repurchase authorization in the amount of \$1,252,961. This share repurchase authorization was in addition to the \$247,039 remaining at that time under the Company's Board of Directors' prior share repurchase authorization announced in July 2016. Accordingly, as of May 2, 2018, the Company has a total of \$544,747 available under the current Board repurchase authorizations for additional share repurchases. Although these share repurchase authorizations do not have expiration dates, the Company remains subject to share repurchase limitations under the terms of its senior secured credit facilities and the indentures governing its senior notes.

## 14. Other comprehensive income

	For the three months ended March 31, 2018				For the three months ended March 31, 2017			
	Interest rate cap agreements	Investment securities	Foreign currency translation adjustments	Accumulated other comprehensive income (loss)	Interest rate cap agreements	Investment securities	Foreign currency translation adjustments	Accumulated other comprehensive (loss) income
Beginning balance	\$(12,408)	\$ 5,662	\$ 19,981	\$ 13,235	\$(12,029)	\$ 2,175	\$(79,789)	\$(89,643)
Cumulative effect of change in accounting principle <sup>(1)</sup>	(2,706)	(5,662)	—	(8,368)	—	—	—	—
Unrealized gains (losses)	1,414	—	19,881	21,295	(5,217)	2,113	13,261	10,157
Related income tax (expense) benefit	(364)	—	—	(364)	2,029	(554)	—	1,475
	1,050	—	19,881	20,931	(3,188)	1,559	13,261	11,632
Reclassification from accumulated other comprehensive income into net income	2,070	—	—	2,070	2,070	(229)	—	1,841
Related income tax (expense) benefit	(533)	—	—	(533)	(805)	89	—	(716)

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	1,537	—	—	1,537	1,265	(140 )	—	1,125
Ending balance	\$(12,527)	\$—	\$ 39,862	\$ 27,335	\$(13,952)	\$ 3,594	\$(66,528 )	\$(76,886 )

Reflects the cumulative effect of a change in accounting principle for ASUs 2016-01 and 2018-03 on classification (1) and measurement of financial instruments and ASU 2018-02 on remeasurement and reclassification of deferred tax effects in accumulated other comprehensive income associated with the 2017 Tax Act.

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Net realized losses on interest rate cap agreements that are reclassified into income are recorded as debt expense in the corresponding consolidated statements of operations. See Note 9 to these condensed consolidated financial statements for further details.

Net realized gains on investment securities reclassified into income for the three months ended March 31, 2017 were recognized in other income in the corresponding consolidated statements of operations. See Note 5 to these condensed consolidated financial statements for further details.

#### 15. Acquisitions and divestitures

##### Routine acquisitions

During the three months ended March 31, 2018, the Company acquired dialysis businesses consisting of one dialysis center located in the U.S. and four dialysis centers located outside the U.S. for a total of \$15,677 in net cash, \$655 in deferred purchase price obligations, and \$2,408 in liabilities assumed. The assets and liabilities for these acquisitions were recorded at their estimated fair values at the dates of the acquisitions and are included in the Company's condensed consolidated financial statements, as are their operating results, from the designated effective dates of the acquisitions.

The initial purchase price allocations for these transactions have been recorded at estimated fair values based on the best information available to management and will be finalized when certain information arranged to be obtained has been received. In particular, certain income tax amounts are pending final evaluation and quantification of pre-acquisition tax contingencies and filing of final tax returns. In addition, valuation of certain working capital items, fixed assets and intangibles are pending final audits and related valuation reports.

The following table summarizes the assets acquired and liabilities assumed in these transactions at their estimated acquisition date fair values:

Current assets	\$1,572
Property and equipment	1,643
Amortizable intangible and other long-term assets	2,563
Goodwill	16,042
Current liabilities	(2,392 )
Noncontrolling interests	(688 )
	\$18,740

Amortizable intangible assets acquired during the first three months of 2018 primarily represent non-compete agreements which had weighted-average estimated useful lives of approximately five years. The total estimated amount of goodwill deductible for tax purposes associated with these acquisitions was approximately \$15,383.

##### Contingent earn-out obligations

The Company has several contingent earn-out obligations associated with acquisitions that could result in the Company paying the former owners of acquired companies a total of up to \$11,555 if certain EBITDA, operating income performance targets or quality margins are met primarily over the next one to six years.

Contingent earn-out obligations are remeasured at fair value at each reporting date until the contingencies are resolved with changes in the liability due to the remeasurement recorded in earnings. See Note 18 to these condensed consolidated financial statements for further details. As of March 31, 2018, the Company has estimated the fair value of these contingent earn-out obligations to be \$6,562, of which a total of \$222 is included in other liabilities and the remaining \$6,340 is included in other long-term liabilities in the Company's consolidated balance sheet.



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The following is a reconciliation of changes in liabilities for contingent earn-out obligations:

	For the three months ended March 31, 2018
Beginning balance	\$6,388
Remeasurement of fair value for contingent earn-out obligations	174
Ending balance	\$6,562

16. Held for sale and discontinued operations

DaVita Medical Group

In December 2017, the Company entered into an equity purchase agreement to sell its DMG division to Collaborative Care Holdings, LLC (Optum), a subsidiary of UnitedHealth Group Inc., for \$4,900,000 in cash, subject to net working capital and other customary adjustments. The transaction is expected to close in 2018 and is subject to regulatory approvals and other customary closing conditions. As a result of this pending transaction, the DMG business has been classified as held for sale and its results of operations are reported as discontinued operations for all periods presented. The following table presents the financial results of discontinued operations related to DMG:

	Three months ended March 31,	
	2018	2017
Revenues	\$1,227,932	\$1,086,985
Expenses	1,226,407	1,074,452
Income from discontinued operations before taxes	1,525	12,533
Income tax expense	7,311	6,100
Net (loss) income from discontinued operations, net of tax	\$(5,786)	\$6,433

The following table presents the financial position of discontinued operations related to DMG:

	March 31, 2018	December 31, 2017
Assets		
Cash and cash equivalents	192,399	179,668
Other current assets	768,388	826,608
Property and equipment, net	410,127	379,945
Intangible assets, net	1,316,462	1,316,550
Other long-term assets	155,385	178,894
Goodwill	2,881,504	2,879,977
Total current assets held for sale	\$5,724,265	\$5,761,642
Liabilities		
Other liabilities	529,354	505,734
Medical payables	505,872	457,040

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Current portion of long-term debt	2,735	2,845
Long-term debt	34,541	35,003
Other long-term liabilities	182,123	184,448
Total current liabilities held for sale	\$ 1,254,625	\$ 1,185,070

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The following table presents cash flows of discontinued operations related to DMG:

	March 31, 2018	March 31, 2017
Net cash provided by operating activities from discontinued operations	156,248	95,585
Net cash used in investing activities from discontinued operations	(33,068 )	(41,686 )
DMG acquisitions		

During the first quarter of 2018, the Company's DMG business acquired one medical business for a total of \$905 in cash and deferred purchase price of \$99. Certain income tax amounts are pending final evaluation and quantification of any pre-acquisition tax contingencies. In addition, valuation of medical claims liabilities and certain other working capital items relating to acquisitions are pending final quantification. The assets and liabilities for all acquisitions were recorded at their estimated fair values at the dates of the acquisitions and are included in the Company's current held for sale assets and liabilities.

#### 17. Variable interest entities

The Company relies on the operating activities of certain legal entities that it does not directly own or control, but over which it has indirect influence and of which it is considered the primary beneficiary. These entities are subject to the consolidation guidance applicable to variable interest entities (VIEs).

Under U.S. generally accepted accounting principles (GAAP), VIEs typically include entities for which (i) the entity's equity is not sufficient to finance its activities without additional subordinated financial support; (ii) the equity holders as a group lack the power to direct the activities that most significantly influence the entity's economic performance, the obligation to absorb the entity's expected losses, or the right to receive the entity's expected returns; or (iii) the voting rights of some investors are not proportional to their obligations to absorb the entity's losses.

The Company has determined that substantially all of the legal entities it is associated with that qualify as VIEs must be included in its consolidated financial statements. A number of these VIEs are within the Company's DMG business, which is classified as held for sale and as a discontinued operation in these condensed consolidated financial statements. The Company manages these entities and provides operating and capital funding as necessary for these entities to accomplish their operational and strategic objectives. A number of these entities are subject to nominee share ownership or share transfer restriction agreements that effectively transfer the majority of the economic risks and rewards of their ownership to the Company. In other cases the Company's management agreements with these entities include both financial terms and protective and participating rights to the entities' operating, strategic and non-clinical governance decisions which transfer substantial powers over and economic responsibility for the entities to the Company. In some cases such entities are subject to broad exclusivity or noncompetition restrictions that benefit the Company. Further, in some cases the Company has contractual arrangements with its related party nominee owners that effectively indemnify these parties from the economic losses from, or entitle the Company to the economic benefits of, these entities.

The analyses upon which these consolidation determinations rest are complex, involve uncertainties, and require significant judgment on various matters, some of which could be subject to different interpretations. At March 31, 2018, these condensed consolidated financial statements include total assets of VIEs of \$852,912 and total liabilities and noncontrolling interests of VIEs to third parties of \$507,962, including assets of \$580,039 and liabilities and noncontrolling interests of \$345,926 related to the Company's DMG business classified as held for sale.

The Company also sponsors certain deferred compensation plans whose trusts qualify as VIEs and the Company consolidates these plans as their primary beneficiary. The assets of these plans are recorded in short-term or long-term investments with matching offsetting liabilities recorded in accrued compensation and benefits and other long-term liabilities. See Note 5 to these condensed consolidated financial statements for disclosures on the assets of these consolidated non-qualified deferred compensation plans.

18. Fair values of financial instruments

The Company measures the fair value of certain assets, liabilities and noncontrolling interests subject to put provisions (temporary equity) based upon certain valuation techniques that include observable or unobservable inputs and assumptions that market participants would use in pricing these assets, liabilities, temporary equity and commitments. The Company has also

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classified certain assets, liabilities and temporary equity that are measured at fair value into the appropriate fair value hierarchy levels as defined by the FASB.

The following table summarizes the Company's assets, liabilities and temporary equity that are measured at fair value on a recurring basis as of March 31, 2018:

	Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
<b>Assets</b>				
Investments in mutual funds and common stock	\$35,544	\$ 35,544	\$ —	\$ —
Interest rate cap agreements	\$2,446	\$ —	\$ 2,446	\$ —
<b>Liabilities</b>				
Contingent earn-out obligations	\$6,562	\$ —	\$ —	\$ 6,562
<b>Temporary equity</b>				
Noncontrolling interests subject to put provisions	\$1,034,501	\$ —	\$ —	\$ 1,034,501

Investments in mutual funds and common stock represent equity securities that are recorded at estimated fair value based upon quoted redemption prices reported by each mutual fund. See Note 5 to these condensed consolidated financial statements for further discussion.

Interest rate cap agreements are recorded at fair value estimated from valuation models utilizing the income approach and commonly accepted valuation techniques that use inputs from closing prices for similar assets and liabilities in active markets as well as other relevant observable market inputs at quoted intervals such as current interest rates, forward yield curves, implied volatility and credit default swap pricing. The Company does not believe the ultimate amount that could be realized upon settlement of these interest rate cap agreements would be materially different from the fair value estimates currently reported. See Note 9 to these condensed consolidated financial statements for further discussion.

The estimated fair value of contingent earn-out obligations are primarily based on unobservable inputs including projected EBITDA. The estimated fair value of these contingent earn-out obligations is remeasured as of each reporting date and could fluctuate based upon any significant changes in key assumptions, such as changes in the Company credit risk-adjusted rate that is used to discount the obligations to present value. See Note 15 to these condensed consolidated financial statements for further discussion.

See Note 11 to these condensed consolidated financial statements for a discussion of the Company's methodology for estimating the fair value of noncontrolling interests subject to put obligations.

The carrying balance of the Company's senior secured credit facilities totaled \$4,546,990 as of March 31, 2018, and the fair value was approximately \$4,616,019 based upon quoted market prices, a level 2 input.

The carrying balance of the Company's senior notes was \$4,461,802 as of March 31, 2018 and their fair value was approximately \$4,433,500, based upon quoted market prices, a level 2 input.

Other financial instruments consist primarily of cash and cash equivalents, accounts receivable, accounts payable, other accrued liabilities and debt. The balances of the Company's financial instruments other than the senior secured credit facilities and the senior notes are presented in the condensed consolidated financial statements at March 31, 2018 at their approximate fair values due to the short-term nature of their settlements.

#### 19. Segment reporting

The Company has consisted of two major divisions, DaVita Kidney Care (Kidney Care) and DMG. The Kidney Care division is comprised of the Company's U.S. dialysis and related lab services business, various ancillary services and

strategic initiatives, including its international operations, and the Company's corporate administrative support. The Company's U.S. dialysis and related lab services business is its largest line of business and is a leading provider of kidney dialysis services in the U.S. for patients suffering from chronic kidney failure, also known as ESRD. The Company's ancillary services and strategic

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initiatives consist primarily of pharmacy services, disease management services, vascular access services, clinical research programs, physician services, direct primary care, ESRD seamless care organizations and comprehensive care, as well as the Company's international operations.

The Company's DMG division is a patient- and physician-focused integrated healthcare delivery and management company with over two decades of providing coordinated outcomes-based medical care in a cost-effective manner. In December 2017, the Company entered into an equity purchase agreement to sell its DMG division to Optum, a subsidiary of UnitedHealth Group Inc. The transaction is expected to close in 2018 and is subject to regulatory approvals and other customary closing conditions. As a result of this pending transaction, the DMG business has been classified as held for sale and its results of operations are reported as discontinued operations for all periods presented in these condensed consolidated financial statements. See Note 16 to these condensed consolidated financial statements for further discussion.

The Company's operating segments have been defined based on the separate financial information that is regularly produced and reviewed by the Company's chief operating decision maker in making decisions about allocating resources to and assessing the financial performance of the Company's various operating lines of business. The chief operating decision maker for the Company is its Chief Executive Officer.

The Company's separate operating segments include its U.S. dialysis and related lab services business, each of its ancillary services and strategic initiatives, its consolidated international kidney care operations in each country and under the Saudi Ministry of Health charter, its equity method investment in the Asia Pacific joint venture, and its other health operations in Europe. The U.S. dialysis and related lab services business qualifies as a separately reportable segment, and all other ancillary services and strategic initiatives operating segments, including the international operating segments, have been combined and disclosed in the other segments category.

The Company's operating segment financial information included in this report is prepared on the internal management reporting basis that the chief operating decision maker uses to allocate resources and assess the financial performance of the Company's operating segments. For internal management reporting, segment operations include direct segment operating expenses but generally exclude corporate administrative support costs, which consist primarily of indirect labor, benefits and long-term incentive-based compensation expenses of certain departments which provide support to all of the Company's various operating lines of business, except to the extent that such costs are charged to and borne by certain ancillary services and strategic initiatives via internal management fees. These corporate administrative support costs are reduced by internal management fees received from the Company's ancillary lines of business.

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The following is a summary of segment net revenues, segment operating margin (loss), and a reconciliation of segment operating margin to consolidated income before income taxes:

	Three months ended	
	March 31,	
	2018	2017
Segment net revenues:		
U.S. dialysis and related lab services		
Patient service revenues:		
External sources	\$2,489,165	\$2,360,861
Intersegment revenues	18,422	11,799
U.S. dialysis and related lab services patient service revenues	2,507,587	2,372,660
Provision for uncollectible accounts	25,199	(106,777 )
Net U.S. dialysis and related lab services patient service revenues	2,532,786	2,265,883
Other revenues <sup>(1)</sup>	5,114	5,311
Total U.S. dialysis and related lab services revenues	2,537,900	2,271,194
Other—Ancillary services and strategic initiatives		
Patient service revenues	102,255	61,644
Other external sources	227,711	310,212
Intersegment revenues	10,199	6,369
Total ancillary services and strategic initiatives revenues	340,165	378,225
Total net segment revenues	2,878,065	2,649,419
Elimination of intersegment revenues	(28,621 )	(18,168 )
Consolidated revenues	\$2,849,444	\$2,631,251
Segment operating margin:		
U.S. dialysis and related lab services	\$433,380	\$944,740
Other—Ancillary services and strategic initiatives	(6,990 )	(58,220 )
Total segment operating margin	426,390	886,520
Reconciliation of segment operating margin to consolidated income before income taxes:		
Corporate administrative support	(15,704 )	(10,592 )
Consolidated operating income	410,686	875,928
Debt expense	(113,516 )	(104,397 )
Other income, net	4,582	3,986
Consolidated income before income taxes	\$301,752	\$775,517

(1) Includes management fees for providing management and administrative services to dialysis centers that are wholly-owned by third parties and legal entities in which the Company owns a noncontrolling equity investment.

Depreciation and amortization expense by reportable segment was as follows:

	Three months ended	
	March 31,	
	2018	2017
U.S. dialysis and related lab services	\$134,776	\$125,029
Other—Ancillary services and strategic initiatives	8,023	7,855
	\$142,799	\$132,884





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Assets by reportable segment were as follows:

	March 31, 2018	December 31, 2017
Segment assets		
U.S. dialysis and related lab services (including equity investments of \$84,985 and \$84,866, respectively)	\$ 11,798,202	\$ 11,776,042
Other—Ancillary services and strategic initiatives (including equity investments of \$160,579 and \$160,668, respectively)	1,419,905	1,410,509
DMG—Held for sale (including equity investments of \$11,642 and \$10,321, respectively)	5,724,265	5,761,642
Consolidated assets	\$ 18,942,372	\$ 18,948,193

Expenditures for property and equipment by reportable segment were as follows:

	Three months ended	
	March 31, 2018	2017
U.S. dialysis and related lab services	\$ 189,049	\$ 173,528
Other—Ancillary services and strategic initiatives	2,345	13,219
DMG—Held for sale	31,049	27,788
	\$ 232,443	\$ 214,535

## 20. Changes in DaVita Inc.'s ownership interest in consolidated subsidiaries

The effects of changes in DaVita Inc.'s ownership interest in consolidated subsidiaries on the Company's equity were as follows:

	Three months ended	
	March 31, 2018	2017
Net income attributable to DaVita Inc.	\$ 178,686	\$ 447,697
Changes in paid-in capital for:		
Sales of noncontrolling interests	76	—
Purchases of noncontrolling interests	(1,994 )	(423 )
Net transfers to noncontrolling interests	(1,918 )	(423 )
Net income attributable to DaVita Inc., net of transfers to noncontrolling interests	\$ 176,768	\$ 447,274

## 21. New accounting standards

On May 28, 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. In 2015, 2016 and 2017, the FASB issued ASU 2015-14, ASU 2016-08, ASU 2016-10, ASU 2016-11, ASU 2016-12, and ASU 2017-10, each of which amends the guidance in ASU 2014-09. These ASUs replaced most existing revenue recognition guidance in GAAP. The Company adopted these ASUs beginning January 1, 2018. See Note 2 for further details.

In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. In February 2018, the FASB issued ASU 2018-03, which provides various related technical corrections and improvements. The Company adopted these ASUs beginning January 1, 2018. See Note 5 for further details.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). The amendments in this ASU revise the accounting related to lessee accounting. Under the new guidance, lessees will be required to recognize a lease liability and a right-of-use asset for substantially all leases with lease terms in excess of twelve months. The new lease guidance also

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simplifies the accounting for sale and leaseback transactions primarily because lessees must recognize lease assets and lease liabilities. The amendments in this ASU are effective for the Company beginning on January 1, 2019 and are to be applied through a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. Early adoption is permitted. The Company has assembled an internal lease task force that meets regularly to discuss and evaluate the overall impact of this guidance on its consolidated financial statements and related disclosures, as well as the expected timing of adoption. The Company is currently gathering and evaluating information from its existing leases and believes that the new standard will have a material impact on its consolidated balance sheet but will not have a material impact on its results of operations or liquidity. The Company expects to adopt this ASU on January 1, 2019, and continues to evaluate the effect that the implementation of this ASU will have on its consolidated financial statements, related disclosures and controls.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. The amendments in this ASU clarify how certain cash receipts and cash payments should be classified on the statement of cash flows. In November 2016, the FASB issued ASU No. 2016-18, Statement of Cash Flows (Topic 230): Restricted cash. The amendments in this ASU require that the statement of cash flows explains the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The adoption of these ASUs did not have a material impact on the Company's consolidated financial statements when adopted on January 1, 2018.

In October 2016, the FASB issued ASU No. 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory. The amendments in this ASU allow entities to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. The current guidance does not allow recognition until the asset has been sold to an outside party. The amendments in this ASU are effective for the Company beginning on January 1, 2018 and are to be applied on a modified retrospective basis. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements when adopted on January 1, 2018.

In August 2017, the FASB issued ASU No. 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities. The amendments in this ASU better align an entity's risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. The amendments in the new ASU are effective for the Company on January 1, 2019 and are to be applied prospectively. The adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements when adopted on January 1, 2019.

In February 2018, the FASB issued ASU No. 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220), Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which allows for the reclassification of certain income tax effects related to the Tax Cuts and Jobs Act between "Accumulated other comprehensive income" and "Retained earnings." This ASU relates to the requirement that adjustments to deferred tax liabilities and assets related to a change in tax laws or rates to be included in "Income from continuing operations", even in situations where the related items were originally recognized in "Other comprehensive income" (rather than in "Income from continuing operations"). The amendments in this ASU are effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years, with early adoption permitted. The Company elected to early adopt this ASU on January 1, 2018 and applied the change in the period of adoption. The adoption of this ASU resulted in the reclassification of an immaterial amount of deferred tax effects from accumulated other comprehensive income to retained earnings via accumulative change in accounting principle effective January 1, 2018. See Note 14 for more details.

22. Condensed consolidating financial statements

The following information is presented in accordance with Rule 3-10 of Regulation S-X. The operating and investing activities of the separate legal entities included in the Company's condensed consolidated financial statements are fully interdependent and integrated. Revenues and operating expenses of the separate legal entities include intercompany charges for management and other administrative services. The Company's senior notes are guaranteed by a substantial majority of its domestic subsidiaries as measured by revenue, income and assets. The subsidiary guarantors have guaranteed the senior notes on a joint and several basis. However, a subsidiary guarantor will be released from its obligations under its guarantee of the senior notes and the indentures governing the senior notes if, in general, there is a sale or other disposition of all or substantially all of the assets of such subsidiary guarantor, including by merger or consolidation, or a sale or other disposition of all of the equity interests in such subsidiary guarantor held by the Company and its restricted subsidiaries, as defined in the indentures;

## DAVITA INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

such subsidiary guarantor is designated by the Company as an unrestricted subsidiary, as defined in the indentures, or otherwise ceases to be a restricted subsidiary of the Company, in each case in accordance with the indentures; or such subsidiary guarantor no longer guarantees any other indebtedness, as defined in the indentures, of the Company or any of its restricted subsidiaries, except for guarantees that are contemporaneously released. The senior notes are not guaranteed by certain of the Company's domestic subsidiaries, any of the Company's foreign subsidiaries, or any entities that do not constitute subsidiaries within the meaning of the indentures, such as corporations in which the Company holds capital stock with less than a majority of the voting power, joint ventures and partnerships in which the Company holds less than a majority of the equity or voting interests, non-owned entities and third parties.

## Condensed Consolidating Statements of Operations

For The Three Months Ended March 31, 2018	DaVita Inc.	Guarantor subsidiaries	Non- Guarantor subsidiaries	Consolidating adjustments	Consolidated total
Patient services revenues	\$—	\$ 1,790,188	\$ 848,401	\$ (47,515 )	\$ 2,591,074
Provision for uncollectible accounts	—	9,628	15,917	—	25,545
Net patient service revenues	—	1,799,816	864,318	(47,515 )	2,616,619
Other revenues	195,565	204,960	70,933	(238,633 )	232,825
Total net revenues	195,565	2,004,776	935,251	(286,148 )	2,849,444
Operating expenses and charges	133,356	1,791,094	800,456	(286,148 )	2,438,758
Operating income	62,209	213,682	134,795	—	410,686
Debt expense	(114,334 )	(52,197 )	(7,375 )	60,390	(113,516 )
Other income, net	104,081	2,523	5,704	(107,726 )	4,582
Income tax expense	14,387	48,944	7,406	—	70,737
Equity earnings in subsidiaries	141,117	66,496	—	(207,613 )	—
Net income from continuing operations	178,686	181,560	125,718	(254,949 )	231,015
Net (loss) income from discontinued operations, net of tax	—	(40,443 )	(12,679 )	47,336	(5,786 )
Net income	178,686	141,117	113,039	(207,613 )	225,229
Less: Net income attributable to noncontrolling interests	—	—	—	(46,543 )	(46,543 )
Net income attributable to DaVita Inc.	\$ 178,686	\$ 141,117	\$ 113,039	\$ (254,156 )	\$ 178,686

## DAVITA INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

For The Three Months Ended March 31, 2017	DaVita Inc.	Guarantor subsidiaries	Non-Guarantor subsidiaries	Consolidating adjustments	Consolidated total
Patient service revenues	\$—	\$ 1,530,726	\$ 929,231	\$ (37,171 )	\$ 2,422,786
Provision for uncollectible accounts	—	(61,053 )	(46,005 )	—	(107,058 )
Net patient service revenues	—	1,469,673	883,226	(37,171 )	2,315,728
Other revenues	221,386	305,618	16,090	(227,571 )	315,523
Total net revenues	221,386	1,775,291	899,316	(264,742 )	2,631,251
Operating expenses	131,910	1,208,820	679,335	(264,742 )	1,755,323
Operating income	89,476	566,471	219,981	—	875,928
Debt expense	(102,664 )	(47,643 )	(12,232 )	58,142	(104,397 )
Other income	100,337	2,803	3,586	(102,740 )	3,986
Income tax expense	33,953	235,865	11,847	—	281,665
Equity earnings in subsidiaries	394,501	162,615	—	(557,116 )	—
Net income from continuing operations	447,697	448,381	199,488	(601,714 )	493,852
Net (loss) income from discontinued operations, net of tax	—	(53,880 )	15,715	44,598	6,433
Net income	447,697	394,501	215,203	(557,116 )	500,285
Less: Net income attributable to noncontrolling interests	—	—	—	(52,588 )	(52,588 )
Net income attributable to DaVita Inc.	\$ 447,697	\$ 394,501	\$ 215,203	\$ (609,704 )	\$ 447,697

## Condensed Consolidating Statements of Comprehensive Income

For The Three Months Ended March 31, 2018	DaVita Inc.	Guarantor subsidiaries	Non-Guarantor subsidiaries	Consolidating adjustments	Consolidated total
Net income	\$ 178,686	\$ 141,117	\$ 113,039	\$ (207,613 )	\$ 225,229
Other comprehensive income	2,587	—	19,881	—	22,468
Total comprehensive income	181,273	141,117	132,920	(207,613 )	247,697
Less: Comprehensive income attributable to noncontrolling interest	—	—	—	(46,543 )	(46,543 )
Comprehensive income attributable to DaVita Inc.	\$ 181,273	\$ 141,117	\$ 132,920	\$ (254,156 )	\$ 201,154

For The Three Months Ended March 31, 2017	DaVita Inc.	Guarantor subsidiaries	Non-Guarantor subsidiaries	Consolidating adjustments	Consolidated total
Net income	\$ 447,697	\$ 394,501	\$ 215,203	\$ (557,116 )	\$ 500,285
Other comprehensive income	(506 )	—	13,261	—	12,755
Total comprehensive income	447,191	394,501	228,464	(557,116 )	513,040
	—	—	—	(52,586 )	(52,586 )

