LEHIGH VALLEY HEALTH NETWORK
AND COMPONENT ENTITIES

Consolidated Financial Statements
As of and for the Years Ended June 30, 2014 and 2013,
Consolidated Schedule of Expenditures of Federal Awards
As of and for the Year Ended June 30, 2014,
with Independent Auditors' Reports Thereon

LEHIGH VALLEY HEALTH NETWORK AND COMPONENT ENTITIES

TABLE OF CONTENTS

KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report

Board of Trustees
Lehigh Valley Health Network:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Lehigh Valley Health Network and Component Entities, which comprise the consolidated statement of financial position as of June 30, 2014, and the related consolidated statements of operations, changes in net assets, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion, the 2014 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Lehigh Valley Health Network and Component Entities as of June 30, 2014, and the results of their operations and their cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.

Other Matter

The accompanying consolidated financial statements of Lehigh Valley Health Network and Component Entities as of June 30, 2013 and for the year then ended were audited by other auditors whose report thereon dated September 4, 2013, expressed an unmodified opinion on those consolidated financial statements.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 22, 2014 on our consideration of Lehigh Valley Health Network and Component Entities' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Lehigh Valley Health Network and Component Entities' internal control over financial reporting and compliance.

KPMG LLP

Philadelphia, Pennsylvania
September 22, 2014

Lehigh Valley Health Network and Component Entities
Consolidated Statements of Financial Position
June 30, 2014 and 2013
(In Thousands)

	2014	2013
Assets		
Current assets:		
Cash and cash equivalents	$44,061	$25,989
Patient accounts receivable, net	240,766	223,856
Other accounts receivable	30,947	17,777
Inventories	24,911	18,696
Prepaids	21,347	15,048
Assets limited under bond debt service fund - current portion	15,329	15,186
Assets limited under primary professional liability arrangements - current portion	5,252	5,392
Total current assets	382,613	321,944
Noncurrent assets:		
Assets whose use is limited or restricted:		
Assets limited by board of trustees for capital improvements	882,792	804,304
Assets limited by board of trustees for retained excess professional liability arrangements	18,488	16,745
Assets limited under primary professional liability arrangements	53,317	45,675
Assets limited by management	31,599	29,475
Assets limited under bond indenture, bond construction, debt service, and debt service reserve agreements - held by trustee	8,452	5,274
Assets restricted by donors and grantors	180,549	151,123
Assets limited to fund deferred compensation and other liabilities	60,010	49,147
Property and equipment, net	831,704	638,460
Partnership investments	9,331	9,481
Goodwill and other noncurrent assets	67,442	38,919
Total noncurrent assets	2,143,684	1,788,603
Total assets	$2,526,297	$2,110,547
Liabilities and net assets		
Current liabilities:		
Accounts payable	$71,756	$59,714
Accrual for estimated third-party payer settlements	11,849	2,419
Accrued compensation	70,532	49,444
Other accrued expenses	40,238	32,054
Pension	4,963	4,054
Professional liability	5,752	5,892
Current portion of long-term debt	14,614	12,303
Current portion of capital lease obligations	352	0
Total current liabilities	220,056	165,880
Noncurrent liabilities:		
Long-term debt, net of current portion	586,740	534,552
Long-term portion of capital lease obligations	104,652	34,817
Deferred compensation and other liabilities funded with matching assets	60,010	49,147
Pension	175,137	176,836
Professional liability	60,108	55,273
Other liabilities	28,964	28,249
Total noncurrent liabilities	1,015,611	878,874
Total liabilities	1,235,667	1,044,754
Net assets:		
Unrestricted:		
Lehigh Valley Health Network and Component Entities	1,084,665	895,304
Noncontrolling interests in subsidiaries	25,416	19,366
Total unrestricted net assets	1,110,081	914,670
Temporarily restricted	129,056	103,382
Permanently restricted	51,493	47,741
Total net assets	1,290,630	1,065,793
Total liabilities and net assets	$2,526,297	$2,110,547

See accompanying notes to consolidated financial statements

Lehigh Valley Health Network and Component Entities
Consolidated Statements of Operations
Years Ended June 30, 2014 and 2013
(In Thousands)

	2014	2013
Patient services and supporting operations		
Revenues		
Net patient service revenue (net of contractual allowances & discounts)	$1,728,865	$1,637,519
Provision for bad debts	(84,505)	(117,493)
Net patient service revenue (net of bad debts)	1,644,360	1,520,026
Other supporting operations revenue	44,415	36,988
Net assets released from restrictions used for operations	5,426	4,858
Total revenues	1,694,201	1,561,872
Expenses		
Salaries and wages	803,143	741,399
Benefits	148,147	146,794
Supplies	293,511	272,036
Purchased services	164,195	155,487
Other	122,655	105,879
Depreciation and amortization	95,398	84,574
Interest expense	25,241	22,719
Total expenses	1,652,290	1,528,888
Operating income	41,911	32,984
Other nonoperating gains and losses		
Realized and unrealized investment earnings	61,247	27,823
Change in net unrealized gains on swaps	991	8,459
Loss on refinancing of debt	0	(4,537)
Contribution received in acquisition of GHHA	72,415	0
Other nonoperating gains and losses, net	134,653	31,745
Revenues and gains in excess of expenses and losses before income taxes	176,564	64,729
Provision for income taxes	(2,076)	(2,935)
Revenues and gains in excess of expenses and losses	174,488	61,794
Noncontrolling interests	(6,527)	(1,890)
Revenues and gains in excess of expenses and losses attributed to Lehigh Valley Health Network and Component Entities	167,961	59,904
Net assets released from restrictions - capital acquisitions	1,472	1,846
Contribution of long lived assets	118	491
Adjustment to funded status of pension plan	(17,853)	69,310
Change in noncontrolling interests	6,050	302
Change in net unrealized (losses) gains on swaps	(30)	290
Change in net unrealized gains on investments	37,693	25,519
Increase in unrestricted net assets	$195,411	$157,662

See accompanying notes to consolidated financial statements

Lehigh Valley Health Network and Component Entities
Consolidated Statements of Changes in Net Assets
Years Ended June 30, 2014 and 2013
(In Thousands)

	2014	2013
Unrestricted net assets		
Revenues and gains in excess of expenses and losses attributed to Lehigh Valley Health Network and Component Entities	$167,961	$59,904
Net assets released from restrictions - capital acquisitions	1,472	1,846
Contribution of long lived assets	118	491
Adjustment to funded status of pension plans	(17,853)	69,310
Change in noncontrolling interests	6,050	302
Change in net unrealized (losses) gains on swaps	(30)	290
Change in net unrealized gains on investments	37,693	25,519
Increase in unrestricted net assets	195,411	157,662
Temporarily restricted net assets		
Contributions	9,660	2,969
Contribution of GHHA restricted net assets	840	0
Reclassification (to) from permanently restricted net assets	(717)	231
Increase in assets temporarily held in trust	0	1
Realized and unrealized investment gains, net	22,907	14,124
Net assets released from restrictions	(7,016)	(7,195)
Increase in temporarily restricted net assets	25,674	10,130
Permanently restricted net assets		
Contributions	2,435	1,252
Reclassification from (to) temporarily restricted & unrestricted net assets	717	(236)
Increase in beneficial interest in perpetual trusts	600	284
Increase in permanently restricted net assets	3,752	1,300
Increase in net assets	224,837	169,092
Net assets, beginning of year	1,065,793	896,701
Net assets, end of period	$1,290,630	$1,065,793

See accompanying notes to consolidated financial statements

Lehigh Valley Health Network and Component Entities
Consolidated Statements of Cash Flows
Years Ended June 30, 2014 and 2013
(In Thousands)

	2014	2013
Cash flows from operating activities:		
Increase in net assets	$224,837	$169,092
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	95,398	84,574
Loss on refinancing of debt	0	4,537
Net realized and unrealized (gains) on unrestricted investments	(83,349)	(37,626)
Restricted contributions received for capital and endowments and related investment (gains)	(28,181)	(11,586)
Adjustment to funded status of pension plans	17,853	(69,310)
Non-cash interest expense	176	212
Change in net unrealized (gains) on swaps	(961)	(8,749)
Provision for bad debts	84,505	117,493
Adjustment to noncontrolling interests due to a change in control of equity investee	(631)	(80)
Changes in assets and liabilities:		
(Increase) in patient accounts receivable, net	(90,231)	(132,347)
(Increase) in prepaids, inventories and other current assets	(21,960)	(2,354)
(Increase) in other noncurrent assets	(20,878)	(4,562)
Decrease (increase) in interest earned but not received on assets whose use is limited or restricted	782	(41)
Increase (decrease) accounts payable	9,157	(1,750)
Increase (decrease) in other accrued expenses	4,104	(2,508)
Increase (decrease) in accrual for estimated third party payer settlements	271	(1,056)
Increase (decrease) in accrued compensation	12,795	(3,838)
(Decrease) in pension liability	(33,551)	(20,803)
Increase in professional liability	3,260	2,198
Acquisition of GHHA	(73,255)	0
Increase in deferred compensation and other liabilities funded with matching assets, and other liabilities	4,797	3,983
Net cash provided by operating activities	104,938	85,479
Cash flows from investing activities:		
Purchases of property and equipment	(172,281)	(100,272)
Contribution of GHHA cash	4,040	0
Purchases of investments	(1,794,225)	(1,040,778)
Proceeds from sales of investments	1,848,712	990,578
Net cash (used in) investing activities	(113,754)	(150,472)
Cash flows from financing activities:		
Proceeds from issuance of long-term debt	38,000	166,085
Payment of financing costs	0	(2,066)
Repayment of debt	(14,253)	(101,177)
Payments made on capital leases	(55)	0
Proceeds from contruction fund	989	0
Proceeds from restricted contributions for capital and endowments	2,208	2,078
Net cash provided by financing activities	26,889	64,920
Net increase (decrease) in cash and cash equivalents	18,073	(73)
Cash and cash equivalents, beginning of year	25,989	26,062
Cash and cash equivalents, end of year	$44,062	$25,989
Supplemental cash flow information:		
Cash paid for interest	$24,070	$19,957
Cash paid for income taxes	$2,045	$2,208
Non-cash capital lease additions	$69,733	$0
Non-cash increase in capital lease obligation	$176	$212
Amounts accrued for purchase of property and equipment in excess of amounts paid	$9,147	$9,762

See accompanying notes to consolidated financial statements

FOR THE YEARS ENDED JUNE 30, 2014 AND 2013 (AMOUNTS IN THOUSANDS OF DOLLARS)

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Lehigh Valley Health Network ("LVHN") is a not-for-profit 501(c)(3) corporation that controls related organizations in a health care delivery network providing a wide array of health care services and products to the Lehigh Valley, Hazleton and surrounding communities in Pennsylvania. The consolidated financial statements of Lehigh Valley Health Network and Component Entities (the "Organization") at June 30, 2014 include the accounts of the following entities:

Entity Name	Income Tax Status
Lehigh Valley Health Network ("LVHN")	Exempt-501(c)3
Lehigh Valley Hospital ("LVH")	Exempt-501(c)3
Lehigh Valley Hospital - Muhlenberg ("LVHM")	Exempt-501(c)3
Lehigh Valley Hospital - Hazleton ("LVHH")	Exempt-501(c)3
Lehigh Valley Physician Group ("LVPG")	Exempt-501(c)3
Muhlenberg Realty Corporation ("MRC")	Exempt-501(c)3
Hazleton Health & Wellness Center ("HHWC")	Exempt-501(c)3
Hazleton Professional Services ("d/b/a Alliance Medical Group")	Exempt-501(c)3
Hazleton Surgical Alliance ("HSA")	Exempt-501(c)3
Health Network Laboratories, L.P. ("HNL") - 97% owned by LVHN	Non-exempt
Health Network Laboratories, LLC	Non-exempt
Lehigh Valley Health Services, Inc. ("LVHS")	Non-exempt
Populytics, Inc	Non-exempt
Spectrum Health Ventures, Inc	Non-exempt
Hazleton Saint Joseph Medical Office Building, Inc.	Non-exempt
LVHN Reciprocal Risk Retention Group ("RRG")	Non-exempt
Lehigh Valley Health Network Realty Holding Company, Inc. ("LVHNRHC")	Exempt-501(c)2
Westgate Professional Center, Inc. ("Westgate")	Non-exempt
Lehigh Valley Anesthesia Services, PC ("LVAS")	Non-exempt
Lehigh Valley Physician Hospital Organization ("LVPHO") - 50% owned by LVHN	Non-exempt
Lehigh Valley Imaging, LLC ("LVI") - 72% owned by LVH	Non-exempt
Lehigh Magnetic Imaging Center ("LMIC") - 77% owned by LVHN	Non-exempt
Hazleton Surgery Center, LLC ("HSC") - 66% owned by HSA	Non-exempt

All significant intercompany balances and transactions have been eliminated.

