

CareAlliance Health Services

(d/b/a Roper St. Francis Healthcare)

Consolidated Financial Statements as of and for the
Years Ended December 31, 2014 and 2013,
Federal Awards Supplemental Information for the
Year Ended December 31, 2014, and
Independent Auditors' Reports

CAREALLIANCE HEALTH SERVICES
(d/b/a Roper St. Francis Healthcare)

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
CareAlliance Health Services
(d/b/a Roper St. Francis Healthcare):

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of CareAlliance Health Services (d/b/a Roper St. Francis Healthcare) ("CareAlliance"), which comprise the consolidated balance sheets as of December 31, 2014 and 2013, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; 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 audits. We conducted our audits 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 auditor's 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 CareAlliance'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 CareAlliance'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 audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of CareAlliance as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Federal Awards Supplemental Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedule of expenditures of federal awards as required by Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is presented for the purpose of additional analysis and is not a required part of the consolidated financial statements.

The schedule of expenditures of federal awards is the responsibility of CareAlliance's management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. Such information has been subjected to the auditing procedures applied in our audits 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 schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the consolidated financial statements taken as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated May 26, 2015 on our consideration of CareAlliance's 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 the 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 CareAlliance's internal control over financial reporting and compliance.

Deloitte + Touche LLP

May 26, 2015 (except for the accompanying Federal Awards Supplemental Information, for which the date is June 17, 2015).

CAREALLIANCE HEALTH SERVICES
(d/b/a Roper St. Francis Healthcare)

CONSOLIDATED BALANCE SHEETS
AS OF DECEMBER 31, 2014 AND 2013

	2014	2013
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 54,745,000	\$ 38,459,000
Patient accounts receivable—less allowances of \$66,514,000 and \$77,146,000 for uncollectible accounts in 2014 and 2013, respectively	107,091,000	103,828,000
Other receivables	16,967,000	12,337,000
Short-term investments	21,657,000	16,586,000
Inventories	11,783,000	10,927,000
Prepaid expenses and other current assets	<u>13,028,000</u>	<u>8,698,000</u>
Total current assets	225,271,000	190,835,000
LONG-TERM INVESTMENTS	153,482,000	169,703,000
ASSETS LIMITED AS TO USE	11,980,000	32,652,000
PROPERTY AND EQUIPMENT—Net	492,460,000	476,531,000
OTHER ASSETS	<u>46,354,000</u>	<u>44,425,000</u>
TOTAL	<u>\$ 929,547,000</u>	<u>\$ 914,146,000</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Current portion of long-term debt	\$ 19,501,000	\$ 26,238,000
Accounts payable	64,647,000	41,233,000
Accrued expenses	72,720,000	71,223,000
Accrued contribution payable to members	<u>14,800,000</u>	<u>31,872,000</u>
Total current liabilities	171,668,000	170,566,000
LONG-TERM DEBT—Net of current portion	316,470,000	312,171,000
OTHER LIABILITIES	<u>71,019,000</u>	<u>58,487,000</u>
Total liabilities	<u>559,157,000</u>	<u>541,224,000</u>
COMMITMENTS AND CONTINGENCIES (Notes 6, 9, 10, and 16)		
NET ASSETS:		
Unrestricted:		
CareAlliance Health Services	349,564,000	355,277,000
Noncontrolling interests in Lowcountry Surgery Center, LLC	<u>210,000</u>	<u>199,000</u>
Total unrestricted net assets	349,774,000	355,476,000
Temporarily restricted	12,641,000	10,149,000
Permanently restricted	<u>7,975,000</u>	<u>7,297,000</u>
Total net assets	<u>370,390,000</u>	<u>372,922,000</u>
TOTAL	<u>\$ 929,547,000</u>	<u>\$ 914,146,000</u>

See notes to consolidated financial statements.

CAREALLIANCE HEALTH SERVICES
(d/b/a Roper St. Francis Healthcare)

CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

	2014	2013
UNRESTRICTED REVENUES:		
Patient service revenue (net of contractual allowances and discounts)	\$ 812,558,000	\$ 774,010,000
Provision for bad debts	<u>(40,417,000)</u>	<u>(42,281,000)</u>
Net patient service revenue	772,141,000	731,729,000
Other revenue	<u>21,594,000</u>	<u>23,828,000</u>
Total unrestricted revenues	<u>793,735,000</u>	<u>755,557,000</u>
EXPENSES:		
Salaries and employee benefits	406,839,000	393,332,000
Supplies	135,812,000	132,974,000
Purchased services	79,154,000	73,148,000
Other expenses	89,269,000	79,018,000
Depreciation and amortization	53,674,000	49,815,000
Interest	<u>9,999,000</u>	<u>10,992,000</u>
Total expenses	<u>774,747,000</u>	<u>739,279,000</u>
OPERATING INCOME	18,988,000	16,278,000
NONOPERATING GAINS (LOSSES):		
Investment gains—net	7,969,000	27,869,000
Change in fair value of interest rate swaps	(12,328,000)	15,693,000
Loss on extinguishment of debt	(6,284,000)	(21,000)
Other—net	<u>(1,765,000)</u>	<u>(3,592,000)</u>
EXCESS OF REVENUES OVER EXPENSES	<u>6,580,000</u>	<u>56,227,000</u>
INCREASE IN UNRESTRICTED NET ASSETS BEFORE MEMBER TRANSACTIONS	<u>\$ 6,580,000</u>	<u>\$ 56,227,000</u>

See notes to consolidated financial statements.

CAREALLIANCE HEALTH SERVICES
(d/b/a Roper St. Francis Healthcare)

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

	2014	2013
UNRESTRICTED NET ASSETS:		
Increase in unrestricted net assets before member transactions	\$ 6,580,000	\$ 56,227,000
Contribution accrued to members	(14,800,000)	(31,872,000)
Contribution from member for acquisitions of property and equipment	2,382,000	1,185,000
Distributions to Lowcountry Surgery Center, LLC members	(30,000)	
Release of restricted funds for capital expenditures	171,000	857,000
Roper St. Francis Foundation transfers	(5,000)	(1,000)
	<u>(5,702,000)</u>	<u>26,396,000</u>
(Decrease) increase in unrestricted net assets		
TEMPORARILY RESTRICTED NET ASSETS:		
Contributions	6,859,000	6,559,000
Investment gains—net	465,000	1,675,000
Net assets released from restrictions	(4,596,000)	(3,493,000)
Release of restricted funds for capital expenditures	(171,000)	(857,000)
Roper St. Francis Foundation transfers	(65,000)	(582,000)
	<u>2,492,000</u>	<u>3,302,000</u>
Increase in temporarily restricted net assets		
PERMANENTLY RESTRICTED NET ASSETS:		
Contributions	614,000	503,000
Investment (losses) gains—net	(6,000)	51,000
Roper St. Francis Foundation transfers	70,000	583,000
	<u>678,000</u>	<u>1,137,000</u>
Increase in permanently restricted net assets		
(DECREASE) INCREASE IN NET ASSETS	(2,532,000)	30,835,000
NET ASSETS:		
Beginning of year	<u>372,922,000</u>	<u>342,087,000</u>
End of year	<u>\$ 370,390,000</u>	<u>\$ 372,922,000</u>

See notes to consolidated financial statements.