Less: Comprehensive income attributable to the  
noncontrolling interests

Comprehensive income attributable to DaVita Inc. \$ 447,191 \$ 394,501 \$ 228,464 \$ (609,702 ) \$ 460,454



## DAVITA INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

## Condensed Consolidating Balance Sheets

As of March 31, 2018	DaVita Inc.	Guarantor subsidiaries	Non-Guarantor subsidiaries	Consolidating adjustments	Consolidated total
Cash and cash equivalents	\$ 122,047	\$—	\$ 236,827	\$—	\$ 358,874
Restricted cash and equivalents	1,003	9,421	78,320	—	88,744
Accounts receivable, net	—	1,257,461	573,129	—	1,830,590
Other current assets	35,555	368,131	267,396	—	671,082
Current assets held for sale	—	5,004,717	719,548	—	5,724,265
Total current assets	158,605	6,639,730	1,875,220	—	8,673,555
Property and equipment, net	413,949	1,554,591	1,216,683	—	3,185,223
Intangible assets, net	224	50,396	62,746	—	113,366
Investments in subsidiaries	10,180,619	3,138,371	—	(13,318,990 )	—
Intercompany receivables	3,593,688	—	1,488,211	(5,081,899 )	—
Other long-term assets and investments	54,952	58,467	218,217	—	331,636
Goodwill	—	4,730,205	1,908,387	—	6,638,592
Total assets	\$ 14,402,037	\$ 16,171,760	\$ 6,769,464	\$(18,400,889)	\$ 18,942,372
Current liabilities	\$ 247,486	\$ 968,018	\$ 477,394	\$—	\$ 1,692,898
Current liabilities held for sale	—	759,020	495,605	—	1,254,625
Intercompany payables	—	3,589,494	1,492,405	(5,081,899 )	—
Long-term debt and other long-term liabilities	8,984,265	674,609	519,393	—	10,178,267
Noncontrolling interests subject to put provisions	589,606	—	—	444,895	1,034,501
Total DaVita Inc. shareholders' equity	4,580,680	10,180,619	3,138,371	(13,318,990 )	4,580,680
Noncontrolling interests not subject to put provisions	—	—	646,296	(444,895 )	201,401
Total equity	4,580,680	10,180,619	3,784,667	(13,763,885 )	4,782,081
Total liabilities and equity	\$ 14,402,037	\$ 16,171,760	\$ 6,769,464	\$(18,400,889)	\$ 18,942,372

## DAVITA INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

As of December 31, 2017	DaVita Inc.	Guarantor subsidiaries	Non-Guarantor subsidiaries	Consolidating adjustments	Consolidated total
Cash and cash equivalents	\$ 149,305	\$—	\$ 358,929	\$—	\$ 508,234
Restricted cash and equivalents	1,002	9,384	300	—	10,686
Accounts receivable, net	—	1,208,715	506,035	—	1,714,750
Other current assets	67,025	595,066	86,955	—	749,046
Current assets held for sale	—	4,992,067	769,575	—	5,761,642
Total current assets	217,332	6,805,232	1,721,794	—	8,744,358
Property and equipment, net	408,010	1,560,390	1,180,813	—	3,149,213
Intangible assets, net	250	50,971	62,606	—	113,827
Investments in subsidiaries	10,009,874	3,085,722	—	(13,095,596 )	—
Intercompany receivables	3,677,947	—	1,313,213	(4,991,160 )	—
Other long-term assets and investments	47,297	68,344	214,875	—	330,516
Goodwill	—	4,732,320	1,877,959	—	6,610,279
Total assets	\$ 14,360,710	\$ 16,302,979	\$ 6,371,260	\$(18,086,756)	\$ 18,948,193
Current liabilities	\$ 238,706	\$ 1,181,139	\$ 436,262	\$—	\$ 1,856,107
Current liabilities held for sale	—	739,294	445,776	—	1,185,070
Intercompany payables	—	3,690,042	1,301,118	(4,991,160 )	—
Long-term debt and other long-term liabilities	8,857,373	682,630	469,587	—	10,009,590
Noncontrolling interests subject to put provisions	574,602	—	—	436,758	1,011,360
Total DaVita Inc. shareholders' equity	4,690,029	10,009,874	3,085,722	(13,095,596 )	4,690,029
Noncontrolling interests not subject to put provisions	—	—	632,795	(436,758 )	196,037
Total equity	4,690,029	10,009,874	3,718,517	(13,532,354 )	4,886,066
Total liabilities and equity	\$ 14,360,710	\$ 16,302,979	\$ 6,371,260	\$(18,086,756)	\$ 18,948,193

DAVITA INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

## Condensed Consolidating Statements of Cash Flows

For The Three Months Ended March 31, 2018	DaVita Inc.	Guarantor subsidiaries	Non-Guarantor subsidiaries	Consolidating adjustments	Consolidated total
Cash flows from operating activities:					
Net income	\$ 178,686	\$ 141,117	\$ 113,039	\$ (207,613 )	\$ 225,229
Changes in operating assets and liabilities and non-cash items included in net income	(82,391 )	32,484	(20,396 )	207,613	137,310
Net cash provided by operating activities	96,295	173,601	92,643	—	362,539
Cash flows from investing activities:					
Additions of property and equipment	(27,356 )	(125,375 )	(79,712 )	—	(232,443 )
Acquisitions	—	(4,417 )	(12,165 )	—	(16,582 )
Proceeds from asset and business sales	—	18,535	—	—	18,535
Proceeds (purchases) from investment sales and other items, net	31,665	(762 )	(541 )	—	30,362
Net cash provided by (used in) investing activities	4,309	(112,019 )	(92,418 )	—	(200,128 )
Cash flows from financing activities:					
Long-term debt and related financing costs, net	116,307	(3,377 )	(8,257 )	—	104,673
Intercompany borrowing (payments)	47,394	(49,783 )	2,389	—	—
Other items	(291,562 )	(2,200 )	(33,458 )	—	(327,220 )
Net cash used in financing activities	(127,861 )	(55,360 )	(39,326 )	—	(222,547 )
Effect of exchange rate changes on cash, cash equivalents and restricted cash	—	—	6,668	—	6,668
Net (decrease) increase in cash, cash equivalents and restricted cash	(27,257 )	6,222	(32,433 )	—	(53,468 )
Less: Net increase in cash, cash equivalents and restricted cash from discontinued operations	—	6,185	11,649	—	17,834
Net (decrease) increase in cash, cash equivalents and restricted cash from continuing operations	(27,257 )	37	(44,082 )	—	(71,302 )
Cash, cash equivalents and restricted cash of continuing operations at beginning of the year	150,307	9,384	359,229	—	518,920
Cash, cash equivalents and restricted cash of continuing operations at end of the period	\$ 123,050	\$ 9,421	\$ 315,147	\$ —	\$ 447,618

## DAVITA INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

For The Three Months Ended March 31, 2017	DaVita Inc.	Guarantor subsidiaries	Non-Guarantor subsidiaries	Consolidating adjustments	Consolidated total
Cash flows from operating activities:					
Net income	\$447,697	\$394,501	\$215,203	\$(557,116)	\$500,285
Changes in operating assets and liabilities and non-cash items included in net income	(149,627)	(142,597)	99,994	557,116	364,886
Net cash provided by operating activities	298,070	251,904	315,197	—	865,171
Cash flows from investing activities:					
Additions of property and equipment	(30,580)	(133,909)	(50,046)	—	(214,535)
Acquisitions	—	(70,237)	(6,999)	—	(77,236)
Proceeds from asset and business sales, net of cash divested	—	46,612	—	—	46,612
(Purchases) proceeds from investment sales and other items, net	(54,150)	(1,951)	51,273	—	(4,828)
Net cash used in investing activities	(84,730)	(159,485)	(5,772)	—	(249,987)
Cash flows from financing activities:					
Long-term debt and related financing costs, net	(27,504)	(4,616)	(4,021)	—	(36,141)
Intercompany borrowing (payments)	338,984	(71,541)	(267,443)	—	—
Other items	3,330	(799)	(25,327)	—	(22,796)
Net cash used in financing activities	314,810	(76,956)	(296,791)	—	(58,937)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	—	—	2,820	—	2,820
Net increase in cash, cash equivalents and restricted cash	528,150	15,463	15,454	—	559,067
Less: Net increase in cash, cash equivalents and restricted cash from discontinued operations	—	15,438	9,055	—	24,493
Net increase in cash, cash equivalents and restricted cash from continuing operations	528,150	25	6,399	—	534,574
Cash, cash equivalents and restricted cash of continuing operations at beginning of the year	549,921	8,687	124,855	—	683,463
Cash, cash equivalents and restricted cash of continuing operations at end of the period	\$1,078,071	\$8,712	\$131,254	—	\$1,218,037

## DAVITA INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

## 23. Supplemental data

The following information is presented as supplemental data as required by the indentures governing the Company's senior notes.

## Condensed Consolidating Statements of Income

For The Three Months Ended March 31, 2018	Consolidated Total	Physician Groups	Unrestricted Subsidiaries	Company and Restricted Subsidiaries <sup>(1)</sup>
Patient service operating revenues	\$2,591,074	\$ —	\$ —	\$ 2,591,074
Provision for uncollectible accounts	25,545	—	—	25,545
Net patient service operating revenues	2,616,619	—	—	2,616,619
Other revenues	232,825	—	—	232,825
Total net operating revenues	2,849,444	—	—	2,849,444
Operating expenses	2,438,758	—	—	2,438,758
Operating income	410,686	—	—	410,686
Debt expense, including refinancing charges	(113,516 )	—	—	(113,516 )
Other income	4,582	—	—	4,582
Income tax expense	70,737	—	—	70,737
Net income from continuing operations	231,015	—	—	231,015
Net (loss) income from discontinued operations, net of tax	(5,786 )	7,397	490	(13,673 )
Net income	225,229	7,397	490	217,342
Less: Net income attributable to noncontrolling interests	(46,543 )	(6,543 )	—	(40,000 )
Net income attributable to DaVita Inc.	\$ 178,686	\$ 854	\$ 490	\$ 177,342

(1) After elimination of the unrestricted subsidiaries and the physician groups.

## Condensed Consolidating Statements of Comprehensive Income

For The Three Months Ended March 31, 2018	Consolidated Total	Physician Groups	Unrestricted Subsidiaries	Company and Restricted Subsidiaries <sup>(1)</sup>
Net income	\$ 225,229	\$ 7,397	\$ 490	\$ 217,342
Other comprehensive income	22,468	—	—	22,468
Total comprehensive income	247,697	7,397	490	239,810
Less: Comprehensive income attributable to the noncontrolling interests	(46,543 )	(6,543 )	—	(40,000 )
Comprehensive income attributable to DaVita Inc.	\$ 201,154	\$ 854	\$ 490	\$ 199,810

(1) After elimination of the unrestricted subsidiaries and the physician groups.



## DAVITA INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

## Condensed Consolidating Balance Sheets

As of March 31, 2018	Consolidated Total	Physician Groups	Unrestricted Subsidiaries	Company and Restricted Subsidiaries <sup>(1)</sup>
Cash and cash equivalents	\$ 358,874	\$—	\$ —	\$ 358,874
Restricted cash and equivalents	88,744	—	—	88,744
Accounts receivable, net	1,830,590	—	—	1,830,590
Other current assets	671,082	133,199	—	537,883
Current assets held for sale	5,724,265	319,968	3,223	5,401,074
Total current assets	8,673,555	453,167	3,223	8,217,165
Property and equipment, net	3,185,223	—	—	3,185,223
Amortizable intangibles, net	113,366	—	—	113,366
Other long-term assets	331,636	—	—	331,636
Goodwill	6,638,592	—	—	6,638,592
Total assets	\$ 18,942,372	\$ 453,167	\$ 3,223	\$ 18,485,982
Current liabilities	\$ 1,692,898	\$—	\$ —	\$ 1,692,898
Current liabilities held for sale	1,254,625	328,493	—	926,132
Payables to parent	—	—	3,223	(3,223 )
Long-term debt and other long-term liabilities	10,178,267	—	—	10,178,267
Noncontrolling interests subject to put provisions	1,034,501	—	—	1,034,501
Total DaVita Inc. shareholders' equity	4,580,680	124,674	—	4,456,006
Noncontrolling interests not subject to put provisions	201,401	—	—	201,401
Shareholders' equity	4,782,081	124,674	—	4,657,407
Total liabilities and shareholder's equity	\$ 18,942,372	\$ 453,167	\$ 3,223	\$ 18,485,982

(1) After elimination of the unrestricted subsidiaries and the physician groups.

DAVITA INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(continued)

(unaudited)

(dollars and shares in thousands, except per share data)

## Condensed Consolidating Statements of Cash Flows

For The Three Months Ended March 31, 2018	Consolidated Total	Physician Groups	Unrestricted Subsidiaries	Company and Restricted Subsidiaries <sup>(1)</sup>
Cash flows from operating activities:				
Net income	\$ 225,229	\$ 7,397	\$ 490	\$ 217,342
Changes in operating and intercompany assets and liabilities and non-cash items included in net income	137,310	(20,189 )	(490 )	157,989
Net cash provided by (used in) operating activities	362,539	(12,792 )	—	375,331
Cash flows from investing activities:				
Additions of property and equipment	(232,443 )	(1,165 )	—	(231,278 )
Acquisitions	(16,582 )	—	—	(16,582 )
Proceeds from asset and business sales	18,535	—	—	18,535
Investments and other items	30,362	(541 )	—	30,903
Net cash used in investing activities	(200,128 )	(1,706 )	—	(198,422 )
Cash flows from financing activities:				
Long-term debt	104,673	—	—	104,673
Intercompany	—	1,082	—	(1,082 )
Other items	(327,220 )	—	—	(327,220 )
Net cash (used in) provided by financing activities	(222,547 )	1,082	—	(223,629 )
Effect of exchange rate changes on cash, cash equivalents and restricted cash	6,668	—	—	6,668
Net decrease in cash, cash equivalents and restricted cash	(53,468 )	(13,416 )	—	(40,052 )
Less: Net increase (decrease) in cash, cash equivalents and restricted cash from discontinued operations	17,834	(13,416 )	—	31,250
Net decrease in cash, cash equivalents and restricted cash from continuing operations	(71,302 )	—	—	(71,302 )
Cash, cash equivalents and restricted cash of continuing operations at beginning of the year	518,920	—	—	518,920
Cash, cash equivalents and restricted cash of continuing operations at end of the period	\$ 447,618	\$ —	\$ —	\$ 447,618

(1) After elimination of the unrestricted subsidiaries and the physician groups.



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

## Forward-looking statements

This Management's Discussion and Analysis of Financial Condition and Results of Operations contains statements that are forward-looking statements within the meaning of the federal securities laws. All statements that do not concern historical facts are forward-looking statements and include, among other things, statements about our expectations, beliefs, intentions and/or strategies for the future. Without limiting the foregoing, statements including the words "expect," "intend," "will," "plan," "anticipate," "believe," "forecast," "guidance," "outlook," "goals," and similar expressions are intended to identify forward-looking statements. These forward-looking statements may include statements regarding our future operations, financial condition and prospects, such as expectations for treatment growth rates, revenue per treatment, expense growth, levels of the provision for uncollectible accounts receivable, operating income, cash flow, operating cash flow, estimated tax rates, estimated charges and accruals, capital expenditures, the development of new dialysis centers and dialysis center acquisitions, government and commercial payment rates, revenue estimating risk and the impact of our level of indebtedness on our financial performance, and including earnings per share. These statements involve substantial known and unknown risks and uncertainties that could cause our actual results to differ materially from those described in the forward-looking statements, including risks resulting from the concentration of profits generated by higher-paying commercial payor plans for which there is continued downward pressure on average realized payment rates, and a reduction in the number of patients under such plans, including as a result of restrictions or prohibitions on the use and/or availability of charitable premium assistance, which may result in the loss of revenues or patients, or our making incorrect assumptions about how our patients will respond to any change in financial assistance from charitable organizations; the extent to which the ongoing implementation of healthcare exchanges or changes in or new legislation, regulations or guidance, or enforcement thereof, including among other things those regarding the exchanges, results in a reduction in reimbursement rates for our services from and/or the number of patients enrolled in higher-paying commercial plans; a reduction in government payment rates under the Medicare End Stage Renal Disease program or other government-based programs; the impact of the Medicare Advantage benchmark structure; risks arising from potential and proposed federal and/or state legislation or regulation, including healthcare-related and labor-related legislation or regulation; the impact of the changing political environment and related developments on the current health care marketplace and on our business, including with respect to the future of the Affordable Care Act, the exchanges and many other core aspects of the current health care marketplace; uncertainties related to the impact of federal tax reform legislation; changes in pharmaceutical practice patterns, reimbursement and payment policies and processes, or pharmaceutical pricing, including with respect to calcimimetics; legal compliance risks, such as our continued compliance with complex government regulations and the provisions of our current Corporate Integrity Agreement (CIA) and current or potential investigations by various government entities and related government or private-party proceedings, and restrictions on our business and operations required by our corporate integrity agreement and other current or potential settlement terms, and the financial impact thereof and our ability to recover any losses related to such legal matters from third parties; continued increased competition from large- and medium-sized dialysis providers and others who compete, or will compete directly with us; our ability to reduce administrative expenses while maintaining targeted levels of service and operating performance, including our ability to achieve anticipated savings from our recent restructurings; our ability to maintain contracts with physician medical directors, changing affiliation models for physicians, and the emergence of new models of care introduced by the government or private sector that may erode our patient base and reimbursement rates, such as accountable care organizations (ACOs), independent practice associations (IPAs) and integrated delivery systems; our ability to complete acquisitions, mergers or dispositions that we might announce or be considering, on terms favorable to us or at all, or to integrate and successfully operate any business we may acquire or have acquired, or to successfully expand our operations and services to markets outside the United States, or to businesses outside of dialysis; noncompliance by us or our business associates with any privacy laws or any security breach involving the misappropriation, loss or other unauthorized use or disclosure of confidential information; the variability of our cash flows; factors that may impact our ability to repurchase stock under our stock repurchase program and the timing of any such stock repurchases, including market conditions, the price of our common stock, our cash flow position, borrowing capacity and leverage

ratios, and legal, regulatory and contractual requirements; the risk that we might invest material amounts of capital and incur significant costs in connection with the growth and development of our international operations, yet we might not be able to operate them profitably anytime soon, if at all; risks arising from the use of accounting estimates, judgments and interpretations in our financial statements; impairment of our goodwill, investments or other assets; the risks and uncertainties associated with the timing, conditions and receipt of regulatory approvals and satisfaction of other closing conditions of the DMG sale transaction and potential disruption in connection with the DMG sale transaction making it more difficult to maintain business and operational relationships; the risk that laws regulating the corporate practice of medicine could restrict the manner in which DMG conducts its business; the risk that the cost of providing services under DMG's agreements may exceed our compensation; the risk that reductions in reimbursement rates, including Medicare Advantage rates, and future regulations may negatively impact DMG's business, revenue and profitability; the risk that DMG may not be able to successfully establish a

presence in new geographic regions or successfully address competitive threats that could reduce its profitability; the risk that a disruption in DMG's healthcare provider networks could have an adverse effect on DMG's business operations and profitability; the risk that reductions in the quality ratings of health maintenance organization plan customers of DMG could have an adverse effect on DMG's business; the risk that health plans that acquire health maintenance organizations may not be willing to contract with DMG or may be willing to contract only on less favorable terms; and the other risk factors set forth in Part II, Item 1A. of this Quarterly Report on Form 10-Q. We base our forward-looking statements on information currently available to us, and we undertake no obligation to update or revise any forward-looking statements, whether as a result of changes in underlying factors, new information, future events or otherwise.

The following should be read in conjunction with our condensed consolidated financial statements.

## Consolidated results of operations

The Company has consisted of two major divisions, DaVita Kidney Care (Kidney Care) and DaVita Medical Group (DMG). Kidney Care is comprised of our U.S. dialysis and related lab services, our ancillary services and strategic initiatives, including our international operations, and our corporate administrative support. Our U.S. dialysis and related lab services business is our largest line of business and is a leading provider of kidney dialysis services in the U.S. for patients suffering from chronic kidney failure, also known as end stage renal disease (ESRD). DMG is a patient- and physician-focused integrated healthcare delivery and management company with over two decades of providing coordinated, outcomes-based medical care in a cost-effective manner.

In December 2017, we entered into an equity purchase agreement to sell our DMG division to Collaborative Care Holdings, LLC (Optum), a subsidiary of UnitedHealth Group Inc. The transaction is expected to close in 2018 and is subject to regulatory approvals and other customary closing conditions. As a result of this pending transaction, the DMG business has been classified as held for sale and its results of operations are reported as discontinued operations for all periods presented and DMG is not included below in this Management's Discussion and Analysis.

The following table is a summary of our consolidated operating results for the first quarter of 2018 compared with the prior sequential quarter and the same quarter of 2017:

	Three months ended					
	March 31, 2018		December 31, 2017		March 31, 2017	
	(dollars in millions)					
Revenues: <sup>(1)</sup>						
Dialysis and related lab patient service revenues	\$2,591		\$2,615		\$2,423	
Provision for uncollectible accounts	26		(149 )		(107 )	
Net dialysis and related lab patient service revenues	2,617		2,465		2,316	
Other revenues	233		316		316	
Total consolidated revenues	2,849	100 %	2,781	100 %	2,631	100 %
Operating expenses and charges:						
Patient care costs	2,036	71 %	1,942	70 %	1,852	70 %
General and administrative	267	9 %	265	10 %	263	10 %
Depreciation and amortization	143	5 %	144	5 %	133	5 %
Provision for uncollectible accounts	(6 )	— %	(6 )	— %	2	— %
Equity investment loss (income)	—	— %	3	— %	(1 )	— %
Investment and other asset impairments	—	— %	280	10 %	15	1 %
Goodwill impairment charges	—	— %	2	— %	24	1 %
Gain on changes in ownership interests, net	—	— %	—	— %	(6 )	— %
Gain on settlement, net	—	— %	—	— %	(527 )	(20 )%
Total operating expenses and charges	2,439	86 %	2,631	95 %	1,755	67 %
Operating income	\$411	14 %	\$150	5 %	\$876	33 %

Certain columns, rows or percentages may not sum or recalculate due to the use of rounded numbers.

On January 1, 2018, we adopted Revenue from Contracts with Customers (Topic 606) using the cumulative effect method for those contracts that were not substantially completed as of January 1, 2018. Results related to (1) performance obligations satisfied beginning on and after January 1, 2018 are presented under Topic 606, while results related to the satisfaction of performance obligations in the prior period continue to be reported in accordance with our historical accounting under Revenue Recognition (Topic 605).



The following table summarizes our consolidated revenues among our reportable segments:

	Three months ended		
	March 31, 2018	December 31, 2017	March 31, 2017
	(dollars in millions)		
Revenues: <sup>(1)</sup>			
U.S. dialysis and related lab services patient service revenues	\$ 2,508	\$ 2,536	\$ 2,373
Provision for uncollectible accounts	25	(148 )	(107 )
U.S. dialysis and related lab services net patient service revenues	2,533	2,388	2,266
Other revenues	5	5	5
Total U.S. dialysis and related lab services revenues	2,538	2,393	2,271
Other—Ancillary services and strategic initiatives other revenues	238	316	316
Other—Ancillary services and strategic initiatives patient service revenues	102	95	62
Total other—ancillary services and strategic initiatives revenues	340	410	378
Elimination of intersegment revenues	(29 )	(23 )	(18 )
Consolidated revenues	\$ 2,849	\$ 2,781	\$ 2,631

Certain columns, rows or percentages may not sum or recalculate due to the use of rounded numbers.

On January 1, 2018, we adopted Topic 606 using the cumulative effect method for those contracts that were not substantially completed as of January 1, 2018. Results related to performance obligations satisfied beginning on (1) and after January 1, 2018 are presented under Topic 606, while results related to the satisfaction of performance obligations in the prior period continue to be reported in accordance with our historical accounting under Revenue Recognition (Topic 605).

The following table summarizes consolidated operating income and adjusted consolidated operating income:

Three months ended

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	March 31, 2018	December 31, 2017	March 31, 2017
	(dollars in millions)		
Operating income:			
U.S. dialysis and related lab services	\$433	\$ 459	\$945
Other—Ancillary services and strategic initiatives	(7 )	(296 )	(58 )
Corporate administrative support	(16 )	(12 )	(11 )
Total consolidated operating income	\$411	\$ 150	\$876
Reconciliation of non-GAAP measures:			
Goodwill impairment charges	\$—	\$ —	\$24
Impairment of investments	—	280	—
Impairment of assets	—	—	15
Gain on settlement, net	—	—	(527 )
Equity investment income related to gain on settlement	—	—	(3 )
Gain on APAC JV ownership changes	—	—	(6 )
Adjusted consolidated operating income <sup>(1)</sup>	\$411	\$ 430	\$380

Certain columns or rows may not sum or recalculate due to the use of rounded numbers.

For the periods presented in the table above adjusted operating income is defined as operating income before certain items which we do not believe are indicative of ordinary results, including goodwill impairment charges, investment and other asset impairments, a net settlement gain, and gains on ownership changes. Adjusted operating income as so defined is a non-GAAP measure and is not intended as a substitute for GAAP operating income. We (1) have presented these adjusted amounts because management believes that these presentations enhance a user's understanding of our normal consolidated operating income by excluding certain items which we do not believe are indicative of our ordinary results of operations. As a result, adjusting for these amounts allows for comparison to our normalized prior period results.

#### Consolidated revenues

Consolidated revenues for the first quarter of 2018 increased by approximately \$68 million, or 2.4%, as compared to the fourth quarter of 2017. This increase was primarily driven by the increase in calcimimetics revenue, as discussed below. Our U.S. dialysis and related lab services revenues increased by approximately \$145 million, primarily due to the administration of calcimimetics and an increase in Medicare bad debt revenue offset by one fewer treatment day, as discussed below. This was partially offset by a decrease of \$70 million in our ancillary services and strategic initiatives net revenues, primarily due to a decline in volume in our pharmaceutical business due to calcimimetics. Ancillary services and strategic initiatives net revenues also decreased due to a reduction in shared savings revenue recognized by our ESRD Seamless Care Organization (ESCO) joint ventures, partially offset by increases in revenues from international expansion, shared savings recognized at DaVita Health Solutions, and VillageHealth revenues from special needs plans, as described below.

Effective January 1, 2018, both oral and IV forms of calcimimetics, a drug class taken by many patients with ESRD to treat mineral bone disorder, became the financial responsibility of our U.S. dialysis and lab services business for our Medicare patients and are included in our payment under Medicare Part B. During the pass-through period, Medicare payment for calcimimetics will be based on a pass through rate of the average sales price plus approximately 4%. CMS has stated intentions to enter calcimimetics into the ESRD bundle in approximately two years. Previously, calcimimetics were reimbursed for Medicare patients through Part D once dispensed from traditional pharmacies, including DaVita Rx.

Consolidated revenues for the first quarter of 2018 increased by approximately \$218 million, or 8.3%, as compared to the first quarter of 2017. This increase was primarily driven by the increase in calcimimetics revenue, as discussed above. Our U.S. dialysis and related lab services revenues increased \$267 million, primarily due to an increase in revenue due to the administration of calcimimetics, an increase in Medicare bad debt revenue, and volume growth from additional treatments, as described below. This increase in consolidated revenues was partially offset by a decrease of approximately \$38 million in our ancillary services and strategic initiatives revenues, primarily due to a decline in volume in our pharmaceutical business due to calcimimetics. Ancillary services and strategic initiatives net revenues also decreased due to a reduction in shared savings revenue recognized by our ESCO joint ventures, partially offset by increases in revenues from international expansion, shared savings recognized at DaVita Health Solutions, and VillageHealth revenues from special needs plans, as described below.