Acquisition/Merger

On April 16, 2013, Lehigh Valley Health Network (LVHN) executed an affiliation agreement with the Greater Hazleton Health Alliance (GHHA) providing for an affiliation between LVHN and Hazleton General Hospital (HGH), and Alliance Medical Group (AMG). The governing documents of GHHA were amended such that effective January 1, 2014, the closing date of the affiliation, GHHA merged into LVHN and LVHN became the sole member of Hazleton General Hospital and component entities. GHHA consisted primarily of HGH, a 150-bed inpatient acute care and rehab hospital also providing emergency care with outpatient services including surgery, diagnostic testing, and therapy provided at the Hazleton Health & Wellness Center, and AMG, a multi-specialty physician group. Pursuant to the affiliation agreement, LVHN has agreed to evaluate and invest in the future facility needs of the Hazleton community. The scope of this investment is subject to determination of the LVHN Board of Trustees, following LVHN's capital planning process and taking into consideration the changing healthcare delivery system. Additionally, the HGH name changed to Lehigh Valley Hospital – Hazleton (LVHH). Lehigh Valley Health Network incurred $3,216 ($2,834 in FY14 and $382 in FY13) and Greater Hazleton Health Alliance incurred $434 in costs related to the acquisition. No consideration was paid to GHHA as a result of the affiliation agreement. LVHN applied the business combination accounting guidance in Financial

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Acquisition/Merger (continued)

Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2010-07, Not-for-Profit Entities (Topic 958-805): Mergers and Acquisitions, to account for this transaction. The guidance primarily characterizes certain business combinations between not-for-profit entities as nonreciprocal transfers of assets resulting in the contribution of the fair value of the acquiree's net assets to the acquirer. Accounting Standards Codification (ASC) 958-805 prescribes that the acquirer recognize the excess of fair value at the acquisition date of unrestricted net assets acquired over the fair value of the consideration transferred as a separate credit in its Consolidated Statement of Operations. Accordingly, LVHN recognized, as a component of Other nonoperating gains and losses, contribution income related to the unrestricted net assets acquired in the transactions of $72,415 in its Consolidated Statements of Operations for the year ended June 30, 2014. LVHN also recorded an increase in restricted net assets of $840 in its Consolidated Statements of Changes in Net Assets for the year ended June 30, 2014 as a result of the affiliations.

The following table summarized the estimated fair values of the assets acquired and liabilities assumed as of the date of the affiliation:

	Jan 1, 2014
Assets:	
Current assets	$18,974
Property and equipment	46,124
Other long-term assets	80,494
Total assets	$145,592
Liabilities:	
Current liabilities	$28,358
Long-term debt	28,765
Other long-term liabilities	15,214
Total liabilities	$72,337
Net assets acquired:	
Unrestricted	$72,415
Temporarily restricted	840
Permanently restricted	0
Total net assets	$73,255
Total liabilities and net assets	$145,592

The following tables summarize the activity attributable to LVHH and AMG since the date of affiliation through June 30, 2014, and LVHN's pro forma combined results as though the affiliation date occurred at the beginning of the fiscal year 2014:

Since affiliation date:	
Operating revenues	$61,289
Operating income	4,114
Changes in net assets:	
Unrestricted	$2,924
Temorarily restricted	85
Permanently restricted	657
Total changes in net assets	$3,666

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Acquisition/Merger (continued)

	2014 LVHN pro forma combined	2013 LVHN pro forma combined
Beginning of fiscal year 2014:		
Operating revenues	$1,752,059	$1,680,346
Net operating income	40,381	42,228
Changes in net assets:		
Unrestricted	$207,276	$167,680
Temorarily restricted	25,837	10,246
Permanently restricted	3,729	1,300
Total changes in net assets	$236,842	$179,226

Basis of Accounting
The consolidated financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America and in accordance with the American Institute of Certified Public Accountants' Audit and Accounting Guide, *Health Care Entities*, and other pronouncements applicable to not-for-profit health care organizations. The Organization evaluated subsequent events through September 22, 2014, the date the financial statements were issued, and determined there were no subsequent events requiring disclosure.

Use of Estimates
The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include the bad debts reserve, contractual allowances, estimated third party payers settlements, professional liabilities, liabilities for pension and other benefits, swaps, alternative investments, and asset retirement obligations.

Trusts
The Organization is the beneficiary in perpetuity of income earned on certain perpetual irrevocable trusts, the funds of which are maintained and administered by independent trustees, and are recognized at the Organization's share of the estimated fair value of the related trust assets and are included in Assets restricted by donors and grantors. The Organization's share of income earned on these trusts is unrestricted.

Cash and Cash Equivalents
Cash and cash equivalents include highly liquid investments purchased with an initial maturity of three months or less, excluding amounts included in assets whose use is limited or restricted. At June 30, 2014 and 2013, the Organization had cash balances at financial institutions that exceeded federal depository insurance limits. Management believes that credit risk related to these deposits is minimal. Cash and cash equivalents are carried at cost, which approximate fair value.

Inventories
Inventories are stated at the lower of first-in, first-out cost or market.

Goodwill
Goodwill represents the excess of the purchase price over the estimated fair value of the net assets or equity acquired.

The Organization evaluates goodwill for impairment annually and whenever events or changes in circumstances indicate that the value of the asset may be impaired. Impairment testing consists of performing internal qualitative assessment and considers other publicly available market information. If the carrying amount of the goodwill exceeds the estimated fair value, an impairment charge to current operations is recorded to reduce the carrying value to the estimated fair value. As of June 30, 2014 and 2013, there was no indication of impairment of goodwill.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Goodwill (continued)
Changes in carrying value of goodwill were as follows at June 30:

Balance at July 1, 2012	$14,848
Goodwill activity FY 2013	5,005
Balance at June 30, 2013	$19,853
Goodwill additions associated with current year acquisitions	28,434
Balance at June 30, 2014	$48,287

Temporarily and Permanently Restricted Net Assets
Temporarily restricted net assets are those whose use by the Organization has been limited by donors and grantors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Organization or outside trustees in perpetuity.

Donor Restricted Gifts
Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received, which is then treated as cost. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the Consolidated Statements of Operations as Net assets released from restrictions used for operations or Net assets released from restrictions – capital acquisitions. In the absence of donor specification that investment income on donated funds be restricted, such income is reported as Realized and unrealized investment earnings of unrestricted net assets.

Pledges
Pledges, less an allowance for uncollectible amounts, are recorded as receivables in the year made. Pledges are reported as additions to either temporarily or permanently restricted net assets at their present value.

Income Taxes
LVHN, its hospitals, and other subsidiaries are generally exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended, except for tax imposed on unrelated business income. LVHN and its component entities account for uncertain tax positions in accordance with ASC Topic 740. The Organization’s for-profit components recognize deferred tax assets and liabilities for the future tax impact of temporary differences between amounts recorded in the consolidated financial statements and their respective tax bases and the future benefit of utilization net operating loss carryforwards. Income taxes of the Organization’s tax-exempt and for-profit components are not material to the accompanying financial statements.

Property and Equipment
Property and equipment is stated at cost, or in the case of donated items, at the fair market value at the date of the gift. Depreciation is recorded over the estimated useful lives of assets, as indicated in the table below, using the straight-line method.

	Lives
Land improvements	2 - 25 years
Buildings and building equipment	5 - 40 years
Fixed and major movable equipment	2 - 20 years

Assets under capital lease are amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the assets. Such amortization is included in depreciation and amortization in the Consolidated Statements of Operations. Interest costs, net of related interest earnings, incurred on related funds acquired through the issuance of tax-exempt bonds is capitalized during the period of construction of capital assets as a component of the cost of acquiring those assets. Capitalized interest for the years ended June 30, 2014 and 2013 was $143 and $0, respectively. Leasehold improvements and software licenses are amortized over the shorter of their useful lives or the term of the lease using the straight-line method. The cost of assets and the related accumulated depreciation are removed from the records upon retirement or other disposition and any gain or loss is included in the Consolidated Statements of Operations.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Asset Retirement Obligations
The Organization recognizes the fair value of a liability for legal obligations associated with conditional asset retirement obligations ("ARO's") in the period in which the liability is incurred. ARO's are accreted to their present value at the end of each reporting period. The associated estimated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and depreciated over their useful life. ARO's are adjusted each year for any liabilities incurred or settled during the period, accretion expense, and any revisions made to the estimated cash flows. The Organization has identified ARO's related to the legally required remediation of asbestos existing within the Organization's facilities. While all hazardous materials within the Organization's facilities are currently contained and meet existing safety standards, the capitalized asset and liability recorded relate to the eventual remediation and removal that is legally required upon the ultimate repair, renovation, or demolition of facilities containing the hazardous materials. ARO liabilities recorded in Other liabilities in the Consolidated Statements of Financial Position at June 30, 2014 and 2013 were $4,759 and $4,867, respectively.

Long-Lived Assets
The Organization assesses the recoverability of its long-lived assets whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Recoverability is based on the estimated fair value of the asset measured using the estimated future cash flows expected to result from the use of the assets and their eventual disposal.

Deferred Financing Costs
Deferred financing costs, principally legal fees and bond issuance costs, are amortized over the period of financing under the straight-line method which approximates the effective interest rate method. Gross deferred financing costs at June 30, 2014 and 2013 were $15,275 and $14,904 respectively. Accumulated amortization of deferred financing costs was $4,537 and $3,817 at June 30, 2014 and 2013, respectively.

Partnership Investments
Partnership investments, primarily joint venture investments, are accounted for at the lower of cost or market for investments in which the Organization does not have the ability to exercise significant influence. Partnership investments in which the Organization has the ability to exercise significant influence are accounted for under the equity method of accounting.

Estimated Third-Party Payer Settlements
The Organization has agreements with third-party payers that provide for payments at amounts different than the Organization's established rates. Payment arrangements include primarily prospectively determined rates per discharge, per visit, and per diem payments and to a lesser extent, reimbursed costs at discounted charges.

Estimated third-party payer settlement liabilities recorded at June 30, 2014 and 2013 were $11,849 and $2,419, respectively. Estimated third-party payer settlement assets recorded at June 30, 2014 and 2013 were $8,513 and $2,967, respectively, and were recorded in Other accounts receivable on the Consolidated Statements of Financial Position.

Noncontrolling Interests in Subsidiaries
The Consolidated Statements of Financial Position include noncontrolling interests that relate to the portion of subsidiaries that are not owned by the Organization. Similarly, the Consolidated Statements of Operations include noncontrolling interests that reflect amounts not attributable to the Organization, which are reported as Noncontrolling interests.

Consolidated Statements of Operations
For purposes of display, transactions deemed to be ongoing, major or central to the provision of health care services are reported as revenues and expenses from Patient services and supporting operations. Peripheral or incidental transactions are reported as Other nonoperating gains and losses.

Patient services and supporting operations revenues and expenses are those revenues and expenses directly related to the provision of patient care, community wellness and education. Other nonoperating gains and losses includes Realized and unrealized investment earnings, Change in net unrealized gains on swaps, Loss on refinancing of debt, Contribution received in acquisition of GHHA, and Noncontrolling interests.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Performance Indicator

In the Consolidated Statements of Operations, the primary indicator of the Organization's results is Revenues and gains in excess of expenses and losses attributed to Lehigh Valley Health Network and Component Entities. Changes in unrestricted net assets that are excluded from the performance indicator, consistent with industry practice, include Net assets released from restrictions – capital acquisitions, Contribution of long lived assets, Adjustment to funded status of pension plan, Change in noncontrolling interests, Change in net unrealized (losses) gains on swaps, and Change in net unrealized gains on investments (except for alternative investments and declines in fair value that are determined by management to be other than temporary, which are reported as realized investment losses).

Net Patient Service Revenue

The Organization records gross patient service revenue in the period that the services are rendered. Net patient service revenue before the provision for bad debts represents gross patient service revenue less provisions for contractual adjustments and uninsured discounts. Payments for services rendered to patients covered by Medicare, Medicaid, and other government programs are generally less than billed charges and, therefore, provisions for contractual adjustments are made to reduce gross patient service revenue to the estimated cash receipts based on each program's principles of payment/reimbursement.

Estimates of contractual allowances for services rendered to patients covered by commercial insurance, including managed care health plans, are primarily based on the payment terms of contractual arrangements, such as predetermined rates per diagnosis, per diem rates or discounted fee for service rates. Revenue related to uninsured patients have uninsured discounts applied; effective July 1, 2013 the uninsured discount is based on the amount generally billed (AGB), as defined in proposed IRS section 501(r).

The Organization records a provision for bad debts related to uninsured accounts net of the AGB discount to record the net self pay accounts receivable at the estimated amounts the Organization expects to collect. Coinsurances and deductibles within the third-party payer agreements are the patient's responsibility and the Organization includes these amounts in the self pay accounts receivable and considers these amounts in its determination of the provision for bad debts based on collection experience.

Net patient accounts receivable includes provisions for bad debts of $77,716 and $150,905 at June 30, 2014 and 2013, respectively. Bad debt reserves are estimated based on the Organization's belief that a patient has the ability to pay for services but payment is not expected to be received.

The provision for bad debts is based on management's assessment of historical and expected collections, business economic conditions, trends in health care coverage, and other collection indicators. Accounts receivable are written off against the provision for bad debts when management determines that recovery is unlikely and the Organization ceases collection efforts. Effective July 1, 2013, the Organization began discounting uninsured accounts using the AGB principle. The policy change decreases the expected payment amount from the uninsured and the necessary reserves for bad debt.

Patient service revenue, net of contractual allowances, discounts, and provisions for bad debts recognized was as follows at June 30, 2014 and 2013:

	2014		2013	
Medicare	$405,295	25%	$372,316	24%
Medicare Managed Care	152,186	9%	138,320	9%
Medicaid	54,408	3%	63,610	4%
Medicaid Managed Care	105,259	6%	76,303	5%
Commercial Insurance	800,330	49%	754,673	50%
Other	107,512	7%	101,102	7%
Uninsured	19,370	1%	13,702	1%
Net patient service revenue (net of bad debts)	$1,644,360	100%	$1,520,026	100%

Net patient service revenue also includes estimates for retroactive adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are recorded on an estimated basis in the period the related services are rendered or when known by the Organization and adjusted in future periods as final settlements are determined. Laws and regulations governing the Medicare and Medicaid programs is complex and subject to interpretation. As a result, there is a reasonable possibility that recorded estimates will change by a material amount in the near term. Changes in prior year estimates increased net patient service revenue by $18,750 and $7,344 in the fiscal years ended June 30, 2014 and 2013, respectively.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Other Supporting Operations Revenue

Other supporting operations revenue primarily includes revenue from grant contracts, property rental, partnership revenue and unrestricted contributions.