CAREALLIANCE HEALTH SERVICES
(d/b/a Roper St. Francis Healthcare)

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
(Decrease) increase in net assets	\$ (2,532,000)	\$ 30,835,000
Adjustments to reconcile (decrease) increase in net assets to net cash flows from operating activities:		
Depreciation	53,206,000	49,288,000
Amortization	468,000	527,000
Amortization of bond discount and premium—net	(159,000)	(378,000)
Contribution accrued to members	14,800,000	31,872,000
Contributions from member and Foundation for acquisitions of property and equipment	(2,382,000)	(1,303,000)
Provision for uncollectible accounts	40,417,000	42,281,000
Realized and unrealized losses (gains) on investments and interest rate swap—net	5,904,000	(41,788,000)
Loss on property and equipment disposals	142,000	1,891,000
Loss on extinguishment of debt	6,284,000	21,000
Changes in operating assets and liabilities:		
Accounts receivable	(49,151,000)	(37,635,000)
Inventories	(856,000)	(11,000)
Prepaid expenses and other current assets	(4,330,000)	(1,065,000)
Accounts payable, accrued expenses, and other liabilities	24,721,000	(7,029,000)
Net cash flows from operating activities	<u>86,532,000</u>	<u>67,506,000</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments and assets limited as to use	(67,375,000)	(70,470,000)
Sales of investments and assets limited as to use	105,001,000	70,140,000
Purchases of property and equipment	(43,476,000)	(19,684,000)
Cash proceeds from sales of property and equipment	1,584,000	1,043,000
Net cash flows from investing activities	<u>(4,266,000)</u>	<u>(18,971,000)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of long-term debt	209,400,000	
Principal payments on long-term debt and capital lease obligations	(235,325,000)	(20,861,000)
Debt issuance costs	(1,996,000)	(253,000)
Contribution paid to members	(31,872,000)	(23,424,000)
Contributions from member and others for acquisitions of property and equipment	2,382,000	1,303,000
Other	(8,569,000)	(1,870,000)
Net cash flows from financing activities	<u>(65,980,000)</u>	<u>(45,105,000)</u>

(Continued)

CAREALLIANCE HEALTH SERVICES
(d/b/a Roper St. Francis Healthcare)

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

	2014	2013
NET CHANGE IN CASH AND CASH EQUIVALENTS	\$ 16,286,000	\$ 3,430,000
CASH AND CASH EQUIVALENTS—Beginning of year	<u>38,459,000</u>	<u>35,029,000</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 54,745,000</u>	<u>\$ 38,459,000</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION—Cash paid for interest	<u>\$ 9,338,000</u>	<u>\$ 10,718,000</u>
SUPPLEMENTAL DISCLOSURES OF NONCASH FINANCING AND INVESTING ACTIVITIES:		
Capital additions financed through accounts payable	<u>\$ 3,406,000</u>	<u>\$ 1,543,000</u>
Capital lease obligations incurred	<u>\$ 24,547,000</u>	<u>\$ 5,613,000</u>
Deemed ownership obligations incurred (Note 6)	<u>\$ 765,000</u>	<u>\$ 2,825,000</u>
See notes to consolidated financial statements.		(Concluded)

CAREALLIANCE HEALTH SERVICES

(d/b/a Roper St. Francis Healthcare)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

1. ORGANIZATION

CareAlliance Health Services (d/b/a Roper St. Francis Healthcare (RSFH)) (“CareAlliance”) is a charitable health care delivery system based in Charleston, South Carolina. CareAlliance provides services at more than 90 sites in five counties. These facilities include three acute care hospitals with 657 licensed beds; one specialty hospital; 15 centers for outpatient services, including surgery, diagnostics, and rehabilitation (physical, occupational, and speech therapies); three industrial medicine sites; five emergency rooms; and two urgent care centers. CareAlliance employs approximately 200 physicians, with a large primary care base and a variety of specialties.

CareAlliance was formed effective August 1, 1998, through the execution of an affiliation agreement between the following founding members (the “Founding Members”), with each member’s respective initial membership percentage:

The Medical Society of South Carolina (MSSC)	63 %
Bon-Secours Health System, Inc. (BSHSI)	27
Carolinas HealthCare System (CHS)	10

RSFH is governed by a thirteen (13)-member board of directors (the “Board of Directors”) appointed by the Founding Members. Subject to certain Nominating Committee approvals, six (6) directors are appointed by each of MSSC and BSHSI and one (1) director is appointed by CHS. It is the Founding Members’ intent that the members of RSFH’s Board of Directors are appointed to such positions because they have a willingness to serve the needs of the system as a whole and not the needs of any individual Founding Member.

The by-laws of RSFH specify certain qualifications of the thirteen (13)-member Board of Directors. At least nine (9) directors must have their primary residence in a community served by the system. Five (5) directors must be physicians actively engaged in the full-time practice of medicine. Five (5) of the directors are appointed to the Board of Directors by virtue of positions held within BSHSI, MSSC, and CHS (“Ex-officio Directors”). Each of the five (5) Ex-officio Directors serves as a director of the corporation for so long as such person holds his or her respective elected or appointed office in their respective Founding Member organization. Directors serve three-year terms and are limited to three consecutive terms. After an absence of at least one (1) year, Ex-officio Directors are again eligible for appointment to the Board of Directors for two consecutive complete terms.

CareAlliance is the sole corporate member and, through its by-laws, has the power to control the financial and business affairs of the following organizations:

- Roper Hospital, Inc. (“Roper Hospital”)
- Bon Secours—St. Francis Xavier Hospital, Inc. (“St. Francis”)
- Roper St. Francis Mount Pleasant Hospital, Inc. (“Mount Pleasant”)
- Roper St. Francis Foundation (“Foundation”)
- Roper St. Francis Physicians Network (“Physician Partners”)

- Roper St. Francis Hospital-Berkeley, Inc. (“Berkeley Hospital”)
- Roper St. Francis Health Alliance (“Health Alliance”)

CareAlliance, Roper Hospital, St. Francis, Mount Pleasant, Foundation, and the Physician Partners are not-for-profit organizations as described in Section 501(c)(3) of the Internal Revenue Code and are exempt from federal and state income taxes.

CareAlliance owns a 50.5% controlling interest in the Lowcountry Surgery Center, LLC (d/b/a Roper St. Francis Eye Surgery Center) (LSC). The remaining 49.5% noncontrolling interests are held by participating physicians. Operations at the LSC began in 2012.

Neither Berkeley Hospital nor Health Alliance had commenced operations as of December 31, 2014.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation—The consolidated financial statements have been prepared under the accrual basis in accordance with accounting principles generally accepted in the United States of America (GAAP) as set forth in the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC).

Principles of Consolidation—The consolidated financial statements of CareAlliance include the accounts of CareAlliance, Roper Hospital (and subsidiaries), St. Francis (and subsidiaries), Mount Pleasant, the Foundation, Physician Partners, and LSC.

Use of Estimates—The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the 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. Significant estimates and assumptions are used for, but not limited to, recognition of net patient service revenue; valuation of accounts receivable, including contractual allowances and provisions for doubtful accounts; liabilities for losses and expenses related to employee health care, workers’ compensation, and professional and general liability risks; valuation of investments and derivative instruments; depreciation of property and equipment; and estimated third-party settlements. Future events and their effects cannot be predicted with certainty; accordingly, management’s accounting estimates require the exercise of judgment. The accounting estimates used in the preparation of the accompanying consolidated financial statements will change as new events occur, as more experience is acquired, as additional information is obtained and as the operating environment changes. Management regularly evaluates the accounting policies and estimates it uses. In general, management relies on historical experience and on other assumptions believed to be reasonable under the circumstances, and may employ outside experts to assist in the evaluation, as considered necessary. Although management believes all adjustments considered necessary for fair presentation have been included, actual results may vary from those estimates.

Cash and Cash Equivalents—For purposes of the consolidated statements of cash flows, CareAlliance considers all highly liquid investments with an original maturity of three months or less at the time of purchase to be cash equivalents, excluding amounts included in investments and assets limited as to use. At December 31, 2013, cash and cash equivalents include a compensating balance of approximately \$4,487,000, held on deposit with a bank to secure a portion of CareAlliance’s other long-term debt. There were no such compensating balances as of December 31, 2014. CareAlliance’s deposits exceeded federally insured limits at December 31, 2014 and 2013.