#### Consolidated operating income

Consolidated operating results for the first quarter of 2018 increased by approximately \$261 million as compared to the fourth quarter of 2017, which included an impairment of \$280 million on our investment in the Asia Pacific joint venture (APAC JV). Excluding this item, adjusted consolidated operating income for the first quarter of 2018 decreased by \$19 million due to a decrease in U.S. dialysis and related lab services operating income of \$26 million and an increase in expenses in our corporate administrative support of \$4 million, partially offset by a decrease in adjusted operating losses in our ancillary and strategic initiatives of \$9 million, as discussed below.

Consolidated operating results for the first quarter of 2018 decreased by \$465 million as compared to the first quarter in 2017, which included an adjustment to the gain on the APAC JV ownership change of \$6 million, a net gain on a settlement with the U.S. Department of Veterans Affairs (VA) of \$530 million, a goodwill impairment charge of \$24 million related to our vascular access reporting unit, and an asset impairment of \$15 million related to the restructuring of our pharmacy business. Excluding these items from the first quarter of 2017, adjusted consolidated operating income for the first quarter of 2018 increased by \$31 million due to an increase in adjusted operating income in U.S. dialysis and related lab services of \$18 million and a decrease in adjusted operating losses in our ancillary and strategic initiatives of \$18 million, partially offset by an increase in expenses in our corporate administrative support of \$5 million, as described below.



## U.S. dialysis and related lab services business

## Results of operations

	Three months ended		
	March 31, 2018	December 31, 2017	March 31, 2017
	(dollars in millions, except per treatment data)		
Revenues: <sup>(1)</sup>			
U.S. dialysis and related lab services patient service revenues	\$2,508	\$2,536	\$2,373
Provision for uncollectible accounts	25	(148)	(107)
U.S. dialysis and related lab services net patient service revenues	2,533	2,388	2,266
Other revenues	5	5	5
Total U.S. dialysis and related lab services revenues	2,538	2,393	2,271
Operating expenses and charges:			
Patient care costs	1,779	1,619	1,548
General and administrative	196	186	188
Depreciation and amortization	135	134	125
Equity investment income	(5)	(5)	(8)
Gain on settlement, net	—	—	(527)
Total operating expenses and charges	2,105	1,934	1,326
Operating income	\$433	\$459	\$945
Reconciliation of non-GAAP measures:			
Gain on settlement, net	—	—	(527)
Equity investment income related to gain on settlement	—	—	(3)
Adjusted operating income <sup>(2)</sup>	\$433	\$459	\$415
Dialysis treatments	7,174,026	7,244,555	6,804,384
Average dialysis treatments per treatment day	92,568	92,287	88,369
Average dialysis and related lab services net revenue per treatment	\$353.05	\$329.68	\$333.00

Certain columns or rows may not sum or recalculate due to the use of rounded numbers.

On January 1, 2018, we adopted Topic 606 using the cumulative effect method for those contracts that were not substantially completed as of January 1, 2018. Results related to performance obligations satisfied beginning on (1) and after January 1, 2018 are presented under Topic 606, while results related to the satisfaction of performance obligations in the prior period continue to be reported in accordance with our historical accounting under Revenue Recognition Topic 605.

For the periods presented in the table above adjusted operating income is defined as operating income before certain items which we do not believe are indicative of ordinary results, including a net settlement gain. Adjusted operating income as so defined is a non-GAAP measure and is not intended as a substitute for GAAP operating (2) income. We have presented these adjusted amounts because management believes that these presentations enhance a user's understanding of our normal consolidated operating income by excluding certain items which we do not believe are indicative of our ordinary results of operations. As a result, adjusting for these amounts allows for comparison to our normalized prior period results.

## Revenues

Dialysis and related lab services' revenues for the first quarter of 2018 increased by approximately \$145 million, or 6.1%, as compared to the fourth quarter of 2017. The increase in dialysis and related lab services' revenues was principally due to an increase in average net revenue per treatment of \$23, partially offset by a decrease in the number of treatments. The increase was primarily related to the administration of calcimimetics, as discussed above, and an

increase in acute revenues due to seasonality. The increase also resulted from an increase in Medicare bad debt revenue of \$24 million due to a policy election made under the new revenue standard to only apply the new guidance to contracts that were not substantially completed as of January 1, 2018. The decrease in the number of treatments was primarily due to one fewer treatment day during the first quarter of 2018 as compared to the fourth quarter of 2017.

Dialysis and related lab services' revenues for the first quarter of 2018 increased by approximately \$267 million, or 11.8%, as compared to the first quarter of 2017. The increase in net revenues was principally due to an increase in our average dialysis net revenue per treatment of approximately \$20 and volume growth from additional treatments. This increase was primarily related to the administration of calcimimetics, as discussed above, as well as the increase in Medicare bad debt revenue of \$24 million due to a policy election made under the new revenue standards. The increase in the number of treatments was primarily attributable to acquired and non-acquired treatment growth and approximately one additional treatment day during the first quarter of 2018 as compared to the first quarter of 2017. In November 2017, CMS published the 2018 final rule for the ESRD Prospective Payment System (PPS), which increased dialysis facilities' bundled payment rate for 2018 relative to prior years. In particular, CMS projects that the 2018 final rule for the ESRD PPS will (i) increase the total payments to all ESRD facilities by 0.5% in 2018 compared to 2017; (ii) increase total payments to hospital-based ESRD facilities by 0.7% in 2018 compared to 2017; and (iii) increase total payments for freestanding facilities by 0.5% in 2018 compared to 2017. The 2018 final rule for ESRD PPS also implements changes to the PPS outlier policy, broadening the pricing methodologies used to determine the cost of certain service drugs and biologicals in computing outlier payments when average sales price data is not available.

#### Operating expenses and charges

**Patient care costs.** Dialysis and related lab services' patient care costs of approximately \$248 per treatment for the first quarter of 2018 increased by approximately \$25 per treatment as compared to the fourth quarter of 2017. The increase was primarily related to the administration of calcimimetics, an increase in labor and benefits costs and an increase in insurance costs. The increase in labor and benefits costs was primarily due to the 401(k) matching program that began in 2018, an increase in payroll taxes, and a decrease in productivity. These increases were partially offset by a decrease in travel expenses and profit sharing expense.

Dialysis and related lab services' patient care costs per treatment for the first quarter of 2018 increased by approximately \$21 per treatment as compared to the first quarter of 2017. The increase was primarily related to the administration of calcimimetics, an increase in labor and benefits costs related to clinical rate increases and the 401(k) matching program that began in 2018, as well as an increase in other direct operating expenses associated with our dialysis centers. These increases were partially offset by a decrease in pharmaceutical costs and intensity.

**General and administrative expenses.** Dialysis and related lab services' general and administrative expenses of approximately \$196 million in the first quarter of 2018 increased by approximately \$10 million as compared to the fourth quarter of 2017. The increase in general and administrative expenses was primarily due to increases in long-term incentive compensation expense, benefit costs related to payroll taxes and the 401(k) matching program that began in 2018, consulting expenses, occupancy costs and asset impairments related to expected center closures. These increases were partially offset by decreases in contract labor and travel expenses.

Dialysis and related lab services' general and administrative expenses for the first quarter of 2018 increased by approximately \$8 million as compared to the first quarter of 2017. This increase was primarily due to increases in benefit costs related to the 401(k) matching program that began 2018, professional fees, asset impairments related to expected center closures and occupancy costs, partially offset by decreases in contract labor and travel expenses.

**Depreciation and amortization.** Depreciation and amortization for dialysis and related lab services was approximately \$135 million for the first quarter of 2018, \$134 million for the fourth quarter of 2017, and \$125 million for the first quarter of 2017. The increase in depreciation and amortization in the first quarter of 2018, as compared to the fourth quarter of 2017 and the first quarter of 2017, was primarily due to growth in newly developed centers as well as acquired centers.

**Equity investment income.** Equity investment income for dialysis and related lab services was approximately \$5 million for the first quarter of 2018, \$5 million for the fourth quarter of 2017, and \$8 million for the first quarter of 2017. Equity investment income in the first quarter of 2018 decreased by approximately \$3 million as compared to the same period in 2017 primarily due to income recognized at our nonconsolidated joint ventures in the first quarter of 2017 related to the gain on the settlement with the VA, as discussed below.

Gain on settlement, net. During the first quarter of 2017, we reached an agreement with the government for amounts owed to us for dialysis services provided from 2005 through 2011 to patients covered by the VA. As a result of this settlement we recognized a one-time net gain of \$527 million, as well as equity investment income of \$3 million, for our share of the

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settlement income recognized by our nonconsolidated joint ventures. As a result, the total effect of this settlement on our operating income was an increase of \$530 million.

#### Segment operating income

Dialysis and related lab services' operating income for the first quarter of 2018 decreased by approximately \$26 million as compared to the fourth quarter of 2017. Operating income was negatively impacted by a decrease in treatments due to one fewer treatment day in the first quarter of 2018 and increases in labor and benefits costs, insurance costs, long-term incentive compensation expense, consulting costs and asset impairments. Operating income was positively impacted by the administration of calcimimetics, a reduction in travel expenses, as well as a decrease in profit sharing costs, as discussed above.

Dialysis and related lab services' operating income for the first quarter of 2018 decreased by approximately \$512 million as compared to the first quarter of 2017, which included a net gain on settlement of \$530 million. Excluding this item from the first quarter of 2017, dialysis and lab services' adjusted consolidated operating income for the first quarter of 2018 increased by approximately \$18 million as compared to the first quarter of 2017. This increase in adjusted operating income was principally due the administration of calcimimetics, as discussed above, as well as approximately one additional treatment day in the first quarter of 2018. Adjusted operating income also benefited from reduced pharmaceutical costs and intensity. Adjusted operating income was negatively impacted by higher labor and benefits costs, increases in asset impairments, other direct operating expenses associated with our dialysis centers, occupancy costs, and long-term incentive compensation expense.

#### Other—Ancillary services and strategic initiatives business

Our other operations include ancillary services and strategic initiatives, which are primarily aligned with our U.S. dialysis and related lab services business, along with our international dialysis operations. As of March 31, 2018, these consisted primarily of pharmacy services, disease management services, vascular access services, clinical research programs, physician services, direct primary care, ESRD seamless care organizations, and comprehensive care as well as our international operations. The ancillary services and strategic initiatives generated approximately \$340 million in revenues for the first quarter of 2018, representing approximately 11.6% of our consolidated revenues. We expect to add additional service offerings to our business and pursue additional strategic initiatives in the future as circumstances warrant, which could include healthcare services not related to dialysis. In addition, in connection with our previously announced capital allocation strategy, in 2018 we plan to continue our evaluation of strategic alternatives for various assets in our portfolio. Any significant change in market conditions, or business performance, or in the political, legislative or regulatory environment, may impact the economic viability of any of our strategic initiatives. If any of our ancillary services or strategic initiatives, such as our pharmacy services and our international operations, are unsuccessful, it would have a negative impact on our business, results of operations and financial condition, and we may determine to exit the line of business. We could incur significant termination costs if we were to exit certain of these lines of business. In addition, we may incur a material write off or an impairment of our investment, including goodwill, in one or more of our ancillary services or strategic initiatives. In that regard, we have taken, and may in the future take, impairment charges related to our ancillary services and strategic initiatives, including in our international and pharmacy businesses.

As of March 31, 2018, we provided dialysis and administrative services to a total of 241 outpatient dialysis centers located in 10 countries outside of the United States. The total net revenues generated from our international operations are provided below.

The following table reflects the results of operations for our ancillary services and strategic initiatives:

	Three months ended		
	March	December	March
	31,	31,	31,
	2018	2017	2017
	(dollars in millions)		
U.S. revenues: <sup>(1)</sup>			
Other revenues	\$237	\$ 316	\$315
Total	237	316	315
International revenues: <sup>(1)</sup>			
Dialysis patient service revenues	102	94	62
Other revenues	1	1	1
Total	103	95	63
Total net revenues <sup>(1)</sup>	\$340	\$ 410	\$378
Operating expenses and charges:			
Operating and other general expenses	\$347	\$ 426	\$403
Goodwill impairment	—	2	24
Investment and other asset impairments	—	280	15
Gain from APAC JV ownership changes	—	—	(6 )
Total operating expenses and charges	347	707	436
Total ancillary services and strategic initiatives operating loss	\$(7 )	\$( 296 )	\$(58 )
U.S. operating loss	\$(5 )	\$( 2 )	\$(53 )
Reconciliation of non-GAAP:			
Goodwill impairment charges	—	—	24
Impairment of other assets	—	—	15
Adjusted operating loss <sup>(2)</sup>	\$(5 )	\$( 2 )	\$(14 )
International operating loss	\$(2 )	\$( 294 )	\$(5 )
Reconciliation of non-GAAP:			
Impairment of investment	—	280	—
Gain on APAC JV ownership changes	—	—	(6 )
Adjusted operating loss <sup>(2)</sup>	\$(2 )	\$( 14 )	\$(11 )
Total adjusted ancillary services and strategic initiatives operating loss <sup>(2)</sup>	\$(7 )	\$( 16 )	\$(25 )

Certain columns, rows or percentages may not sum or recalculate due to the use of rounded numbers.

On January 1, 2018, we adopted Topic 606 using the cumulative effect method for those contracts that were not substantially completed as of January 1, 2018. Results related to performance obligations satisfied beginning on (1) and after January 1, 2018 are presented under Topic 606, while results related to the satisfaction of performance obligations in the prior period continue to be reported in accordance with our historical accounting under Revenue Recognition Topic 605.

For the periods presented in the table above, adjusted operating loss is defined as operating loss before certain items which we do not believe are indicative of ordinary results, including goodwill impairment charges, investment and other asset impairments, and gains on ownership changes. Adjusted operating loss as so defined is (2) a non-GAAP measure and is not intended as a substitute for GAAP operating loss. We have presented these adjusted amounts because management believes that these presentations enhance a user's understanding of our normal consolidated operating income by excluding certain items which we do not believe are indicative of our ordinary results of operations. As a result, adjusting for these amounts allows for comparison to our normal prior period results.

Revenues

Revenues from our ancillary services and strategic initiatives for the first quarter of 2018 decreased by approximately \$70 million, or 17.1%, as compared to the fourth quarter of 2017. This decrease was primarily due to a decline in volume in our pharmaceutical business due to a shift of calcimimetics to reimbursement for Medicare patients under Medicare Part B which is

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now billed in our U.S. dialysis and related lab services business, as discussed above, as well as a decrease in shared savings revenue recognized by our ESCO joint ventures, partially offset by an increase in revenues from our international expansion due to acquired and non-acquired growth, an increase in shared savings recognized at DaVita Health Solutions and an increase in VillageHealth revenues from special needs plans.

Revenues from our ancillary services and strategic initiatives for the first quarter of 2018 decreased by approximately \$38 million, or 10.1%, as compared to the first quarter of 2017. This decrease was primarily due to a decline in volume in our pharmaceutical business due to a shift of calcimimetics to reimbursement for Medicare patients under Medicare Part B which is now billed in our U.S. dialysis and related services lab business as well as a decrease in shared savings revenue recognized by our ESCO joint ventures, partially offset by an increase in revenues from our international expansion due to acquired and non-acquired growth, an increase in shared savings recognized at DaVita Health Solutions and an increase in VillageHealth revenues from special needs plans.

#### Operating and general expenses

Ancillary services and strategic initiatives operating expenses for the first quarter of 2018 decreased by approximately \$79 million from the fourth quarter of 2017, primarily related to decreases in pharmaceutical costs due to decreased volume related to calcimimetics, partially offset by an increase in medical costs at VillageHealth related to the cost of calcimimetics in our special needs plans.

Ancillary services and strategic initiatives operating expenses for the first quarter of 2018 decreased by approximately \$56 million, as compared to the first quarter of 2017, primarily related to decreases in pharmaceutical costs due to decreased volume related to calcimimetics, partially offset by an increase in medical costs at VillageHealth related to the cost of calcimimetics in our special needs plans and an increase in expenses associated with our international operations.

Goodwill and other asset impairment charges. During the first quarter of 2017, we recognized goodwill impairment charges of \$24 million at our vascular access reporting unit. This charge resulted primarily from changes in our outlook as our partners and operators continued to evaluate potential changes in operations, including termination of their management services agreements and center closures, as a result of recent changes in Medicare reimbursement. There is no goodwill remaining at our vascular access reporting unit. During the first quarter of 2017, we also recognized other asset impairment charges of \$15 million related to a planned restructuring of our pharmacy business. During the fourth quarter of 2017, we recognized a non-cash other-than-temporary impairment charge of \$280 million on our investment in the Asia Pacific joint venture (APAC JV) due to changes in our expectation for the joint venture resulting from continuing market research and assessments by both us and the APAC JV.

Gain on changes in ownership interests in Asia Pacific joint venture. As a result of our agreement with Khazanah Nasional Berhad (Khazanah) and Mitsui and Co., Ltd (Mitsui) concerning the APAC JV, we recorded an additional \$6 million non-cash gain during the three months ended March 31, 2017 related to a change in estimate of pending post-closing adjustments for the formation of this joint venture.

#### Segment operating losses

Ancillary services and strategic initiatives operating loss for the first quarter of 2018 decreased by approximately \$289 million from the fourth quarter of 2017, which included an impairment of \$280 million on our investment in the APAC JV, as described above. Excluding this item, adjusted operating losses decreased by \$9 million, primarily due to improvement in our international business and shared savings recognized at DaVita Health Solutions, partially offset by increased losses at our pharmacy business, as described above.

Ancillary services and strategic initiatives operating loss for the first quarter of 2018 decreased by approximately \$51 million from the first quarter of 2017, which included an adjustment to the gain on the APAC JV ownership change of \$6 million, a goodwill impairment charge of \$24 million related to our vascular access reporting unit, and an asset impairment of \$15 million related to the restructuring of our pharmacy business. Excluding these items from the first quarter of 2017, adjusted operating losses decreased by \$18 million, primarily due to shared savings recognized at DaVita Health Solutions in the first quarter of 2018, improvement in our international business offset by an increase in adjusted losses at our pharmacy business.





#### Corporate-level charges

Debt expense. Debt expense was \$114 million in the first quarter of 2018, \$109 million in the fourth quarter of 2017 and \$104 million in the first quarter of 2017. Debt expense increased by \$5 million as compared to the fourth quarter of 2017 and by \$10 million as compared to the first quarter of 2017, primarily due to an increase in our average interest rate and due to an increase in our average outstanding balance.

Corporate administrative support. Corporate administrative support consists primarily of labor, benefits and long-term incentive compensation expense, as well as professional fees for departments which provide support to all of our various operating lines of business. This is partially offset by internal management fees charged to our other lines of business for that support.

Corporate administrative support costs were approximately \$16 million in the first quarter of 2018, \$12 million in the fourth quarter of 2017 and \$11 million in the first quarter of 2017. Corporate administrative support costs in the first quarter of 2018 as compared to the fourth quarter of 2017 and the first quarter of 2017 increased primarily due to a reduction in internal management fees charged to our ancillary lines of business.

Other income. Other income was \$5 million for the first quarter of 2018, \$5 million for the fourth quarter of 2017 and \$4 million in the first quarter of 2017. The slight increase in other income for the first quarter of 2018 as compared to the first quarter of 2017 was primarily due to foreign currency gains offset by decreases in interest and investment income.

#### Noncontrolling interests

Net income attributable to noncontrolling interests was \$47 million for the first quarter of 2018 compared to \$37 million for the fourth quarter of 2017 and \$53 million for the first quarter of 2017. The increase in net income attributable to noncontrolling interests in the first quarter of 2018 compared to the fourth quarter of 2017 was primarily due to noncontrolling interest recognized at DMG. The decrease in net income attributable to noncontrolling interests in the first quarter of 2018 compared to the first quarter of 2017 was primarily due to additional income to noncontrolling interests related to the net gain on the settlement with the VA of \$24 million and an increase in the profitability of certain joint ventures, partially offset by a net \$7 million decrease in noncontrolling interests related to the goodwill impairment at our vascular access reporting unit in the first quarter of 2017.

#### Accounts receivable

Our consolidated total accounts receivable balances at March 31, 2018 and December 31, 2017 were \$1,831 million and \$1,715 million, respectively, which represented approximately 59 days and 57 days, respectively, net of allowance for uncollectible accounts. The increase in consolidated day sales outstanding (DSO) of two days was primarily related to our other ancillary services and strategic initiatives businesses, offset by a decrease of one day in DSO at our U.S. dialysis and related lab services business as we continue to adjust and refine our collection operations for new protocols. Our DSO calculation is based on the current quarter's average revenues per day. There were no significant changes during the first quarter of 2018 from the fourth quarter of 2017 in the amount of unreserved accounts receivable over one year old or the amounts pending approval from third-party payors.

#### Liquidity and capital resources

Consolidated cash flow from operations during the first quarter of 2018 was \$363 million, of which \$206 million was from continuing operations, compared with consolidated cash flows during the first quarter of 2017 of \$865 million, of which \$770 million was from continuing operations. The decrease in cash flow from continuing operations in the first quarter of 2017 was primarily due to the payment received in the first quarter of 2017 from the settlement with the VA as well as the timing of tax payments and other working capital items. Non-operating cash outflows for the first quarter of 2018 included capital asset expenditures of \$232 million, including \$114 million for new center developments and relocations and \$119 million for maintenance and information technology. In addition, during the quarter ended March 31, 2018, we spent \$17 million for acquisitions, paid distributions to noncontrolling interests of \$45 million, and repurchased a total of 4,197,304 shares of our common stock for \$298 million, of which \$16 million remained unsettled at March 31, 2018. Non-operating cash outflows for the first quarter of 2017 included capital asset expenditures of \$215 million, including \$127 million for new center developments and relocations and \$88 million for maintenance and information technology. In addition, we spent \$77 million for acquisitions and paid distributions to noncontrolling interests of \$43 million.

During the first quarter of 2018, our U.S. dialysis and related lab services business opened 28 dialysis centers, acquired one dialysis center, closed one dialysis center and added one center which we operate under a management and administrative

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service agreement. In addition, our international dialysis operations acquired four dialysis centers and closed one dialysis center. Our APAC JV also acquired two dialysis centers and closed one dialysis center.

During the first quarter of 2017, our U.S. dialysis and related lab services business opened 24 dialysis centers, acquired 12 dialysis centers and closed three dialysis centers. In addition, our international dialysis operations acquired three dialysis centers and opened four dialysis centers. Our APAC JV also opened one dialysis center.

During the first quarter of 2018, our DMG business acquired one private medical practice. During the first quarter of 2017, DMG acquired one private medical practice and one primary care physician practice.

Also during the first three months of 2018, we made mandatory principal payments under our senior secured credit facilities totaling \$25.0 million on Term Loan A and \$8.8 million on Term Loan B.

#### Cap agreements

As of March 31, 2018, we maintained several currently effective interest rate cap agreements that were entered into in November 2014 with notional amounts totaling \$3.5 billion. These cap agreements became effective September 30, 2016 and have the economic effect of capping the LIBOR variable component of our interest rate at a maximum of 3.50% on an equivalent amount of our debt. These cap agreements expire on June 30, 2018. As of March 31, 2018, these cap agreements had an immaterial fair value. During the three months ended March 31, 2018, we recognized debt expense of \$2.1 million from these caps. During the three months ended March 31, 2018, we recorded an immaterial loss in other comprehensive income due to a decrease in the unrealized fair value of these cap agreements. As of March 31, 2018, we also maintained several forward interest rate cap agreements that were entered into in October 2015 with notional amounts totaling \$3.5 billion. These forward cap agreements will become effective June 29, 2018 and will have the economic effect of capping the LIBOR variable component of our interest rate at a maximum of 3.50% on an equivalent amount of our debt. These cap agreements expire on June 30, 2020. As of March 31, 2018, the total fair value of these cap agreements was an asset of approximately \$2.4 million. During the three months ended March 31, 2018, we recorded a gain of \$1.4 million in other comprehensive income due to an increase in the unrealized fair value of these forward cap agreements.

#### Other items

On March 29, 2018, we entered into an Increase Joinder Agreement under our existing senior secured credit facilities. Pursuant to this Increase Joinder Agreement, we entered into an additional \$995 million Term Loan A-2. The new Term Loan A-2 bears interest at LIBOR plus an interest rate margin of 1.00%. As of March 31, 2018, we have initially drawn \$452 million of the Term Loan A-2 and we can draw up to an incremental \$543 million on Term Loan A-2 through its maturity date in June 2019.

As of March 31, 2018, our Term Loan B debt bears interest at LIBOR plus an interest rate margin of 2.75%. Term Loan B is subject to interest rate caps if LIBOR should rise above 3.50%. Term Loan A bears interest at LIBOR plus an interest rate margin of 2.00%. The capped portion of Term Loan A is \$131.3 million if LIBOR should rise above 3.50%. In addition, the uncapped portion of Term Loan A, which is subject to the variability of LIBOR, is \$618.8 million. Term Loan A-2 is subject to the variability of LIBOR plus an interest rate margin of 1.00%. Interest rates on our senior notes are fixed by their terms.

Our weighted average effective interest rate on the senior secured credit facilities at the end of the quarter was 4.67%, based on the current margins in effect of 2.00% for Term Loan A, 1.00% for Term Loan A-2, and 2.75% for Term Loan B, as of March 31, 2018.

Our overall weighted average effective interest rate during the quarter ended March 31, 2018 was 4.87% and as of March 31, 2018 was 4.98%.

As of March 31, 2018, our interest rates are fixed on approximately 51% of our total debt.

As of March 31, 2018, we had no outstanding balance on our \$1.0 billion revolving line of credit under our senior secured credit facilities, of which approximately \$14.4 million was committed for outstanding letters of credit. We also have approximately \$22.4 million of additional outstanding letters of credit related to our Kidney Care business and \$0.2 million of committed outstanding letters of credit related to our DMG business, which is backed by a certificate of deposit.



We believe that we will generate significant operating cash flows and will have sufficient liquidity to fund our scheduled debt service and other obligations for the foreseeable future, including the next 12 months, under the terms of our debt agreements. Our primary sources of liquidity are cash from operations and cash from borrowings.

#### Goodwill

We elected to early adopt ASU No. 2017-04, Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment, effective January 1, 2017. The amendments in this ASU simplify the test for goodwill impairment by eliminating the second step in the assessment. All goodwill impairment tests performed during 2017 and 2018 have been performed under this new guidance.

During the three months ended March 31, 2018, we did not recognize any goodwill impairment charges.

During the three months ended March 31, 2017, we recognized a goodwill impairment charge of \$24 million at our vascular access reporting unit. This charge resulted primarily from changes in our outlook as our partners and operators continued to evaluate potential changes in operations, including termination of their management services agreements and center closures, as a result of recent changes in Medicare reimbursement. There is no goodwill remaining at our vascular access reporting unit.

For the reporting units considered at risk as of December 31, 2017 listed in the table below, there have been no major changes in the business, prospects, or expected future results of these reporting units from their latest assessment date through March 31, 2018. Based on the most recent assessments, we determined that reductions in reimbursement rates, changes in actual or expected growth rates, or other significant adverse changes in expected future cash flows or valuation assumptions could result in goodwill impairment charges in the future for the following reporting units, which remain at risk of goodwill impairment as of March 31, 2018:

Reporting unit	Goodwill		Sensitivities	
	balance as of March 31, 2018 (in millions)	Carrying amount coverage <sup>(1)</sup>	Operating income <sup>(2)</sup>	Discount rate <sup>(3)</sup>
Kidney Care Germany	\$ 338	13.7%	(1.6)%	(11.1)%
Kidney Care Portugal	\$ 48	16.9%	(1.9)%	(6.0)%
Kidney Care Poland	\$ 48	11.8%	(1.9)%	(6.0)%

(1) Excess of estimated fair value of the reporting unit over its carrying amount as of the latest assessment date.