Meaningful Use

Under the Health Information Technology for Economic and Clinical Health (HITECH) Act, qualifying acute care hospitals are eligible for incentive payments from both Medicare and Medicaid for achieving prescribed standards for the meaningful use of electronic health records. The Organization records amounts earned as Other supporting operations revenue when the Organization has met the compliance requirements as set forth by Medicare and Medicaid. The Organization reported as Other supporting operations revenue $10,727 and $4,580 from both Medicare and Medicaid at June 30, 2014 and 2013, respectively.

Patient Accounts Receivable

Patient accounts receivable for which the Organization receives payment under cost reimbursement, prospective payment formulas, or negotiated rates, which cover the majority of patient services, are stated at the estimated net amounts receivable from payers, which are generally less than the established billing rates of the Organization. Patient accounts receivable is reported at its net realizable value.

Concentrations of Credit Risk

The Organization grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payer agreements. The mix of net receivables from patients and third-party payers was as follows at June 30:

	2014	2013
Medicare	19%	19%
Medicare Managed Care	7%	6%
Medicaid	9%	10%
Medicaid Managed Care	7%	6%
Commercial Insurance	36%	34%
Other	6%	5%
Self Pay	16%	20%
Total	100%	100%

Estimated Medical Malpractice Costs

The Organization uses a combination of commercial insurance and self-insurance arrangements to provide for medical malpractice costs. The self-insured arrangements include actuarially determined estimates of the ultimate costs for both reported claims and claims incurred but not reported (IBNR) and include the primary layer provided through the RRG, and the self-insured excess layer. The Medical Care Availability and Reduction of Error (MCARE) layer provides coverage between the self-insured primary layer and the self-insured excess layer and is provided by the Pennsylvania Insurance Department funded through direct assessments. Commercial insurance is used to provide additional excess coverage beyond the self-insured excess layer.

Self-insured loss reserves are the Organization's best estimate based on actuarial estimates of the ultimate net cost of settling losses on incurred claims. The estimates are reviewed and adjusted, as necessary, as experience develops or new information becomes known. The Organization believes that the loss reserves are adequate; however, the ultimate settlement of losses may vary significantly from the amounts recorded in the accompanying consolidated financial statements.

The June 30, 2014 and 2013 consolidated financial statements include actuarially determined self-insured medical malpractice expenses of $11,949 and $9,618, respectively, and are reported as Other expense in the Consolidated Statements of Operations. Corresponding reserves are reported as current and non-current Professional liability in the Consolidated Statements of Financial Position. Commercial excess insurance expense and MCARE assessments totaled $6,179 and $5,243 for the years ended June 30, 2014 and 2013, respectively, and were recorded in Other expense in the Consolidated Statements of Operations.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets Whose Use is Limited

Investments in equity securities with readily determinable fair values and all investments in debt securities are reported at fair value in the Consolidated Statements of Financial Position. The Organization also invests in a diversified program of alternative investment funds. These investments utilize a "fund of funds" approach resulting in diversified multistrategy, multimanager investments. Certain investments include liquidation restrictions of 5 to 90 days notice prior to withdrawal. The Organization reports these investments at their net asset value, which approximates fair value.

Investment income or loss (including realized gains and losses on investments, unrealized gains and losses on alternative investments, and interest and dividends) is reported as Realized and unrealized investment earnings unless the income or loss is restricted by donor or law, in which case investment income or loss is recorded as a component of Temporarily restricted net assets. Unrealized gains and losses on investments with a readily determinable fair value are excluded from Revenues and gains in excess of expenses and losses but are reported as increases or decreases in Unrestricted net assets unless the income or loss is restricted by donor or law, in which case investment income or loss is recorded as a component of Temporarily restricted net assets.

Investments, in general, are exposed to various risks such as interest rate, credit and overall market volatility. As such, it is reasonably possible that changes in the value of investments will occur in the near term and that such changes could materially affect the amounts reported in the consolidated financial statements.

Assets whose use is limited includes (1) Assets set aside by the Board of Trustees (the "Board") for future purposes over which the Board retains control and may at its discretion subsequently use for capital improvements, (2) Assets limited by the Board for retained excess professional liability arrangements, (3) Assets limited under primary professional liability arrangements, (4) Assets limited internally designated by management for various purposes, (5) Assets limited under bond indenture, bond construction, debt service, and debt service reserve agreements – held by trustee, (6) Assets restricted by donors and grantors, and (7) Assets limited to fund deferred compensation and other liabilities.

In addition, Assets whose use is limited also includes Assets limited under bond indenture, bond construction, debt service funds, and debt service reserve agreements, related to the Organization's outstanding tax exempt bonds (see note 3). Bond construction funds are held by a trustee and are established to hold bond proceeds until the Organization has incurred capital expenditures in accordance with the allowable uses of issued bonds. The Organization is required to fund to a trustee its scheduled monthly and semi-annual (January 1 and July 1) debt service payments 1-15 days in advance of the payment dates. This funding is reflected in the Consolidated Statements of Financial Position in the Current assets section reported as Assets limited under bond debt service. For certain outstanding bond issues, the Organization is required to maintain debt service reserve funds with a trustee. These funds are available to pay debt service in the event the Organization fails to make such payments.

2. ASSETS WHOSE USE IS LIMITED OR RESTRICTED AND PARTNERSHIP INVESTMENTS

Investments carried primarily at fair value and other assets carried at cost at June 30, 2014 and 2013 are summarized as follows:

	Short-term investments	U.S. government, agencies, and authorities	Corporate bonds	Fixed income mutual funds	Marketable equity securities	Equity mutual funds	Alternative investments (C)	Other investments (A)	Accrued interest	Total
2014										
Assets whose use is limited or restricted:										
under bond debt service fund - current portion	$15,329	$0	$0	$0	$0	$0	$0	$0	$0	$15,329
under primary professional liability arrangements - current portion	22	1,118	2,736	0	0	1,359	0	0	17	5,252
by board of trustees for capital improvements	7,335	51,521	125,715	126,597	41,707	359,915	169,075	0	927	882,792
by board of trustees for retained excess professional liability arrangements	285	1,146	2,793	2,068	1,007	7,241	3,927	0	21	18,488
under primary professional liability arrangements	376	9,357	22,889	1,484	709	15,576	2,784	0	142	53,317
by management (B)	22	250	775	6,031	1,239	11,984	2,813	8,477	8	31,599
under bond indenture, bond construction, debt service, and debt service reserve agreements - held by trustee	5,161	3,277	0	0	0	0	0	0	14	8,452
by donors and grantors	239	1,638	3,906	42,377	9,139	83,952	18,411	20,838	49	180,549
to fund deferred compensation and other liabilities	3,916	2,808	6,936	6,861	398	36,562	0	2,487	42	60,010
Partnership investments	0	0	0	0	0	0	0	9,331	0	9,331
Total investments	$32,685	$71,115	$165,750	$185,418	$54,199	$516,589	$197,010	$41,133	$1,220	$1,265,119
2013										
Assets whose use is limited or restricted:										
under bond debt service fund - current portion	$15,186	$0	$0	$0	$0	$0	$0	$0	$0	$15,186
under primary professional liability arrangements - current portion	18	1,930	1,871	0	51	1,355	153	0	14	5,392
by board of trustees for capital improvements	1,925	199,515	187,994	13,037	39,459	246,249	114,535	0	1,590	804,304
by board of trustees for retained excess professional liability arrangements	41	4,261	4,029	0	844	5,018	2,518	0	34	16,745
under primary professional liability arrangements	136	15,850	15,337	0	627	11,728	1,878	0	119	45,675
by management (B)	298	2,831	2,829	0	1,147	11,328	2,539	8,477	26	29,475
under bond indenture, bond construction, debt service, and debt service reserve agreements - held by trustee	5,274	0	0	0	0	0	0	0	0	5,274
by donors and grantors	196	17,699	17,682	49	7,994	76,322	16,414	14,612	155	151,123
to fund deferred compensation and other liabilities	3,869	6,073	8,745	0	444	27,290	0	2,662	64	49,147
Partnership investments	0	0	0	0	0	0	0	9,481	0	9,481
Total investments	$26,943	$248,159	$238,487	$13,086	$50,566	$379,290	$138,037	$35,232	$2,002	$1,131,802

(A) Includes $8,174 and $6,939 representing the Organization's interest in certain perpetual trusts stated at net present value at June 30, 2014 and 2013, respectively (see Note 1). Includes $10,094 and $5,176 of pledges receivable at June 30, 2014 and 2013, respectively (see Note 14). Includes other investments, primarily cash surrender value of life insurance of $4,234 and $4,336 at June 30, 2014 and 2013, respectively. Includes partnership investments of $9,331 and 9,481 at June 30, 2014 and 2013, respectively. Includes an unrestricted gift of land valued at $8,250 at June 30, 2014 and 2013. Includes $1,050 representing LVH's remaining interest in the Elsa K. Farr Trust at June 30, 2014 and 2013, respectively.

(B) Assets limited by management are primarily unspent unrestricted gift proceeds invested until used, and the unrestricted gift of land described in note (A) above.

(C) Includes $197,010 and $138,037 in alternative investments at June 30, 2014 and 2013, respectively. Because alternative investments are not readily marketable, the estimated fair value is subject to uncertainty and, therefore, may differ from the fair value that would have been used had a ready market existed, and such differences could be material (see Note 13).

2. ASSETS WHOSE USE IS LIMITED OR RESTRICTED AND PARTNERSHIP INVESTMENTS (Continued)

The following schedule summarizes the investment earnings and its classification in the Consolidated Statements of Operations and Consolidated Statements of Changes in Net Assets for the years ended June 30:

	2014	2013
Income:		
Interest and dividend income	$18,416	$18,372
Net realized gains on investments	45,665	15,474
Net unrealized gains on investments	57,766	33,620
Total	$121,847	$67,466
Reported as follows:		
Consolidated Statements of Operations:		
Other nonoperating gains and losses - Realized and unrealized investment earnings	$61,247	$27,823
Change in net unrealized gains on investments	37,693	25,519
Consolidated Statements of Changes in Net Assets:		
Temporarily restricted net assets - Realized and unrealized investment gains, net	22,907	14,124
Total	$121,847	$67,466

Other Than Temporary Impairment

The Organization recognizes other than temporary impairment on equity securities when: (1) in management's judgment, a decline in value is not temporary or (2) when the Organization, through its investment managers, has made a decision to sell the equity security at an amount below its carrying value, or (3) when the Organization determines it does not have the ability and intent to hold an investment for a sufficient period of time for a recovery of fair value.

The Organization evaluates other than temporary impairment on debt securities by determining: (1) if the Organization has the intent to sell the debt security or (2) if it is more likely than not that the Organization will be required to sell the debt security before its anticipated recovery; and (3) assessing whether a credit loss exists, that is, where the Organization believes that the present value of the cash flows expected to be collected from the security are less than the amortized cost basis of the security.

When an other than temporary impairment is recognized, the security is written down to fair value as the new cost basis, and the amount of the write-down is recorded as a realized loss.

During years ended June 30, 2014 and 2013, assessments of other than temporary impairment were performed on each security held by the Organization. Factors considered in determining whether an other than temporary impairment existed included: the financial condition, business prospects and creditworthiness of the issuer, and the length of time and extent to which fair value had been less than cost for equity securities or amortized cost for fixed income securities.

The other than temporary impairment losses recorded during the years ended June 30, 2014 and 2013 were $7,574 and $4,388, respectively. These losses are reported in Realized and unrealized investment earnings in the Consolidated Statements of Operations.

In addition to the above, certain other investments had fair values below cost at June 30, 2014 and 2013 but were determined to not be other than temporarily impaired due to the Organization's ability and intent to hold the securities until recovery of fair value.

2. ASSETS WHOSE USE IS LIMITED OR RESTRICTED AND PARTNERSHIP INVESTMENTS (Continued)

Other Than Temporary Impairment (continued)
The following table presents the unrealized losses and fair value of these investments, aggregated by investment category and length of time individual securities have been in a continuous unrealized loss position.

	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized loss	Fair Value	Unrealized loss	Fair Value	Unrealized loss
2014						
Equity mutual funds	$0	$0	$0	$0	$0	$0
Alternative investments	0	0	0	0	0	0
Total	$0	$0	$0	$0	$0	$0
2013						
Equity mutual funds	$6,982	($54)	$133,499	($1,023)	$140,481	($1,077)
Alternative investments	42,476	(5,832)	0	0	42,476	(5,832)
Total	$49,458	($5,886)	$133,499	($1,023)	$182,957	($6,909)

The unrealized losses on investments in marketable equity securities were caused by a combination of economic, industry, and company factors. The Organization's marketable equity securities portfolios are diversified. The nature of a diversified portfolio is that at any point in time some holdings are reasonably expected to reflect market losses. Since the declines in market value of equity securities are not considered severe in nature on a security by security basis, the financial condition and near term prospects of the issuer are not in question, and the Organization has the ability and intent to hold to recovery, the Organization does not consider those investments to be other than temporarily impaired at June 30, 2014 and 2013.