Receivables—Receivables are reported at the net realizable amounts due from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Substantially all CareAlliance’s accounts receivable are related to providing healthcare services to patients. Collection of these accounts receivable is CareAlliance’s primary source of cash and is critical to operating performance. CareAlliance’s primary collection risks relate to uninsured patients and outstanding patient balances for which the primary or secondary insurance has paid some but not all of the outstanding balance, with the remaining outstanding balance (generally deductibles and co-payments) owed by the patient.

The process of estimating the allowance for doubtful accounts requires CareAlliance to estimate the collectability of patient accounts receivable, which is primarily based on our collection history, adjusted for expected recoveries. CareAlliance collects substantially all its of third-party insured receivables, which include receivables from governmental agencies. Collections are impacted by the economic ability of patients to pay and the effectiveness of collection efforts. Significant changes in payor mix, business office operations, economic conditions or trends in federal and state governmental healthcare coverage could affect the collection of accounts receivable. CareAlliance also continually reviews overall reserve adequacy by monitoring historical cash collections as a percentage of trailing net revenue, as well as by analyzing current period gross revenue and admissions by payor classification, aged accounts receivable by payor, and days revenue outstanding.

The allowance for doubtful accounts was \$66,514,000 and \$77,146,000 as of December 31, 2014 and 2013, respectively. The decrease in the allowance for doubtful accounts between 2013 and 2014 is primarily a result of improvements in bad debt recoveries, improvements in the qualification of Medicaid patients, and a reduction in charge rates.

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

Property and Equipment—Property and equipment is stated at cost or, in the case of donated property, at fair market value at the time of donation. Property and equipment held for sale is stated at the lower of cost or fair value. Assets are depreciated using the straight-line method over their estimated useful lives. Expenditures that materially increase values, change capacities, or extend useful lives are capitalized. Routine maintenance, repairs, and replacements are charged to expense when incurred.

CareAlliance capitalizes purchased software that is ready for service and software development costs incurred on significant projects starting from the time that the preliminary project stage is completed and management commits to funding a project until the project is substantially complete and the software is ready for its intended use. Capitalized costs include direct material and service costs and payroll and payroll-related costs. Training and maintenance costs related to software development are expensed as incurred. Capitalized software costs are amortized using the straight-line method over the estimated useful life of the underlying system.

The following is a summary of the estimated useful lives used in computing depreciation:

Buildings	40 years
Building improvements	5–25 years
Equipment and software	3–20 years

Long-Term Investments and Assets Limited as to Use—Long-term investments, including investments classified as assets limited as to use, consist of debt and equity securities held in common collective trust funds, other debt and equity securities and money market funds, and investments in limited partnerships. Investments in common collective trust funds, equity securities with readily determinable fair values, and all investments in debt securities and money market funds are classified as trading securities and measured at fair value at the balance sheet date. Management determined that the trading security category is appropriate based on CareAlliance’s investment strategy and policies. Investment managers may execute individual purchases and sales of investments without prior approval from CareAlliance as long as they comply with CareAlliance’s investment strategy and policies. Investment gains or losses on trading securities are included in the excess of revenues over expenses, unless the income or loss is restricted by donor or laws.

CareAlliance has elected the fair value option to account for its investments in limited partnerships, which are not readily marketable and are less liquid than CareAlliance’s other investments. Management determined the fair value option is appropriate based on CareAlliance’s investment strategy and policies with respect to investments in limited partnerships. Management estimates the fair value of its investments in limited partnerships based on information provided by the fund managers. Investment income or loss from investments in limited partnerships is included in the excess of revenues over expenses. Assets limited as to use primarily include assets held by trustees under indenture agreements and designated net assets set aside by the Board of Directors for future capital improvements, over which the Board of Directors retains control and may at its discretion subsequently use for other purposes.

Short-Term Investments—Short-term investments consist of marketable debt securities, which are intended to be used to meet current liabilities, and, therefore, are reported as current assets in the consolidated balance sheets. Gains and losses on short-term investments are included in the excess of revenues over expenses.

Other Assets—Other assets consist primarily of deferred financing costs incurred during the issuance of revenue bonds, temporarily and permanently restricted assets of the Foundation, and goodwill. Goodwill represents acquisition costs in excess of the fair value of the net identifiable tangible and intangible assets of businesses purchased. Goodwill was \$16,432,000 and \$16,432,000 as of December 31, 2014 and 2013, respectively. CareAlliance subjects goodwill to an impairment evaluation on an annual basis, or more frequently if events or circumstances indicate that assets might be impaired. There was no impairment of goodwill as of or during the years ended December 31, 2014 and 2013.

Contribution Accrued to Members—In accordance with its by-laws and the terms of the affiliation agreement between its Founding Members, CareAlliance is required to make annual cash contributions to its members, in accordance with their respective membership interest percentages, equal to 50% of System Free Cash Flow as defined in CareAlliance’s by-laws. The determination of System Free Cash Flow and the timing of related cash contributions have been adjusted from time to time by mutual agreement of CareAlliance and its Founding Members. The Founding Members have also agreed to limit CareAlliance’s total annual cash contribution to the Founding Members to \$14.8 million beginning with the contribution amount for the year ended December 31, 2014. MSSC has the right to remove the limit on the annual distribution, but must give CareAlliance at least a three-year notice prior to removing the limit on the annual distribution. As of December 31, 2014 and 2013, CareAlliance has recorded liabilities for the contribution payable to members of \$14,800,000 and \$31,872,000, respectively, related to the System Free Cash Flow.

CareAlliance’s Founding Members have also entered into a liquidity replenishment agreement whereby the Founding Members agreed to contribute cash to CareAlliance if days cash on hand (as defined in the

agreement) is below 75 days as of any biannual measurement date (measured as of June 30 and December 31) or if below 85 days as of any biannual measurement date and 90 days thereafter. In either event, the Founding Members agree to contribute cash to CareAlliance so that it maintains a minimum of 85 days cash on hand.

Derivative Financial Instruments—CareAlliance uses derivative financial instruments primarily to manage its exposure to movements in interest rates. Interest rate swaps are contractual agreements between two parties for the exchange of interest payments on a notional principal amount at agreed-upon fixed or floating rates, for defined periods. Interest rate swaps are stated at fair value in the accompanying consolidated balance sheets, with the change in fair value recorded as realized gains (losses) and included in nonoperating gains (losses) in the accompanying consolidated statements of operations. CareAlliance does not enter into derivative financial instruments for trading purposes.

Donor-Restricted Gifts—Unconditional promises to give cash and other assets to CareAlliance are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. 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 as other revenue in the consolidated statements of operations. Donor-restricted contributions whose restrictions are met within the same year are reported as unrestricted support and are included in other revenue in the consolidated statements of operations.

Net Assets—CareAlliance has three net asset groups as follows:

Unrestricted—Unrestricted net assets consist of all resources of CareAlliance that have no donor-imposed restrictions. Certain of these resources have been designated by CareAlliance’s Board of Directors to serve certain long-term program objectives of CareAlliance, or have been limited by contractual agreements with outside parties. These assets are included with assets limited as to use.

Temporarily Restricted—Temporarily restricted net assets consist of contributions and related investment income for which CareAlliance’s use is limited through externally imposed stipulations as to a specific time or purpose.

Permanently Restricted—Permanently restricted net assets consist of contributions and related investment income restricted by donors to be maintained by CareAlliance in perpetuity. The portion of a donor-restricted endowment fund that is classified as permanently restricted is not reduced by losses on investments in the fund, except to the extent required by the donor, including losses related to specific investments that the donor requires the organization to hold. Investment income from donor-restricted endowment funds that is not permanently restricted is classified as temporarily restricted until appropriated for expenditure by CareAlliance. Losses on the investments of donor-restricted endowment funds are recorded as a reduction of temporarily restricted net assets to the extent that donor-imposed temporary restrictions on net appreciation of the fund have not been met before the loss occurs. Any remaining losses reduce unrestricted net assets and are excluded from the excess of revenues over expenses. Gains that restore the fair value of the assets of the endowment fund to the required level are classified as increases in unrestricted net assets and are excluded from the excess of revenues over expenses.