(2) Potential impact on estimated fair value of a sustained, long-term reduction of 3% in operating income as of the latest assessment date.

(3) Potential impact on estimated fair value of an increase in discount rates of 100 basis points as of the latest assessment date.

Except as described above, none of our various other reporting units were considered at risk of significant goodwill impairment as of March 31, 2018. Since the dates of our last annual goodwill impairment tests, there have been certain developments, events, changes in operating performance and other changes in key circumstances that have affected our businesses. However, these changes did not cause management to believe it is more likely than not that the fair value of any of our reporting units would be less than their respective carrying amounts as of March 31, 2018.

#### Long-term incentive compensation

Long-term incentive program (LTIP) compensation includes both stock-based awards (principally stock-settled stock appreciation rights, restricted stock units and performance stock units) as well as long-term performance-based cash awards. Long-term incentive compensation expense, which was primarily general and administrative in nature, was attributed among our U.S. dialysis and related lab services business, corporate administrative support, and ancillary services and strategic initiatives.

Our stock-based compensation awards are measured at their estimated fair values on the date of grant if settled in shares or at their estimated fair values at the end of each reporting period if settled in cash. The value of stock-based awards so measured is recognized as compensation expense on a cumulative straight-line basis over the vesting terms of the awards, adjusted for expected forfeitures.

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During the three months ended March 31, 2018, we granted 11,490 stock-settled stock appreciation rights with an aggregate grant-date fair value of \$0.2 million and a weighted-average expected life of approximately 3.7 years. We also granted 60,339 stock units with an aggregate grant-date fair value of \$4 million and a weighted-average expected life of approximately 1.0 years.

Long-term incentive compensation expense of \$15 million in the first quarter of 2018 was flat as compared to the fourth quarter of 2017 and the first quarter of 2017.

As of March 31, 2018, there was \$92 million in total estimated but unrecognized compensation expense for LTIP awards outstanding, including \$62 million related to stock-based compensation arrangements under our equity compensation and employee stock purchase plans. We expect to recognize the performance-based cash component of these LTIP costs over a weighted average remaining period of 1.1 years and the stock-based component of these LTIP costs over a weighted average remaining period of 1.3 years.

#### Stock repurchases

During the quarter ended March 31, 2018, we repurchased a total of 4,197,304 shares of our common stock for \$298 million at an average price of \$71.09 per share. We have also repurchased 4,350,135 shares of our common stock for \$276 million at an average price of \$63.44 per share, subsequent to March 31, 2018.

On October 10, 2017, our Board of Directors approved an additional share repurchase authorization in the amount of approximately \$1.3 billion. This share repurchase authorization was in addition to the approximately \$247 million remaining at that time under our Board of Directors' prior share repurchase authorization announced in July 2016. Accordingly, as of May 2, 2018, we have a total of approximately \$545 million available under the current Board repurchase authorizations for additional share repurchases. Although these share repurchase authorizations do not have expiration dates, we remain subject to share repurchase limitations under the terms of our senior secured credit facilities and the indentures governing our senior notes.

#### Off-balance sheet arrangements and aggregate contractual obligations

In addition to the debt obligations reflected on our balance sheet, we have commitments associated with operating leases and letters of credit, as well as potential obligations associated with our equity investments in nonconsolidated businesses and to dialysis centers that are wholly-owned by third parties. Substantially all of our U.S. dialysis facilities are leased. We have potential obligations to purchase the equity interests held by third parties in several of our majority-owned joint ventures and other nonconsolidated entities. These obligations are in the form of put provisions that are exercisable at the third-party owners' discretion within specified periods as outlined in each specific put provision. If these put provisions were exercised, we would be required to purchase the third-party owners' equity interests at either the appraised fair market value or a predetermined multiple of earnings or cash flows attributable to the equity interests put to us, which is intended to approximate fair value. The methodology we use to estimate the fair values of noncontrolling interests subject to put provisions assumes the higher of either a liquidation value of net assets or an average multiple of earnings, based on historical earnings, patient mix and other performance indicators that can affect future results, as well as other factors. The estimated fair values of noncontrolling interests subject to put provisions are a critical accounting estimate that involves significant judgments and assumptions and may not be indicative of the actual values at which the noncontrolling interests may ultimately be settled, which could vary significantly from our current estimates. The estimated fair values of noncontrolling interests subject to put provisions can fluctuate and the implicit multiple of earnings at which these noncontrolling interests obligations may be settled will vary significantly depending upon market conditions including potential purchasers' access to the capital markets, which can impact the level of competition for dialysis and non-dialysis related businesses, the economic performance of these businesses and the restricted marketability of the third-party owners' equity interests. The amount of noncontrolling interests subject to put provisions that employ a contractually predetermined multiple of earnings rather than fair value are immaterial. For additional information see Note 11 to the condensed consolidated financial statements.

We also have certain other potential commitments to provide operating capital to several dialysis centers that are wholly-owned by third parties or businesses in which we maintain a noncontrolling equity interest as well as to physician-owned vascular access clinics or medical practices that we operate under management and administrative services agreements.





The following is a summary of these contractual obligations and commitments as of March 31, 2018 (in millions):

	Remainder of 2018	1-3 years	4-5 years	After 5 years	Total
Scheduled payments under contractual obligations:					
Long-term debt	\$ 121	\$4,520	\$1,269	\$3,312	\$9,222
Interest payments on the senior notes	156	710	401	202	1,469
Interest payments on Term Loan B <sup>(1)</sup>	119	387	—	—	506
Interest payments on Term Loan A <sup>(2)</sup>	21	13	—	—	34
Interest payments on Term Loan A-2 <sup>(2)</sup>	10	6	—	—	16
Kidney Care capital lease obligations	16	67	46	175	304
Kidney Care operating leases	349	1,194	610	1,129	3,282
DMG capital lease obligations	36	—	—	—	36
DMG operating leases	66	215	101	248	630
	\$ 894	\$7,112	\$2,427	\$5,066	\$15,499
Potential cash requirements under other commitments:					
Letters of credit	\$ 37	\$—	\$—	\$—	\$37
Noncontrolling interests subject to put provisions	651	202	94	88	1,035
Non-owned and minority owned put provisions	28	28	—	—	56
Operating capital advances	1	2	1	1	5
Purchase commitments	320	875	251	—	1,446
	\$ 1,037	\$1,107	\$346	\$89	\$2,579

(1) Assuming no changes to LIBOR-based interest rates as Term Loan B currently bears interest at LIBOR plus an interest rate margin of 2.75%.

(2) Based upon current LIBOR-based interest rates in effect at March 31, 2018 plus an interest rate margin of 2.00% for Term Loan A and plus an interest rate margin of 1.00% for Term Loan A-2.

In addition to the commitments listed above, we have committed to purchase a certain amount of our hemodialysis products and supplies at fixed prices through 2018 and a certain amount of our peritoneal dialysis products and supplies at fixed prices through 2022, as set forth in the contract for each year, from Baxter Healthcare Corporation (Baxter) in connection with purchase agreements. We also have an agreement with Fresenius Medical Care (Fresenius), currently extended through 2020, which commits us to purchase a certain amount of dialysis equipment, parts and supplies.

Our total expenditures for the three months ended March 31, 2018 on such products for Fresenius was approximately 3% and for Baxter hemodialysis products and supplies was 2% of our total U.S. dialysis and related lab services operating costs. The actual amount of such purchases in future years will depend upon a number of factors, including the operating requirements of our centers, the number of centers we acquire and growth of our existing centers.

In January 2017, we entered into a six year sourcing and supply agreement with Amgen USA Inc. (Amgen) that expires on December 31, 2022. Under the terms of this agreement, we will purchase EPO in amounts necessary to meet no less than 90% of our requirements for erythropoiesis stimulating agents (ESAs) through the expiration of the contract from Amgen. The actual amount of EPO that we will purchase will depend upon the amount of EPO administered during dialysis as prescribed by physicians and the overall number of patients that we serve.

Settlements of approximately \$34 million of existing income tax liabilities for unrecognized tax benefits, including interest, penalties and other long-term tax liabilities, are excluded from the table above as reasonably reliable estimates of their timing cannot be made.

Supplemental Information Concerning Certain Physician Groups and Unrestricted Subsidiaries

The following information is presented as supplemental data as required by the indentures governing our senior notes.



We provide services to certain physician groups, including those within our DMG business, which while consolidated in our financial statements for financial reporting purposes, are not subsidiaries of or owned by us, do not constitute “Subsidiaries” as defined in the indentures governing our outstanding senior notes, and do not guarantee those senior notes. In addition, we have entered into management agreements with these physician groups pursuant to which we receive management fees from the physician groups.

As of March 31, 2018, if these physician groups were not consolidated in our financial statements, our consolidated assets would have been approximately \$18.489 billion and our consolidated other liabilities would have been approximately \$3.271 billion. Our consolidated indebtedness would have remained approximately \$9.526 billion since almost all of these physician groups are classified as held for sale with DMG. For the quarter ended March 31, 2018, if these physician groups were not consolidated in our financial statements, our consolidated net income would have been reduced by approximately \$854 thousand. Our consolidated total net revenues and consolidated operating income would have remained approximately \$2.849 billion and \$410.7 million, respectively, since almost all of these physician groups are included in discontinued operations.

In addition, our DMG business owns a 67% equity interest in California Medical Group Insurance (CMGI), which is an Unrestricted Subsidiary as defined in the indentures governing our outstanding senior notes, and does not guarantee those senior notes. DMG's equity interest in CMGI is accounted for under the equity method of accounting, meaning that, although CMGI is not consolidated in our financial statements for financial reporting purposes, our consolidated income statement reflects our pro rata share of CMGI's net income within net loss from discontinued operations. For the three months ended March 31, 2018, excluding DMG's equity investment income attributable to CMGI, our consolidated net income would be lower by approximately \$490 thousand. See Note 23 to the consolidated financial statements for further details.

#### New Accounting Standards

See discussion of new accounting standards in Note 21 to the condensed consolidated financial statements included in Part I, Item 1 of this report.

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

## Interest rate sensitivity

The tables below provide information about our financial instruments that are sensitive to changes in interest rates. The table below presents principal repayments and current weighted average interest rates on our debt obligations as of March 31, 2018. The variable rates presented reflect the weighted average LIBOR rates in effect for all debt tranches plus interest rate margins in effect as of March 31, 2018. Term Loan A currently bears interest at LIBOR plus an interest rate margin of 2.00%. Term Loan A and the revolving line of credit are subject to adjustment depending upon changes in certain of our financial ratios, including a leverage ratio. Term Loan A-2 currently bears interest at LIBOR plus an interest rate margin of 1.00%. Term Loan B currently bears interest at LIBOR plus an interest rate margin of 2.75%.

	Expected maturity date							Total	Average interest rate	Fair Value
	2018	2019	2020	2021	2022	2023	Thereafter			
	(dollars in millions)									
Long term debt:										
Fixed rate	\$30	\$32	\$28	\$26	\$1,275	\$26	\$3,485	\$4,902	51.34 %	\$4,835
Variable rate	\$107	\$1,175	\$45	\$3,281	\$8	\$6	\$2	\$4,624	48.66 %	\$4,670
	Notional Contract maturity date									Fair Value
	Amount	2018	2019	2020	2021	2022	Receive variable			
	(dollars in millions)									
Cap agreements	\$7,000	\$3,500	\$—	\$3,500	\$—	\$—	LIBOR above 3.5%	\$2		

On March 29, 2018, we entered into an Increase Joinder Agreement under our senior secured credit facilities. Pursuant to this Increase Joinder Agreement, we entered into an additional \$995 million Term Loan A-2. The new Term Loan A-2 bears interest at LIBOR plus an interest rate margin of 1.00%. As of March 31, 2018, we have initially drawn \$452 million of the Term Loan A-2, and we can draw up to an incremental \$543 million on Term Loan A-2 through its maturity date in June 2019.

Our senior secured credit facilities, which include Term Loan A, Term Loan A-2, and Term Loan B, consist of various individual tranches of debt that can range in maturity from one month to twelve months (currently, all tranches are one month in duration). For Term Loan A, Term Loan A-2, and Term Loan B, each tranche bears interest at a LIBOR rate that is determined by the duration of such tranche plus an interest rate margin. The LIBOR variable component of the interest rate for each tranche is reset as such tranche matures and a new tranche is established. LIBOR can fluctuate significantly depending upon conditions in the credit and capital markets.

As of March 31, 2018, our Term Loan A bears interest at LIBOR plus an interest rate margin of 2.00%, our Term Loan A-2 bears interest at LIBOR plus an interest rate margin of 1.00%, and our Term Loan B debt bears interest at LIBOR plus an interest rate margin of 2.75%. LIBOR was higher than the 0.75% embedded LIBOR floor on Term Loan B, resulting in Term Loan B being subject to LIBOR-based interest rate volatility on the LIBOR variable component of our interest rate as of March 31, 2018. The LIBOR-based interest component is limited to a maximum LIBOR rate of 3.50% on the outstanding principal debt on Term Loan B and \$131.3 million on Term Loan A as a result of the interest rate cap agreements, as described below.

As of March 31, 2018, we maintained several currently effective interest rate cap agreements that were entered into in November 2014 with notional amounts totaling \$3.5 billion. These cap agreements became effective September 30, 2016 and have the economic effect of capping the LIBOR variable component of our interest rate at a maximum of 3.50% on an equivalent amount of our debt. These cap agreements expire on June 30, 2018. As of March 31, 2018, these cap agreements had an immaterial fair value. During the three months ended March 31, 2018, we recognized debt expense of \$2.1 million from these caps. During the three months ended March 31, 2018, we recorded an immaterial loss in other comprehensive income due to a decrease in the unrealized fair value of these cap agreements. As of March 31, 2018, we also maintained several forward interest rate cap agreements that were entered into in October 2015 with notional amounts totaling \$3.5 billion. These forward cap agreements will become effective June 29, 2018 and will have the economic effect of capping the LIBOR variable component of our interest rate at a

maximum of 3.50% on an equivalent amount of our debt. These cap agreements expire on June 30, 2020. As of March 31, 2018, the total fair value of

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these cap agreements was an asset of approximately \$2.4 million. During the three months ended March 31, 2018, we recorded a gain of \$1.4 million in other comprehensive income due to an increase in the unrealized fair value of these forward cap agreements.

Our weighted average effective interest rate on the senior secured credit facilities at the end of the quarter was 4.67%, based on the current margins in effect of 2.00% for Term Loan A, 1.00% for Term Loan A-2 and 2.75% for Term Loan B, as of March 31, 2018.

As of March 31, 2018, our Term Loan B debt bears interest at LIBOR plus an interest rate margin of 2.75%. Term Loan B is also subject to interest rate caps if LIBOR should rise above 3.50%. Term Loan A bears interest at LIBOR plus an interest rate margin of 2.00% and Term Loan A-2 bears interest at LIBOR plus an interest rate margin of 1.00%.

Our overall weighted average effective interest rate during the three months ended March 31, 2018 was 4.87% and as of March 31, 2018 was 4.98%.

As of March 31, 2018, we had undrawn revolving credit facilities totaling \$1.0 billion, of which approximately \$14.4 million was committed for outstanding letters of credit. The remaining amount is unencumbered. We also have approximately \$22.4 million of additional outstanding letters of credit related to our Kidney Care business and \$0.2 million of committed outstanding letters of credit related to our DMG business, which is backed by a certificate of deposit.

#### Exchange rate sensitivity

While our business is predominantly conducted in the U.S. we have developing operations in ten other countries as well. For consolidated financial reporting purposes, the U.S. dollar is our reporting currency. However, the functional currencies of our operating businesses in other countries are typically those of the countries in which they operate. Therefore, changes in the rate of exchange between the U.S. dollar and the local currencies in which our international operations are conducted affect our results of operations and financial position as reported in our consolidated financial statements.

We have consolidated the balance sheets of our non-U.S. dollar denominated operations into U.S. dollars at the exchange rates prevailing at the balance sheet date and have translated their revenues and expense at the average exchange rates for the period. Additionally, our individual subsidiaries are exposed to transactional risks mainly resulting from intercompany transactions between and among subsidiaries with different functional currencies. This exposes the subsidiaries to fluctuations in the rate of exchange between the invoicing or obligation currencies and the currency in which their local operations are conducted.

#### Item 4. Controls and Procedures

Management has established and maintains disclosure controls and procedures designed to ensure that information required to be disclosed in the reports that it files or submits pursuant to the Securities Exchange Act of 1934, as amended, or Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosures.

At the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures in accordance with the Exchange Act requirements. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective for timely identification and review of material information required to be included in the Company's Exchange Act reports, including this report. Management recognizes that these controls and procedures can provide only reasonable assurance of desired outcomes, and that estimates and judgments are still inherent in the process of maintaining effective controls and procedures.

Beginning January 1, 2018, we adopted FASB Accounting Standards Codification Topic 606, Revenue from Contracts with Customers. Although the new standard is expected to have an immaterial impact on our ongoing net income, we did implement new business processes and related control activities in order to maintain appropriate controls over financial reporting. There was no other change in our internal control over financial reporting that was

identified during the evaluation that occurred during the fiscal quarter covered by this report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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## PART II.

### OTHER INFORMATION

#### Item 1. Legal Proceedings

The information required by this Part II, Item 1 is incorporated herein by reference to the information set forth under the caption "Contingencies" in Note 10 to the condensed consolidated financial statements included in this report.

#### Item 1A. Risk Factors

An updated description of the risk factors associated with our business is set forth below. This description includes any material changes to and supersedes the description of the risk factors previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2017. The risks and uncertainties discussed below are not the only ones facing our business. Please read the cautionary notice regarding forward-looking statements in Item 2 of Part I of this Quarterly Report on Form 10-Q under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Risk factors related to our overall business:

If we fail to adhere to all of the complex government laws and regulations that apply to our business, we could suffer severe consequences that could have a material adverse effect on our business, results of operations, financial condition and stock price.

Our operations are subject to extensive federal, state and local government laws and regulations, such as Medicare and Medicaid payment rules and regulations, federal and state anti-kickback laws, the Stark Law and analogous state self-referral prohibition statutes, the 21<sup>st</sup> Century Cures Act, Federal Acquisition Regulations, the False Claims Act (FCA), the Civil Monetary Penalty statute, the Foreign Corrupt Practices Act (FCPA) and federal and state laws regarding the collection, use and disclosure of patient health information (e.g., Health Insurance Portability and Accountability Act of 1996 (HIPAA)) and the storage, handling, shipment, disposal and/or dispensing of pharmaceuticals and blood products and other biological materials. The Medicare and Medicaid reimbursement rules impose complex and extensive requirements upon healthcare providers as well. Moreover, the various laws and regulations that apply to our operations are often subject to varying interpretations and additional laws and regulations potentially affecting providers continue to be promulgated that may impact us. A violation or departure from any of these legal requirements may result in government audits, lower reimbursements, significant fines and penalties, the potential loss of certification, recoupment efforts or voluntary repayments, among other things.

We endeavor to comply with all legal requirements; however, there is no guarantee that we will be able to adhere to all of the complex government regulations that apply to our business. We further endeavor to structure all of our relationships with physicians and providers to comply with state and federal anti-kickback and physician self-referral laws. We utilize considerable resources to monitor laws and regulations and implement necessary changes. However, the laws and regulations in these areas are complex, changing and often subject to varying interpretations. For example, if an enforcement agency were to challenge the level of compensation that we pay our medical directors or the number of medical directors whom we engage, we could be required to change our practices, face criminal or civil penalties, pay substantial fines or otherwise experience a material adverse effect on our business, results of operations and financial condition as a result of a challenge to these arrangements.

In addition, failure to report and return overpayments within 60 days of when the overpayment is identified and quantified can lead to a violation of the FCA and associated penalties, as described in further detail below, and exclusion and penalties under the federal Civil Monetary Penalty statute, including civil monetary penalties of up to \$20,000 (adjusted for inflation) for each item or service for which a person received an identified overpayment and failed to report and return such overpayment. These obligations to report and return overpayments could subject our procedures for identifying and processing overpayments to greater scrutiny. We have made investments in resources to decrease the time it takes to identify, quantify and process overpayments, and we may be required to make additional investments in the future. From time to time we may conduct internal compliance reviews, the results of which may involve the identification of overpayments or other liabilities. An acceleration in our ability to identify and process overpayments could result in us refunding overpayments to government and other payors more rapidly than we have in the past which could have a material adverse effect on our operating cash flows. Overpayments subject us to refunds and related damages and potential liabilities.

Additionally, the federal government has used the FCA to prosecute a wide variety of alleged false claims and fraud allegedly perpetrated against Medicare, Medicaid and other federally funded health care programs. Moreover, amendments to

the federal Anti-Kickback Statute in the 2010 Affordable Care Act (ACA) make claims tainted by anti-kickback violations potentially subject to liability under the FCA, including qui tam or whistleblower suits. The penalties for a violation of the FCA range from \$5,500 to \$11,000 (adjusted for inflation) for each false claim plus three times the amount of damages caused by each such claim which generally means the amount received directly or indirectly from the government. On January 29, 2018, the Department of Justice (DOJ) issued a final rule announcing adjustments to FCA penalties, under which the per claim penalty range increases to a range from \$11,181 to \$22,363 for penalties assessed after January 29, 2018, so long as the underlying conduct occurred after November 2, 2015. Given the high volume of claims processed by our various operating units, the potential is high for substantial penalties in connection with any alleged FCA violations.

In addition to the provisions of the FCA, which provide for civil enforcement, the federal government can use several criminal statutes to prosecute persons who are alleged to have submitted false or fraudulent claims for payment to the federal government.

Certain civil investigative demands received by us or our subsidiaries specifically reference that they are in connection with FCA investigations alleging, among other things, that we or our subsidiaries presented or caused to be presented false claims for payment to the government. See Note 10 to the condensed consolidated financial statements included in this report for further details.

We are subject to a Corporate Integrity Agreement (CIA) which, for our domestic dialysis business, requires us to report probable violations of criminal, civil or administrative laws applicable to any federal health care program for which penalties or exclusions may be authorized under applicable healthcare laws and regulations. See "If we fail to comply with our Corporate Integrity Agreement, we could be subject to substantial penalties and exclusion from participation in federal healthcare programs that could have a material adverse effect on our business, results of operations and financial condition."

If any of our operations are found to violate these or other government laws or regulations, we could suffer severe consequences that would have a material adverse effect on our business, results of operations, financial condition and stock price, including:

- Suspension or termination of our participation in government payment programs;
- Refunds of amounts received in violation of law or applicable payment program requirements;
- Loss of required government certifications or exclusion from government payment programs;
- Loss of licenses required to operate healthcare facilities or administer pharmaceuticals in some of the states in which we operate;
- Reductions in payment rates or coverage for dialysis and ancillary services and related pharmaceuticals;
- Criminal or civil liability, fines, damages or monetary penalties for violations of healthcare fraud and abuse laws, including the federal Anti-Kickback Statute, Stark Law violations, FCA or other failures to meet regulatory requirements;
- Enforcement actions by governmental agencies and/or state claims for monetary damages by patients who believe their protected health information (PHI) has been used, disclosed or not properly safeguarded in violation of federal or state patient privacy laws, including HIPAA and the Privacy Act of 1974;
- Mandated changes to our practices or procedures that significantly increase operating expenses;
- Imposition of and compliance with corporate integrity agreements that could subject us to ongoing audits and reporting requirements as well as increased scrutiny of our billing and business practices which could lead to potential fines;
- Termination of various relationships and/or contracts related to our business, including joint venture arrangements, medical director agreements, real estate leases and consulting agreements with physicians; and
- Harm to our reputation which could impact our business relationships, affect our ability to obtain financing and decrease access to new business opportunities, among other things.

We are, and may in the future be, a party to various lawsuits, demands, claims, qui tam suits, governmental investigations and audits (including investigations or other actions resulting from our obligation to self-report suspected violations of law) and other legal matters, any of which could result in, among other things, substantial financial penalties or awards against us, substantial payments made by us, required changes to our business practices, exclusion from future participation in the Medicare, Medicaid and other federal healthcare programs and possible criminal penalties, any of which could have a material adverse effect on our business, results of operations and financial condition and materially harm our reputation.

We are the subject of a number of investigations and audits by governmental agencies. In addition, we are, and may in the future be, subject to other investigations and audits by state or federal governmental agencies and/or private civil qui tam complaints filed by relators and other lawsuits, demands, claims and legal proceedings, including investigations or other actions resulting from our obligation to self-report suspected violations of law.

Responding to subpoenas, investigations and other lawsuits, claims and legal proceedings as well as defending ourselves in such matters will continue to require management's attention and cause us to incur significant legal expense. Negative findings or terms and conditions that we might agree to accept as part of a negotiated resolution of pending or future legal or regulatory matters could result in, among other things, substantial financial penalties or awards against us, substantial payments made by us, harm to our reputation, required changes to our business practices, exclusion from future participation in the Medicare, Medicaid and other federal healthcare programs and, in certain cases, criminal penalties, any of which could have a material adverse effect on us. It is possible that criminal proceedings may be initiated against us and/or individuals in our business in connection with investigations by the federal government. Other than as described in Note 10 to the condensed consolidated financial statements included in this report, we cannot predict the ultimate outcomes of the various legal proceedings and regulatory matters to which we are or may be subject from time to time, including those described in the aforementioned sections of this report, or the timing of their resolution or the ultimate losses or impact of developments in those matters, which could have a material adverse effect on our business results of operations and financial condition. See Note 10 to the condensed consolidated financial statements included in this report for further details regarding these and other matters.

Disruptions in federal government operations and funding create uncertainty in our industry and could have a material adverse effect on our business, results of operations and financial condition.

A substantial portion of our revenues is dependent on federal healthcare program reimbursement, and any disruptions in federal government operations could have a material adverse effect on our business, results of operations and financial condition. If the U.S. government defaults on its debt, there could be broad macroeconomic effects that could raise our cost of borrowing funds, and delay or prevent our future growth and expansion. Any future federal government shutdown, U.S. government default on its debt and/or failure of the U.S. government to enact annual appropriations could have a material adverse effect on our business, results of operations and financial condition. Additionally, disruptions in federal government operations may negatively impact regulatory approvals and guidance that are important to our operations, and create uncertainty about the pace of upcoming healthcare regulatory developments.

Healthcare reform could have a material adverse effect on our business, financial condition and results of operations. We cannot predict how employers, private payors or persons buying insurance might react to the changes brought on by federal and state healthcare reform legislation, including the ACA and any subsequent legislation, or what form many of these regulations will take before implementation.

The ACA introduced healthcare insurance exchanges, which provide a marketplace for eligible individuals and small employers to purchase healthcare insurance. The business and regulatory environment continues to evolve as the exchanges mature, and statutes and regulations are challenged, changed and enforced. If commercial payor participation in the exchanges continues to decrease, it could have a material adverse effect on our business, results of operations and financial condition. Although we cannot predict the short- or long-term effects of legislative or regulatory changes, we believe that future market changes could result in more restrictive commercial plans with lower reimbursement rates or higher deductibles and co-payments that patients may not be able to pay. To the extent that changes in statutes or regulations, or enforcement of statutes or regulations regarding the exchanges, or changes in other market conditions result in a reduction in reimbursement rates for our services from commercial and/or

government payors, it could have a material adverse effect on our business, results of operations and financial condition.