3. LONG-TERM DEBT

Long-term debt consists of the following at June 30:	2014	2013
Hospital Revenue Bonds, Series A of 1994 (net of unamortized bond discount of $2 and $3 at June 30, 2014 and 2013, respectively) at a fixed rate of 7.000% due in various amounts through July 1, 2016.	$3,973	$5,127
Hospital Revenue Bonds, Series A of 2005 At variable rates of interest (0.104% and 0.134% at June 30, 2014 and 2013, respectively) due in various amounts through July 1, 2025. These bonds are privately held and the interest rate is indexed and resets on a monthly basis. See Page 20 "Swap Agreements".	46,900	48,400
Hospital Revenue Bonds, Series B of 2005 At a fixed rate of 5.000% due in various amounts through July 1, 2035.	81,000	81,000
Hospital Revenue Bonds, Series A of 2008 (net of unamortized bond premium of $280 and $292 at June 30, 2014 and 2013, respectively) at fixed rates ranging from 4.000% to 5.000% due in various amounts through July 1, 2038.	66,411	67,742
Hospital Revenue Bonds, Series B of 2008 At variable rates of interest (0.104% and 0.134% at June 30, 2014 and 2013, respectively) due in various amounts through July 1, 2028. These bonds are privately held and the interest rate is indexed and resets on a monthly basis. See Page 21 "Swap Agreements".	84,155	86,235
Hospital Revenue Bonds, Series C of 2008 At variable rates of interest (0.111% and 0.143% at June 30, 2014 and 2013, respectively) due in various amounts through July 1, 2029. These bonds are privately held and reprice daily.	57,005	57,915
Hospital Revenue Bonds, Series A of 2011 At variable rates of interest (0.104% and 0.134% at June 30 , 2014 and 2013, respectively) due in various amounts through July 1, 2029. These bonds are privately held and reprice daily.	21,500	23,685
Hospital Revenue Bonds, Series A of 2012 At variable rates of interest (0.139% and 0.185% at June 30, 2014 and 2013, respectively) due in various amounts through July 1, 2021. These bonds are privately held and the interest rate is indexed and resets on a monthly basis. See Page 21 "Swap Agreements".	13,975	16,885

3. LONG-TERM DEBT (Continued)

	2014	2013
Hospital Revenue Bonds, Series B of 2012 (net of unamortized bond premium of $2,459 and $2,576 at June 30, 2014 and 2013, respectively) at fixed rates ranging from 3.000% to 4.000% due in various amounts through July 1, 2043.	154,693	154,856
Revenue Note, Series 2012 At a fixed rate of 3.600% through January 2022 and variable rates of LIBOR plus 225 basis points thereafter.	27,415	0
Capital Lease Liability on The Center for Orthopedic Medicine and The LVHN Surgery Center located on Tilghman Street. Payable in monthly installments through December 2025 with subsequent renewal and purchase options.	20,433	0
Capital Lease Liability on clinical equipment located at Hazleton. Payable in monthly installments through March 2016.	262	0
Capital Lease Liability on LVHN - One City Center located in downtown Allentown. Payable in monthly installments through May 2034 with subsequent renewal options.	49,316	0
Capital Lease Liability on parking deck and The Center for Advanced Health Care MOB located on LVH campus at Cedar Crest & I78. Payable in monthly installments through February 2027 with subsequent renewal options.	34,993	34,817
Mortgage liability to National Penn Bank for Hazleton Health & Wellness Center located at Hazleton and payable in monthly installments at an interest rate of 3.86%	1,515	0
Mortgage liability to PNC Bank on property located at 794 Roble Road, Allentown PA for future expansion of HNL operations. At a fixed rate of 2.82% and payable in annual installments through July 2043.	38,000	0
Mortgage liability to Firstrust Bank on property located at 2649 Schoenersville Road, Bethlehem, PA containing a medical office building on the LVHM campus. At a fixed rate of 4% with monthly payments of $33 through March 2016.	4,812	5,010
Total debt (net of unamortized bond premium and discount of $2,737 and $2,865 at June 30, 2014 and 2013, respectively)	$706,358	$581,672
Less current maturities	(14,966)	(12,303)
Total long-term debt, net of current portion	$691,392	$569,369

Maturities of Long-Term Debt

Scheduled principal maturities on long-term debt (excluding capital lease obligations) for the next five fiscal years and thereafter are as follows:

	Long-Term Debt
2015	$14,614
2016	20,477
2017	16,539
2018	17,208
2019	17,823
Thereafter	511,956
Total principal for long-term debt	$598,617

Long-Term Debt – Authority Bond Issues

LVHN, LVH, LVHM, and LVHH (the "Obligated Group") have borrowed funds through revenue bonds issued by the Lehigh County General Purpose Authority (the "Authority"). The proceeds were used in part to finance certain facilities of the Obligated Group. The revenue bonds are secured by a pledge of revenue of the Obligated Group. For accounting purposes, the revenue bonds are treated as though they are the debt of the entity which received the proceeds.

Issuance of Tax-Exempt Bonds – Series B of 2012

In December 2012, the Obligated Group issued $152,280 net of issuance premium of $2,645 in fixed rate Hospital Revenue Bonds, Series B of 2012 to finance a variety of capital investments and refinance $80,641 of fixed rate Hospital Revenue Bonds. Proceeds from the issuance included $78,675 to pay for capital projects and related costs, $15,950 to refinance the 2001B bonds, $57,655 to refinance the 2003A bonds, and cost of issuance fees of $1,860. A loss on refinancing of $3,990 was recorded and is reported as Loss on refinancing of debt in Other nonoperating gains and losses in the 2013 Consolidated Statements of Operations.

3. LONG-TERM DEBT (Continued)

Capital Leases
In August 2005, LVH entered into a lease arrangement with a third party to finance the construction of a 133,000 square foot medical office building to house The Center for Advanced Health Care and an adjacent 892 space parking deck. The lease has an initial term of 20 years with an optional renewal for 9 years and an additional optional renewal for another 11 years with a bargain purchase price option at the end of the second renewal. Lease payments are approximately $2,369 to $2,580 annually over the next five years and are subject to annual adjustments. Interest expense related to this financing is recorded throughout the life of the financing.

In March 2011, Greater Hazleton Health Alliance (GHHA) entered into a lease arrangement with a third party to lease clinical laboratory equipment. The lease has a term of 5 years with an obligation to purchase all the equipment for one dollar at the end of the term. The governing documents of GHHA were amended effective January 1, 2014, the closing date of the affiliation between LVHN and GHHA, where upon, GHHA merged into LVHN and LVHN became the sole member of Hazleton General Hospital.

In August 2012, the Organization entered into a lease arrangement with a third party to lease 186,000 square feet in a newly constructed office building in downtown Allentown. LVHN-One City Center houses a fitness center along with numerous sports medicine services and administrative office space. The lease has an initial term of 20 years beginning June 2014 with an optional renewal of 9 years and 11 months and an additional optional renewal of 10 years.

In November 2013, the Organization entered into a lease arrangement with a third party to lease 60,000 square feet in a former hospital and adjacent medical building to house The Center for Orthopedic Medicine-Tilghman, The LVHN Surgery Center-Tilghman and ExpressCARE-Tilghman. The lease has an initial term of 12 years beginning December 2013 with a bargain purchase option at the end of the initial term or two optional renewal terms of 5 years each.

Minimum future payments on capital lease payments for the next five fiscal years and thereafter are as follows:

	Principal	Interest	Scheduled Payments
2015	$352	$6,566	$6,918
2016	634	6,581	7,215
2017	611	6,596	7,207
2018	708	6,608	7,316
2019	837	6,615	7,452
Thereafter	61,739	86,809	148,548
Totals for capital leases	$64,881	$119,775	$184,656

Issuance of Mortgage
In December 2013, Health Network Labs issued $38,000 in bank debt for property located at 794 Roble Road payable in annual installments through July 2043.

Swap Agreements
The Organization has hedged its long term exposure to rising interest rates on portions of its variable rate debt through the participation in interest rate swaps. As of June 30, 2014, interest rate swap agreements with external counter parties were in place on the Series A of 2005 Bonds (the "2005 Swap"), the Series B of 2008 Bonds (the "2006 Swaps"), and Series A of 2012 (the "2012 Swap") bonds. These interest rate swaps effectively convert these variable rate bonds to a fixed rate. The Swaps carry a fair value based on long term interest rates and are further described in the table below:

3. LONG-TERM DEBT (Continued)

Swap Agreements (continued)

		Asset Derivatives	
		Fair Value	
Derivatives designated as hedging instruments	Consolidated Statements of Financial Position - location	2014	2013
Interest rate contracts - 2012 Swaps	Goodwill and other noncurrent assets	$90	$120

		Liability Derivatives	
		Fair Value	
Derivatives not designated as hedging instruments	Consolidated Statements of Financial Position - location	2014	2013
Interest rate contracts - 2005 Swap	Other liabilities	$5,984	$6,288
Interest rate contracts - 2006 Swaps	Other liabilities	11,204	11,891
Total derivatives not designated as hedging		$17,188	$18,179
Total derivatives, net		$17,098	$18,059

For the years ended June 30, 2014 and 2013, the 2005 and 2006 Swaps were determined to be ineffective hedges for accounting purposes and as a result did not qualify for hedge accounting treatment. Consequently, changes in the Swaps fair values are reported as a component of Other nonoperating gains and losses. The 2012 Swaps are considered to be effective hedges and qualify for hedge accounting treatment where all changes in the Swaps' fair values are reported as other changes in unrestricted net assets.

The below table presents the unrealized gains and losses on the 2005, 2006, and 2012 Swaps within the Consolidated Statements of Operations for the years ended June 30:

		Amount of unrealized gains (losses) recognized in	
Derivatives not designated as hedging instruments	Location of losses on ineffective portion	2014	2013
Interest rate contracts - 2005 Swap	Other nonoperating gains and losses - Change in net unrealized gains on swaps	$304	$2,992
Interest rate contracts - 2006 Swaps	Other nonoperating gains and losses - Change in net unrealized gains on swaps	687	5,467
Total derivatives not designated as hedging instruments		$991	$8,459
Derivatives designated as hedging instruments	Location of losses on effective portion		
Interest rate contracts - 2012 Swaps	Change in net unrealized (losses) gains on swaps	($30)	$290
Total derivatives		$961	$8,749

In addition to the above, the 2005, 2006, and 2012 Swaps also impose collateralization requirements on both parties if certain conditions occur. Collateralization for the 2005, 2006, or 2012 Swaps was not required as of June 30, 2014.

For the 2005 and 2006 Swaps, where Merrill Lynch is the counter party, no collateralization is required as long as LVHN maintains its current credit rating of A1 (Moody's) and A+ (S & P), regardless of the market value of the 2005 and 2006 Swaps. In addition, a change in the credit ratings of LVHN will trigger increasing or decreasing alternate collateral thresholds. For example, if LVHN's credit rating drops to A2/A, this would trigger a consolidated threshold of negative $15 million. Should the consolidated market value of both the 2005 and 2006 Swaps drop below the consolidated threshold, the difference between the market value and threshold would need to be established as collateral.

3. LONG-TERM DEBT (Continued)

Swap Agreements (continued)
For the 2006 Swap, where Goldman Sachs is the counter party, a $10 million collateral threshold is in place as long as LVHN maintains its current credit rating of A1 (Moody's) and A+ (S & P). Should the market value of the 2006 Swap drop below negative $10 million, the difference between the market value and threshold would need to be established as collateral. In addition, a change in the credit ratings of LVHN will trigger alternate collateral thresholds. For example, a credit rating drop to A2/A lowers the collateral threshold to $7 million for which a swap market value less than the $7 million would require collateralization by the difference between the market value and the threshold.

For the 2012 Swap, where JPMorgan is the counter party, a consolidated $5 million collateral threshold is in place as long as LVHN maintains its current credit rating of A1 (Moody's) and A+ (S & P). Should the consolidated market value of the 2012 Swaps drop below negative $5 million the difference between the individual market values and corresponding thresholds would need to be established as collateral. In addition, a change in the credit ratings of LVHN will trigger increasing or decreasing alternate collateral thresholds.

As of June 30, 2014, the 2005 and 2006 Swaps, where Merrill Lynch is the counter party, had negative market values of $5,984 and $5,628 respectively, and the 2006 Swap where Goldman Sachs is the counterparty had a market value of negative $5,576 and the 2012 Swaps where JPMorgan is the counterpart had positive market values of $39 and $51 for the 2012A and 2012B, respectively. Accordingly, collateralization for the 2005, 2006, and 2012 Swaps was not required as of June 30, 2014.

Lines of Credit
LVHN and LVH have a consolidated line of credit, expiring January 31, 2015, available which provide for borrowings and letters of credit up to an aggregate of $19,000 at June 30, 2014 and 2013. Although no borrowings were outstanding against this line of credit at June 30, 2014, a total of $5,015, in the form of letters of credit were committed as of June 30, 2014 and 2013, and is described further in the table below. The remaining amount available under the line of credit at June 30, 2014 and 2013 was $13,985.

The following schedule summarizes the letters of credit commitments outstanding at June 30:

Beneficiary	Purpose	2014	2013
South Carolina Dept Of Insurance	RRG capitalization collateral	$4,980	$4,980
City of Bethlehem, PA	LVHM North Campus expansion collateral	35	35
Total letters of credit commitments outstanding		$5,015	$5,015

Restrictive Covenants
The indentures for the Obligated Group's bonds incorporate certain restrictive covenants as provided in the 1987 Master Trust Bond Indenture regarding issuance of additional indebtedness on behalf of the Obligated Group. Additional long-term indebtedness, including, among other things, long-term indebtedness which may be secured on a parity with the 1987 bonds, may be incurred if either: (i) the revenues available for debt service of the Obligated Group for the fiscal year immediately preceding the incurrence of the proposed long-term indebtedness were at least equal to 125% of the sum of (a) the debt service requirements on all long-term indebtedness of the Obligated Group outstanding immediately preceding the incurrence of the proposed long-term indebtedness, and (b) the maximum annual debt service requirements on the long-term indebtedness to be incurred; or (ii) immediately after the incurrence of the proposed long-term indebtedness, the total outstanding long-term indebtedness of the Obligated Group will not exceed 66 2/3% of principal amount of all long-term indebtedness plus the unrestricted net assets of the Obligated Group.

The 1994 Series A bonds include requirements to maintain a Debt Service Coverage Ratio of at least 110%, or if such percentage cannot be achieved in any fiscal year as a result of restrictions imposed under applicable laws and regulations (including cost containment requirements, restrictions on rates or revenues or reimbursement regulations or policies imposed by governmental third-party payers) or as a result of restrictions or policies imposed by private third-party payers affecting any particular Obligated Issuer or Issuers, at least 100%. If the covenant is not met, the engagement of a consultant is required. However, failure to meet the covenant will not be an event of default as long as the Debt Service Coverage Ratio for the Obligated Group is at least 100%, the Debt Service Coverage Ratio for all Obligated Issuers which were not affected by such laws or regulations, as referred to above, is at least 110%, a consultant is engaged and a good faith effort is made to implement the recommendations of the consultant.