Net Patient Service Revenue—Net patient service revenue is reported at the estimated net realizable amounts due from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive

adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. For uninsured patients that do not qualify for charity care, CareAlliance recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated or provided by policy). On the basis of historical experience, a significant portion of CareAlliance's uninsured patients will be unable or unwilling to pay for the services provided. Thus, CareAlliance records a significant provision for bad debts related to uninsured patients in the period the services are provided.

Electronic Health Records (EHR) Incentives—The American Recovery and Reinvestment Act of 2009 established incentive payments under the Medicare and Medicaid programs for certain professionals and hospitals that meaningfully use certified EHR technology. The EHR incentive payments to hospitals include a base amount, plus a discharge-related portion, which is calculated by the Centers for Medicare and Medicaid Services (CMS) based on the hospital's most recently filed cost report and are subject to adjustment upon settlement of the cost report for the hospital's fiscal year that begins after the beginning of the payment year. A hospital may receive incentive payments for up to four years, provided that it successfully demonstrates meaningful use for each applicable EHR reporting period. CareAlliance recognizes revenue for EHR incentive payments in the period in which it is reasonably assured that it will comply with the applicable EHR meaningful use requirements. EHR incentive revenues are recognized ratably over the applicable meaningful use reporting period and are included in other revenue in the consolidated statements of operations. CareAlliance recognized EHR incentive revenues of \$4,436,000 and \$8,491,000 for the years ended December 31, 2014 and 2013, respectively. CareAlliance's attestations regarding the meaningful use of EHR technology are subject to audit by the federal government or its designee.

Charity Care—CareAlliance provides care to patients who meet certain criteria under its charity care policies without charge or at amounts less than its established rates. Because CareAlliance does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. CareAlliance estimates the direct and indirect costs of providing charity care using a calculated ratio of costs to gross charges for each facility.

Operating Income—Transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported as income from operations. Peripheral or incidental transactions are reported as nonoperating gains and losses.

Excess of Revenues over Expenses—The consolidated statements of operations include excess of revenues over expenses. Changes in unrestricted net assets, which are excluded from excess of revenues over expenses, consistent with industry practice, include contributions restricted for purchases of property and equipment and permanent transfers of assets to and from affiliates for other than goods and services.

Income Taxes—CareAlliance, Roper Hospital, St. Francis, Mount Pleasant, the Foundation, and Physician Partners are not-for-profit organizations as described in Section 501(c)(3) of the Internal Revenue Code and are generally exempt from federal and state income taxes. The LSC is a limited liability company. Under current laws, income or loss of limited liability companies is included in the income tax returns of the members. Accordingly, no provision for income taxes is made in the consolidated financial statements.

Although CareAlliance is generally exempt from federal and state income taxes, it evaluates whether there are any uncertain tax positions that fail to meet the more-likely-than-not threshold for recognition in the consolidated financial statements. Uncertain tax positions may include the characterization of income, such as a characterization of income as passive, a decision to exclude reporting taxable income

in a tax return, or a decision to classify a transaction, entity, or other position in a tax return as tax exempt. The tax benefit from an uncertain tax position is recognized when it is more likely than not that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes, based on the technical merits. CareAlliance had no unrecognized tax positions as of December 31, 2014 and 2013, and does not expect that unrecognized tax benefits will materially increase within the next 12 months. Tax years from 2011 through 2013 are subject to examination by the federal and state taxing authorities. There are no income tax examinations currently in process.

Interest and penalties related to uncertain tax positions, if any, would be recognized in the consolidated financial statements as income tax expense.

Fair Value of Financial Instruments—See Note 15 for classification of CareAlliance’s financial assets and liabilities accounted for at fair value.

Risks and Uncertainties—CareAlliance’s investments consist of various combinations of equity securities, fixed income securities, money market funds, and other investment securities. Investment securities are exposed to various risks, such as interest rate, market, and credit. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risks in the near term could materially affect CareAlliance’s investment balances reported in the consolidated balance sheets.

The Patient Protection and Affordable Care Act (PPACA) was signed into law on March 23, 2010. In addition, the Health Care and Education Affordability Reconciliation Act (“Reconciliation Act”), which contains a number of amendments to PPACA, was signed into law on March 30, 2010. These health care bills (collectively, the “Reform Legislation”) seek to increase the number of persons with access to health insurance in the United States by requiring substantially all US citizens to maintain medical insurance coverage. The Reform Legislation also provides for material reductions in the growth of Medicare program spending, including reductions in Medicare market basket updates and Medicare disproportionate share hospital (DSH) funding. From time to time, CMS revises the reimbursement systems used to reimburse health care providers, which may include additional changes to the Medicare Severity-Diagnosis Related Group system and other payment systems. These changes may result in reduced Medicare payments.

The Reform Legislation also includes provisions aimed at reducing fraud, waste, and abuse in the health care industry. These provisions allocate significant additional resources to federal enforcement agencies and expand the use of private contractors to recover potentially inappropriate Medicare and Medicaid payments. The Reform Legislation amends several existing federal laws, including the Medicare Anti-Kickback Statute and the False Claims Act, making it easier for government agencies and private plaintiffs to prevail in lawsuits brought against health care providers. These amendments also make it easier for potentially severe fines and penalties to be imposed on health care providers accused of violating applicable laws and regulations.

Management is in the process of assessing the impact the Reform Legislation may have on CareAlliance’s consolidated financial position, results of operations, or cash flows.

Subsequent Events—CareAlliance has evaluated subsequent events from the end of the most recent fiscal year through May 26, 2015, the date the consolidated financial statements were issued.

Recently Issued Accounting Guidance—In May 2012, the FASB issued amendments to the classification of the sale proceeds of donated financial assets in the statement of cash flows. The amendments require not-for-profit (NFP) entities to classify cash receipts from the sale of donated

financial assets consistently with cash donations received in the statement of cash flows if those cash receipts were from the sale of donated financial assets that upon receipt were directed without the NFP imposing any limitations for sale and were converted nearly immediately into cash. The new guidance is effective for fiscal years beginning after June 15, 2013. The adoption of this guidance did not have a material effect on CareAlliance's consolidated financial statements.

In February 2013, the FASB issued guidance for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this guidance is fixed at the reporting date. The new guidance requires entities to measure these obligations as the sum of the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. The new guidance is effective for nonpublic entities for fiscal years ending after December 15, 2014. The adoption of this guidance had no impact on CareAlliance's consolidated financial statements.

In April 2014, the FASB issued amendments to the guidance for reporting discontinued operations, such that a disposal of a component of an entity or a group of components of an entity is required to be reported in discontinued operations, if the disposal represents a strategic shift that has, or will have, a major effect on an entity's operations and financial results. The amendments require an entity to present, for each comparative period, the assets and liabilities of a disposal group that includes a discontinued operation separately in the asset and liability sections, respectively, of the statement of financial position, as well as additional disclosures about discontinued operations. Additionally, the amendments require disclosures about a disposal of an individually significant component of an entity that does not qualify for discontinued operations presentation in the financial statements and expands the disclosures about an entity's significant continuing involvement with a discontinued operation. The new guidance is effective for fiscal years beginning after December 15, 2014. CareAlliance has not yet determined the impact on its consolidated financial statements from the adoption of this guidance.

In May 2014, the FASB issued amendments to the revenue recognition guidance that affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards. The core principle of the new guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new guidance is effective for fiscal years beginning after December 15, 2017. CareAlliance has not yet determined the impact on its consolidated financial statements from the adoption of this guidance.

In August 2014, the FASB issued new guidance on management's responsibility in evaluating whether there is substantial doubt about the reporting entity's ability to continue as a going concern and about related footnote disclosures. For each reporting period, management will be required to evaluate whether there are conditions or events that raise substantial doubt about the reporting entity's ability to continue as a going concern within one year from the date the financial statements are issued. The new guidance is effective for fiscal years ending after December 15, 2016. CareAlliance has not yet determined the impact on its consolidated financial statements from the adoption of this guidance.