The ACA also added several new tax provisions that, among other things, impose various fees and excise taxes, and limit compensation deductions for health insurance providers and their affiliates. These rules could negatively impact our cash flow and tax liabilities. In addition, the ACA broadened the potential for penalties under the FCA for the knowing and improper

retention of overpayments collected from government payors and reduced the timeline to file Medicare claims. As a result, we made significant investments in new resources to accelerate the time it takes us to identify, quantify and process overpayments and we deployed significant resources to reduce our timeline and improve our claims processing methods to ensure that our Medicare claims are filed in a timely fashion. However, we may be required to make additional investments in the future. Failure to timely identify, quantify and return overpayments may result in significant penalties, which could have a material adverse effect on our business, results of operations and financial condition. Failure to file a claim within the one year window could result in payment denials, adversely affecting our business, results of operations and financial condition.

With the ACA, new models of care emerge and evolve and other initiatives in the government or private sector may arise, which could adversely impact our business. For example, the Centers for Medicare and Medicaid Services (CMS) Innovation Center (Innovation Center) is currently working with various healthcare providers to develop, refine and implement Accountable Care Organizations (ACOs) and other innovative models of care for Medicare and Medicaid beneficiaries, including Bundled Payments for Care Improvement Initiative, Comprehensive ESRD Care Model (CEC Model) (which includes the development of end stage renal disease (ESRD) Seamless Care Organizations), the Duals Demonstration, and other models. We are currently participating in the CEC Model with the Innovation Center, including with organizations in Arizona, Florida, and adjacent markets in New Jersey and Pennsylvania. Our U.S. dialysis business may choose to participate in additional models either as a partner with other providers or independently. Even in areas where we are not directly participating in these or other Innovation Center models, some of our patients may be assigned to an ACO, another ESRD Care Model, or another program, in which case the quality and cost of care that we furnish will be included in an ACO's, another ESRD Care Model's, or other program's calculations. Additionally, CMS instituted new screening procedures, as required by the ACA, which we expect will delay the Medicare contractor approval process, potentially causing a delay in reimbursement. We anticipate the new screening and enrollment requirements will require additional personnel and financial resources and will potentially delay the enrollment and revalidation of our centers which in turn will delay payment. These delays could adversely affect our business, results of operations and financial condition. The Bipartisan Budget Act of 2018 (BBA) revised the manner in which beneficiaries are assigned to an ACO, specifically giving ACOs the choice to have beneficiaries assigned prospectively at the beginning of a performance year and giving beneficiaries the option to voluntarily align to the ACO in which the beneficiary's main primary care provider participates. While prospective assignment may allow ACOs to identify beneficiaries for whom they will be held accountable and proactively take steps to ensure appropriate care, the ultimate impact of such changes on our business, results of operations and financial condition is not yet known.

Other ACA reform measures allow CMS to place a moratorium on new enrollment of providers and to suspend payment to providers upon a credible allegation of fraud from any source. These types of reform measures, as well as other measures, could adversely affect our business, results of operations, and financial condition, depending on the scope and breadth of the implementing regulations.

There is also a considerable amount of uncertainty as to the prospective implementation of the ACA and what similar measures or other changes might be enacted at the federal and/or state level. There have been multiple attempts through legislative action and legal challenges to repeal or amend the ACA. In addition, the 2016 Presidential and Congressional elections and subsequent developments in 2017 and 2018 have caused the future state of the exchanges and other ACA reforms to be unclear. For example, in October 2017, the federal government announced that cost-sharing reduction payments to insurers would end, effective immediately, unless Congress appropriated the funds, and, in December 2017, Congress passed the Tax Cuts and Jobs Act, which includes a provision that eliminates the penalty under the ACA's individual mandate effective January 1, 2019 and could impact the future state of the exchanges. Further, in February 2018, Congress passed the BBA which, among other things, repealed the Independent Payment Advisory Board that was established by the ACA and intended to reduce the rate of growth in Medicare spending. While certain provisions of the BBA may increase the scope of benefits available for certain chronically ill Federal health care program beneficiaries beginning in 2020, the ultimate impact of such changes cannot be predicted. While there may be significant changes to the healthcare environment in the future, the specific changes and their timing are not yet apparent. As a result, there is considerable uncertainty surrounding the ACA including the

exchanges, and, indeed, many core aspects of the current health care marketplace. Previously enacted reforms and future changes could have a material adverse effect on our business, financial condition and results of operations, including, for example, by limiting the scope of coverage or the number of patients who are able to obtain coverage through the exchanges and other health insurance programs, lowering or eliminating the cost-sharing reduction subsidies under the ACA, lowering our reimbursement rates, and/or increasing our expenses.

In addition, in December 2016, CMS published an interim final rule that questioned the use of charitable premium assistance for ESRD patients and would have established new conditions for coverage standards for dialysis facilities. In January 2017, a federal district court in Texas issued a preliminary injunction on CMS' interim final rule and in June 2017, at the request of CMS, the court stayed the proceedings while CMS pursues new rulemaking options. In November 2017, when CMS published the 2018 final rule that updates payment policies and rates under the ESRD Prospective Payment System (PPS),

and the 2019 proposed Notice of Benefit and Payment Parameters, it did not pursue further discussion or rule making related to charitable premium assistance or propose changes to historical charitable premium assistance guidelines. This does not preclude CMS or another regulatory agency or legislative authority from issuing a new rule or guidance that challenges charitable premium assistance. In February 2018, SB 1156 was introduced in the California legislature. If passed and signed into law in its current form, SB 1156 would impose certain restrictions on a patient's use of charitable premium assistance in the state of California. Any law, rule, or guidance issued by CMS or other regulatory or legislative authorities, including individual states, restricting or prohibiting the ability of patients with access to alternative coverage from selecting a marketplace plan on or off exchange, and/or otherwise restricting or prohibiting the use of charitable premium assistance, could adversely impact dialysis centers across the U.S. making certain centers economically unviable, restrict the ability of dialysis patients to obtain and maintain optimal insurance coverage, and have a material adverse effect on our business, results of operations, and financial condition. Privacy and information security laws are complex, and if we fail to comply with applicable laws, regulations and standards, including with respect to third-party service providers that utilize sensitive personal information on our behalf, or if we fail to properly maintain the integrity of our data, protect our proprietary rights to our systems or defend against cybersecurity attacks, we may be subject to government or private actions due to privacy and security breaches, any of which could have a material adverse effect on our business, financial condition and results of operations or materially harm our reputation.

We must comply with numerous federal and state laws and regulations in both the U.S. and the foreign jurisdictions in which we operate governing the collection, dissemination, access, use, security and privacy of PHI, including HIPAA and its implementing privacy, security, and related regulations, as amended by the federal Health Information Technology for Economic and Clinical Health Act (HITECH) and collectively referred to as HIPAA. We are also required to report known breaches of PHI consistent with applicable breach reporting requirements set forth in applicable laws and regulations. From time to time, we may be subject to both federal and state inquiries or audits related to HIPAA, HITECH and related state laws associated with complaints, desk audits, and self-reported breaches. If we fail to comply with applicable privacy and security laws, regulations and standards, including with respect to third-party service providers that utilize sensitive personal information, including PHI, on our behalf, properly maintain the integrity of our data, protect our proprietary rights, or defend against cybersecurity attacks, it could materially harm our reputation or have a material adverse effect on our business, results of operations and financial condition.

Data protection laws are evolving globally, and may add additional compliance costs and legal risks to our international operations. In Europe, the new General Data Protection Regulation (GDPR) becomes effective on May 25, 2018. The GDPR applies to entities that are established in the European Union (EU), as well as extends the scope of EU data protection laws to foreign companies processing data of individuals in the EU. The GDPR imposes a comprehensive data protection regime with penalties of up to the greater of 4% of worldwide turnover or €20 million. The costs of compliance with, and other burdens imposed by, the GDPR and other new laws, regulations and policies implementing the GDPR may impact our European operations and/or limit the ways in which we can provide services or use personal data collected while providing services.

Information security risks have significantly increased in recent years in part because of the proliferation of new technologies, the use of the Internet and telecommunications technologies to conduct our operations, and the increased sophistication and activities of organized crime, hackers, terrorists and other external parties, including foreign state agents. Our business and operations rely on the secure processing, transmission and storage of confidential, proprietary and other information in our computer systems and networks, including sensitive personal information, including PHI, social security numbers, and credit card information of our patients, teammates, physicians, business partners and others.

We are continuously implementing multiple layers of security measures through technology, processes, and our people. We utilize security technologies to protect and maintain the integrity of our information systems and data and our defenses are monitored and routinely tested internally and by external parties. Despite these efforts, our facilities and systems and those of our third-party service providers may be vulnerable to privacy and security incidents; security attacks and breaches; acts of vandalism or theft; computer viruses and other malicious code; coordinated



attacks by a variety of actors, including activist entities or state sponsored cyberattacks; emerging cybersecurity risks; cyber risk related to connected devices; misplaced or lost data; programming and/or human errors; or other similar events that could impact the security, reliability, and availability of our systems. Internal or external parties may attempt to circumvent our security systems, and we have in the past, and expect that we will in the future, experience external attacks on our network including reconnaissance probes, denial of service attempts, malicious software attacks including ransomware or other attacks intended to render our internal operating systems or data unavailable, and phishing attacks or business email compromise. Cybersecurity requires ongoing investment and diligence against evolving threats. Emerging and advanced security threats, including coordinated attacks, require additional layers of security which may disrupt or impact efficiency of operations. As with any security program, there always exists the risk that

employees will violate our policies despite our compliance efforts or that certain attacks may be beyond the ability of our security and other systems to detect. There can be no assurance that investments and diligence will be sufficient to prevent or timely discover an attack.

Any security breach involving the misappropriation, loss or other unauthorized disclosure or use of confidential information, including PHI, financial data, competitively sensitive information, or other proprietary data, whether by us or a third party, could have a material adverse effect on our business, financial condition, and results of operations and materially harm our reputation. We may be required to expend significant additional resources to modify our protective measures, to investigate and remediate vulnerabilities or other exposures, or to make required notifications. The occurrence of any of these events could, among other things, result in interruptions, delays, the loss or corruption of data, cessations in the availability of systems and liability under privacy and security laws, all of which could have a material adverse effect on our business, financial condition or results of operations, materially harm our reputation and trigger regulatory actions and private party litigation. If we are unable to protect the physical and electronic security and privacy of our databases and transactions, we could be subject to potential liability and regulatory action, our reputation and relationships with our patients and vendors would be harmed, and our business, results of operations and financial condition could be materially and adversely affected. Failure to adequately protect and maintain the integrity of our information systems (including our networks) and data, or to defend against cybersecurity attacks, could subject us to monetary fines, civil suits, civil penalties or criminal sanctions and requirements to disclose the breach publicly, and could further result in a material adverse effect on our business, results of operations and financial condition or harm our reputation. As malicious cyber activity escalates, including activity that originates outside of the United States, the risks we face relating to transmission of data and our use of service providers outside of our network, as well as the storing or processing of data within our network, intensify. There have been increased international, federal and state and other privacy, data protection and security enforcement efforts and we expect this trend to continue. While we maintain cyber liability insurance, this insurance may not cover us for all types of losses and may not be sufficient to protect us against the amount of all losses.

We may engage in acquisitions, mergers, joint ventures or dispositions, which may affect our results of operations, debt-to-capital ratio, capital expenditures or other aspects of our business, and if businesses we acquire have liabilities we are not aware of, we could suffer severe consequences that would have a material adverse effect on our business, results of operations and financial condition.

Our business strategy includes growth through acquisitions of dialysis centers and other businesses, as well as entry into joint ventures. We may engage in acquisitions, mergers, joint ventures or dispositions or expand into new business models, which may affect our results of operations, debt-to-capital ratio, capital expenditures or other aspects of our business. There can be no assurance that we will be able to identify suitable acquisition targets or merger partners or buyers for dispositions or that, if identified, we will be able to agree to terms with merger partners, acquire these targets or make these dispositions on acceptable terms or on the desired timetable. There can also be no assurance that we will be successful in completing any acquisitions, mergers or dispositions that we announce, executing new business models or integrating any acquired business into our overall operations. There is no guarantee that we will be able to operate acquired businesses successfully as stand-alone businesses, or that any such acquired business will operate profitably or will not otherwise have a material adverse effect on our business, results of operations and financial condition. Further, we cannot be certain that key talented individuals at the business being acquired will continue to work for us after the acquisition or that they will be able to continue to successfully manage or have adequate resources to successfully operate any acquired business. In addition, certain of our newly and previously acquired dialysis centers and facilities have been in service for many years, which may result in a higher level of maintenance costs. Further, our facilities, equipment and information technology may need to be improved or renovated to maintain or increase operational efficiency, compete for patients and medical directors, or meet changing regulatory requirements. Increases in maintenance costs and capital expenditures could have a material adverse effect on our financial condition, results of operations and cash flows.

Businesses we acquire may have unknown or contingent liabilities or liabilities that are in excess of the amounts that we originally estimated, and may have other issues, including those related to internal controls over financial reporting or issues that could affect our ability to comply with healthcare laws and regulations and other laws applicable to our

expanded business. As a result, we cannot make any assurances that the acquisitions we consummate will be successful. Although we generally seek indemnification from the sellers of businesses we acquire for matters that are not properly disclosed to us, we are not always successful. In addition, even in cases where we are able to obtain indemnification, we may discover liabilities greater than the contractual limits, the amounts held in escrow for our benefit (if any), or the financial resources of the indemnifying party. In the event that we are responsible for liabilities substantially in excess of any amounts recovered through rights to indemnification or alternative remedies that might be available to us, or any applicable insurance, we could suffer severe consequences that could have a material adverse effect on our business, results of operations and financial condition.

Additionally, joint ventures, including our Asia Pacific Joint Venture, and minority investments inherently involve a lesser degree of control over business operations, thereby potentially increasing the financial, legal, operational and/or compliance risks associated with the joint venture or minority investment. In addition, we may be dependent on joint venture partners, controlling shareholders or management who may have business interests, strategies or goals that are inconsistent with ours. Business decisions or other actions or omissions of the joint venture partner, controlling shareholders or management may adversely affect the value of our investment, result in litigation or regulatory action against us, result in reputational harm to us or adversely affect the value of our investment or partnership.

If we are unable to compete successfully, including implementing our growth strategy and/or retaining our physicians and patients, it could adversely affect our business, results of operations and financial condition.

Acquisitions, patient retention and medical director and physician retention are important parts of our growth strategy. We face intense competition from other companies for acquisition targets. In our U.S. dialysis business, we continue to face increased competition from large and medium-sized providers, among others, which compete directly with us for the limited acquisition targets as well as for individual patients and medical directors. In addition, we compete for individual patients, physicians and medical directors based in part on the quality of our facilities. Moreover, as we continue our international expansion into various international markets, we will face competition from large and medium-sized providers for these acquisition targets as well. As we and our competitors continue to grow and open new dialysis centers, each center is required by applicable regulations to have a medical director, and we may not be able to retain an adequate number of nephrologists to serve as medical directors. Because of the ease of entry into the dialysis business and the ability of physicians to be medical directors for their own centers, competition for growth in existing and expanding markets is not limited to large competitors with substantial financial resources. Individual nephrologists have opened their own dialysis units or facilities. There also has been growing interest by non-traditional dialysis providers and others to enter the dialysis space and develop innovative technologies that could be disruptive to the industry. Although these potential new competitors may face operational and/or financial challenges, if their efforts to offer dialysis services or develop innovative technology are successful and we are unable to effectively compete, it could negatively impact our business. In addition, Fresenius USA, our largest competitor, manufactures a full line of dialysis supplies and equipment in addition to owning and operating dialysis centers. This may give it cost advantages over us because of its ability to manufacture its own products or prevent us from accessing existing or new technology on a cost-effective basis, see further discussion regarding risks associated with our suppliers under the heading below, "If certain of our suppliers do not meet our needs, if there are material price increases, if we are not reimbursed or adequately reimbursed for drugs we purchase or if we are unable to effectively access new technology or superior products, it could negatively impact our ability to effectively provide the services we offer and could have a material adverse effect on our business, results of operations and financial condition." If we are not able to effectively implement our growth strategy, including by making acquisitions at the desired pace or at all; continue to maintain the expected or desired level of non-acquired growth; if we face significant patient attrition to our competitors or as a result of new technology; or if physicians choose not to refer to our clinics, it could adversely affect our business, results of operations and financial condition.

If certain of our suppliers do not meet our needs, if there are material price increases, if we are not reimbursed or adequately reimbursed for drugs we purchase or if we are unable to effectively access new technology or superior products, it could negatively impact our ability to effectively provide the services we offer and could have a material adverse effect on our business, results of operations and financial condition.

We have significant suppliers that may be the sole or primary source of products critical to the services we provide, or to which we have committed obligations to make purchases, sometimes at particular prices. If any of these suppliers do not meet our needs for the products they supply, including in the event of a product recall, shortage or dispute, and we are not able to find adequate alternative sources, if we experience material price increases from these suppliers that we are unable to mitigate, or if some of the drugs that we purchase are not reimbursed or not adequately reimbursed by commercial or government payors, it could have a material adverse impact on our business, results of operations and financial condition. In addition, the technology related to the products critical to the services we provide is subject to new developments which may result in superior products. If we are not able to access superior products on a cost-effective basis or if suppliers are not able to fulfill our requirements for such products, we could face patient

attrition which could have a material adverse effect on our business, results of operations and financial condition. DMG operates in a different line of business from our historical business, and we face challenges managing DMG and may not realize anticipated benefits.

DaVita Medical Group (DMG) operates in a different line of business from our historical business. We may not have the expertise, experience and resources to pursue all of our businesses at once, and we may be unable to successfully operate all businesses in the combined company. The administration of DMG requires implementation of appropriate operations,

management, forecasting, and financial reporting systems and controls. We have experienced difficulties in effectively implementing these and other systems. The management of DMG requires and will continue to require the focused attention of our management team, including a significant commitment of its time and resources. The need for management to focus on these matters could have a material adverse effect on our business, results of operations and financial condition. If the DMG operations continue to be less profitable than we currently anticipate or we do not have the experience, the appropriate expertise or the resources to pursue all businesses in the combined company, our results of operations and financial condition may be materially and adversely affected. In that regard, we have taken goodwill impairment charges of \$1.093 billion in total and may continue incurring additional impairment charges. Laws regulating the corporate practice of medicine could restrict the manner in which DMG and other subsidiaries of ours are permitted to conduct their respective business, and the failure to comply with such laws could subject these entities to penalties or require a restructuring of these businesses.

Some states have laws that prohibit business entities, such as DMG and other subsidiaries of ours, including but not limited to, Nephrology Practice Solutions, Paladina Health, DaVita Health Solutions, VillageHealth, and Lifeline, from practicing medicine, employing physicians to practice medicine, exercising control over medical decisions by physicians (also known collectively as the corporate practice of medicine) or engaging in certain arrangements, such as fee-splitting, with physicians. In some states these prohibitions are expressly stated in a statute or regulation, while in other states the prohibition is a matter of judicial or regulatory interpretation. Of the states in which DMG currently operates, California, Colorado, Nevada and Washington generally prohibit the corporate practice of medicine, and other states may as well.

DMG and other DaVita entities operate by maintaining long-term contracts with their associated physician groups which are each owned and operated by physicians and which employ or contract with additional physicians to provide physician services. Under these arrangements, DMG and such other DaVita entities provide management services and receive a management fee for providing non-medical management services; however, DMG and such other DaVita entities do not represent that they offer medical services, and do not exercise influence or control over the practice of medicine by the physicians or the associated physician groups.

In addition to the above management arrangements, DMG has certain contractual rights relating to the orderly transfer of equity interests in certain of its physician groups through succession agreements and other arrangements with their physician equity holders. However, such equity interests cannot be transferred to or held by DMG or by any non-professional organization. Accordingly, neither DMG nor DMG's subsidiaries directly own any equity interests in any physician groups in California, Colorado, Nevada and Washington. The other DaVita entities operating in these and multiple other states have similar agreements and arrangements. In the event that any of these associated physician groups fail to comply with the management arrangement or any management arrangement is terminated and/or DMG or any of the other DaVita entities is unable to enforce its contractual rights over the orderly transfer of equity interests in its associated physician groups, such events could have a material adverse effect on the business, results of operations and financial condition of DMG and such other DaVita entities.

It is possible that a state regulatory agency or a court could determine that DMG's agreements with physician equity holders of certain managed California, Colorado, Nevada and Washington associated physician groups and the way DMG carries out these arrangements as described above, either independently or coupled with the management services agreements with such associated physician groups, are in violation of the corporate practice of medicine doctrine. As a result, these arrangements could be deemed invalid, potentially resulting in a loss of revenues and an adverse effect on results of operations derived from such associated physician groups. Such a determination could force a restructuring of DMG's management arrangements with associated physician groups in California, Colorado, Nevada and/or Washington, which might include revisions of the management services agreements, including a modification of the management fee and/or establishing an alternative structure that would permit DMG to contract with a physician network without violating the corporate practice of medicine prohibition. There can be no assurance that such a restructuring would be feasible, or that it could be accomplished within a reasonable time frame without a material adverse effect on DMG's business, results of operations and financial condition. These same risks exist for the other DaVita entities utilizing similar structures.

In December 2013, DaVita Health Plan of California, Inc. (DHPC) obtained a restricted Knox-Keene license in California, which permits DHPC to contract with health plans in California to accept global risk without violating the corporate practice of medicine prohibition. However, DMG and DMG's Colorado, Nevada and Washington associated physician groups, as well as those physician equity holders of associated physician groups who are subject to succession agreements with DMG, could be subject to criminal or civil penalties or an injunction for practicing medicine without a license or aiding and abetting the unlicensed practice of medicine.

The level of our current and future debt could have an adverse impact on our business and our ability to generate cash to service our indebtedness and for other intended purposes depends on many factors beyond our control.

We have substantial debt outstanding, we recently incurred a substantial amount of additional debt in connection with our entry into the Increase Joinder Agreement, and we may continue to incur additional indebtedness in the future. For additional details regarding specific risks we face regarding the sale of DMG, see the discussion in the risk factors under the heading "Risk factors related to the sale of DMG." Our inability to generate sufficient cash to service our substantial indebtedness and for other intended purposes could have important consequences to you, for example, it could:

- make it difficult for us to make payments on our debt securities;
- increase our vulnerability to general adverse economic and industry conditions;
- require us to dedicate a substantial portion of our cash flows from operations to payments on our indebtedness, thereby reducing the availability of our cash flow to fund working capital, capital expenditures, acquisitions and investments, repurchases of stock at the levels intended or announced, or at all, and other general corporate purposes;
- limit our flexibility in planning for, or reacting to, changes in our business and the markets in which we operate;
- expose us to interest rate volatility that could adversely affect our business, results of operations and financial condition, and our ability to service our indebtedness;
- place us at a competitive disadvantage compared to our competitors that have less debt; and
- limit our ability to borrow additional funds, or to refinance existing debt on favorable terms when otherwise available.

In addition, we may continue to incur additional indebtedness in the future, and the amount of that additional indebtedness may be substantial. Although the indentures governing our senior notes and the agreement governing our senior secured credit facilities include covenants that could limit our indebtedness, we currently have the ability to incur substantial additional debt. The related risks described above could intensify, in particular, if there is a delay in closing the sale of DMG or the sale of DMG does not close, or if new debt is added to current debt levels.

Our ability to make payments on our indebtedness, to fund planned capital expenditures and expansion efforts, including any strategic acquisitions we may make in the future, to repurchase our stock at the levels intended or announced and to meet our other liquidity needs, will depend on our ability to generate cash. This, to a certain extent, is subject to general economic, financial, competitive, regulatory and other factors that are beyond our control.

After the pending sale of DMG closes, our cash flows will be reduced accordingly. We cannot provide assurances that our business will generate sufficient cash flows from operations in the future or that future borrowings will be available to us in an amount sufficient to enable us to service our indebtedness or to fund other liquidity needs, including those described above. If we are unable to generate sufficient funds to service our outstanding indebtedness or to meet our other liquidity needs, including the intended purposes described above, we may be required to refinance, restructure, or otherwise amend some or all of such obligations, sell assets, change our intended or announced uses or strategy for capital deployment, including for stock repurchases, reduce capital expenditures or planned expansions or raise additional cash through the sale of our equity. We cannot make any assurances that any such refinancing, restructurings, sales of assets, or issuances of equity can be accomplished or, if accomplished, can be accomplished on favorable terms or that if accomplished that they would raise sufficient funds to meet these obligations or our other liquidity needs.

The borrowings under our senior secured credit facilities are guaranteed by a substantial portion of our direct and indirect wholly owned domestic subsidiaries, including certain of DMG's subsidiaries, and are secured by a substantial portion of our and our subsidiaries' assets, including those of certain of DMG's subsidiaries. After the sale of DMG closes, we will have fewer assets with which to secure future debt or refinance or restructure existing debt. This will likely reduce the total amount of secured debt that we will be able to incur and may increase the interest rate we are required to pay on our existing secured debt and any secured debt we issue in the future. In addition, by reducing the amount of assets available to meet the claims of our secured creditors, it may also adversely affect the interest rates on our existing unsecured debt and any unsecured debt we issue in the future.



We may be subject to liability claims for damages and other expenses that are not covered by insurance or exceed our existing insurance coverage that could have a material adverse effect on our business, results of operations, financial condition and reputation.

Our operations and how we manage our Company may subject us, as well as our officers and directors to whom we owe certain defense and indemnity obligations, to litigation and liability for damages. Our business, profitability and growth prospects could suffer if we face negative publicity or we pay damages or defense costs in connection with a claim that is outside the scope or limits of coverage of any applicable insurance coverage, including claims related to adverse patient events, contractual disputes, professional and general liability and directors' and officers' duties. In addition, we have received notices of claims from commercial payors and other third parties, as well as subpoenas and CIDs from the federal government, related to our business practices, including our historical billing practices and the historical billing practices of acquired businesses. Although the ultimate outcome of these claims cannot be predicted, an adverse result with respect to one or more of these claims could have a material adverse effect on our business, results of operations and financial condition. We maintain insurance coverage for those risks we deem are appropriate to insure against and make determinations about whether to self-insure as to other risks or layers of coverage. However, a successful claim, including a professional liability, malpractice or negligence claim which is in excess of any applicable insurance coverage, or that is subject to our self-insurance retentions, could have a material adverse effect on our business, results of operations, financial condition and reputation. Additionally, as a result of the broad scope of our DMG division's medical practice, we are exposed to medical malpractice claims, as well as claims for damages and other expenses, that may not be covered by insurance or for which adequate limits of insurance coverage may not be available.

In addition, if our costs of insurance and claims increase, then our earnings could decline. Market rates for insurance premiums and deductibles have been steadily increasing. Our business, results of operations and financial condition could be materially and adversely affected by any of the following:

- the collapse or insolvency of our insurance carriers;
- further increases in premiums and deductibles;
- increases in the number of liability claims against us or the cost of settling or trying cases related to those claims; or
- an inability to obtain one or more types of insurance on acceptable terms, if at all.

If we fail to successfully maintain an effective internal control over financial reporting, the integrity of our financial reporting could be compromised, which could have a material adverse effect on our ability to accurately report our financial results and the market's perception of our business and our stock price.

The integration of acquisitions and addition of new business lines into our internal control over financial reporting has required and will continue to require significant time and resources from our management and other personnel and has increased, and will continue to, increase our compliance costs. Failure to maintain an effective internal control environment could have a material adverse effect on our ability to accurately report our financial results and the market's perception of our business and our stock price. In addition, we could be required to restate our financial results in the event of a significant failure of our internal control over financial reporting or in the event of inappropriate application of accounting principles.