3. LONG-TERM DEBT (Continued)

Restrictive Covenants (continued)

The 2005 Series A bonds include requirements to (a) maintain a Debt Service Coverage Ratio of 1.25, (b) maintain Days Cash on Hand of at least 70 days and (c) maintain an Indebtedness Ratio not to exceed 66 2/3%. However, failure to maintain any of these covenants will not be a violation if it is remedied by the end of the next fiscal quarter. Failure to maintain a Debt Service Coverage Ratio of 1.00, Days Cash on Hand of at least 60 days or an Indebtedness Ratio of not greater than 70% is an event of default and LVHN would have 30 days to cure the default. In the event of default, the bank has the right to accelerate the bonds, at which time LVHN would have at least 30 days to repurchase some or all of the bonds from the bank or remarket the bonds. Failure to maintain a Debt Service Coverage Ratio of 1.25, Days Cash on Hand of at least 60 days or an Indebtedness Ratio of not greater than 0.67 to 1 requires the engagement of a consultant. Also, failure to maintain a Debt Service Coverage Ratio of at least 1.75 or maintain Days Cash on Hand of at least 90 days will result in the requirement to immediately fund a Debt Service Reserve account in the amount of $6.1 million.

The 2005 Series B bonds include requirements to (a) maintain a Debt Service Coverage Ratio of 1.25, (b) maintain Days Cash on Hand of at least 60 days and (c) maintain an Indebtedness Ratio not to exceed 0.67 to 1. If any of the preceding covenants are not met; the engagement of a consultant is required. Also, failure to maintain a Debt Service Coverage Ratio of at least 1.75 or maintain Days Cash on Hand of at least 90 days will result in the requirement to immediately fund a Debt Service Reserve account in the amount of $8.1 million. Upon issuance the 2005 Series B bonds required the establishment of a Debt Service Reserve account in the amount of $5.0 million which remained in place at June 30, 2014 and 2013. If additional funding of the Series B Debt Service Reserve is required as described above, the amount of funding required will be reduced by the current $5.0 million Series 2005 B Debt Service Reserve, resulting in an additional funding requirement of $3.1 million. This debt service account is reported under Noncurrent assets as Assets limited under bond indenture, bond construction, debt service, and debt service reserve agreements – held by trustee in the Consolidated Statements of Financial Position.

The 2008 Series A bonds include requirements to (a) maintain a Debt Service Coverage Ratio of 1.25, (b) maintain Days Cash on Hand of at least 60 days and (c) maintain an Indebtedness Ratio not to exceed 0.67 to 1. If any of the preceding covenants are not met the engagement of a consultant is required. Also, failure to maintain a Debt Service Coverage Ratio of at least 1.75 or maintain Days Cash on Hand of at least 90 days will result in the requirement to immediately fund a Debt Service Reserve account in the amount of $4.7 million.

The 2008 Series B bonds include requirements to (a) maintain a Debt Service Coverage Ratio of 1.25, (b) maintain Days Cash on Hand of at least 70 days and (c) maintain an Indebtedness Ratio not to exceed 66 2/3%. However, failure to maintain any of these covenants will not be a violation if it is remedied by the end of the next fiscal quarter. Failure to maintain a Debt Service Coverage Ratio of 1.00, Days Cash on Hand of at least 60 days or an Indebtedness Ratio of not greater than 70% is an event of default and LVHN would have 30 days to cure the default. In the event of default, the bank has the right to accelerate the bonds, at which time LVHN would have at least 30 days to repurchase some or all of the bonds from the bank or remarket the bonds. Failure to maintain a Debt Service Coverage Ratio of 1.25, Days Cash on Hand of at least 65 days or an Indebtedness Ratio of not greater than 0.67 to 1 requires the engagement of a consultant. Also, failure to maintain a Debt Service Coverage Ratio of at least 1.75 or maintain Days Cash on Hand of at least 90 days will result in the requirement to immediately fund a Debt Service Reserve account in the amount of $9.6 million.

The 2008 Series C bonds include requirements to (a) maintain a Debt Service Coverage Ratio of 1.25, (b) maintain Days Cash on Hand of at least 70 days and (c) maintain an Indebtedness Ratio not to exceed 70%. However, failure to maintain the Debt Service Coverage or Days Cash on Hand covenants will not be a violation if it is remedied by the end of the next fiscal quarter. Failure to maintain a Debt Service Coverage Ratio of 1.00, Days Cash on Hand of at least 60 days or an Indebtedness Ratio of not greater than 70% is an event of default and LVHN would have 30 days to cure the default. In the event of default, the bank has the right to accelerate the bonds, at which time LVHN would have to repurchase some or all of the bonds from the bank or remarket the bonds.

The 2011 Series A bonds include requirements to (a) maintain a Debt Service Coverage Ratio of 1.25, (b) maintain Days Cash on Hand of at least 70 days and (c) maintain an Indebtedness Ratio not to exceed 66 2/3%. However, failure to maintain any of these covenants will not be a violation if it is remedied by the end of the next fiscal quarter. Failure to maintain a Debt Service Coverage Ratio of 1.00, Days Cash on Hand of at least 60 days or an Indebtedness Ratio of not greater than 70% is an event of default and LVHN would have 30 days to cure the default. In the event of default, the bank has the right to accelerate the bonds, at which time LVHN would have at least 30 days to repurchase some or all of the bonds from the bank or remarket the bonds.

3. LONG-TERM DEBT (Continued)

Restrictive Covenants (continued)
The 2012 Series A bonds include requirements to (a) maintain a Debt Service Coverage Ratio of 1.25, (b) maintain Days Cash on Hand of at least 70 days and (c) maintain an Indebtedness Ratio not to exceed 70%. However, failure to maintain the Debt Service Coverage or Days Cash on Hand covenants will not be a violation if it is remedied by the end of the next fiscal quarter. Failure to maintain a Debt Service Coverage Ratio of 1.00, Days Cash on Hand of at least 60 days or an Indebtedness Ratio of not greater than 70% is an event of default and LVHN would have 30 days to cure the default. In the event of default, the bank has the right to accelerate the bonds, at which time LVHN would have to repurchase some or all of the bonds from the bank or remarket the bonds.

The 2012 Series B bonds include requirements to maintain a Debt Service Coverage Ratio of at least 1.25, or if such percentage cannot be achieved in any fiscal year as a result of restrictions imposed under applicable laws and regulations (including cost containment requirements, restrictions on rates or revenues or reimbursement regulations or policies imposed by governmental third-party payers) or as a result of restrictions or policies imposed by private third-party payers affecting any particular Obligated Issuer or Issuers, at least 1.0. If the covenant is not met, the engagement of a consultant is required. However, failure to meet the covenant will not be an event of default as long as the Debt Service Coverage Ratio for the Obligated Group is at least 1.0, the Debt Service Coverage Ratio for all Obligated Issuers which were not affected by such laws or regulations, as referred to above, is at least 1.0, a consultant is engaged and a good faith effort is made to implement the recommendations of the consultant.

The series 2012 Revenue Note includes requirements to (a) maintain a Debt Service Coverage Ratio of 1.25, (b) maintain Days Cash on Hand of at least 70 days and (c) maintain an Indebtedness Ratio not to exceed 66 2/3%. However, failure to maintain any of these covenants will not be a violation if it is remedied by the end of the next fiscal quarter. Failure to maintain a Debt Service Coverage Ratio of 1.00, Days Cash on Hand of at least 60 days or an Indebtedness Ratio of not greater than 70% is an event of default and LVHN would have 30 days to cure the default. In the event of default, the bank has the right to accelerate the notes.

For the years ended June 30, 2014 and 2013, the financial covenants noted above were met and the Obligated Group was not aware of any instances of non-compliance with its other covenants.

4. PROPERTY AND EQUIPMENT, NET

Property and equipment and accumulated depreciation and amortization consist of the following at June 30:

	2014	2013
Land and land improvements	$76,716	$67,156
Buildings and building equipment	958,486	848,311
Fixed and major movable equipment	497,022	446,473
Assets under capital lease	102,713	32,188
Construction in progress	71,167	46,728
Total original cost	1,706,104	1,440,856
Accumulated depreciation and amortization	(874,400)	(802,396)
Property and equipment, net	$831,704	$638,460

Depreciation and amortization expense for the years ended June 30, 2014 and 2013 was $94,166 and $83,362, respectively. Depreciation of assets under capital lease included in depreciation and amortization expense was $2,106 and $1,414 at June 30, 2014 and 2013, respectively. Accumulated depreciation relating to the assets under capital lease was $11,288 and $9,182 at June 30, 2014 and 2013, respectively, and is included in accumulated depreciation.

The Organization under construction projects has commitments of approximately $24,744 as of June 30, 2014.

5. FUNCTIONAL EXPENSES

The Organization provides a wide array of health care services to patients and members of the community within its service area. Expenses related to providing these services, including provision for income taxes, were as follows for the years ended June 30:

	2014	%	2013	%
Health care services	$1,550,778	94%	$1,433,517	94%
General and administrative	103,588	6%	98,306	6%
Total	$1,654,366	100%	$1,531,823	100%

General and administrative expenses include expenses for organizational administrative activities, primarily human resources, management, legal, and financial services. The categorization of expenses as health care services versus general and administrative follows the guidance provided for similar expense reporting in the annual Internal Revenue Service (IRS) Form 990.

Effective July 1, 2012, the Organization adopted the provisions of Accounting Standards Update ("ASU") 2011-07, "Health Care Entities (Topic 954)*: Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities".* As a result of retrospectively reclassifying the Provision for bad debts associated with patient service revenue from an operating expense to a deduction from patient service revenue (net of contractual allowances and discounts), the Functional expenses disclosure above is also reported on a retrospective basis.

6. FUNDS HELD BY FIDUCIARY

LVH is the primary beneficiary of the Dorothy Rider Pool Health Care Trust (the "Pool Trust") which was established through the estate of a former director of LVH. The fair value of the Pool Trust at June 30, 2014 and 2013 was $85,205 and $79,538, respectively. The assets of the Pool Trust are not included in the accompanying consolidated financial statements. Under the general provisions of the Trust, distributions from the Pool Trust are to be made to or for the benefit of LVH to supplement, not replace, LVH's ordinary operating expenses, so that LVH can be operated and managed in a manner that will improve its medical standards, knowledge and procedures, and sustain at the highest level of quality the health maintenance and hospital care it provides to members of the community it serves. Under certain circumstances, distributions from the Pool Trust may be made to other designated health care related organizations. Distributions to LVH from the Pool Trust were $2,930 and $3,518 for the years ended June 30, 2014 and 2013, respectively, and are reported as a component of Other supporting operations revenue.

7. CHARITY CARE

As a community organization, all revenues and gains in excess of expenses and losses of the Organization are, or will be, used for the repayment of debt, acquisition of equipment and facilities, and to provide for the present and future health care needs of the patients and communities it serves. The Organization provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates regardless of their ability to pay. Because the Organization does not pursue collection of amounts determined to qualify as charity care, they are not reported as patient service revenues. The amount of charity care to patients for the years ended June 30, 2014 and 2013, at cost, was $29,007 and $25,767 respectively. Costs of these services were estimated by calculating a ratio of overall cost to gross charges for all patients and then applying this ratio to gross charges for patients receiving charity care.

8. BAD DEBTS

In instances where the Organization believes a patient has the ability to pay for services and, after appropriate collection effort, payment is not made; the amount of services not paid is written-off as bad debts. Amounts recorded as Provision for bad debts do not include charity care. The amount of Provision for bad debts for the years ended June 30, 2014 and 2013, was $84,505 and $117,493, respectively. Effective July 1, 2013, the Organization began discounting uninsured accounts using the amount generally billed (AGB) principal. The AGB, as defined in proposed IRS section 501(r), is the average payment amount of private insurers and Medicare. The policy change decreases net patient revenue before bad debts and provision for bad debts but does not change net patient service revenue (net of bad debts).

9. RETIREMENT PLAN

The Organization provides employees with a variety of retirement plan options through a combination of defined benefit and defined contribution benefit plans based on an employee's hire date. Effective January 1, 2014, with the addition of the Lehigh Valley Hospital Hazleton (formerly the Hazleton General Hospital), these plans are reviewed separately below in greater detail.

Lehigh Valley Health Network Defined Benefit Retirement Plan (excluding LVHH)
Prior to July 1, 2006, the Organization's retirement plan ("the Plan") was a noncontributory defined benefit plan that covered all full-time and certain part-time employees. In order to provide increased flexibility to employees, effective July 1, 2006, additional retirement plan options were implemented. Employees hired prior to April 1, 2006, had the choice of selecting between 1) a noncontributory defined benefit option (the previous plan), 2) a combination of noncontributory defined benefit option with reduced benefits plus a contributory matched savings plan benefit in accordance with the Plan, or 3) a noncontributory defined contribution benefit with a matched savings plan benefit in accordance with the Plan. Employees hired on April 1, 2006 or later have the choice of selecting between options 2 and 3 above, the previous noncontributory defined benefit option (option 1 above) is not available to employees hired after April 1, 2006. During 2011 the Organization further modified pension plan options available to employees in the future. Employees hired on or after October 1, 2011 can participate only in option 3 above. In addition, future benefit accruals for active participants in the defined benefit plan are phased to frozen status in the future with all active employees transitioning to the defined contribution plan as of January 1, 2017.

The following applies to the defined benefit component of the retirement plan:

Information for the noncontributory defined benefit option regarding funded status, net periodic pension cost, benefit obligation, assumptions, etc., as of June 30, 2014 and 2013, is presented below and on the following pages and includes the impact of employee selection of pension benefit options. The Plan's assets described below and on the following pages are not included in the consolidated financial statements of the Organization.

Description of Investment Policies
The primary investment objective for the Plan's assets is to achieve long term growth subject to prudent risk constraints.