In April 2015, the FASB issued amendments to the guidance on accounting for cloud computing arrangements. The amendments provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software

license, the customer should account for the arrangement as a service contract. The new guidance is effective for fiscal years beginning after December 15, 2015. CareAlliance has not yet determined the impact on its consolidated financial statements from the adoption of this guidance.

In May 2015, the FASB issued amendments to the fair value disclosure guidance for investments in certain entities that calculate net asset value (NAV) or its equivalent. The new guidance removes from the fair value hierarchy investments for which the NAV is used as a practical expedient to measure fair value. Instead, an entity will be required to include those investments as a reconciling line item so that the total fair value amount of investments in the fair value hierarchy disclosure is consistent with the amount on the balance sheet. The new guidance is effective for fiscal years beginning after December 15, 2015. CareAlliance has not yet determined the impact on its consolidated financial statements from the adoption of this guidance.

3. CHARITY CARE

In accordance with CareAlliance's mission to improve the health of its communities, CareAlliance facilities accept patients regardless of their ability to pay. CareAlliance offers financial assistance to patients who meet established financial assistance guidelines. Patients with an annual income of 399% or less of the federal poverty guidelines may be eligible for charity adjustments. CareAlliance offers Medical Indigency Adjustments for patients, whose medical expenses outweigh their ability to pay, constituting a financial hardship. CareAlliance also offers flexible payment plans, charity adjustments to patients who are homeless, and discounts for uninsured patients who do not qualify for its charity care program.

The estimated cost of traditional charity care provided by CareAlliance under its charity care policy was \$48,473,000 and \$35,108,000 for the years ended December 31, 2014 and 2013, respectively.

In addition to traditional charity care, management estimates the unpaid cost of services provided under the Medicaid program to be \$7,620,000 and \$6,041,000 for the years ended December 31, 2014 and 2013, respectively. CareAlliance also provides community benefit programs and services for the general community, mainly for indigent patients but also for people with chronic health risks. Examples of these programs include health promotion and education, free clinics and screenings, and other community services. Management estimates the unreimbursed costs of community benefit programs and services to be \$5,315,000 and \$8,990,000 for the years ended December 31, 2014 and 2013, respectively.

4. NET PATIENT SERVICE REVENUE

CareAlliance has agreements with third-party payors that provide for payments to CareAlliance at amounts different from its established rates. A summary of the payment arrangements with major third-party payors is as follows:

Medicare and Medicaid—Inpatient acute care services rendered to program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient nonacute care services, certain outpatient services, and defined capital and medical education costs related to beneficiaries are paid based on a cost reimbursement methodology. Outpatient services are paid at prospectively determined rates. CareAlliance is reimbursed for cost-reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by CareAlliance and audits thereof by the fiscal intermediary. CareAlliance's cost reports have been audited by the Medicare intermediary through December 31, 2011 and by the Medicaid intermediary through December 31, 2010.

Other—CareAlliance has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payments to CareAlliance under these agreements includes prospectively determined rates per day or discharge and discounts from established charges.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Final determination of amounts due from Medicare and Medicaid programs is subject to review by these programs. Changes resulting from final determination are reflected as changes in estimates, generally in the year of determination. In the opinion of management, adequate provision has been made for adjustments, if any, that may result from such reviews. Net patient service revenue increased by approximately \$11,297,000 and \$2,847,000 for the years ended December 31, 2014 and 2013, respectively, due to the effect of settlement adjustments. There were no settlements with commercial payors during the years ended December 31, 2014 and 2013. During the years ended December 31, 2014 and 2013, CareAlliance established liabilities of \$2,055,000 and \$1,157,000, respectively, for estimated future settlements related to net patient service revenue recognized during those years. These liabilities are included in accrued expenses in the accompanying consolidated balance sheets.

During 2006, the state of South Carolina (the “State”) implemented changes to the method of funding the Medicaid disproportionate share and upper payment limit programs. Under the new plan, providers are assessed a quarterly tax and receive periodic Medicaid disproportionate share and upper payment limit payments from the State. The tax assessment was \$15,332,000 and \$15,623,000 for the years ended December 31, 2014 and 2013, respectively, and is recorded as an operating expense in the accompanying consolidated statements of operations. CareAlliance received approximately \$17,062,000 and \$22,200,000 of disproportionate share and upper payment limit payments from the State in 2014 and 2013, respectively, which are recorded in patient service revenue (net of contractual allowances and discounts) within the accompanying consolidated statements of operations. Funds received under the upper payment limit program may be subject to a retroactive settlement process. Management continues to evaluate the settlement process related to the upper payment limit payment program and has recorded adequate liabilities as of December 31, 2014 and 2013, in accrued expenses in the accompanying consolidated balance sheets. Future receipts of the Medicaid disproportionate share and supplemental payment program reimbursement are not guaranteed.

Payments received or to be received under these and other payment arrangements with third-party payors were less than amounts due at established rates by approximately \$1,359,339,000 and \$1,387,992,000 for the years ended December 31, 2014 and 2013, respectively.

Patient service revenue (net of contractual allowances and discounts) for the years ended December 31, 2014 and 2013, is summarized as follows:

	2014	2013
Third-party payors	\$ 765,294,000	\$ 726,636,000
Self-pay	<u>47,264,000</u>	<u>47,374,000</u>
Total patient service revenue (net of contractual allowances and discounts)	<u>\$ 812,558,000</u>	<u>\$ 774,010,000</u>

5. INVESTMENTS AND ASSETS LIMITED AS TO USE

Investments and assets limited as to use as of December 31, 2014 and 2013, are summarized as follows:

	2014	2013
Marketable equity securities	\$ 18,539,000	\$ 21,166,000
Debt securities—short-term investments	21,657,000	16,586,000
Debt securities—self-insurance trust	1,502,000	1,504,000
Bond trustee held funds—short-term investments	10,478,000	31,148,000
Investments in common collective trust funds:		
Marketable domestic equity securities	44,944,000	50,333,000
Marketable international equity securities	23,167,000	29,791,000
Marketable debt securities	28,909,000	30,323,000
Investments in limited partnerships:		
Private real estate fund	17,553,000	16,108,000
Private hedge funds	<u>39,493,000</u>	<u>38,220,000</u>
 Total	 <u>\$206,242,000</u>	 <u>\$235,179,000</u>

The investments were included in the captions in the consolidated balance sheets as of December 31, 2014 and 2013, as follows:

	2014	2013
Short-term investments	<u>\$ 21,657,000</u>	<u>\$ 16,586,000</u>
Long-term investments	<u>153,482,000</u>	<u>169,703,000</u>
Assets limited as to use:		
Board designated—self-insured trust	1,502,000	1,504,000
Bond trustee held funds	<u>10,478,000</u>	<u>31,148,000</u>
Total assets limited as to use	<u>11,980,000</u>	<u>32,652,000</u>
Other assets	<u>19,123,000</u>	<u>16,238,000</u>
 Total	 <u>\$206,242,000</u>	 <u>\$235,179,000</u>

Investment gains (losses) from long-term investments and assets limited as to use for the years ended December 31, 2014 and 2013, consist of the following:

	2014	2013
Interest and dividend income—net of investment fees	\$ 1,545,000	\$ 1,774,000
Net realized gains on sales of investments	8,986,000	3,543,000
Net change in unrealized (losses) gains on investments	<u>(2,562,000)</u>	<u>22,552,000</u>
 Total investment gains—net	 <u>\$ 7,969,000</u>	 <u>\$27,869,000</u>

CareAlliance had no unfunded commitments with respect to these funds as of December 31, 2014 and 2013.