Deterioration in economic conditions and further disruptions in the financial markets could have a material adverse effect on our business, results of operations and financial condition.

Deterioration in economic conditions could have a material adverse effect on our business, results of operations and financial condition. Among other things, the potential decline in federal and state revenues that may result from such conditions may create additional pressures to contain or reduce reimbursements for our services from Medicare, Medicaid and other government sponsored programs. Increases in job losses in the U.S. as a result of adverse economic conditions has and may continue to result in a smaller percentage of our patients being covered by an employer group health plan and a larger percentage being covered by lower paying Medicare and Medicaid programs. Employers may also select more restrictive commercial plans with lower reimbursement rates. To the extent that payors are negatively impacted by a decline in the economy, we may experience further pressure on commercial rates, a further slowdown in collections and a reduction in the amounts we expect to collect. In addition, uncertainty in the financial markets could adversely affect the variable interest rates payable under our credit facilities or could make it

more difficult to obtain or renew such facilities or to obtain other forms of financing in the future, if at all. Any or all of these factors, as well as other consequences of a deterioration in economic conditions which cannot currently be anticipated, could have a material adverse effect on our business, results of operations and financial condition.

We could be subject to adverse changes in tax laws, regulations and interpretations or challenges to our tax positions. We are subject to tax laws and regulations of the U.S. federal, state and local governments as well as various foreign jurisdictions. We compute our income tax provision based on enacted tax rates in the jurisdictions in which we operate. As the tax rates vary among jurisdictions, a change in earnings attributable to the various jurisdictions in which we operate could result in an unfavorable change in our overall tax provision.

From time to time, changes in tax laws or regulations may be proposed or enacted that could adversely affect our overall tax liability. For example, the recent U.S. tax legislation enacted on December 22, 2017 represents a significant overhaul of the U.S. federal tax code. This tax legislation significantly reduced the U.S. statutory corporate tax rate and made other changes that have and will reduce our effective U.S. federal tax rate in current and future periods. However, the tax legislation also included a number of provisions, including, but not limited to, the limitation or elimination of various deductions or credits (including for interest expense and for performance-based compensation under Section 162(m)), the imposition of taxes on certain cross-border payments or transfers, the changing of the timing of the recognition of certain income and deductions or their character, and the limitation of asset basis under certain circumstances, any of which could significantly and adversely affect our U.S. federal income tax position. The legislation also made significant changes to the tax rules applicable to insurance companies and other entities with which we do business. The estimated impact of the new law is based on management's current knowledge and assumptions. We are continuing to evaluate the overall impact of this tax legislation on our operations and U.S. federal and state income tax position. The actual impact of the new law could be materially different from our current estimates based on our actual results, or our further analysis of the new law or any guidance and regulations that may be issued in the future. There can be no assurance that changes in tax laws or regulations, both within the U.S. and the other jurisdictions in which we operate, will not materially and adversely affect our effective tax rate, tax payments, financial condition and results of operations. Similarly, changes in tax laws and regulations that impact our patients, business partners and counterparties or the economy generally may also impact our financial condition and results of operations.

In addition, tax laws and regulations are complex and subject to varying interpretations, and any significant failure to comply with applicable tax laws and regulations in all relevant jurisdictions could give rise to substantial penalties and liabilities. We are regularly subject to audits by tax authorities and, although we believe our tax estimates are appropriate, the final determination of tax audits and any related litigation could be materially different from our historical income tax provisions and accruals. Any changes in enacted tax laws (such as the recent U.S. tax legislation), rules or regulatory or judicial interpretations; any adverse outcome in connection with tax audits in any jurisdiction; or any change in the pronouncements relating to accounting for income taxes could materially and adversely impact our effective tax rate, tax payments, financial condition and results of operations.

Expansion of our operations to and offering our services in markets outside of the U.S. subjects us to political, economic, legal, operational and other risks that could have a material adverse effect on our business, results of operations and financial condition.

We are continuing to expand our operations by offering our services and entering new lines of business in certain markets outside of the U.S., which increases our exposure to the inherent risks of doing business in international markets. Depending on the market, these risks include those relating to:

- changes in the local economic environment;
- political instability, armed conflicts or terrorism;
- social changes;
- intellectual property legal protections and remedies;
- trade regulations;
- procedures and actions affecting approval, production, pricing, reimbursement and marketing of products and services;
- foreign currency;
- repatriating or moving to other countries cash generated or held abroad, including considerations relating to tax-efficiencies and changes in tax laws;



- export controls;
- lack of reliable legal systems which may affect our ability to enforce contractual rights;
- changes in local laws or regulations;
- potentially longer ramp-up times for starting up new operations and for payment and collection cycles;
- financial and operational, and information technology systems integration;
- failure to comply with U.S. laws, such as the FCPA, or local laws that prohibit us, our partners, or our partners' or our intermediaries from making improper payments to foreign officials for the purpose of obtaining or retaining business; and
- data and privacy restrictions.

Issues relating to the failure to comply with any of the above may also impact our domestic business and/or raise scrutiny on our domestic practices.

Additionally, some factors that will be critical to the success of our international business and operations will be different than those affecting our domestic business and operations. For example, conducting international operations requires us to devote significant management resources to implement our controls and systems in new markets, to comply with local laws and regulations and to overcome the numerous new challenges inherent in managing international operations, including those based on differing languages, cultures and regulatory environments, and those related to the timely hiring, integration and retention of a sufficient number of skilled personnel to carry out operations in an environment with which we are not familiar.

Any expansion of our international operations through acquisitions or through organic growth could increase these risks. Additionally, while we may invest material amounts of capital and incur significant costs in connection with the growth and development of our international operations, including to start up or acquire new operations, we may not be able to operate them profitably on the anticipated timeline, or at all.

These risks could have a material adverse effect on our business, results of operations and financial condition.

Risk factors related to the sale of DMG:

The announcement and pendency of the sale of DMG may adversely affect our business, results of operations and financial condition.

The announcement and pending sale of DMG may be disruptive to our business and may adversely affect our relationships with current and prospective teammates, patients, physicians, payors, suppliers and other business partners. Uncertainties related to the pending sale of DMG may impair our ability to attract, retain and motivate key personnel and could cause suppliers and other business partners to defer entering into contracts with us or seek to change existing business relationships with us. The loss or deterioration of significant business and operational relationships could have an adverse effect on our business, results of operations and financial condition. In addition, activities relating to the pending sale and related uncertainties could divert the attention of our management and other teammates from our day-to-day business or disrupt our operations in preparation for and during the post-closing separation of DMG. It is also possible that we could have stranded costs following the closing of the pending sale, which could be material. If we are unable to effectively manage these risks, our business, results of operations and financial condition may be adversely affected.

If we fail to complete the proposed sale of DMG, or if there is a significant delay in completing the sale, our business, results of operations, financial condition and stock price may be materially adversely affected.

The completion of the proposed sale of DMG is subject to customary closing conditions, including the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and the approval of a notice of material modification by the California Department of Managed Health Care. If any condition to the closing of the sale of DMG is neither satisfied nor, where permissible, waived, the sale of DMG will not be completed. In addition, satisfying the closing conditions to the sale of DMG may take longer than expected. Regulators may impose material conditions, terms, obligations, costs or restrictions in connection with their approval of or consent to the sale of DMG, which could delay completion of the transaction, or if such approvals or consents are not obtained, could prevent completion of the transaction. There can be no assurance that all of the closing conditions will be satisfied or waived or that other events will not



intervene to delay, or result in a failure to close, the sale of DMG. In addition, either we or Optum may terminate the equity purchase agreement if, among other things, the sale has not been consummated by June 4, 2018 (subject to two three-month extensions that can be exercised by either party unilaterally). If the equity purchase agreement is terminated and our Board of Directors seeks an alternative transaction or another acquiror for the sale of the DMG business, we may not be able to negotiate a transaction with another party on terms comparable to, or better than, the terms of the equity purchase agreement with Optum.

If the sale of DMG is not completed for any reason, investor confidence could decline. A failed transaction may result in negative publicity and may affect our relationships with teammates, patients, physicians, payors, suppliers, regulators and other business partners. In addition, in the event of a failed transaction, we will have expended significant management resources in an effort to complete the sale, we have incurred additional debt in anticipation of receiving the sale proceeds but not have received the sale proceeds to repay such debt, and we will have incurred significant transaction costs, including legal fees, financial advisor fees and other related costs, without any commensurate benefit. Accordingly, if the proposed sale of DMG is not completed, or if there is a significant delay in completing the sale, our business, results of operations, financial condition and stock price may be materially adversely affected.

Our liquidity following the close of our pending sale of DMG and our planned subsequent entry into new external financing arrangements may be less than we anticipate, and we may use the proceeds from the pending sale of DMG and other available funds, including external financing and cash flow from operations, in ways that may not improve our results of operations or enhance the value of our common stock.

The purchase price for the sale of the DMG business is subject to customary adjustments, both upward and downward, which could be significant. Following the pending DMG sale, we plan to use sale proceeds and other available funds, including from external financing and cash flow from operations, to repay debt, make significant stock repurchases and for general corporate purposes, which may include growth investments. A number of factors may impact our ability to repurchase stock and the timing of any such stock repurchases, including market conditions, the price of our common stock, our results of operations, cash flow and financial condition, available financing, leverage ratios, and legal, regulatory and contractual requirements and restrictions. Accordingly, the actual amount of common stock we repurchase may be less, perhaps substantially, and the period of time over which we make any stock repurchases may be substantially longer, than we currently anticipate. In addition, we may identify investments or other uses for our available funds (other than the DMG sale proceeds that we plan to use to repay debt) that we believe are more attractive than our current intended uses. Further, there can be no assurance that any investment will yield a favorable return.

Under the terms of the equity purchase agreement, we are subject to certain contractual restrictions while the sale of DMG is pending, and certain post-closing contractual obligations that, in some cases, could have a material adverse effect on our business, results of operations and financial condition.

Under the terms of the equity purchase agreement, we are subject to certain restrictions on the conduct of the DMG business prior to completing the sale of DMG, which may adversely affect our ability to execute certain of our business strategies, including the ability in certain cases to enter into or amend contracts, acquire or dispose of assets, incur indebtedness or incur capital expenditures. Such limitations could negatively affect our business and operations prior to the completion of the sale of DMG. Each of these risks may be exacerbated by delays or other adverse developments with respect to the completion of the sale of DMG.

In addition, we agreed to retain certain liabilities of the DMG business for which we have certain indemnification rights against the original 2012 HealthCare Partners (HCP) sellers. An escrow was established in connection with our acquisition of the DMG business from the HCP sellers as security for these indemnification rights, including with respect to the OIG investigation into certain patient diagnosis coding practices. We have submitted an indemnification claim against the sellers secured by the escrow for any and all liabilities incurred relating to these matters and intend to pursue recovery from the escrow. However, we can make no assurances that the indemnification and escrow will cover the full amount of our potential losses related to these matters, which could have a material adverse effect on our business, results of operations and financial condition.





Risk factors related to our U.S. dialysis and related lab services, ancillary services and strategic initiatives:

If patients in commercial plans are subject to restriction in plan designs or the average rates that commercial payors pay us decline significantly, it would have a material adverse effect on our business, results of operations and financial condition.

Approximately 31% of our U.S. dialysis and related lab services net revenues for the three months ended March 31, 2018 were generated from patients who have commercial payors (including hospital dialysis services) as their primary payor. The majority of these patients have insurance policies that pay us on terms and at rates that are generally significantly higher than Medicare rates. The payments we receive from commercial payors generate nearly all of our profit and all of our nonacute dialysis profits come from commercial payors. We continue to experience downward pressure on some of our commercial payment rates as a result of general conditions in the market, including as employers shift to less expensive options for medical services, recent and future consolidations among commercial payors, increased focus on dialysis services and other factors. In addition, many commercial payors that sell individual plans both on and off exchange have publicly announced losses in the marketplace. These payors may seek discounts on rates for marketplace plans on and off exchange. Commercial payment rates could be materially lower in the future.

We continuously are in the process of negotiating existing and potential new agreements with commercial payors who aggressively negotiate terms with us. Sometimes many significant agreements are being renegotiated at the same time. In the event that our continual negotiations result in overall commercial rate reductions in excess of overall commercial rate increases, the cumulative effect could have a material adverse effect on our business, results of operations and financial condition. Consolidations have significantly increased the negotiating leverage of commercial payors. Our negotiations with payors are also influenced by competitive pressures, and we may experience decreased contracted rates with commercial payors or experience decreases in patient volume as our negotiations with commercial payors continue. In addition to downward pressure on contracted commercial payor rates, payors have been attempting to design and implement plans to restrict access to coverage, and the duration and/or the breadth of benefits, which may result in decreased payments. In addition, payors have been attempting to impose restrictions and limitations on patient access to commercial exchange plans and non-contracted or out-of-network providers, and in some circumstances designate our centers as out-of-network providers. Rates for commercial exchange products and out-of-network providers are on average higher than rates for government products and in-network providers, respectively.

A number of commercial payors have incorporated policies into their provider manuals limiting or refusing to accept charitable premium assistance from non-profit organizations, such as the American Kidney Fund, which may impact the number of patients who are able to afford commercial exchange plans. Paying for coverage is a significant financial burden for many patients, and ESRD disproportionately affects the low-income population. Charitable premium assistance supports continuity of coverage and access to care for patients, many of whom are unable to continue working full-time as a result of their severe condition. A material restriction in patients' ability to access charitable premium assistance may restrict the ability of dialysis patients to obtain and maintain optimal insurance coverage, and may adversely impact a large number of dialysis centers across the U.S. by making certain centers economically unviable, and may have a material adverse effect on our business, results of operations and financial condition.

We also believe commercial payors have or will begin to restructure their benefits to create disincentives for patients to stay with commercial insurance or to select or remain with out-of-network providers. In addition, payors may seek to decrease payment rates for out-of-network providers. Decreases in the number of patients with commercial plans, decreases in out-of-network rates and restrictions on out-of-network access, our turning away new patients in instances where we are unable to come to agreement on rates, or decreases in contracted rates could result in a significant decrease in our overall revenues derived from commercial payors. If the average rates that commercial payors pay us decline significantly, or if we see a decline in commercial patients, it would have a material adverse effect on our business, results of operations and financial condition. For additional details regarding specific risks we face regarding regulatory changes that could result in fewer patients covered under commercial plans or an increase of patients covered under more restrictive commercial plans with lower reimbursement rates, see the discussion in the

risk factor under the heading "Healthcare reform could have a material adverse effect on our business, financial condition and results of operations."

If the number of patients with higher-paying commercial insurance declines, it could have a material adverse effect on our business, results of operations and financial condition.

Our revenue levels are sensitive to the percentage of our patients with higher-paying commercial insurance coverage.

A patient's insurance coverage may change for a number of reasons, including changes in the patient's or a family member's employment status. Any changes impacting our highest paying commercial payors will have a disproportionate impact on us. In

addition, many patients with commercial and government insurance rely on financial assistance from charitable organizations, such as the American Kidney Fund. Certain payors have challenged our patients' and other providers' patients' ability to utilize assistance from charitable organizations for the payment of premiums, including through litigation and other legal proceedings. Regulators have also questioned the use of charitable premium assistance for ESRD patients. CMS or another regulatory agency or legislative authority may issue a new rule or guidance that challenges charitable premium assistance. If any of these challenges to kidney patients' use of premium assistance are successful or restrictions are imposed on the use of financial assistance from such charitable organizations such that kidney patients are unable to obtain, or continue to receive or receive for a limited duration, such financial assistance, it could have a material adverse effect on our business, results of operations and financial condition. In addition, if our assumptions about how kidney patients will respond to any change in financial assistance from charitable organizations are incorrect, it could have a material adverse effect on our business, results of operations and financial condition.

When Medicare becomes the primary payor, the payment rate we receive for that patient decreases from the employer group health plan or commercial plan rate to the lower Medicare payment rate. The number of our patients who have government-based programs as their primary payors could increase and the percentage of our patients covered under commercial insurance plans could be negatively impacted as a result of improved mortality or declining macroeconomic conditions. To the extent there are sustained or increased job losses in the U.S., independent of whether general economic conditions improve, we could experience a decrease in the number of patients covered under commercial plans and/or an increase in uninsured and underinsured patients. We could also experience a further decrease in the payments we receive for services if changes to the healthcare regulatory system result in fewer patients covered under commercial plans or an increase of patients covered under more restrictive commercial plans with lower reimbursement rates. In addition, our continual negotiations with commercial payors under existing and potential new agreements could result in a decrease in the number of our patients covered by commercial plans to the extent that we cannot reach agreement with commercial payors on rates and other terms, resulting in termination or non-renewals of existing agreements and our inability to enter into new agreements. Commercial payors have taken and may continue to take steps to control the cost of and/or the eligibility for access to healthcare services, including relative to products on and off the healthcare exchanges. These efforts could impact the number of our patients who are eligible to enroll in commercial insurance plans, and remain on the plans, including plans offered through healthcare exchanges. Additionally, we continue to experience higher amounts of write-offs due to uninsured and underinsured patients, which has resulted in an increase in uncollectible accounts. Commercial payors could also cease paying in the primary position after providing 30 months of coverage resulting in a material reduction in payment as the patient moves to Medicare primary. If there is a significant reduction in the number of patients under higher-paying commercial plans relative to government-based programs that pay at lower rates or a significant increase in the number of patients that are uninsured and underinsured, it would have a material adverse effect on our business, results of operations and financial condition.

Changes in the structure of and payment rates under the Medicare ESRD program could have a material adverse effect on our business, results of operations and financial condition.

Approximately 44% of our U.S. dialysis and related lab services net revenues for the three months ended March 31, 2018 were generated from patients who have Medicare as their primary payor. For patients with Medicare coverage, all ESRD payments for dialysis treatments are made under a single bundled payment rate which provides a fixed payment rate to encompass all goods and services provided during the dialysis treatment, including pharmaceuticals that were historically separately reimbursed to the dialysis providers, such as erythropoietin (EPO), vitamin D analogs and iron supplements, irrespective of the level of pharmaceuticals administered or additional services performed, except in the case of calcimimetics, which are subject to a transitional drug add-on payment adjustment for the Medicare Part B ESRD payment. Most lab services are also included in the bundled payment. Under the ESRD PPS, the bundled payments to a dialysis facility may be reduced by as much as 2% based on the facility's performance in specified quality measures set annually by CMS through the ESRD Quality Incentive Program, which was established by the Medicare Improvements for Patients and Providers Act of 2008. The bundled payment rate is also adjusted for certain patient characteristics, a geographic usage index and certain other factors. In addition, the ESRD PPS is

subject to rebasing, which can have a positive financial effect, or a negative one if the government fails to rebase in a manner that adequately addresses the costs borne by dialysis facilities. Similarly, as new drugs, services or labs are added to the ESRD bundle, CMS' failure to adequately calculate the costs associated with the drugs, services or labs could have a material adverse effect on our business, results of operations and financial condition.

The current bundled payment system presents certain operating, clinical and financial risks, which include:

- Risk that our rates are reduced by CMS. Uncertainty about future payment rates remains a material risk to our business. Each year, CMS publishes a final rule for the PPS, which has been phasing in reductions to the PPS base rate mandated by the American Taxpayer Relief Act of 2012 as modified by the Protecting Access to Medicare Act of 2014.

Risk that CMS, through its contracted Medicare Administrative Contractors (MACs) or otherwise, implements Local Coverage Determinations (LCDs) or other decisions that limit the frequency a provider can bill Medicare for home dialysis treatments or other rules that may impact reimbursement. Such coverage determinations could have an adverse impact on our revenue. There is also risk commercial insurers could incorporate the requirements or limitations associated with such LCDs into their contracted terms with dialysis providers, which could have an adverse impact on our revenue.

Risk that a MAC, or multiple MACs, change their interpretations of existing regulations, manual provisions and/or guidance; or seek to implement or enforce new interpretations that are inconsistent with how we have interpreted existing regulations, manual provisions and/or guidance.

Risk that increases in our operating costs will outpace the Medicare rate increases we receive. We expect operating costs to continue to increase due to inflationary factors, such as increases in labor and supply costs, including increases in maintenance costs and capital expenditures to improve, renovate and maintain our facilities, equipment and information technology to meet changing regulatory requirements, regardless of whether there is a compensating inflation-based increase in Medicare payment rates or in payments under the bundled payment rate system.

Risk of federal budget sequestration cuts. As a result of the Budget Control Act of 2011 and the BBA, an annual 2% reduction to Medicare payments took effect on April 1, 2013 and has been extended through 2027. These across-the-board spending cuts have affected and will continue to adversely affect our business, results of operations and financial condition.

Risk that, if our clinical systems fail to accurately capture the data we report to CMS in connection with claims for which at least part of the government's payments to us is based on clinical performance or patient outcomes or co-morbidities, we might be over-reimbursed by the government, which could subject us to certain liability. For example, CMS published a final rule that implemented a provision of the ACA, requiring providers to report and return Medicare and Medicaid overpayments within the later of (a) 60 days after the overpayment is identified, or (b) the date any corresponding cost report is due, if applicable. An overpayment impermissibly retained under this statute could subject us to liability under the FCA, exclusion, and penalties under the federal Civil Monetary Penalty statute. For additional details regarding the risks we face for failing to adhere to our Medicare and Medicaid regulatory compliance obligations, see the risk factor above under the heading "If we fail to adhere to all of the complex government laws and regulations that apply to our business, we could suffer severe consequences that could have a material adverse effect on our business, results of operations, financial condition and stock price."

Changes in state Medicaid or other non-Medicare government-based programs or payment rates could have a material adverse effect on our business, results of operations and financial condition.

Approximately 25% of our U.S. dialysis and related lab services net revenues for the three months ended March 31, 2018 were generated from patients who have state Medicaid or other non-Medicare government-based programs, such as coverage through the Department of Veterans Affairs (VA), as their primary coverage. As state governments and other governmental organizations face increasing budgetary pressure, we may in turn face reductions in payment rates, delays in the receipt of payments, limitations on enrollee eligibility or other changes to the applicable programs. For example, certain state Medicaid programs and the VA have recently considered, proposed or implemented payment rate reductions.

The VA adopted Medicare's bundled PPS pricing methodology for any veterans receiving treatment from non-VA providers under a national contracting initiative. Since we are a non-VA provider, these reimbursements are tied to a percentage of Medicare reimbursement, and we have exposure to any dialysis reimbursement changes made by CMS. Approximately 3% of our dialysis services revenues for the three months ended March 31, 2018 were generated by the VA.

In 2013, we entered into a five-year Nationwide Dialysis Services contract with the VA which is subject to one-year renewal periods, consistent with all provider agreements with the VA under this contract. During the length of the contract, the VA has elected not to make adjustments to reimbursement percentages that are tied to a percentage of Medicare reimbursement rates. These agreements provide the VA with the right to terminate the agreements without cause on short notice. Should the VA renegotiate, or not renew or cancel these agreements for any reason, we may cease accepting patients under this program and may be forced to close centers or experience lower reimbursement

rates, which could have a material adverse effect on our business, results of operations and financial condition.

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State Medicaid programs are increasingly adopting Medicare-like bundled payment systems, but sometimes these payment systems are poorly defined and are implemented without any claims processing infrastructure, or patient or facility adjusters. If these payment systems are implemented without any adjusters and claims processing changes, Medicaid payments will be substantially reduced and the costs to submit such claims may increase, which will have a negative impact on our business, results of operations and financial condition. In addition, some state Medicaid program eligibility requirements mandate that citizen enrollees in such programs provide documented proof of citizenship. If our patients cannot meet these proof of citizenship documentation requirements, they may be denied coverage under these programs, resulting in decreased patient volumes and revenue. These Medicaid payment and enrollment changes, along with similar changes to other non-Medicare government programs could reduce the rates paid by these programs for dialysis and related services, delay the receipt of payment for services provided and further limit eligibility for coverage which could have a material adverse effect on our business, results of operations and financial condition.

Changes in clinical practices, payment rates or regulations impacting pharmaceuticals could have a material adverse effect on our business, results of operations and financial condition and negatively impact our ability to care for patients.

Medicare bundles certain pharmaceuticals into the PPS at industry average doses and prices. Any variation above the industry average may be subject to partial reimbursement through the PPS outlier reimbursement policy.

Commercial payors have increasingly examined their administration policies for pharmaceuticals and, in some cases, have modified those policies. Changes in labeling of pharmaceuticals in a manner that alters physician practice patterns, including their independent determinations as to appropriate dosing, or accepted clinical practices, and/or changes in private and governmental payment criteria, including the introduction of administration policies could have a material adverse effect on our business, results of operations and financial condition. Further increased utilization of certain pharmaceuticals for patients for whom the cost of which is included in a bundled reimbursement rate, or further decreases in reimbursement for pharmaceuticals that are not included in a bundled reimbursement rate, could also have a material adverse effect on our business, results of operations and financial condition.

Additionally, as of January 1, 2018, calcimimetics became part of the Medicare Part B ESRD payment, but subject to its transitional drug add-on payment adjustment. We implemented processes designed to provide the drug as required under the applicable regulations and prescribed by physicians and have entered into agreements to provide for access to and distribution of the drug. If Medicare Advantage plans and/or Medicaid do not pay as required or the processes we have implemented to provide the drug do not perform as anticipated, then we could be subject to both financial and operational risk, among other things.

We may be subject to increased inquiries or audits from a variety of governmental bodies or claims by third parties, which would require management's attention and could result in significant legal expense. Any negative findings could result in substantial financial penalties or repayment obligations, the imposition of certain obligations on and changes to our practices and procedures as well as the attendant financial burden on us to comply with the obligations, or exclusion from future participation in the Medicare and Medicaid programs, and could have a material adverse effect on our business, results of operations and financial condition.

If we fail to comply with our Corporate Integrity Agreement, we could be subject to substantial penalties and exclusion from participation in federal healthcare programs that could have a material adverse effect on our business, results of operations and financial condition.

In October 2014, we entered into a Settlement Agreement with the United States and relator David Barbetta to resolve the then pending 2010 and 2011 U.S. Attorney physician relationship investigations and paid \$406 million in settlement amounts, civil forfeiture, and interest to the United States and certain states. In connection with the resolution of these matters, and in exchange for the OIG's agreement not to exclude us from participating in the federal healthcare programs, we have entered into a five-year CIA with the OIG. The CIA (i) requires that we maintain certain elements of our compliance programs; (ii) imposes certain expanded compliance-related requirements during the term of the CIA; (iii) requires ongoing monitoring and reporting by an independent monitor, imposes certain reporting, certification, records retention and training obligations, allocates certain oversight responsibility to the Board's Compliance Committee, and necessitates the creation of a Management Compliance Committee and the

retention of an independent compliance advisor to the Board; and (iv) contains certain business restrictions related to a subset of our joint venture arrangements, including our agreeing to (1) unwind 11 joint venture transactions that were created through partial divestitures to, or partial acquisitions from, nephrologists, and that cover 26 of our 2,119 clinics that existed at the time we entered into the Settlement Agreement, all of which have been completed, (2) not enter into certain types of partial divestiture joint venture transactions with nephrologists during the term of the CIA, (3) non-enforcement of certain patient-related non-solicitation restrictions, and (4) certain other restrictions. The costs associated with



compliance with the CIA could be substantial and may be greater than we currently anticipate. In addition, in the event of a breach of the CIA, we could become liable for payment of certain stipulated penalties, and could be excluded from participation in federal healthcare programs. The OIG has notified us in the past that it considered us to be in breach of the CIA, and we cannot provide any assurances that we may not be found in breach of the CIA in the future. In general, the costs associated with compliance with the CIA, or any liability or consequences associated with a breach, could have a material adverse effect on our business, results of operations and financial condition. For our domestic dialysis business, we are required under the CIA to report to the OIG (i) probable violations of criminal, civil or administrative laws applicable to any federal health care program for which penalties or exclusions may be authorized under applicable laws and regulations; (ii) substantial overpayments of amounts of money we have received in excess of the amounts due and payable under the federal healthcare program requirements; and (iii) employment of or contracting with individuals ineligible from participating in the federal healthcare programs (we refer to these collectively as Reportable Events). We have provided the OIG notice of Reportable Events, and we may identify and report additional events in the future. If any of our operations are found to violate government laws and regulations, we could suffer severe consequences that could have a material adverse effect on our business, results of operations, financial condition and stock price, including those consequences described under the risk factor "If we fail to adhere to all of the complex government laws and regulations that apply to our business, we could suffer severe consequences that could have a material adverse effect on our business, results of operations, financial condition and stock price."