Plan Assets
During fiscal year 2014 the Finance Committee of the Board of Trustees approved new asset allocation targets for the LVHN Plan's assets. As of June 30, 2014 the transition of investments to this new asset allocation was still in progress and is expected to be completed early in fiscal year 2015. Asset allocation targets, which are permitted to be +/- 3-5%, approved by the Finance Committee of the Board of Trustees , and the Plan's actual asset allocation, by investment category, at June 30, was:

LVHN Plan Assets (excluding LVHH)

	2014		2013	
Investment category	Actual	Target	Actual	Target
Domestic equity	27.7%	25.0%	32.4%	30.0%
International equity - developed markets	21.2%	19.0%	21.2%	20.0%
International equity - emerging markets	6.2%	6.0%	0.0%	0.0%
Private equity	1.8%	0.0%	2.2%	5.0%
Hedge funds	4.5%	7.5%	5.3%	5.0%
Real estate securities	4.3%	0.0%	4.8%	5.0%
Private core real estate	0.0%	7.5%	0.0%	0.0%
Commodities contracts	0.0%	0.0%	5.1%	5.0%
Bank loan funds	4.8%	5.0%	0.0%	0.0%
Fixed income	29.5%	30.0%	29.0%	30.0%
Total	100.0%	100.0%	100.0%	100.0%

Determination of Expected Return on Plan Assets
To develop the expected return on Plan assets assumption reported below, the Organization considered the current level of expected returns on risk free investments (primarily government bonds), the historical level of the risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns of each class. The expected return for each asset class was weighted based on the target asset allocation to develop the expected long-term rate of return on assets assumption for the portfolio. This resulted in the selection of the 7.0% return on plan assets assumptions for 2014 and 2013.

9. RETIREMENT PLAN (Continued)

The following tables present the categorization of LVHN's Plan assets according to the levels of valuation risk described in Note 13 at June 30:

LVHN Plan Assets 2014

Type of Investment	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$0	$9,540	$0	$9,540
Equity securities:				
Domestic equity	211,043	0	0	211,043
International equity - developed markets	161,625	0	0	161,625
International equity - emerging markets	47,205			47,205
Real estate equity	32,473	0	0	32,473
Fixed income:				
U.S. Treasury securities and obligations of U.S. Government agencies	61,818	13,439	0	75,257
Corporate bonds	0	134,785	0	134,785
Asset-backed securities	0	4,549	0	4,549
Collateralized mortgage obligations	0	1,290	0	1,290
Bank loan funds	0	0	36,685	36,685
Hedge funds (multi-strategy)	0	13,651	20,751	34,402
Private equity	0	0	12,343	12,343
Total assets at fair value	$514,164	$177,254	$69,779	$761,197

LVHN Plan Assets 2013

Type of Investment	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$0	$8,398	$0	$8,398
Equity securities:				
Domestic equity	195,269	0	0	195,269
International equity - developed markets	128,082	0	0	128,082
Real estate equity	28,516	0	0	28,516
Fixed income:				
U.S. Treasury securities and obligations of U.S. Government agencies	101,921	21,896	0	123,817
Corporate bonds	0	41,196	0	41,196
Asset-backed securities	0	1,596	0	1,596
Collateralized mortgage obligations	0	232	0	232
Hedge funds (multi-strategy)	0	13,140	18,639	31,779
Commodities contracts	0	30,827	0	30,827
Private equity	0	0	13,132	13,132
Total assets at fair value	$453,788	$117,285	$31,771	$602,844

9. RETIREMENT PLAN (Continued)

The Plan's use of Level 3 unobservable inputs, as described in Note 13, as of June 30, 2014 and 2013 accounted for 9.2% and 5.3%, respectively, of the total fair value of investments. The following table summarizes changes in Level 3 assets measured at fair value at June 30, 2014 and 2013:

2014	Bank loan funds	Private equity	Hedge funds	Total
Balance at July 1, 2013	$0	$13,132	$18,639	$31,771
Realized investment earnings	0	938	0	938
Net appreciation in market value of investments	173	1,246	2,112	3,531
Purchases	36,512	0	0	36,512
Sales	0	(2,973)	0	(2,973)
Balance at June 30, 2014	$36,685	$12,343	$20,751	$69,779

2013	Bank loan funds	Private equity	Hedge funds	Total
Balance at July 1, 2012	$0	$13,602	$21,926	$35,528
Realized investment earnings	0	673	27	700
Net appreciation in market value of investments	0	671	1,886	2,557
Purchases	0	171	16,728	16,899
Sales	0	(1,985)	(21,928)	(23,913)
Balance at June 30, 2013	$0	$13,132	$18,639	$31,771

For the years ended June 30, 2014 and 2013, respectively, there were no transfers between valuation levels.

Additional Pension Information

The Organization uses a June 30 measurement date for the Plan. The following tables set forth the Plan's funded status at June 30, benefits paid, and employer contributions made during the fiscal years ended June 30, 2014 and 2013 and certain other information and amounts recognized in the consolidated financial statements at June 30:

	2014	2013
Change in benefit obligation		
Projected benefit obligation at beginning of year	$779,680	$787,465
Service cost	23,269	26,356
Interest cost	39,447	36,450
Actuarial loss (gain)	93,303	(57,086)
Benefits paid	(15,828)	(13,505)
Projected benefit obligation at end of year	$919,871	$779,680
Change in plan assets		
Fair value of plan assets at beginning of year	$602,844	$519,616
Actual return on plan assets	117,390	39,096
Employer contributions	56,791	57,637
Benefits paid	(15,828)	(13,505)
Fair value of plan assets at end of year	$761,197	$602,844
Funded status at end of year	($158,674)	($176,836)
Amounts recognized in the statements of financial position consists of:		
Accrued pension liability - noncurrent portion	(158,674)	(176,836)
Net amount recognized	($158,674)	($176,836)
Amounts recognized in unrestricted net assets but not yet recognized in net periodic benefit cost		
Prior service costs	$0	$5
Net loss	151,107	136,721
Total amount recognized in unrestricted net assets	$151,107	$136,726

9. RETIREMENT PLAN (Continued)

Additional Pension Information (continued)

	2014	2013
Components of net periodic benefit cost (NPBC)		
Service cost	$23,269	$26,356
Interest cost	39,447	36,450
Expected return on plan assets	(43,651)	(37,726)
Amortization of prior service cost	5	9
Recognized actuarial loss	5,178	10,815
Net periodic benefit cost (pension expense)	$24,248	$35,904
Other changes in plan assets and benefit obligation recognized in unrestricted net assets		
Net actuarial loss (gain)	$19,564	($58,456)
Amortization of loss	(5,178)	(10,815)
Amortization of prior service cost	(5)	(9)
Total loss (gain) recognized in unrestricted net assets	$14,381	($69,280)
Balance at beginning of year	($176,836)	($267,849)
Annual pension expense	(24,248)	(35,904)
Adjustments to funded status of pension plan	(14,381)	69,280
Annual contributions	56,791	57,637
Balance at end of year	($158,674)	($176,836)
Accumulated benefit obligation at year end	$844,949	$705,824
Weighted - average assumptions used to determine projected benefit obligation		
Discount rate	4.614%	5.124%
Rate of compensation increase	3.500%	3.500%
Weighted - average assumptions used for NPBC development		
Discount rate	5.124%	4.689%
Expected return on plan assets	7.000%	7.000%
Rate of compensation increase	3.500%	3.500%

The actuarial net loss and prior service cost that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year are $5,260 and $0, respectively.

Estimated Future Benefit Payments

Future payments on an undiscounted basis to participants in the Plan are expected to occur as follows:

Fiscal 2015	$21,756
Fiscal 2016	24,909
Fiscal 2017	28,168
Fiscal 2018	31,996
Fiscal 2019	36,074
Fiscal 2020-2024	245,771
Total	$388,674

Expected contributions for the defined benefit plan are $53,000 for the year ended June 30, 2014.

Lehigh Valley Hospital Hazleton Defined Benefit Retirement Plans

The Lehigh Valley Hospital Hazleton (formerly Hazleton General Hospital) sponsors two defined benefit pension plans for its employees, Hazleton-St. Joseph Medical Center (HSJMC) and Hazleton General Hospital (HGH). The plans provide benefits based on years of service and final average salary. The pension plan of HSJMC was frozen in September 2005 when it ceased providing patient services and terminated all active employees. HGH froze its defined benefit pension plan in December 2006.

9. RETIREMENT PLAN (Continued)

Lehigh Valley Hospital Hazleton Defined Benefit Retirement Plans (continued)

The following applies to the defined benefit retirement plans:

Information for the noncontributory defined benefit plans regarding funded status, net periodic pension cost, benefit obligation, assumptions, etc., as of June 30, 2014, is presented below and on the following pages and includes the impact of employee selection of pension benefit options. The Plan's assets described below and on the following pages are not included in the consolidated financial statements of the Organization.

Description of Investment Policies
The primary investment objective for the Plan's assets is to achieve long term growth subject to prudent risk constraints.

Plan Assets
Asset allocation targets, which are permitted to be +/- 10%, approved by the Finance Committee of the Board of Trustees, and the Plan's actual asset allocation, by investment category, at June 30 were:

LVHH Plan Assets

	2014	
Investment category	Actual	Target
Equity	63.5%	60.0%
Fixed income	36.5%	40.0%
Total	100.0%	100.0%

Determination of Expected Return on Plan Assets
To develop the expected return on Plan assets assumption reported below, the Organization considered the current level of expected returns on risk free investments (primarily government bonds), the historical level of the risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns of each class. The expected return for each asset class was weighted based on the target asset allocation to develop the expected long-term rate of return on assets assumption for the portfolio. This resulted in the selection of the 7.0% return on plan assets assumptions for 2014. Due to the acquisition of GHHA in the current fiscal year no comparative information is presented at June 30, 2013.

The following table presents the categorization of LVHH's Plan assets according to the levels of valuation risk described in Note 13 at June 30:

LVHH Plan Assets 2014

Type of Investment	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$0	$1,584	$0	$1,584
Equity securities				
Equity	25,494	0	0	25,494
Fixed income				
U.S. Treasury securities and obligations of U.S. Government agencies	0	5,964	0	5,964
Corporate bonds	0	7,106	0	7,106
Total assets at fair value	$25,494	$14,654	$0	$40,148

The Plan's did not invest in any Level 3 unobservable securities as of June 30, 2014 and there were no transfers between valuation levels.

9. RETIREMENT PLAN (Continued)

Additional Pension Information

The following tables set forth the Plan's funded status at June 30, benefits paid, and employer contributions made for the 6 month period ended June 30, 2014 and certain other information and amounts recognized in the consolidated financial statements at June 30, 2014. Due to the acquisition in the current fiscal year no comparative information is presented at June 30, 2013.

	2014
Change in benefit obligation	
Projected benefit obligation at beginning of year	$51,713
Interest cost	1,204
Actuarial loss	4,010
Benefits paid	(996)
Projected benefit obligation at end of year	$55,931
Change in plan assets	
Fair value of plan assets at beginning of year	$38,791
Actual return on plan assets	1,856
Employer contributions	497
Benefits paid	(996)
Fair value of plan assets at end of year	$40,148
Funded status at end of year	($15,783)
Amounts recognized in the statements of financial position consists of:	
Accrued pension liability - noncurrent portion	$15,783
Net amount recognized	$15,783
Amounts recognized in unrestricted net assets but not yet recognized in net periodic benefit cost	
Net loss	$13,275
Total amount recognized in unrestricted net assets	$13,275
Components of net periodic benefit cost (NPBC)	
Interest cost	$1,204
Expected return on plan assets	(1,352)
Recognized actuarial loss	104
Net periodic benefit cost (pension expense)	($44)
Other changes in plan assets and benefit obligation recognized in unrestricted net assets	
Net actuarial loss	$3,506
Amortization of loss	(103)
Total loss recognized in unrestricted net assets	$3,403
Reconciliation of accrued pension cost	
Balance at beginning of year	($12,921)
Annual pension expense	44
Adjustments to funded status of pension plan	(3,403)
Annual contributions	497
Balance at end of year	($15,783)
Accumulated benefit obligation at year end	$55,931
Weighted - average assumptions used to determine projected benefit obligation	
Discount rate	4.200%
Rate of compensation increase	0.000%
Weighted - average assumptions used for NPBC development	
Discount rate	4.700%
Expected return on plan assets	7.000%
Rate of compensation increase	0.000%

The actuarial net loss and prior service cost that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year are $406 and $0, respectively.

9. RETIREMENT PLAN (Continued)

Estimated Future Benefit Payments

Future payments on an undiscounted basis to participants in the Plan are expected to occur as follows:

Fiscal 2015	$2,029
Fiscal 2016	2,112
Fiscal 2017	2,207
Fiscal 2018	2,336
Fiscal 2019	2,443
Fiscal 2020-2024	14,024
Total	$25,151

The following applies to the defined contribution and matched savings components of the retirement plan of LVHN including Lehigh Valley Hospital - Hazleton:

During the years ended June 30, 2014 and 2013, the Organization made contributions of $14.5 million and $12.2 million, respectively, to the defined contribution component of the Plan and recorded $15.3 million and $13.0 million, respectively, in related pension expense. The liability recognized under the Current liabilities Pension in the Consolidated Statements of Financial Position at June 30, 2014 and 2013 for the defined contribution component of the Plan was $4.7 million and $3.9 million, respectively. Total expected contributions to the defined contribution component of the Plan in fiscal year 2015 are $16.7 million.

During the years ended June 30, 2014 and 2013, the Organization made contributions of $7.3 million and $6.6 million, respectively, to the matched savings benefit component of the Plan and recorded $7.4 million and $6.6 million, respectively, in related pension expense. The liability recognized under the Current liabilities Pension in the Consolidated Statements of Financial Position at June 30, 2014 and 2013 for the matched savings benefit component of the Plan was $0.3 million and $0.1 million, respectively. Total expected contributions to the matched savings component of the Plan in fiscal year 2015 are $8.0 million.