6. PROPERTY AND EQUIPMENT

A summary of property and equipment as of December 31, 2014 and 2013, is as follows:

	2014	2013
Land	\$ 37,287,000	\$ 36,505,000
Land improvements	8,942,000	8,947,000
Buildings and improvements	518,772,000	515,485,000
Equipment	305,242,000	287,084,000
Leased equipment under capital lease obligations	<u>30,532,000</u>	<u>19,308,000</u>
	900,775,000	867,329,000
Less accumulated depreciation	<u>442,455,000</u>	<u>395,117,000</u>
	458,320,000	472,212,000
Construction in progress	<u>34,140,000</u>	<u>4,319,000</u>
Total property and equipment—net	<u>\$ 492,460,000</u>	<u>\$ 476,531,000</u>

Depreciation expense and capital lease-related amortization expense for the years ended December 31, 2014 and 2013, amounted to approximately \$53,674,000 and \$49,815,000, respectively. Accumulated amortization for equipment under capital lease obligations as of December 31, 2014 and 2013, was \$15,895,000 and \$12,056,000, respectively.

At December 31, 2014, CareAlliance had commitments for information technology investments of approximately \$60,000,000 through 2021.

In July 2009, Roper Hospital entered into an agreement with RSFH West Ashley Cancer Center, LLC (WACC) to lease a portion of a medical office building (WACC MOB) located on the St. Francis campus. CareAlliance owns a 9.26% interest in WACC (following a sale of 116.67 units effective August 2013) that is accounted for under the equity method and has guaranteed a portion of WACC's construction loan up to 200% of its equity investment in WACC. CareAlliance's equity method investment in WACC was \$46,000 and \$72,000 as of December 31, 2014 and 2013, respectively, and is included in other assets in the consolidated balance sheets. CareAlliance has determined that it is the deemed owner of the WACC MOB under GAAP due to its ownership interest in and continuing involvement with WACC. Accordingly, CareAlliance recorded an asset (included in property and equipment—net) amounting to \$14,109,000 at December 31, 2014, and a corresponding liability (included in other liabilities) amounting to \$15,858,000 at December 31, 2014, for the cost of construction of the WACC MOB. Construction of the WACC MOB was completed in 2010.

In June 2011, CareAlliance entered into an agreement with MSSC related to the relocation of CareAlliance's existing data facilities to land owned by MSSC in the city of North Charleston, South Carolina. MSSC has agreed to borrow up to \$18,000,000 for the acquisition of the land and construction and equipping of the new data center to be leased to CareAlliance upon completion. CareAlliance has determined that it is the deemed owner of the data center under GAAP due to its involvement in the construction of the asset. Accordingly, CareAlliance recorded an asset (included in property and equipment—net) amounting to \$18,013,000 at December 31, 2014, and a corresponding liability (included in other liabilities) amounting to \$17,775,000 at December 31, 2014 for the cost of the land and construction of the data center. Construction of the data center was complete as of May 1, 2013.

7. ACCRUED LIABILITIES

Accrued liabilities as of December 31, 2014 and 2013, consist of the following:

	2014	2013
Accrued compensation	\$ 48,988,000	\$ 44,862,000
Self-insurance liabilities	10,489,000	9,939,000
Interest	809,000	1,526,000
Estimated third-party liabilities	10,663,000	12,979,000
Other accrued liabilities	<u>1,771,000</u>	<u>1,917,000</u>
Total accrued expenses	<u>\$ 72,720,000</u>	<u>\$ 71,223,000</u>

8. LONG-TERM DEBT

Long-term debt as of December 31, 2014 and 2013, consists of the following:

	2014	2013
Tax-Exempt Fixed Rate Serial Bonds (“Series 1999A”), bearing interest at a rate of 5.125%, refinanced in 2014	\$ -	\$ 13,165,000
Tax-Exempt Variable Rate Direct Purchase Bonds (“Series 2004B-1”), bearing interest at a rate of 0.959% at December 31, 2014, maturing through 2030	20,475,000	20,475,000
Tax-Exempt Fixed Rate Term Bonds (“Series 2004B-1”), bearing interest at rates ranging from 4.50%-5.00%, refinanced in 2014		30,510,000
Tax-Exempt Variable Rate Direct Purchase Bonds (“Series 2004B-2”), bearing interest at a rate of 0.959% at December 31, 2014, maturing through 2033	19,000,000	19,000,000
Tax-Exempt Fixed Rate Serial Bonds (“Series 2007A”), bearing interest at a rate of 5.0%, refinanced in 2014		19,520,000
Tax-Exempt Variable Rate Direct Purchase Bonds (“Series 2007B”), bearing interest at a rate of 0.959% at December 31, 2014, maturing through 2037	80,000,000	80,000,000
Tax-Exempt Variable Rate Revenue Note (“Series 2009”), bearing interest at an adjusted LIBOR rate of 2.2557% at December 31, 2013, matured in 2014		7,187,000
Tax-Exempt Variable Rate Revenue Note (“Series 2010”), bearing interest at an adjusted LIBOR rate of 1.415% at December 31, 2013, refinanced in 2015		30,000,000
Tax-Exempt Fixed Rate Serial Bonds (“Series 2011”), bearing interest at a rate of 2.74%, maturing through 2019	22,365,000	28,475,000
Tax-Exempt Fixed Rate Bonds (“Series 2012A”), bearing interest at a rate of 2.26%, maturing through 2025	31,935,000	31,935,000
Tax-Exempt Variable Rate Bonds (“Series 2012B”), bearing interest at a rate of 1.00125%, maturing through 2028	47,265,000	47,265,000
Taxable Variable Rate Bonds (“Series 2014A”), bearing interest at a rate of 0.5550% at December 31, 2014, maturing 2015 through 2016	14,435,000	
Tax-exempt Fixed Rate Bonds (“Series 2014B”), bearing interest at a rate of 2.34%, maturing through 2024	21,390,000	
Tax-exempt Variable Rate Bonds (“Series 2014C”), bearing interest at a rate of 0.74175% at December 31, 2014, maturing through 2021	30,000,000	
Tax-exempt Fixed Rate Bonds (“Series 2014D”), bearing interest at a rate of 2.04%, maturing through 2026	21,105,000	
Other debt	<u>28,001,000</u>	<u>9,816,000</u>
	335,971,000	337,348,000
Less unamortized discount		(239,000)
Plus unamortized premium		<u>1,300,000</u>
	335,971,000	338,409,000
Less current maturities	<u>(19,501,000)</u>	<u>(26,238,000)</u>
Total long-term debt—net	<u>\$ 316,470,000</u>	<u>\$ 312,171,000</u>

Revenue Bonds—All of the bonds outstanding at December 31, 2014 and 2013, are governed by a master trust indenture (the “Master Indenture”) and related agreements. CareAlliance, Roper Hospital, St. Francis Hospital, Mount Pleasant Hospital, and the Physician Partners (the “Obligated Group”) are jointly and severally liable for obligations issued under the Master Indenture. The bonds are collateralized by a pledge of the Obligated Group’s gross revenue and the funds and accounts established under the Master Indenture. Additionally, the periodic payment of interest and principal is unconditionally guaranteed through municipal bond insurance for 2004B-1, 2004B-2 and 2007B bond issuances. Among other financial covenants, the Master Indenture requires the Obligated Group to maintain a debt service coverage ratio of not less than 1.1 to 1.0, debt-to-capitalization ratio of no more than 65%, and days cash on hand of not less than 75 days. The Supplemental Master Indentures for the Series 2004 bonds and after require the Obligated Group to maintain a debt service coverage ratio of 1.25 to 1.0. In addition, the supplemental master indentures for each bond series contain certain provisions that provide for establishment of reserve funds, funded by CareAlliance, and collateralization of the bonds through CareAlliance’s property and equipment in the event that certain minimum financial covenants and credit ratings are not maintained. The Obligated Group was in compliance with all such provisions of the Master Indenture and related agreements as of and during the year ended December 31, 2014. The net assets of the Obligated Group are in excess of 90% of the net assets of CareAlliance. All of CareAlliance’s debt can be prepaid without penalty with the exception of the Series 2012A bonds which, if prepaid, are subject to a redemption premium determined based on the difference between the stated interest rate of the bonds and the bond equivalent yield for US Treasury securities with similar maturities.