Delays in state Medicare and Medicaid certification or other licensing and/or anything impacting the licensing of our dialysis centers could adversely affect our business, results of operations and financial condition.

Before we can begin billing for patients treated in our outpatient dialysis centers who are enrolled in government-based programs, we are required to obtain state and federal certification for participation in the Medicare and Medicaid programs. As state agencies responsible for surveying dialysis centers on behalf of the state and Medicare program face increasing budgetary pressure, certain states are having difficulty keeping up with certifying dialysis centers in the normal course resulting in significant delays in certification. If state governments continue to have difficulty keeping up with certifying new centers in the normal course and we continue to experience significant delays in our ability to treat and bill for services provided to patients covered under government programs, it could cause us to incur write-offs of investments or accelerate the recognition of lease obligations in the event we have to close centers or our centers' operating performance deteriorates, and it could have an adverse effect on our business, results of operations and financial condition. Although the BBA passed in February 2018 allows organizations approved by the Department of Health and Human Services (HHS) to accredit dialysis facilities and imposes certain timing requirements regarding the initiation of initial surveys to determine if certain conditions and requirements for payment have been satisfied, we cannot predict the ultimate impact of these changes. In addition to certifications for Medicare and Medicaid, some states have licensing requirements for ESRD facilities. Delays in licensure, denials of licensure, or withdrawal of licensure could also adversely affect our business, results of operations and financial condition.

If our joint ventures were found to violate the law, we could suffer severe consequences that would have a material adverse effect on our business, results of operations and financial condition.

As of March 31, 2018, we owned a controlling interest in numerous dialysis-related joint ventures, which represented approximately 24% of our net U.S. dialysis and related lab services net revenues for the three months ended March 31, 2018. In addition, we also owned noncontrolling equity investments in several other dialysis related joint ventures. We may continue to increase the number of our joint ventures. Many of our joint ventures with physicians or physician groups also have certain physician owners providing medical director services to centers we own and operate. Because our relationships with physicians are governed by the federal and state anti-kickback statutes, we have sought to structure our joint venture arrangements to satisfy as many federal safe harbor requirements as we believe are commercially reasonable. However, although our joint venture arrangements do not satisfy all of the elements of any safe harbor under the federal Anti-Kickback Statute, they are not automatically prohibited under the federal Anti-Kickback Statute but are susceptible to government scrutiny. For example, in October 2014, we entered into a Settlement Agreement with the United States and relator David Barbetta to resolve the then pending 2010 and

2011 U.S. Attorney physician relationship investigations regarding certain of our joint ventures and paid \$406 million in settlement amounts, civil forfeiture, and interest to the United States and certain states. For further details, see "If we fail to comply with our Corporate Integrity Agreement, we could be subject to substantial penalties and exclusion from participation in federal healthcare programs that could have a material adverse effect on our business, results of operations and financial condition".

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There are significant risks associated with estimating the amount of dialysis revenues and related refund liabilities that we recognize, and if our estimates of revenues and related refund liabilities are materially inaccurate, it could impact the timing and the amount of our revenues recognition or have a material adverse effect on our business, results of operations and financial condition.

There are significant risks associated with estimating the amount of U.S. dialysis and related lab services revenues and related refund liabilities that we recognize in a reporting period. The billing and collection process is complex due to ongoing insurance coverage changes, geographic coverage differences, differing interpretations of contract coverage and other payor issues. Determining applicable primary and secondary coverage for approximately 198,400 U.S. patients at any point in time, together with the changes in patient coverage that occur each month, requires complex, resource-intensive processes. Errors in determining the correct coordination of benefits may result in refunds to payors. Revenues associated with Medicare and Medicaid programs are also subject to estimating risk related to the amounts not paid by the primary government payor that will ultimately be collectible from other government programs paying secondary coverage, the patient's commercial health plan secondary coverage or the patient. Collections, refunds and payor retractions typically continue to occur for up to three years and longer after services are provided. We generally expect our range of U.S. dialysis and related lab services revenues estimating risk to be within 1% of net revenues for the segment. If our estimates of U.S. dialysis and related lab services revenues and related refund liabilities are materially inaccurate, it could impact the timing and the amount of our revenues recognition and have a material adverse impact on our business, results of operations and financial condition.

Our ancillary services and strategic initiatives, including our pharmacy services and our international operations, that we invest in now or in the future may generate losses and may ultimately be unsuccessful. In the event that one or more of these activities is unsuccessful, our business, results of operations and financial condition may be negatively impacted and we may have to write off our investment and incur other exit costs.

Our ancillary services and strategic initiatives are subject to many of the same risks, regulations and laws, as described in the risk factors related to our dialysis business set forth in this Part II, Item 1A, and are also subject to additional risks, regulations and laws specific to the nature of the particular strategic initiative. We expect to add additional service offerings to our business and pursue additional strategic initiatives in the future as circumstances warrant, which could include healthcare services not related to dialysis. Many of these initiatives require or would require investments of both management and financial resources and can generate significant losses for a substantial period of time and may not become profitable in the expected timeframe or at all. There can be no assurance that any such strategic initiative will ultimately be successful. Any significant change in market conditions, or business performance, or in the political, legislative or regulatory environment, may impact the economic viability of any of these strategic initiatives.

If any of our ancillary services or strategic initiatives, including our pharmacy services and our international operations, are unsuccessful, it would have a negative impact on our business, results of operations and financial condition, and we may determine to exit that line of business. We could incur significant termination costs if we were to exit certain of these lines of business. In addition, we may incur a material write-off or an impairment of our investment, including goodwill, in one or more of our ancillary services or strategic initiatives. In that regard, we have taken, and may in the future take, impairment charges related to our ancillary services and strategic initiatives, including in our international and pharmacy businesses.

If a significant number of physicians were to cease referring patients to our dialysis centers, whether due to regulatory or other reasons, it would have a material adverse effect on our business, results of operations and financial condition. Physicians, including medical directors, choose where they refer their patients. Some physicians prefer to have their patients treated at dialysis centers where they or other members of their practice supervise the overall care provided as medical director of the center. As a result, referral sources for many of our centers include the physician or physician group providing medical director services to the center.

Our medical director contracts are for fixed periods, generally ten years, and at any given time a large number of them could be up for renewal at the same time. Medical directors have no obligation to extend their agreements with us and if we are unable to enforce noncompetition provisions contained in terminated medical director agreements, our former medical directors may choose to provide medical director services for competing providers or establish their

own dialysis centers in competition with ours. Neither our current nor former medical directors have an obligation to refer their patients to our centers.

The aging of the nephrologist population and opportunities presented by our competitors may negatively impact a medical director's decision to enter into or extend his or her agreement with us. Moreover, different affiliation models in the changing healthcare environment that limit a nephrologist's choice in where he or she can refer patients, such as an increase in

the number of physicians becoming employed by hospitals or a perceived decrease in the quality of service levels at our centers, may limit a nephrologist's ability or desire to refer patients to our centers or otherwise negatively impact treatment volumes.

In addition, we may take actions to restructure existing relationships or take positions in negotiating extensions of relationships to assure compliance with the federal Anti-Kickback Statute, Stark Law and other similar laws. If the terms of any existing agreement are found to violate applicable laws, we may not be successful in restructuring the relationship, which could lead to the early termination of the agreement. These actions, in an effort to comply with applicable laws and regulations, could negatively impact the decision of physicians to extend their medical director agreements with us. If we are unable to obtain qualified medical directors to provide supervision of the operations and care provided at our dialysis centers, it could affect physicians' desire to refer patients to our dialysis centers. If a significant number of physicians were to cease referring patients to our dialysis centers, it would have a material adverse effect on our business, results of operations and financial condition.

If there are shortages of skilled clinical personnel, or if changes to state staffing ratios are implemented with which we are required to comply, we may experience disruptions in our business operations and increases in operating expenses, among other things, which could have a material adverse effect on our business, results of operations and financial condition.

We face increasing labor costs generally, and in particular, face increased labor costs and difficulties in hiring nurses due to a nationwide shortage of skilled clinical personnel. We compete for nurses with hospitals and other healthcare providers. This nursing shortage may limit our ability to expand our operations. Furthermore, changes in certification requirements can impact our ability to maintain sufficient staff levels, including to the extent our teammates are not able to meet new requirements, among other things. In addition, if we experience a higher than normal turnover rate for our skilled clinical personnel, our operations and treatment growth may be negatively impacted, which could adversely affect our business, results of operations and financial condition.

In addition, currently pending and potential future ballot initiatives or referendums, legislation or policy changes could cause us to incur substantial costs to challenge and prepare for and, if implemented, impose additional requirements on our operations, including increases in the required staffing levels or staffing ratios for clinical personnel, minimum transition times between treatments, limits on how much patients may be charged for care, limitations as to the amount that can be spent on certain medical costs, and a ceiling on the percent of profit for such care. Changes such as these mandated by currently pending and future ballot initiatives or referendums, legislation or policy changes would likely materially reduce our revenues and increase our operating expense and impact our ability to staff our clinics to the new, elevated staffing levels, in particular given the ongoing nationwide shortage of healthcare workers, especially nurses. Any of these events or circumstances could materially reduce our revenues and increase our operating and other costs, require us to close dialysis centers, reduce shifts or negatively impact employee relations, treatment growth and productivity, and could have a material adverse effect on our business, results of operations and financial condition.

Our business is labor intensive and could be materially adversely affected if we are unable to maintain satisfactory relations with our employees or if union organizing activities or legislative changes result in significant increases in our operating costs or decreases in productivity.

Our business is labor intensive, and our financial and operating results have been and continue to be subject to variations in labor-related costs, productivity and the number of pending or potential claims against us related to labor and employment practices. Political or other efforts at the national or local level could result in actions or proposals that increase the likelihood or success of union organizing activities at our facilities and union organizing activities could increase for other reasons. Labor and employment claims, including the filing of class action suits, or work stoppages, wages and benefits or adverse outcomes of these types of claims could trend upwards. Any of these events or circumstances could have a material adverse effect on our employee relations, treatment growth, productivity, business, results of operations and financial condition.

Complications associated with our billing and collections system could materially adversely affect our business, results of operations and financial condition.

Our billing system is critical to our billing operations. If there are defects in the billing system, we may experience difficulties in our ability to successfully bill and collect for services rendered, including a delay in collections, a reduction in the amounts collected, increased risk of retractions from and refunds to commercial and government payors, an increase in our provision for uncollectible accounts receivable and noncompliance with reimbursement regulations, any or all of which could materially adversely affect our results of operations.

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Risk factors primarily related to DMG:

DMG is subject to many of the same risks to which our dialysis business is subject.

As a participant in the healthcare industry, DMG is subject to many of the same risks as our dialysis business is, as described in the risk factors set forth above in this Part II, Item 1A, any of which could have a material adverse effect on DMG's business, results of operations and financial condition.

Under most of DMG's agreements with health plans, DMG assumes some or all of the risk that the cost of providing services will exceed its compensation.

Approximately 83% of DMG's revenue for the three months ended March 31, 2018 is derived from fixed per member per month (PMPM) fees paid by health plans under capitation agreements with DMG or its associated physician groups. While there are variations specific to each arrangement, DMG, through DHPC, a subsidiary of HealthCare Partners Holdings, LLC and a restricted Knox-Keene licensed entity, and, in certain instances, DMG's associated physician groups, generally contract with health plans to receive a PMPM fee for professional services and assume the financial responsibility for professional services only. In some cases, the health plans separately enter into capitation contracts with third parties (typically hospitals) who receive directly a PMPM fee and assume contractual financial responsibility for hospital services. In other cases, the health plan does not pay any portion of the PMPM fee to the hospital, but rather administers claims for hospital expenses itself. In both scenarios, DMG enters into managed care-related administrative services agreements or similar arrangements with those third parties (typically hospitals) under which DMG agrees to be responsible for utilization review, quality assurance, and other managed care-related administrative functions and claim payments. As compensation for such administrative services, DMG is entitled to receive a percentage of the amount by which the institutional capitation revenue received from health plans exceeds institutional expenses; any such risk-share amount to which DMG is entitled is recorded as medical revenues, and DMG is also responsible for a percentage of any short-fall in the event that institutional expenses exceed institutional revenues. To the extent that members require more care than is anticipated and/or the cost of care increases, aggregate fixed PMPM amounts, or capitation payments, may be insufficient to cover the costs associated with treatment. If medical costs and expenses exceed estimates, except in very limited circumstances, DMG will not be able to increase the PMPM fee received under these risk agreements during their then-current terms and could, directly or indirectly through its contracts with its associated physician groups, suffer losses with respect to such agreements.

Changes in DMG's or its associated physician groups' anticipated ratio of medical expense to revenue can significantly impact DMG's financial results. Accordingly, the failure to adequately predict and control medical costs and expenses and to make reasonable estimates and maintain adequate accruals for incurred but not reported claims, could have a material adverse effect on DMG's business, results of operations and financial condition.

Historically, DMG's and its associated physician groups' medical costs and expenses as a percentage of revenue have fluctuated. Factors that may cause medical expenses to exceed estimates include:

- the health status of members;
- higher than expected utilization of new or existing healthcare services or technologies;
- an increase in the cost of healthcare services and supplies, including pharmaceuticals, whether as a result of inflation or otherwise;
- changes to mandated benefits or other changes in healthcare laws, regulations and practices;
- periodic renegotiation of provider contracts with specialist physicians, hospitals and ancillary providers;
- periodic renegotiation of contracts with DMG's affiliated primary care physicians and specialists;
- changes in the demographics of the participating members and medical trends;
- contractual or claims disputes with providers, hospitals or other service providers within and outside of a health plan's network;
- the occurrence of catastrophes, major epidemics or acts of terrorism; and
- the reduction of health plan premiums.

Risk-sharing arrangements that DMG and its associated physician groups have with health plans and hospitals could result in their costs exceeding the corresponding revenues, which could reduce or eliminate any shared risk profitability.

Most of the agreements between health plans and DMG and its associated physician groups contain risk-sharing arrangements under which the physician groups can earn additional compensation from the health plans by coordinating the provision of quality, cost-effective healthcare to members. However, such arrangements may require the physician group to assume a portion of any loss sustained from these arrangements, thereby reducing DMG's net income. Under these risk-sharing arrangements, DMG and its associated physician groups are responsible for a portion of the cost of hospital services or other services that are not capitated. The terms of the particular risk-sharing arrangement allocate responsibility to the respective parties when the cost of services exceeds the related revenue, which results in a deficit, or permit the parties to share in any surplus amounts when actual costs are less than the related revenue. The amount of non-capitated medical and hospital costs in any period could be affected by factors beyond the control of DMG, such as changes in treatment protocols, new technologies, longer lengths of stay by the patient and inflation. Certain of DMG's agreements with health plans stipulate that risk-sharing pool deficit amounts are carried forward to offset any future years' surplus amounts DMG would otherwise be entitled to receive. DMG accrues for any such risk-sharing deficits. To the extent that such non-capitated medical and hospital costs are higher than anticipated, revenue may not be sufficient to cover the risk-sharing deficits the health plans and DMG are responsible for, which could have a material adverse effect on DMG's business, results of operations and financial condition.

Renegotiation, renewal or termination of capitation agreements with health plans could have a material adverse effect on DMG's business, results operations and financial condition.

Under most of DMG's and its associated physician groups' capitation agreements with health plans, the health plan is generally permitted to modify the benefit and risk obligations and compensation rights from time to time during the terms of the agreements. If a health plan exercises its right to amend its benefit and risk obligations and compensation rights, DMG and its associated physician groups are generally allowed a period of time to object to such amendment. If DMG or its associated physician group so objects, under some of the risk agreements, the relevant health plan may terminate the applicable agreement upon 90 to 180 days written notice. If DMG or its associated physician groups enter into capitation contracts or other risk sharing arrangements with unfavorable economic terms, or a capitation contract is amended to include unfavorable terms, DMG could, directly or indirectly through its contracts with its associated physician groups, suffer losses with respect to such contract. Since DMG does not negotiate with CMS or any health plan regarding the benefits to be provided under their Medicare Advantage plans, DMG often has just a few months to familiarize itself with each new annual package of benefits it is expected to offer. Depending on the health plan at issue and the amount of revenue associated with the health plan's risk agreement, the renegotiated terms or termination could have a material adverse effect on DMG's business, results of operations and financial condition. If DMG's agreements or arrangements with any physician equity holder(s) of associated physicians, physician groups or independent practice associations (IPAs) are deemed invalid under state law, including laws against the corporate practice of medicine, or federal law, or are terminated as a result of changes in state law, or if there is a change in accounting standards by the Financial Accounting Standards Board (FASB) or the interpretation thereof affecting consolidation of entities, it could have a material adverse effect on DMG's consolidation of total revenues derived from such associated physician groups.

DMG's financial statements are consolidated in accordance with applicable accounting standards and include the accounts of its majority-owned subsidiaries and certain non-owned DMG-associated and managed physician groups. Such consolidation for accounting and/or tax purposes does not, is not intended to, and should not be deemed to, imply or provide to DMG any control over the medical or clinical affairs of such physician groups. In the event of a change in accounting standards promulgated by FASB or in interpretation of its standards, or if there is an adverse determination by a regulatory agency or a court, or a change in state or federal law relating to the ability to maintain present agreements or arrangements with such physician groups, DMG may not be permitted to continue to consolidate the total revenues of such organizations. A change in accounting for consolidation with respect to DMG's present agreement or arrangements would diminish DMG's reported revenues but would not be expected to materially



and adversely affect its reported results of operations, while regulatory or legal rulings or changes in law interfering with DMG's ability to maintain its present agreements or arrangements could materially diminish both revenues and results of operations.

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If DHPC is not able to satisfy financial solvency or other regulatory requirements, we could become subject to sanctions and its license to do business in California could be limited, suspended or terminated, which could have a material adverse effect on DMG's business, results of operations and financial condition.

Knox-Keene requires healthcare service plans operating in California to comply with financial solvency and other requirements overseen by the California Department of Managed HealthCare (DMHC). Under Knox-Keene, DHPC is required to, among other things:

- Maintain, at all times, a minimum tangible net equity (TNE);

- Submit periodic financial solvency reports to the DMHC containing various data regarding performance and financial solvency;

- Comply with extensive regulatory requirements; and

- Submit to periodic regulatory audits and reviews concerning DHPC operations and compliance with Knox-Keene.

In the event that DHPC is not in compliance with the provisions of Knox-Keene, we could be subject to sanctions, or limitations on, or suspension of its license to do business in California, which could have a material adverse effect on DMG's business, results of operations and financial condition.

If DMG's associated physician group is not able to satisfy the California DMHC's financial solvency requirements, DMG's associated physician group could become subject to sanctions and DMG's ability to do business in California could be limited or terminated, which could have a material adverse effect on DMG's business, results of operations and financial condition.

The California DMHC has instituted financial solvency regulations to monitor the financial solvency of capitated physician groups. Under these regulations, DMG's associated physician group is required to, among other things: Maintain, at all times, a minimum cash-to-claims ratio (where cash-to-claims ratio means the organization's cash, marketable securities and certain qualified receivables, divided by the organization's total unpaid claims liability). The regulation currently requires a cash-to-claims ratio of 0.75.

- Submit periodic reports to the California DMHC containing various data and attestations regarding performance and financial solvency, including incurred but not reported calculations and documentation, and attestations as to whether or not the organization was in compliance with Knox-Keene requirements related to claims payment timeliness, had maintained positive TNE (i.e., at least \$1.00) and had maintained positive working capital (i.e., at least \$1.00).

In the event that DMG's associated physician group is not in compliance with any of the above criteria, DMG's associated physician group could be subject to sanctions, or limitations on, or removal of, its ability to do business in California, which could have a material adverse effect on DMG's business, results of operations and financial condition.

Reductions in Medicare Advantage health plan reimbursement rates stemming from healthcare reforms and any future related regulations could have a material adverse effect on DMG's business, results of operations and financial condition.

A significant portion of DMG's revenue is directly or indirectly derived from the monthly premium payments paid by CMS to health plans for medical services provided to Medicare Advantage enrollees. As a result, DMG's results of operations are, in part, dependent on government funding levels for Medicare Advantage programs. Any changes that limit or reduce Medicare Advantage reimbursement levels, such as reductions in or limitations of reimbursement amounts or rates under programs, reductions in funding of programs, expansion of benefits without adequate funding, elimination of coverage for certain benefits, or elimination of coverage for certain individuals or treatments under programs, could have a material adverse effect on DMG's business, results of operations and financial condition.

Each year, CMS issues a final rule to establish the Medicare Advantage benchmark payment rates for the following calendar year. Any reduction to Medicare Advantage rates impacting DMG that is greater compared to the industry average rate may have material adverse effect on DMG's business, results of operations and financial condition. The final impact of the Medicare Advantage rates can vary from any estimate we may have and may be further impacted by the relative growth of DMG's Medicare Advantage patient volumes across markets as well as by the benefit plan designs submitted. It is possible that



we may underestimate the impact of the Medicare Advantage rates on our business, which could have a material adverse effect on DMG's business, results of operations and financial condition.

We took impairment charges against the goodwill of several of our DMG reporting units in five of the ten quarters since the fourth quarter of 2015 based on continuing developments in our DMG business, including recent annual updates to Medicare Advantage benchmark reimbursement rates, changes in our expectations concerning future government reimbursement rates and our expected ability to mitigate them, medical cost and utilization trends, commercial pricing pressures, commercial membership rates, underperformance of certain at-risk reporting units and other market factors. We may also need to take additional impairment charges against earnings in a future period, depending on the impact of continuing developments on the value of our DMG business. Specifically, if DMG's fair value less the costs incurred in the sale of DMG falls below its carrying amount, we may need to recognize additional impairment charges on this business, and the amount of such charges, if any, could be significant. Our estimates of the fair value of this business rely on certain estimates and assumptions, including the terms and pricing agreed for the sale of this business, as well as applicable market multiples, discount and long-term growth rates, market data and future reimbursement rates, as applicable. Our estimates of the fair value of the DMG business could differ from the actual value that a market participant would pay for this business.

DMG's Medicare Advantage revenues may continue to be volatile in the future, which could have a material adverse impact on DMG's business, results of operations and financial condition.

The ACA contains a number of provisions that negatively impact Medicare Advantage plans, each of which could have a material adverse effect on DMG's business, results of operations and financial condition. These provisions include the following:

Medicare Advantage benchmarks for 2011 were frozen at 2010 levels. From 2012 through 2016, Medicare Advantage benchmark rates were phased down from prior levels. The new benchmarks were fully phased-in in 2017 and range between 95% and 115% of the Medicare Fee-for-Service (Medicare FFS) costs, depending on a plan's geographic area. If our costs escalate faster than can be absorbed by the level of revenues implied by these benchmark rates, then it could have a material adverse effect on DMG's business and results of operations.

• Rebates received by Medicare Advantage plans that were reduced, with larger reductions for plans failing to receive certain quality ratings.

The Secretary of the HHS has been granted the explicit authority to deny Medicare Advantage plan bids that propose significant increases in cost sharing or decreases in benefits. If the bids submitted by plans contracted with DMG are denied, this could have a material adverse effect on DMG's business and results of operations.

• Medicare Advantage plans with medical loss ratios below 85% are required to pay a rebate to the Secretary of HHS. The rebate amount is the total revenue under the contract year multiplied by the difference between 85% and the plan's actual medical loss ratio. The Secretary of HHS will halt enrollment in any plan failing to meet this ratio for three consecutive years, and terminate any plan failing to meet the ratio for five consecutive years. If a DMG-contracting Medicare Advantage plan experiences a limitation on enrollment or is otherwise terminated from the Medicare Advantage program, it could have a material adverse effect on DMG's business and results of operations.

• Prescription drug plans are required to provide coverage of certain drug categories on a list developed by the Secretary of HHS, which could increase the cost of providing care to Medicare Advantage enrollees, and thereby reduce DMG's revenues and earnings. The Medicare Part D premium amount subsidized for high-income beneficiaries has been reduced, which could lower the number of Medicare Advantage enrollees, which would have a negative impact on DMG's business and results of operations.

• CMS increased coding intensity adjustments for Medicare Advantage plans beginning in 2014 and continuing through 2018, which reduces CMS payments to Medicare Advantage plans, which in turn will likely reduce the amounts payable to DMG and its associated physicians, physician groups, and IPAs under its capitation agreements.

Recent legislative and executive efforts to enact further healthcare reform legislation have caused the future state of the exchanges, other ACA reforms, and many core aspects of the current U.S. health care system to be unclear. For example, in October 2017, the federal government announced that cost-sharing reduction payments to insurers would end, effective immediately, unless Congress appropriated the funds, and, in December 2017, Congress passed the Tax

Cuts and Jobs Act, which includes a provision that eliminates the penalty under the ACA's individual mandate effective January 1, 2019 and could impact the future state of the exchanges. Further, in February 2018, Congress passed the BBA which, among other things, repealed the Independent Payment Advisory Board that was established by the ACA and intended to reduce the rate of growth

in Medicare spending. While certain provisions of the BBA may increase the scope of benefits available for certain chronically ill Federal health care program beneficiaries beginning in 2020, the ultimate impact of such changes cannot be predicted. While specific changes and their timing are not yet apparent, enacted reforms and future legislative, regulatory, or executive changes could have a material adverse effect on DMG's business, results of operations and financial condition.

There is also uncertainty regarding both Medicare Advantage payment rates and beneficiary enrollment, which, if reduced, would reduce DMG's overall revenues and net income. For example, although the Congressional Budget Office (CBO) predicted in 2010 that Medicare Advantage participation would drop substantially by 2020, the CBO has more recently predicted, without taking into account potential future reforms, that enrollment in Medicare Advantage (and other contracts covering Medicare Parts A and B) could reach 31 million by 2027. Although Medicare Advantage enrollment increased by approximately 5.6 million, or by 50%, between the enactment of the ACA in 2010 and 2015, there can be no assurance that this trend will continue. Further, fluctuation in Medicare Advantage payment rates are evidenced by CMS's annual announcement of the expected average change in revenue from the prior year: for 2018, CMS announced an average increase of 0.45%; and for 2019, 1.8%. Uncertainty over Medicare Advantage enrollment and payment rates present a continuing risk to DMG's business.

According to the Kaiser Family Foundation (KFF), Medicare Advantage enrollment continues to be highly concentrated among a few payors, both nationally and in local regions. In 2017, the KFF reported that three payors together accounted for more than half of Medicare Advantage enrollment and eight firms accounted for approximately 75% of the lives. In 441 counties in 2018, only one company will offer Medicare Advantage plans. Consolidation among Medicare Advantage plans in certain regions, or the Medicare program's failure to attract additional plans to participate in the Medicare Advantage program, could have a material adverse effect on DMG's business, results of operations and financial condition.