10. COMMITMENTS AND CONTINGENCIES

Operating Leases

Rental expense reported on the Other expense line of the Consolidated Statements of Operations for the years ended June 30, 2014 and 2013 was $26,519 and $25,296, respectively.

Minimum future rentals under non-cancelable operating leases with terms in excess of one year as of June 30, 2014 are as follows:

Fiscal Year	Real Estate	Vehicles	Equipment	Total
2015	$15,607	$385	$173	$16,165
2016	$15,266	$274	$156	$15,696
2017	$13,285	$149	$137	$13,571
2018	$10,883	$67	$2	$10,952
2019	$8,778	$10	$1	$8,789
Thereafter	$48,294	$0	$0	$48,294

Litigation

The Organization is involved in litigation and regulatory investigations arising in the course of business. Based on the opinion of in-house legal counsel and risk management, who routinely consult and work with external legal counsel, management estimates that these matters will be resolved without material adverse effect on the Organization's future consolidated financial position or results from operations.

11. TEMPORARILY AND PERMANENTLY RESTRICTED NET ASSETS

Temporarily restricted net assets were available for the following purposes for the years ended June 30:

	2014	2013
Purchase of capital assets	$557	$245
Specific health care services and education	128,499	103,137
Total temporarily restricted net assets	$129,056	$103,382

Permanently restricted net assets, which total $51,493 and $47,741 at June 30, 2014 and 2013, respectively, are required to be held in perpetuity with the expendable income earned thereon to be used to support health care services and education.

12. ENDOWMENT FUNDS

Endowment funds are defined as funds established by donors or the Board of Trustees to provide the Organization with either a permanent source of income or a source of income for a specified period of time. The Organization's endowment funds consist of 119 and 113 individual donor-restricted funds at June 30, 2014 and 2013, respectively, established for a variety of purposes hereinafter referred to as the "LVHN Endowment Fund". The Organization does not have Board Designated endowment funds or unrestricted endowment funds.

Interpretation of Relevant Law

The Organization has interpreted Pennsylvania law as requiring preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds when explicit donor stipulations requiring permanent maintenance of the historical fair value are present. As a result of this interpretation, the Organization classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment when explicit donor stipulations requiring permanent maintenance of the historical fair value are present, (b) the original value of the subsequent gifts to the permanent endowment when explicit donor stipulations requiring permanent maintenance of the historical fair value are present, and (c) accumulations of investment earnings to the permanent endowment in cases where the donor explicitly instructed a portion of investment earnings be added to the permanent fund. The remaining portion of the donor-restricted endowment funds comprised of accumulated investment earnings not required to be maintained in perpetuity is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Organization in a manner consistent with donors' stipulations. The Organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: duration and preservation of the fund, purposes of the donor-restricted endowment fund, general economic conditions, the possible effect of inflation and deflation, the expected total return from income and the appreciation of investments, other resources of the Organization, and the investment policies of the Organization.

The net asset composition of the LVHN Endowment Fund, which the Organization actively managed, at June 30, was as follows:

	Temporarily restricted	Permanently restricted	Total
2014			
Donor restricted endowment funds	$96,089	$43,319	$139,408
2013			
Donor restricted endowment funds	$80,032	$40,802	$120,834

12. ENDOWMENT FUNDS (Continued)

Changes in the LVHN Endowment fund net assets at June 30 were as follows:

2014	Temporarily restricted	Permanently restricted	Total
Endowment net assets, beginning of year	$80,032	$40,802	$120,834
Investment Return:			
Investment income	2,271	0	2,271
Net appreciation (realized and unrealized)	16,770	0	16,770
Total investment return	19,041	0	19,041
Contributions	37	2,435	2,472
Reclassification to permanently restricted from temporarily restricted	0	82	82
Appropriation of endowment assets for expenditures (expense)	(3,021)	0	(3,021)
Endowment net assets, end of year	$96,089	$43,319	$139,408

2013	Temporarily restricted	Permanently restricted	Total
Endowment net assets, beginning of year	$71,329	$39,786	$111,115
Investment Return:			
Investment income	1,785	0	1,785
Net appreciation (realized and unrealized)	9,754	0	9,754
Total investment return	11,539	0	11,539
Contributions	74	1,252	1,326
Reclassification from permanently restricted to temporarily restricted and unrestricted net assets - other supporting operations revenue	0	(236)	(236)
Appropriation of endowment assets for expenditures (expense)	(2,910)	0	(2,910)
Endowment net assets, end of year	$80,032	$40,802	$120,834

Investment Return Objectives

The Organization has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Organization must hold in perpetuity and assets with donor specified annual spending limitations and in some cases purpose restrictions applicable for a specified period of time after which any remaining assets become unrestricted. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a diversified manner that is intended to produce results that over the long term will average 3 to 4 percentage points above the consumer price index while assuming a moderate level of investment risk. Actual returns in any given year may vary from this amount.

12. ENDOWMENT FUNDS (Continued)

To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). During fiscal year 2014 the Finance Committee of the Board of Trustees approved new asset allocation targets for the LVHN Endowment assets. As of June 30, 2014 the transition of investments to this new asset allocation was still in progress and is expected to be completed in fiscal year 2015. As a result, certain asset classes were temporarily outside their target range at June 30, 2014. The actual and target investment allocations, by investment category, were as follows for the LVHN Endowment assets as of June 30, 2014:

LVHN Endowment assets	Actual %	Target %
Domestic equity	26%	26%
International equity - developed markets	20%	20%
International equity - emerging markets	7%	6%
Real estate securities	5%	0%
Private core real estate	0%	10%
Bank loans	6%	6%
Fixed income	30%	22%
Hedge funds	6%	10%
Total	100%	100%

Spending Policy and How the Investment Objectives Relate to Spending Policy

The Organization has a policy of appropriating for distribution each year between 4 and 5 percent of the LVHN Endowment Fund's total fair value, including accumulated total investment returns. In establishing this policy, the Organization considered the long-term expected return on its endowments which is expected to exceed the allowable spending, and therefore over the long term, the Organization expects its endowment funds to grow. This is consistent with the Organization's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term, as well as, to provide additional real growth through new gifts and investment return.

13. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used by the Organization in estimating the fair value of its financial instruments:

Cash and cash equivalents, patient accounts receivables, prepaid expenses, accounts payable, estimated third party settlements, and all other current liabilities are reported at carrying values which approximate fair value because of the short term nature of these accounts.

Assets whose use is limited or restricted is comprised of short-term investments, marketable equity securities, equity mutual funds, corporate and U.S. Government obligations, fixed income mutual funds, real estate securities, commodities contracts, and perpetual trusts which are reported at amounts which approximate fair value based on quoted market prices and other relevant information. Alternative investments, which include commodity contracts, bank loan funds, and hedge funds, are carried at the net asset value provided by the management of the alternative investment partnerships or funds.

Assets and liabilities recorded at fair value in the Consolidated Statements of Financial Position are categorized based upon the level of judgment associated with the inputs used to measure their fair value. In situations where more than one level of input is used to determine the fair value of an asset or liability, the asset or liability categorization within the fair value hierarchy is based on the lowest (that requiring the most judgment) level of significant input to its valuation. Hierarchical levels directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities are described below.

The availability of observable inputs for valuation of investments varies and is affected by a wide variety of factors. When the valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires significantly more judgment. The degree of judgment exercised by management in determining fair value is greatest for investments categorized as Level 3. For investments in this category, the Organization considers prices and inputs that are current as of the measurement date. In periods of market dislocation the observability of prices and inputs may be reduced.

13. FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Level 1 – Valuations based on quoted prices in active markets for *identical* assets or liabilities that the Organization has the ability to access. Since valuations are based on quoted prices that are readily and regularly available in active markets, valuation of these products do not entail a significant degree of judgment. Level 1 primarily includes those investments traded on active exchanges or markets.

Level 2 – Valuations based on quoted prices in active markets for *similar* assets or liabilities, quoted in markets that are not active or for which an identical asset or liability was not traded on the financial statement date or where all significant inputs are not observable, directly or indirectly. Level 2 primarily includes investments in U.S. Treasury securities and obligations of U.S. government agencies, together with municipal bonds, corporate debt securities, commercial mortgage and asset-backed securities, certain residential mortgage-backed securities that are generally investment grade, certain equity securities, hedge funds, and commodity contracts. The Organization based the fair value of hedge funds and commodity contracts on the fair value of the underlying reported net asset values of each fund held. The hedge funds, a fund of funds investment, totaling $44,124 and $42,476 at June 30, 2014 and 2013 respectively, has a redemption period of 15 days. Commodity contracts, a fund of commodity contracts, at June 30, 2013, have a redemption period of 5 days.

Level 3 – Valuations based on inputs that are unobservable and significant to the overall fair value measurement. These are generally organization or individual investment manager generated inputs and are not observable market based inputs. Material assumptions and factors considered in the valuation may include, but are not limited to, operational activity of private equity holdings, reliance on third party estimates, share valuations, and appraisals. Level 3 investments include investments in hedge funds, bank loan funds, and perpetual trusts. The Organization based the fair value of hedge funds, a fund of funds investment of $56,141 and $50,424 at June 30, 2014 and 2013, respectively, and bank loan funds of $96,745 at June 30, 2014, on the fair value of the underlying reported net asset values of each fund held. The hedge fund and bank loan funds require a redemption period of 30-90 days.

The following tables present the categorization of the Organization's investments according to the valuation levels described above at June 30:

2014

Type of Investment	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$14,360	$19,250	$0	$33,610
Equity securities:				
Domestic equity	278,828	0	0	278,828
International equity - developed markets	181,178	0	0	181,178
International equity - emerging markets	57,644	0	0	57,644
Real estate equity	53,314	0	0	53,314
Fixed income:				
U.S. Treasury securities and obligations of U.S. Government agencies	24,598	40,895	0	65,493
Corporate bonds	185,645	61,526	0	247,171
Asset-backed securities	0	50,198	0	50,198
Collateralized mortgage obligations	0	36,810	0	36,810
Banking and finance	0	22,794	0	22,794
Bank loan funds	0	0	96,745	96,745
Hedge funds (multi-strategy)	0	44,124	56,141	100,265
Perpetual trust	0	0	8,174	8,174
Other	0	4,006	0	4,006
Other assets - swap assets	0	90	0	90
Total assets at fair value	$795,567	$279,693	$161,060	$1,236,320
Liabilities at Fair Value				
Other liabilities - swap liabilities	$0	$17,188	$0	$17,188

13. FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

2013

Type of Investment	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$6,012	$22,730	$0	$28,742
Equity securities:				
Domestic equity	238,645	0	0	238,645
International equity - developed markets	141,437	0	0	141,437
Real estate equity	49,673	0	0	49,673
Fixed income :				
U.S. Treasury securities and obligations of U.S. Government agencies	131,008	63,445	0	194,453
Corporate bonds	13,606	115,330	0	128,936
Asset-backed securities	0	69,121	0	69,121
Collateralized mortgage obligations	0	67,394	0	67,394
Banking and finance	0	40,198	0	40,198
Hedge funds (multi-strategy)	0	42,476	50,424	92,900
Commodities contracts	0	45,137	0	45,137
Perpetual trust	0	0	6,939	6,939
Other	0	4,108	0	4,108
Other assets - swap assets	0	120	0	120
Total assets at fair value	$580,381	$470,059	$57,363	$1,107,803
Liabilities at Fair Value				
Other liabilities - swap liabilities	$0	$18,179	$0	$18,179

The fair value of the Organizations interest rate swaps was determined based on the comparison of the present value of the fixed rate payments the Organization is committed to make to the present value of the variable rate payments the Organization is expected to receive from the swap counterparties. The variable payments were based on estimated future interest rates using current LIBOR based interest rate models.

The Organization’s use of Level 3 unobservable inputs at June 30, 2014 and 2013 accounted for 13.0% and 5.1%, respectively, of the total fair value of investments. The following tables summarize changes in Level 3 assets measured at fair value at June 30:

2014	Bank loan funds	Hedge funds	Perpetual trusts	Total
Balance at July 1, 2013	$0	$50,424	$6,939	$57,363
Change in net unrealized gains on investments	933	5,717	0	6,650
Increase in beneficial interest in perpetual trusts	0	0	1,235	1,235
Purchases	95,812	0	0	95,812
Balance at June 30, 2014	$96,745	$56,141	$8,174	$161,060

2013	Bank loan funds	Hedge funds	Perpetual trusts	Total
Balance at July 1, 2012	$0	$89,694	$0	$89,694
Realized investment earnings	0	1,569	0	1,569
Change in net unrealized gains (loss) on investments	0	4,603	0	4,603
Transfer from level 2	0	0	6,655	6,655
Increase in beneficial interest in perpetual trusts	0	0	284	284
Purchases	0	44,258	0	44,258
Sales	0	(89,700)	0	(89,700)
Balance at June 30, 2013	$0	$50,424	$6,939	$57,363

13. FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

The fair value of long-term debt, which was estimated at $609,062 and $529,870 at June 30, 2014 and 2013, respectively, was determined using the Organization's current borrowing rates for similar types of borrowing arrangements. The recorded value of long-term debt reported in the consolidated Statements of Financial Position at June 30, 2014 and 2013 was $601,354 and $546,855, respectively. The excess of fair value over recorded value for long-term debt at June 30, 2014 indicates market interest rates for debt of similar term and quality were lower than the weighted average interest rates of the Organization's outstanding debt. The excess of recorded value over fair value for long-term debt at June 30, 2013 indicates market interest rates for debt of similar term and quality were higher than the weighted average interest rates of the Organization's outstanding debt

14. PLEDGES RECEIVABLE

Included in assets restricted by donors in the Consolidated Statements of Financial Position are the following pledges receivable at June 30:

	2014	2013
Pledges receivable within next fiscal year	$3,848	$3,112
Pledges receivable in future periods beyond next fiscal year	6,871	2,538
Total pledges receivable before unamortized discount and allowance for uncollectible pledges	10,719	5,650
Less: unamortized discount	(282)	(258)
Less: allowance for uncollectible pledges	(343)	(216)
Net pledges receivable	$10,094	$5,176
Amounts due in:		
Less than one year	$3,848	$3,112
One to five years	6,198	2,064
More than five years	673	474
Total	$10,719	$5,650

Cash payments received applicable to prior pledges were $3,184 and $2,002 for the years ended June 30, 2014 and 2013, respectively. Pledges written off as uncollectible were $5 and $1 for the years ended June 30, 2014 and 2013, respectively. The Organization's policy regarding the recording of pledges receivable in the consolidated financial statements requires pledges to be in writing, signed by the donor, and to indicate the specific amount of the pledge and expected timing the pledge payment will be received. The Organization does not record pledges based on bequests or life insurance. The Organization's historical write off of pledges receivable has been in the 1-5% range. The allowance for uncollectible pledges as of June 30, 2014 and 2013 were $343 (4%) and $216 (4%), respectively.