The Series 1999A and 1999B, and Series 2004A and 2004B bonds are limited obligations of Charleston County, South Carolina (the “County”), payable by the County solely from the loan repayments to be made by the Obligated Group. The Series 2007A, 2007B, 2011, and 2012 bonds are limited obligations of the South Carolina Jobs-Economic Development Authority (the “Authority”), payable by the Authority solely from the loan repayments of the Obligated Group.

On June 24, 2014, the Authority issued \$59,925,000 Series 2014A, 2014B, and 2014D revenue bonds pursuant to a Bond Purchase and Loan Agreement dated June 24, 2014, among the Authority, Wells Fargo Bank, and CareAlliance. The Series 2014A taxable variable rate revenue bonds were issued in the amount of \$14,435,000 to defease all outstanding Series 1999A Charleston County, South Carolina Revenue Bonds. The Series 2014A bonds bear interest at the London InterBank Offered Rate (LIBOR), plus 0.40% per annum. The Series 2014B tax-exempt fixed rate revenue bonds were issued in the amount of \$24,385,000 to defease all outstanding Series 2004B-1 Charleston County, South Carolina Revenue Bonds. The Series 2014B bonds bear interest at 2.34%. The Series 2014D tax-exempt fixed rate revenue bonds were issued in the amount of \$21,105,000 to defease all outstanding Series 2007A South Carolina Jobs-Economic Development Authority Revenue Bonds. The Series 2014D bonds bear interest at 2.04%.

On June 24, 2014, the Authority issued \$30,000,000 Series 2014C tax-exempt variable rate revenue bonds pursuant to a Bond Purchase and Loan Agreement dated June 24, 2014, among the Authority, TD Bank, N.A., and CareAlliance. The Series 2014C bonds were issued to refund the Series 2010 South Carolina Jobs-Economic Development Authority Revenue Note. The Series 2014C bonds bear interest at 69% multiplied by the sum of (i) LIBOR, plus (ii) 0.92% per annum.

On June 24, 2014, CareAlliance converted \$19,000,000 Series 2004B-2 bonds from variable rate demand bonds to direct purchase bonds with Wells Fargo. The bonds bear interest at 70% multiplied by LIBOR, plus 0.85% per annum.

On June 24, 2014, CareAlliance refinanced \$20,475,000 Series 2004B-1 direct purchase bonds and \$80,000,000 Series 2007B direct purchase bonds with Wells Fargo for a 7-year term bearing interest at 70% multiplied by LIBOR, plus 0.85% per annum.

On September 1, 2012, the Authority issued \$31,935,000 Series 2012A tax-exempt fixed rate revenue bonds pursuant to a Bond Purchase and Loan Agreement dated September 1, 2012, among the Authority, TD Bank, N.A., and CareAlliance. The bond proceeds were loaned to the Obligated Group for the purpose of (i) refunding \$31,935,000 of the outstanding principal amount of the Series 1999A bonds, and (ii) to pay costs of issuing the Series 2012A bonds. The bonds bear interest at 2.26% per annum.

On September 1, 2012, the Authority issued \$47,265,000 Series 2012B tax-exempt variable rate revenue bonds pursuant to a Bond Purchase and Loan Agreement dated September 1, 2012, among the Authority, TD Bank, N.A., and CareAlliance. The bond proceeds were loaned to the Obligated Group for the purpose of (i) refunding \$17,265,000 of the outstanding principal amount of the Series 1999A bonds, and defraying the cost of certain capital improvements; and (ii) to pay costs of issuing 2012B bonds. The bonds bear interest at 75% multiplied by the sum of (i) LIBOR, plus (ii) 1.18% per annum.

On August 31, 2011, the Authority issued \$39,855,000 Series 2011 tax-exempt fixed rate revenue bonds pursuant to a Note Purchase and Loan Agreement dated August 1, 2011, among the Authority, Wells Fargo Bank, and CareAlliance. The bond proceeds were used for the purpose of refunding a portion of the Charleston County, South Carolina Revenue Bonds, Series 1999A.

On September 1, 2009, the Authority issued a \$12,500,000 Series 2009 tax-exempt variable rate revenue note pursuant to a Note Purchase and Loan Agreement dated September 1, 2009, among the Authority, Branch Banking and Trust Company, and CareAlliance. The note proceeds were loaned to Obligated Group for the purpose of expanding Physician Partners through the acquisition of the assets of Lowcountry Medical Associates. All outstanding principal and interest fully matured on September 15, 2014.

On November 1, 2007, the Authority issued \$130,000,000 of revenue bonds, Series 2007A and 2007B. The bond proceeds were loaned to the Obligated Group for the acquisition, constructing, and equipping of the new 85-bed Mount Pleasant hospital facility in Mount Pleasant, South Carolina.

On July 1, 2004, the County issued \$99,480,000 of Revenue Bonds, Series 2004A, 2004B-1, and 2004B-2. The bond proceeds were loaned to the Obligated Group for construction of a patient care tower and a parking garage at Roper Hospital. The Series 2004B-1 Bonds are subject to mandatory sinking fund payments beginning in 2010. The Series 2004B-2 Bonds are subject to mandatory sinking fund payments beginning in 2030. The Series 2004A Bonds fully matured on August 15, 2013.

Other Long-Term Debt—Other long-term debt consists of notes payable and various capital lease obligations. At December 31, 2014 and 2013, notes payable consists of 3.62% to 6.3% notes payable and a variable rate term loan totaling \$902,000 and \$2,419,000, respectively. At December 31, 2014 and 2013, capital lease obligations, which are collateralized by leased equipment, amount to \$27,099,000 and \$7,397,000, respectively, at an interest rate of approximately 6.0%. CareAlliance's capital lease obligations expire in 2014 through 2021.

Scheduled maturities of long-term debt as of December 31, 2014, are as follows:

Years Ending December 31	Long-Term Debt	Capital Lease Obligations
2015	\$ 13,099,000	\$ 7,201,000
2016	12,599,000	7,199,000
2017	13,471,000	5,224,000
2018	14,849,000	3,402,000
2019	15,234,000	2,392,000
Thereafter	<u>239,620,000</u>	<u>4,079,000</u>
	308,872,000	29,497,000
Less amounts representing interest on capital lease obligations		<u>(2,398,000)</u>
Total	<u>\$ 308,872,000</u>	<u>\$ 27,099,000</u>

During 2014 or 2013, CareAlliance capitalized no interest costs related to borrowings for capital projects.

9. DERIVATIVE FINANCIAL INSTRUMENTS

During 2004, CareAlliance entered into an interest rate hedge related to \$19,000,000 of its variable rate debt. The effect of this hedge is to convert the variable rate of this amount of the debt to a fixed rate of 3.81%. At December 31, 2014 and 2013, the fair value of the hedge was \$(5,738,000) and \$(3,667,000), respectively, and is recorded in other liabilities in the accompanying consolidated balance sheets.

During 2006, CareAlliance entered into an interest rate hedge related to \$80,000,000 of the \$130,000,000 debt issued in 2007. The effect of this hedge is to convert the variable rate of this amount of the debt to a fixed rate of 3.56%. At December 31, 2014 and 2013, the fair value of the hedge was \$(23,762,000) and \$(12,702,000), respectively, and is recorded in other liabilities in the accompanying consolidated balance sheets.

During 2010, CareAlliance entered into an interest rate hedge related to the \$30,000,000 debt issued in 2010. The effect of this hedge is to convert the variable rate of this amount of the debt to a fixed rate of 3.06%. At December 31, 2014 and 2013, the fair value of the hedge was \$(875,000) and \$(795,000), respectively, and is recorded in other liabilities in the accompanying consolidated balance sheets.