DMG's operations are dependent on competing health plans and, at times, a health plan's and DMG's economic interests may diverge.

For the three months ended March 31, 2018, 71% of DMG's consolidated capitated medical revenues were earned through contracts with three health plans.

DMG expects that, going forward, substantially all of its revenue will continue to be derived from its contracts with health plans. Each health plan may immediately terminate any of DMG's contracts and/or any individual credentialed physician upon the occurrence of certain events. They may also amend the material terms of the contracts under certain circumstances. Failure to maintain the contracts on favorable terms, for any reason, would materially and adversely affect DMG's results of operations and financial condition. A material decline in the number of members could also have a material adverse effect on DMG's results of operations.

Notwithstanding each health plan's and DMG's current shared interest in providing service to DMG's members who are enrolled in the subject health plans, the health plans may have different and, at times, opposing economic interests from those of DMG. The health plans provide a wide range of health insurance services across a wide range of geographic regions, utilizing a vast network of providers. As a result, they and DMG may have different views regarding the proper pricing of services and/or the proper pricing of the various service providers in their provider networks, the cost of which DMG bears to the extent that the services of such service providers are utilized. These health plans may also have different views than DMG regarding the efforts and expenditures that they, DMG, and/or other service providers should make to achieve and/or maintain various quality ratings. In addition, several health plans have acquired or announced their intent to acquire provider organizations. If health plans with which DMG contracts acquire a significant number of provider organizations, they may not continue to contract with DMG or contract on less favorable terms or seek to prevent DMG from acquiring or entering into arrangements with certain providers. Similarly, as a result of changes in laws, regulations, consumer preferences, or other factors, the health plans may find it in their best interest to provide health insurance services pursuant to another payment or reimbursement structure. In the event DMG's interests diverge from the interests of the health plans, DMG may have limited recourse or alternative options in light of its dependence on these health plans. There can be no assurances that DMG will continue to find it mutually beneficial to work with these health plans. As a result of various restrictive provisions that appear in some of the managed care agreements with health plans, DMG may at times have limitations

on its ability to cancel an agreement with a particular health plan and immediately thereafter contract with a competing health plan with respect to the same service area.

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DMG and its associated physicians, physician groups and IPAs and other physicians may be required to continue providing services following termination or renegotiation of certain agreements with health plans.

There are circumstances under federal and state law pursuant to which DMG and its associated physician groups, IPAs and other physicians could be obligated to continue to provide medical services to DMG members in their care following a termination of their applicable risk agreement with health plans and termination of the receipt of payments thereunder. In certain cases, this obligation could require the physician group or IPA to provide care to such member following the bankruptcy or insolvency of a health plan. Accordingly, the obligations to provide medical services to DMG members (and the associated costs) may not terminate at the time the applicable agreement with the health plan terminates, and DMG may not be able to recover its cost of providing those services from the health plan, which could have a material adverse effect on DMG's business, results of operations and financial condition.

DMG operates primarily in California, Florida, Nevada, New Mexico, Washington and Colorado and may not be able to successfully establish a presence in new geographic regions.

DMG derives substantially all of its revenue from operations in California, Florida, Nevada, New Mexico, Washington and Colorado (which we refer to as the Existing Geographic Regions). As a result, DMG's exposure to many of the risks described herein is not mitigated by a greater diversification of geographic focus. Furthermore, due to the concentration of DMG's operations in the Existing Geographic Regions, it may be adversely affected by economic conditions, natural disasters (such as earthquakes or hurricanes), or acts of war or terrorism that disproportionately affect the Existing Geographic Regions as compared to other states and geographic markets. To expand the operations of its network outside of the Existing Geographic Regions, DMG must devote resources to identify and explore perceived opportunities. Thereafter, DMG must, among other things, recruit and retain qualified personnel, develop new offices, establish potential new relationships with one or more health plans, and establish new relationships with physicians and other healthcare providers. The ability to establish such new relationships may be significantly inhibited by competition for such relationships and personnel in the healthcare marketplace in the targeted new geographic regions. Additionally, DMG may face the risk that a substantial portion of the patients served in a new geographic area may be enrolled in a Medicare FFS program and will not desire to transition to a Medicare Advantage program, such as those offered through the health plans that DMG serves, or they may enroll with other health plans with whom DMG does not contract to receive services, which could reduce substantially DMG's perceived opportunity in such geographic area. In addition, if DMG were to seek to expand outside of the Existing Geographic Regions, DMG would be required to comply with laws and regulations of states that may differ from the ones in which it currently operates, and could face competitors with greater knowledge of such local markets. DMG anticipates that any geographic expansion may require it to make a substantial investment of management time, capital and/or other resources. There can be no assurance that DMG will be able to establish profitable operations or relationships in any new geographic markets.

Reductions in the quality ratings of the health plans DMG serves could have a material adverse effect on its business, results of operations and financial condition.

As a result of the ACA, the level of reimbursement each health plan receives from CMS is dependent, in part, upon the quality rating of the Medicare plan. Such ratings impact the percentage of any cost savings rebate and any bonuses earned by such health plan. Since a significant portion of DMG's revenue is expected to be calculated as a percentage of CMS reimbursements received by these health plans with respect to DMG members, reductions in the quality ratings of a health plan that DMG serves could have a material adverse effect on its business, results of operations and financial condition.

Given each health plan's control of its plans and the many other providers that serve such plans, DMG believes that it will have limited ability to influence the overall quality rating of any such plan. The BBA passed in February 2018 implements certain changes to prevent artificial inflation of star ratings for Medicare Advantage plans offered by the same organization. In addition, CMS has terminated plans that have had a rating of less than three stars for three consecutive years, whereas Medicare Advantage plans with five stars are permitted to conduct enrollment throughout almost the entire year. Although CMS' authority to terminate plans solely for failing to achieve the minimum quality star ratings has been suspended through the end of plan year 2018, low quality ratings can still potentially lead to the termination of a plan that DMG serves, DMG may not be able to prevent the potential termination of a contracting



plan or a shift of patients to other plans based upon quality issues which could, in turn, have a material adverse effect on DMG's business, results of operations and financial condition.

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DMG's records and submissions to a health plan may contain inaccurate or unsupported information regarding risk adjustment scores of members, which could cause DMG to overstate or understate its revenue and subject it to various penalties.

DMG, on behalf of itself and its associated physicians, physician groups and IPAs, submits to health plans claims and encounter data that support the Medicare Risk Adjustment Factor (RAF) scores attributable to members. These RAF scores determine, in part, the revenue to which the health plans and, in turn, DMG is entitled for the provision of medical care to such members. The data submitted to CMS by each health plan is based, in part, on medical charts and diagnosis codes prepared and submitted by DMG. Each health plan generally relies on DMG and its employed or affiliated physicians to appropriately document and support such RAF data in DMG's medical records. Each health plan also relies on DMG and its employed or affiliated physicians to appropriately code claims for medical services provided to members. Erroneous claims and erroneous encounter records and submissions could result in inaccurate PMPM fee revenue and risk adjustment payments, which may be subject to correction or retroactive adjustment in later periods. This corrected or adjusted information may be reflected in financial statements for periods subsequent to the period in which the revenue was recorded. DMG might also need to refund a portion of the revenue that it received, which refund, depending on its magnitude, could damage its relationship with the applicable health plan and could have a material adverse effect on DMG's business, results of operations and financial condition.

In June 2015, we received a subpoena from the OIG requesting information relating to our and our subsidiaries' (including DMG's and its subsidiary JSA's) provision of services to Medicare Advantage plans and related patient diagnosis coding and risk adjustment submissions and payments. See Note 10 to the condensed consolidated financial statements included in this report for further details and discussions of legal proceedings elsewhere in these Risk Factors.

Additionally, CMS audits Medicare Advantage plans for documentation to support RAF-related payments for members chosen at random. The Medicare Advantage plans ask providers to submit the underlying documentation for members that they serve. It is possible that claims associated with members with higher RAF scores could be subject to more scrutiny in a CMS or plan audit. There is a possibility that a Medicare Advantage plan may seek repayment from DMG should CMS make any payment adjustments to the Medicare Advantage plan as a result of its audits. The plans also may hold DMG liable for any penalties owed to CMS for inaccurate or unsupported RAF scores provided by DMG. In addition, DMG could be liable for penalties to the government under the FCA that range from \$5,500 to \$11,000 (adjusted for inflation) for each false claim, plus up to three times the amount of damages caused by each false claim, which can be as much as the amounts received directly or indirectly from the government for each such false claim. On January 29, 2018, the DOJ issued a final rule announcing adjustments to FCA penalties, under which the per claim penalty range increases from \$11,181 to \$22,363 for penalties assessed after January 29, 2018, so long as the underlying conduct occurred after November 2, 2015.

CMS has indicated that payment adjustments will not be limited to RAF scores for the specific Medicare Advantage enrollees for which errors are found but may also be extrapolated to the entire Medicare Advantage plan subject to a particular CMS contract. CMS has described its audit process as plan-year specific and stated that it will not extrapolate audit results for plan years prior to 2011. Because CMS has not stated otherwise, there is a risk that payment adjustments made as a result of one plan year's audit would be extrapolated to prior plan years after 2011. There can be no assurance that a health plan will not be randomly selected or targeted for review by CMS or that the outcome of such a review will not result in a material adjustment in DMG's revenue and profitability, even if the information DMG submitted to the plan is accurate and supportable.

Separately, as described in further detail in Note 10 to the condensed consolidated financial statements included in this report, in March 2015, JSA, a subsidiary of DMG, received a subpoena from the OIG that relates, in part, to risk adjustment practices and data. See also discussions of legal proceedings elsewhere in these Risk Factors.

A failure to accurately estimate incurred but not reported medical expense could adversely affect DMG's results of operations.

Patient care costs include estimates of future medical claims that have been incurred by the patient but for which the provider has not yet billed DMG. These claim estimates are made utilizing actuarial methods and are continually evaluated and adjusted by management, based upon DMG's historical claims experience and other factors, including

an independent assessment by a nationally recognized actuarial firm. Adjustments, if necessary, are made to medical claims expense and capitated revenues when the assumptions used to determine DMG's claims liability changes and when actual claim costs are ultimately determined.

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Due to the inherent uncertainties associated with the factors used in these estimates and changes in the patterns and rates of medical utilization, materially different amounts could be reported in DMG's financial statements for a particular period under different conditions or using different, but still reasonable, assumptions. It is possible that DMG's estimates of this type of claim may be inadequate in the future. In such event, DMG's results of operations could be adversely impacted. Further, the inability to estimate these claims accurately may also affect DMG's ability to take timely corrective actions, further exacerbating the extent of any adverse effect on DMG's results of operations. DMG faces certain competitive threats which could reduce DMG's profitability and increase competition for patients. DMG faces certain competitive threats based on certain features of the Medicare programs, including the following: As a result of the direct and indirect impacts of the ACA, many Medicare beneficiaries may decide that an original Medicare FFS program is more attractive than a Medicare Advantage plan. As a result, enrollment in the health plans DMG serves may decrease.

Managed care companies offer alternative products such as regional preferred provider organizations (PPOs) and private FFS plans. Medicare PPOs and private FFS plans allow their patients more flexibility in selecting physicians than Medicare Advantage health plans, which typically require patients to coordinate care with a primary care physician. The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 has encouraged the creation of regional PPOs through various incentives, including certain risk corridors, or cost reimbursement provisions, a stabilization fund for incentive payments, and special payments to hospitals not otherwise contracted with a Medicare Advantage plan that treat regional plan enrollees. The formation of regional Medicare PPOs and private FFS plans may affect DMG's relative attractiveness to existing and potential Medicare patients in their service areas.

The payments for the local and regional Medicare Advantage plans are based on a competitive bidding process that may indirectly cause a decrease in the amount of the PMPM fee or result in an increase in benefits offered.

The annual enrollment process and subsequent lock-in provisions of the ACA may adversely affect DMG's level of revenue growth as it will limit the ability of a health plan to market to and enroll new Medicare beneficiaries in its established service areas outside of the annual enrollment period.

CMS allows Medicare beneficiaries who are enrolled in a Medicare Advantage plan with a quality rating of 4.5 stars or less to enroll in a 5-star rated Medicare Advantage plan at any time during the benefit year. Therefore, DMG may face a competitive disadvantage in recruiting and retaining Medicare beneficiaries.

In addition to the competitive threats intrinsic to the Medicare programs, competition among health plans and among healthcare providers may also have a negative impact on DMG's profitability. For example, due to the large population of Medicare beneficiaries, DMG's Existing Geographic Regions have become increasingly attractive to health plans that may compete with DMG. DMG may not be able to continue to compete profitably in the healthcare industry if additional competitors enter the same market. If DMG cannot compete profitably, the ability of DMG to compete with other service providers that contract with competing health plans may be substantially impaired. Furthermore, if DMG is unable to obtain new members or experiences a loss of existing members to competitors during the open enrollment period for Medicare it could have a material adverse effect on DMG's business, results of operations and financial condition.

DMG competes directly with various regional and local companies that provide similar services in DMG's Existing Geographic Regions. DMG's competitors vary in size and scope and in terms of products and services offered. DMG believes that some of its competitors and potential competitors may be significantly larger than DMG and have greater financial, sales, marketing and other resources. Furthermore, it is DMG's belief that some of its competitors may make strategic acquisitions or establish cooperative relationships among themselves.

A disruption in DMG's healthcare provider networks could have a material adverse effect on DMG's operations and profitability.

In any particular service area, healthcare providers or provider networks could refuse to contract with DMG, demand higher payments, or take other actions that could result in higher healthcare costs, disruption of benefits to DMG's members, or difficulty in meeting applicable regulatory or accreditation requirements. In some service areas, healthcare providers or provider networks may have significant market positions. If healthcare providers or provider networks refuse to contract with DMG, use their market position to negotiate favorable contracts, or place DMG at a

competitive disadvantage, then DMG's ability to market or to be profitable in those service areas could be adversely affected. DMG's provider networks could also be

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disrupted by the financial insolvency of a large provider group. Any disruption in DMG's provider networks could result in a loss of members or higher healthcare costs.

DMG's revenues and profits could be diminished if DMG fails to retain and attract the services of key primary care physicians.

Key primary care physicians with large patient enrollment could retire, become disabled, terminate their provider contracts, get lured away by a competing independent physician association or medical group, or otherwise become unable or unwilling to continue practicing medicine or contracting with DMG or its associated physicians, physician groups or IPAs. In addition, DMG's associated physicians, physician groups and IPAs could view the business model as unfavorable or unattractive to such providers, which could cause such associated physicians, physician groups or IPAs to terminate their relationships with DMG. Moreover, given limitations relating to the enforcement of post-termination noncompetition covenants in California, it would be difficult to restrict a primary care physician from competing with DMG's associated physicians, physician groups or IPAs. As a result, members who have been served by such physicians could choose to enroll with competitors' physician organizations or could seek medical care elsewhere, which could reduce DMG's revenues and profits. Moreover, DMG may not be able to attract new physicians to replace the services of terminating physicians or to service its growing membership.

Participation in ACO programs is subject to federal regulation, supervision, and evolving regulatory developments that may result in financial liability.

The ACA established the Medicare Shared Savings Program (MSSP) for ACOs, which took effect in January 2012. Under the MSSP, eligible organizations are accountable for the quality, cost and overall care of Medicare beneficiaries assigned to an ACO and may be eligible to share in any savings below a specified benchmark amount. The Secretary of HHS is also authorized, but not required, to use capitation payment models with ACOs. DMG has formed an MSSP ACO through a subsidiary, which operates in California, Florida, and Nevada and is evaluating whether to participate in more ACOs in the future. The continued development and expansion of ACOs will have an uncertain impact on DMG's revenue and profitability. DaVita Kidney Care is also participating as a dialysis provider in Arizona, Florida, New Jersey, and Pennsylvania for the Innovation Center's CEC Model.

The ACO programs are relatively new and therefore operational and regulatory guidance is limited. It is possible that the operations of DMG's subsidiary ACO may not fully comply with current or future regulations and guidelines applicable to ACOs, may not achieve quality targets or cost savings, or may not attract or retain sufficient physicians or patients to allow DMG to meet its objectives. Additionally, poor performance could put the DMG ACO at financial risk with a potential obligation to CMS. Traditionally, other than fee-for-service billing by the medical clinics and healthcare facilities operated by DMG, DMG has not directly contracted with CMS and has not operated any health plans or provider sponsored networks. Therefore, DMG may not have the necessary experience, systems or compliance to successfully achieve a positive return on its investment in the ACO or to avoid financial or regulatory liability. DMG believes that its historical experience with fully delegated managed care will be applicable to operation of its subsidiary ACO, but there can be no such assurance.

California hospitals may terminate their agreements with HealthCare Partners Affiliates Medical Group and DaVita Health Plan of California, Inc. (formerly HealthCare Partners Plan, Inc., and, together with HealthCare Partners Affiliates Medical Group (AMG)) or reduce the fees they pay to DMG.

In California, AMG maintains significant hospital arrangements designed to facilitate the provision of coordinated hospital care with those services provided to members by AMG and its associated physicians, physician groups and IPAs. Through contractual arrangements with certain key hospitals, AMG provides utilization review, quality assurance and other management services related to the provision of patient care services to members by the contracted hospitals and downstream hospital contractors. In the event that any one of these key hospital agreements is amended in a financially unfavorable manner or is otherwise terminated, such events could have a material adverse effect on DMG's business, results of operations and financial condition.

DMG's professional liability and other insurance coverage may not be adequate to cover DMG's potential liabilities. DMG maintains primary professional liability insurance and other insurance coverage through California Medical Group Insurance Company, Risk Retention Group, an Arizona corporation in which DMG is the majority owner, and through excess coverage contracted through third-party insurers. DMG believes such insurance is adequate based on

its review of what it believes to be all applicable factors, including industry standards. Nonetheless, potential liabilities may not be covered by insurance, insurers may dispute coverage or may be unable to meet their obligations, the amount of insurance coverage and/or

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related reserves may be inadequate, or the amount of any DMG self-insured retention may be substantial. There can be no assurances that DMG will be able to obtain insurance coverage in the future, or that insurance will continue to be available on a cost-effective basis, if at all. Moreover, even if claims brought against DMG are unsuccessful or without merit, DMG would have to defend itself against such claims. The defense of any such actions may be time-consuming and costly and may distract DMG management's attention. As a result, DMG may incur significant expenses and may be unable to effectively operate its business.

Changes in the rates or methods of third-party reimbursements may materially adversely affect DMG business, results of operations and financial condition.

Any negative changes in governmental capitation or FFS rates or methods of reimbursement for the services DMG provides could have a material adverse effect on DMG's business, results of operations and financial condition. Since governmental healthcare programs generally reimburse on a fee schedule basis rather than on a charge-related basis, DMG generally cannot increase its revenues from these programs by increasing the amount it charges for its services. Moreover, if DMG's costs increase, DMG may not be able to recover its increased costs from these programs. Government and private payors have taken and may continue to take steps to control the cost, eligibility for, use, and delivery of healthcare services due to budgetary constraints, and cost containment pressures as well as other financial issues. DMG believes that these trends in cost containment will continue. These cost containment measures, and other market changes in non-governmental insurance plans have generally restricted DMG's ability to recover, or shift to non-governmental payors, any increased costs that DMG experiences. DMG's business, results of operations and financial condition may be materially adversely affected by these cost containment measures, and other market changes.

DMG's business model depends on numerous complex management information systems and any failure to successfully maintain these systems or implement new systems could materially harm DMG's operations and result in potential violations of healthcare laws and regulations.

DMG depends on a complex, specialized, and integrated management information system and standardized procedures for operational and financial information, as well as for DMG's billing operations. DMG may experience unanticipated delays, complications or expenses in implementing, integrating, and operating these integrated systems. Moreover, DMG may be unable to enhance its existing management information system or implement new management information systems where necessary. DMG's management information system may require modifications, improvements or replacements that may require both substantial expenditures as well as interruptions in operations. DMG's ability to implement and operate its integrated systems is subject to the availability of information technology and skilled personnel to assist DMG in creating and maintaining these systems.

DMG's failure to successfully implement and maintain all of its systems could have a material adverse effect on its business, financial condition and results of operations. For example, DMG's failure to successfully operate its billing systems could lead to potential violations of healthcare laws and regulations. If DMG is unable to handle its claims volume, or if DMG is unable to pay claims timely, DMG may become subject to a health plan's corrective action plan or de-delegation until the problem is corrected, and/or termination of the health plan's agreement with DMG. This could have a material adverse effect on DMG's operations and profitability. In addition, if DMG's claims processing system is unable to process claims accurately, the data DMG uses for its incurred but not reported estimates could be incomplete and DMG's ability to accurately estimate claims liabilities and establish adequate reserves could be adversely affected. Finally, if DMG's management information systems are unable to function in compliance with applicable state or federal rules and regulations, including medical information confidentiality laws such as HIPAA, possible penalties and fines due to this lack of compliance could have a material adverse effect on DMG's financial condition, and results of operations.

DMG may be impacted by eligibility changes to government and private insurance programs.

Due to potential decreased availability of healthcare through private employers, the number of patients who are uninsured or participate in governmental programs may increase. The ACA has increased the participation of individuals in the Medicaid program in states that elected to participate in the expanded Medicaid coverage. A shift in payor mix from managed care and other private payors to government payors as well as an increase in the number of uninsured patients may result in a reduction in the rates of reimbursement to DMG or an increase in uncollectible



receivables or uncompensated care, with a corresponding decrease in net revenue. Changes in the eligibility requirements for governmental programs such as the Medicaid program under the ACA and state decisions on whether to participate in the expansion of such programs also could increase the number of patients who participate in such programs and the number of uninsured patients. Even for those patients who remain in private insurance plans, changes to those plans could increase patient financial responsibility, resulting in a greater risk of

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uncollectible receivables. These factors and events could have a material adverse effect on DMG's business, results of operations and financial condition.

Negative publicity regarding the managed healthcare industry generally or DMG in particular could adversely affect DMG's results of operations or business.

Negative publicity regarding the managed healthcare industry generally, the Medicare Advantage program or DMG in particular, may result in increased regulation and legislative review of industry practices that further increase DMG's costs of doing business and adversely affect DMG's results of operations or business by:

- requiring DMG to change its products and services;

- increasing the regulatory, including compliance, burdens under which DMG operates, which, in turn, may negatively impact the manner in which DMG provides services and increase DMG's costs of providing services;

- adversely affecting DMG's ability to market its products or services through the imposition of further regulatory restrictions regarding the manner in which plans and providers market to Medicare Advantage enrollees; or

- adversely affecting DMG's ability to attract and retain members.

Risk factors related to ownership of our common stock:

Provisions in our charter documents, compensation programs and Delaware law may deter a change of control that our stockholders would otherwise determine to be in their best interests.

Our charter documents include provisions that may deter hostile takeovers, delay or prevent changes of control or changes in our management, or limit the ability of our stockholders to approve transactions that they may otherwise determine to be in their best interests. These include provisions prohibiting our stockholders from acting by written consent; requiring 90 days advance notice of stockholder proposals or nominations to our Board of Directors (or 120 days for nominations made using proxy access); and granting our Board of Directors the authority to issue preferred stock and to determine the rights and preferences of the preferred stock without the need for further stockholder approval.

Most of our outstanding employee stock-based compensation awards include a provision accelerating the vesting of the awards in the event of a change of control. We also maintain a change of control protection program for our employees who do not have a significant number of stock awards, which has been in place since 2001, and which provides for cash bonuses to the employees in the event of a change of control. Based on the market price of our common stock and shares outstanding on March 31, 2018, these cash bonuses would total approximately \$464 million if a change of control transaction occurred at that price and our Board of Directors did not modify this program. These change of control provisions may affect the price an acquirer would be willing to pay for our Company.

We are also subject to Section 203 of the Delaware General Corporation Law that, subject to exceptions, would prohibit us from engaging in any business combinations with any interested stockholder, as defined in that section, for a period of three years following the date on which that stockholder became an interested stockholder.

These provisions may discourage, delay or prevent an acquisition of our Company at a price that our stockholders may find attractive. These provisions could also make it more difficult for our stockholders to elect directors and take other corporate actions and could limit the price that investors might be willing to pay for shares of our common stock.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

## (c) Share repurchases

The following table summarizes the Company's repurchases of its common stock during the first quarter of 2018:

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Approximate dollar value of shares that may yet be purchased under the plans or programs (in millions)
January 1-31, 2018	519,227	\$ 76.63	519,227	\$ 1,079.3
February 1-28, 2018	937,180	73.63	937,180	1,010.3
March 1-31, 2018	2,740,897	69.17	2,740,897	820.7
Total	4,197,304	\$ 71.09	4,197,304	

On October 10, 2017, our Board of Directors approved an additional share repurchase authorization in the amount of approximately \$1.253 billion. This share repurchase authorization was in addition to the approximately \$247 million remaining at that time under our Board of Directors' prior share repurchase authorization announced in July 2016. We are authorized to make purchases from time to time in the open market or in privately negotiated transactions, including without limitation, through accelerated share repurchase transactions, derivative transactions, tender offers, Rule 10b5-1 plans or any combination of the foregoing, depending upon market conditions and other considerations. During the quarter ended March 31, 2018, we repurchased a total of 4,197,304 shares of our common stock for approximately \$298 million at an average price of \$71.09 per share. As of May 2, 2018, we had approximately \$545 million remaining in Board authorizations available for share repurchases under our stock repurchase program.

Although these share repurchase authorizations have no expiration dates, we are subject to share repurchase limitations under the terms of the senior secured credit facilities and the indentures governing our senior notes.

Items 3, 4 and 5 are not applicable

## Item 6. Exhibits

## (a) Exhibits

The information required by this Item is set forth in the Index to Exhibits that precedes the signature page of this Quarterly Report on Form 10-Q.

INDEX TO EXHIBITS

Exhibit  
Number

- 10.1 Amendment to Stock Appreciation Rights Agreements, entered into effective as of March 1, 2018, by and between DaVita Inc. and Carol Anthony Davidson. ü\*
- 10.2 DaVita Inc. Non-Employee Director Compensation Policy, adopted on March 29, 2018. ü\*
- 10.3 Consulting Agreement, made and entered into as of April 9, 2018, by and between DaVita Inc. and Jeanine Jiganti. ü\*
- 12.1 Ratio of earnings to fixed charges. ü
- 31.1 Certification of the Chief Executive Officer, dated May 3, 2018, pursuant to Rule 13a-14(a) or 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. ü
- 31.2 Certification of the Chief Financial Officer, dated May 3, 2018, pursuant to Rule 13a-14(a) or 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. ü
- 32.1 Certification of the Chief Executive Officer, dated May 3, 2018, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. ü
- 32.2 Certification of the Chief Financial Officer, dated May 3, 2018, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. ü
- 101.INS XBRL Instance Document. ü
- 101.SCH XBRL Taxonomy Extension Schema Document. ü
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document. ü
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document. ü
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document. ü
- 101.PRE XBRL Taxonomy Extension Presentation, Linkbase Document. ü  
ü Filed herewith.
- \*Management contract or executive compensation plan or arrangement.

SIGNATURE

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

DAVITA INC.

BY: /s/ JAMES K. HILGER  
James K. Hilger  
Chief Accounting Officer\*

Date: May 3, 2018

\*Mr. Hilger has signed both on behalf of the Registrant as a duly authorized officer and as the Registrant's principal accounting officer.