15. RECENT ACCOUNTING PRONOUNCEMENTS

In July 2011, the FASB issued ASU 2011-07, "Health Care Entities (Topic 954)*: Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*." This ASU requires an HCO to change the presentation of their statement of operations by reclassifying the provision for bad debts associated with patient service revenue from an operating expense to a deduction from patient service revenue (net of contractual allowances and discounts). Additionally, an HCO is required to provide enhanced disclosure about their policies for recognizing revenue and assessing bad debts. The ASU also requires disclosures of patient service revenue (net of contractual allowances and discounts) as well as qualitative and quantitative information about changes in the allowance for doubtful accounts. This guidance is effective for annual reporting periods ending after December 15, 2012. The income statement presentation change was required to be adopted on a retrospective basis but the enhanced disclosures were permitted to be adopted either retrospectively or prospectively. On July 1, 2012, the Organization adopted this guidance and included the enhanced disclosures on a prospective basis in Note 1.

KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

Board of Trustees
Lehigh Valley Health Network:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the consolidated financial statements of Lehigh Valley Health Network and Component Entities, which comprise the consolidated statement of financial position as of June 30, 2014, and the related consolidated statements of operations, changes in net assets, and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated September 22, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered Lehigh Valley Health Network and Component Entities' internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of Lehigh Valley Health Network and Component Entities' internal control. Accordingly, we do not express an opinion on the effectiveness of Lehigh Valley Health Network and Component Entities' internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Lehigh Valley Health Network and Component Entities' consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Lehigh Valley Health Network and Component Entities' internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Lehigh Valley Health Network and Component Entities' internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Philadelphia, Pennsylvania
September 22, 2014

KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report on Compliance for Each Major Program; Report on Internal Control Over Compliance; and Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*

Board of Trustees
Lehigh Valley Health Network:

Report on Compliance for Each Major Federal Program

We have audited Lehigh Valley Health Network and Component Entities' compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Lehigh Valley Health Network and Component Entities' major federal programs for the year ended June 30, 2014. Lehigh Valley Health Network and Component Entities' major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of Lehigh Valley Health Network and Component Entities' major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Lehigh Valley Health Network and Component Entities' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of Lehigh Valley Health Network and Component Entities' compliance.

Opinion on Each Major Federal Program

In our opinion, Lehigh Valley Health Network and Component Entities complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2014.

Report on Internal Control Over Compliance

Management of the Lehigh Valley Health Network and Component Entities is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Lehigh Valley Health Network and Component Entities' internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Lehigh Valley Health Network and Component Entities' internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Report on Consolidated Schedule of Expenditures of Federal Awards Required by OMB Circular A- 133

We have audited the consolidated financial statements of Lehigh Valley Health Network and Component Entities as of and for the year ended June 30, 2014, and have issued our report thereon dated September 22, 2014, which contained an unmodified opinion on those consolidated financial statements. Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidated schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidated schedule of expenditure of federal awards is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

Philadelphia, Pennsylvania
November 5, 2014

LEHIGH VALLEY HEALTH NETWORK AND COMPONENT ENTITIES

CONSOLIDATED SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014

Program Title / Grant Name	Federal CFDA Number	Direct Funding Award No.	Pass-Through Entity Identifying No.	Federal Expenditures
RESEARCH AND DEVELOPMENT CLUSTER:				
U.S. Department of Health and Human Services:				
Cancer Treatment Research				
Pass-through from American College of Radiology				
Radiation Therapy Oncology Group	93.395		N/A	$ 100
Pass-through from Brigham and Women's Hospital, Inc.				
ACOSOG Competing Renewal	93.395		7U10CA076001	2,100
Alliance for Clinical Trials in Oncology	93.395		N/A	2,425
Pass-through from Childrens Hospital of Philadelphia				
Children's Oncology Group Chair Grant -PCR (Per Case Reimbursement)	93.395		FP00013744_SUB77_01	26,150
Children's Oncology Group Chair Grant -PCR (Per Case Reimbursement)	93.395		FP00015221_SUB289_01	5,850
Children's Oncology Group Chair Grant -WI (Work Intensity)	93.395		FP00013013_SUB449_01	5,400
Pass-through from H. Lee Moffitt Cancer Center and Research Institute Hospital Inc.				
Gynecologic Oncology Group Clinical Trials	93.395		63191	4,250
NRG Oncology	93.395		63191	1,200
Pass-through from Pennsylvania State University				
Eastern Cooperative Oncology Group	93.395		N/A	23,550
Pass-through from Mayo Clinic Rochester				
North Central Cancer Treatment Group (Ancillary & Tissue Credits)	93.395		3U01CA025224-33	12,742
Cancer Control				
Pass-through from Mayo Clinic Rochester				
North Central Cancer Treatment Group (Cancer Control Payments)	93.399		3U01CA025224-33	27,750
Pass-through from National Surgical Adjuvant Breast and Bowel Project Foundation, Inc.				
Community Clinical Oncology Program	93.399		TFED41S2EXT-064	10,000
Trans-HIH Recovery Act Research Support				
Pass-through from EMMES Corporation				
ARRA-Platelet-Oriented Inhibition in New TIA	93.701		3310-101	15,600
Pass-through from The Feinstein Institute for Medical Research				
ARRA-Recovery After Initial Schizophrenia Episode (RAISE)	93.701		LEH01	2,543
Non-ARRA Recovery After Initial Schizophrenia Episode (RAISE)	93.LEH01-NON-ARRA		LEH01-NON-ARRA	9,635
Non-ARRA Recovery After Initial Schizophrenia Episode (RAISE)	93.HHSN-271-2009-00019-C		HHSN-271-2009-00019-C	464
Cardiovascular Disease Research				
Pass-through from New England Research Institutes Inc.				
Phosphodiesterase Type 5 Inhibition with Tadalafil Changes Outcomes in Heart Failure (PITCH - HF)	93.837		N/A	2,500
Extramural Research Programs in the Neurosciences and Neurological Disorders				
Pass-through from Regents of the University of Minnesota				
Antihypertensive Treatment of Acute Cerebral Hemorrhage ATACH-II	93.853		N000936914	1,332
Pass-through from Rutgers, The State University of New Jersey				
Carotid Revascularization Endarterectomy vs Stenting Trial	93.853		99-705	6,925
Pass-through from Trustees of Columbia University, New York				
Warfarin vs. Aspirin in Reduced Cardiac Ejection Fraction	93.853		10 (GG004432)	1,000
Child Health and Human Development Extramural Research				
Pass-through from Trustees of Columbia University, New York				
Antenatal Late Preterm Steroids	93.865		4(GG001346)	692
A Randomized Trial to Prevent Congenital Cytomegalovirus Infections	93.865		4(GG001346)	43,763
An Observational Study of Hepatitis C Virus in Pregnancy	93.865		4(GG001346)	8,854
TOTAL RESEARCH AND DEVELOPMENT CLUSTER				**$ 214,825**

LEHIGH VALLEY HEALTH NETWORK AND COMPONENT ENTITIES

CONSOLIDATED SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014

Program Title / Grant Name	Federal CFDA Number	Direct Funding Award No.	Pass-Through Entity Identifying No.		Federal Expenditures
DIRECT FUNDING:					
U.S. Department of Health and Human Services:					
Research on Healthcare Costs, Quality and Outcomes - AHRQ Data Flow & Clinical Outcomes in Perinatal Continuum of Care System	93.226	5R18HS018649-02		$	192,330
Research on Healthcare Costs, Quality and Outcomes - AHRQ Data Flow & Clinical Outcomes in Perinatal Continuum of Care System	93.226	5R18HS018649-03			256,225
NEPQR Grant - Nurse Education, Practice, Quality, and Retention - Interprofessional Collaborative Practice	93.359	5 UD7HP25050-02-00			608,036
Grant to Provide Outpatient EIS with Respect to HIV Diseases - Ryan White Part C Outpatient EIS Program	93.918	6 H76HA00078-22-02			557,902
Grant to Provide Outpatient EIS with Respect to HIV Diseases - Ryan White Part C Outpatient EIS Program	93.918	6 H76HA00078-23-00			159,306
Ryan White HIV/AIDS Dental Reimbursement and Community Based Dental Partnership Grants - Dental Reimbursement Program	93.924	1 T22HA26428-01-00			21,787
Total U.S. Department Of Health And Human Services				**$**	**1,795,586**
TOTAL DIRECT FUNDING				**$**	**1,795,586**
OTHER PASS-THROUGH FUNDS:					
U.S. Department of Housing and Urban Development:					
Housing Opportunities for Persons with Aids					
Pass-through from AIDSNET					
HOPWA Housing Services	14.241		13-001	$	170,018
U.S. Department of Health and Human Services:					
Maternal and Child Health Federal Consolidated Programs					
Pass-through from Children's Hospital of Philadelphia					
Hemophilia Treatment Centers (SPRANS)	93.110		3209610514		4,978
Disabilities Prevention					
CDC through American Thrombosis and Hemstasis Network					
Pass-through from Children's Hospital of Philadelphia					
Public Health Surveillance for the Prevention of Complications of Bleeding and Clotting Disorders	93.184		823258-09-02		10,609
ARRA - State Grants to Promote Health Information Technology					
Pass-through from Commonwealth of Pennsylvania Department of Health					
ARRA- PEDS Community Shared Services Health Information Exchange	93.719		4100060827		531,879
National Bioterrorism Hospital Preparedness Program					
Pass-through from Commonwealth of Pennsylvania Department of Health					
Hospital Preparedness Program-LVH	93.889		4100062645		72,570
Hospital Preparedness Program-LVHM	93.889		4100062646		32,223
Maternal and Child Health Services Block Grant to the States					
Pass-through from Commonwealth of Pennsylvania Department of Health					
Cystic Fibrosis	93.994		4100058884-SAF3		10,000
HIV Care Formula Grants					
Pass-through from AIDSNET					
Ryan White Care Act Title II Funds for Case Mgmt	93.917		13-001		300,661
Ryan White Care Act Title II Funds for Patient Care	93.917		13-001		19,763
Total U.S. Department of Health and Human Services				**$**	**982,683**
TOTAL OTHER PASS-THROUGH FUNDS				**$**	**1,152,701**
TOTAL FEDERAL AWARDS				**$**	**3,163,112**

(Concluded)

LEHIGH VALLEY HEALTH NETWORK AND COMPONENT ENTITIES

NOTES TO THE CONSOLIDATED SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS FOR THE YEAR ENDED JUNE 30, 2014

---

1. BASIS OF PRESENTATION

The accompanying Consolidated Schedule of Expenditures of Federal Awards (the "Schedule") presents the activity of all federal financial assistance programs administered by Lehigh Valley Health Network and Component Entities for the year ended June 30, 2014. The information in this Schedule is presented in accordance with the requirements of the Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations.* Expenditures are reported on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

2. FEDERAL CFDA NUMBERS

The Catalog of Federal Domestic Assistance ("CFDA") numbers listed on the Schedule were obtained from the grant/contract agreements. Program titles preceded by "ARRA" represent programs administered under the American Recovery and Reinvestment Act.

3. SUBRECIPIENTS EXPENDITURES

Of the federal expenditures presented in the Schedule, Lehigh Valley Health Network and Component Entities provided federal awards of $302,071 for CFDA#93.226, Research on Healthcare Costs, Quality and Outcomes - AHRQ-Data Flow & Clinical Outcomes in Perinatal Continuum of Care System, to a subrecipient, Lehigh University in the year ended June 30, 2014.

******

Section I - Summary of Auditors' Results

Consolidated Financial Statements

The independent auditors' report on the consolidated financial statements expressed an unmodified opinion.

Internal control over financial reporting:

• Material weakness(es) identified?	______ yes	__X__ no
• Significant deficiency(ies) identified?	______ yes	__X__ none reported
Noncompliance material to consolidated financial statements noted?	______ yes	__X__ no

Federal Awards

Internal control over major programs:

• Material weakness(es) identified?	______ yes	__X__ no
• Significant deficiency(ies) identified?	______ yes	__X__ none reported

The independent auditors' report on compliance with requirements applicable to major federal award programs expressed an unmodified opinion.

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133?	______ yes	__X__ no

Identification of Major Programs:

CFDA Number(s)	Name of Federal Program	Grant Name
93.719	ARRA - State Grants to Promote Health Information Technology	ARRA - PEDS Community Shares Services Health Information Exchange
93.917	HIV Care Formula Grants	Ryan White Care Act Title II Funds for Case Mgmt & Patient Care

Dollar threshold used to distinguish between Type A and Type B programs:	$300,000	
Auditee qualified as low-risk auditee?	X yes	_____ no

Section II — Financial Statement Findings

No matters were reported.

Section III — Federal Award Findings and Questioned Costs

No matters were reported.