During 2011, CareAlliance entered into interest rate hedges related to the outstanding fixed rate bonds Series 1999A, 2004 B-1, and 2007A. The effect of these hedges is to retain the basis risk between paying a tax-exempt floating rate (SIFMA) and receiving a taxable rate (LIBOR) through a basis swap. At December 31, 2014 and 2013, the fair value of these hedges was \$786,000 and \$(97,000), respectively, and is recorded in other assets and other liabilities in the accompanying consolidated balance sheets.

The change in fair value of interest rate hedges for the years ended December 31, 2014 and 2013, was \$(12,328,000) and \$15,693,000, and is recorded as a realized (loss) gain and included within nonoperating gains (losses) in the accompanying consolidated statements of operations for the years ended December 31, 2014 and 2013, respectively.

Payments of fixed rate interest to be made by CareAlliance under its interest rate hedges are insured by financial guaranty insurance policies issued by Assured Guaranty Ltd (AG). CareAlliance's interest rate hedge agreements contain provisions that require CareAlliance's debt to maintain certain credit ratings from Moody's Investors Services, Inc. ("Moody's"). If the credit ratings for CareAlliance's debt were to fall below "Baa3" for Moody's, it would be in violation of these provisions, and the counterparties to the interest rate hedges could demand settlement of the interest rate hedges. In addition, the interest rate hedge agreements contain provisions that require AG to maintain a credit rating of "A3" or higher from Moody's. If AG's credit rating were to fall below these levels, then the counterparties to the interest rate hedges could require CareAlliance to post collateral on interest rate hedges in a net liability position in excess of certain thresholds that are determined based on the credit ratings for CareAlliance's debt. The threshold in effect for each interest rate hedge agreement as of December 31, 2014, is \$5,000,000 based on CareAlliance's credit rating as of December 31, 2014. CareAlliance was not required to post collateral on any of its interest rate hedge agreements as of December 31, 2014 or 2013, based on AG's credit ratings as of those dates.

10. LEASE OBLIGATIONS

CareAlliance leases various equipment and buildings used in its operations. Future lease payments on operating leases that have initial or remaining noncancelable lease terms in excess of one year and deemed ownership obligations (Note 6) as of December 31, 2014, are as follows:

Years Ending December 31	Operating Leases	Deemed Ownership Obligations (Note 6)	Total
2015	\$ 16,448,000	\$ 2,522,000	\$ 18,970,000
2016	11,164,000	2,571,000	13,735,000
2017	7,314,000	2,621,000	9,935,000
2018	6,029,000	2,672,000	8,701,000
2019	4,822,000	2,726,000	7,548,000
Thereafter	<u>8,934,000</u>	<u>29,705,000</u>	<u>38,639,000</u>
Total minimum future rentals	<u>\$ 54,711,000</u>	<u>\$ 42,817,000</u>	<u>\$ 97,528,000</u>

Rent expense for building space for the years ended December 31, 2014 and 2013, was approximately \$19,598,000 and \$18,773,000, respectively.

The future operating lease payments above include approximately \$8,891,000 payable to MSSC under a 10-year master lease for medical office building space that began in fiscal 2010. Also included in the deemed ownership obligations above is approximately \$17,775,000 payable to MSSC under a lease for CareAlliance's data center that began in fiscal 2013.

CareAlliance also leases office space to physicians. The rental income from these leases for the years ended December 31, 2014 and 2013, was approximately \$1,869,000 and \$1,689,000, respectively, and is included in other nonoperating income in the consolidated statements of operations.

11. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets as of December 31, 2014 and 2013, are available for the following purposes:

	2014	2013
Building and equipment	\$ 3,496,000	\$ 3,592,000
Indigent care	4,039,000	2,538,000
Hospital service lines	2,691,000	1,540,000
Education	1,491,000	1,456,000
Community health improvement	656,000	766,000
Sponsorships	<u>268,000</u>	<u>257,000</u>
Total temporarily restricted	<u>\$12,641,000</u>	<u>\$10,149,000</u>

Net assets were released from temporary restrictions by incurring expenses satisfying the restriction purposes as follows:

	2014	2013
Hospital service lines	\$1,272,000	\$ 631,000
Education	398,000	441,000
Indigent care, community health, and other	2,677,000	2,175,000
Other	<u>249,000</u>	<u>246,000</u>
Total net assets released from restrictions	<u>\$4,596,000</u>	<u>\$3,493,000</u>

12. PERMANENTLY RESTRICTED NET ASSETS AND BOARD-DESIGNATED FUNDS

CareAlliance's endowment funds consist of approximately 30 donor-restricted individual funds established for a variety of purposes and board-designated funds set aside for capital expenditures and self-insurance.

On an annual basis, CareAlliance requests funds from the Foundation for reimbursement of expenditures incurred specifically related to unrestricted or temporarily restricted purposes. The Foundation has developed an investment policy for all its investable assets whose general purpose is to preserve the capital and purchasing power of the Foundation and to produce sufficient investment earnings for current and future spending needs. The Foundation has adopted a total return strategy whose asset allocation is designed to give balance to the overall structure of the Foundation's investment program over a long-term period.

The endowment net asset composition by fund type as of December 31, 2014, is composed of the following:

Endowment Net Asset Composition by Fund Type as of December 31, 2014				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Board designated—				
Self-insurance trust	\$ 1,502,000	\$ -	\$ -	\$ 1,502,000
Donor-restricted:				
Undesignated			436,000	436,000
Building and equipment		970,000	503,000	1,473,000
Indigent care		7,000	230,000	237,000
Hospital service lines		865,000	5,032,000	5,897,000
Education		1,064,000	1,487,000	2,551,000
Community health improvement		98,000	287,000	385,000
Total funds	\$ 1,502,000	\$ 3,004,000	\$ 7,975,000	\$ 12,481,000

The endowment net asset composition by fund type as of December 31, 2013, is composed of the following:

Endowment Net Asset Composition by Fund Type as of December 31, 2013				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Board designated—				
Self-insurance trust	\$ 1,504,000	\$ -	\$ -	\$ 1,504,000
Donor-restricted:				
Undesignated			440,000	440,000
Building and equipment		199,000	502,000	701,000
Indigent care		68,000	230,000	298,000
Hospital service lines		1,451,000	4,413,000	5,864,000
Education		1,067,000	1,489,000	2,556,000
Community health improvement		80,000	223,000	303,000
Total funds	\$ 1,504,000	\$ 2,865,000	\$ 7,297,000	\$ 11,666,000

Changes in endowment assets for the years ended December 31, 2014 and 2013, consisted of the following:

Year Ended December 31, 2014	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets—beginning of year	\$ 1,504,000	\$ 2,865,000	\$ 7,297,000	\$ 11,666,000
Investment (loss) income	(2,000)	469,000	5,000	472,000
Contributions			614,000	614,000
Appropriations of endowment assets for expenditure		(310,000)		(310,000)
Other changes—change in value of split-interest agreements			(11,000)	(11,000)
Transfers		(20,000)	70,000	50,000
Endowment net assets—end of year	\$ 1,502,000	\$ 3,004,000	\$ 7,975,000	\$ 12,481,000

Year Ended December 31, 2013	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets—beginning of year	\$1,487,000	\$1,319,000	\$6,160,000	\$ 8,966,000
Investment (loss) income	(1,000)	1,786,000	19,000	1,804,000
Contributions			503,000	503,000
Appropriations of endowment assets for expenditure		(222,000)		(222,000)
Other changes—change in value of split-interest agreements			31,000	31,000
Transfers	<u>18,000</u>	<u>(18,000)</u>	<u>584,000</u>	<u>584,000</u>
Endowment net assets—end of year	<u>\$1,504,000</u>	<u>\$2,865,000</u>	<u>\$7,297,000</u>	<u>\$11,666,000</u>

13. RETIREMENT PLANS

CareAlliance has established the FutureSaver 403(b) Retirement Plan, a matching savings plan for all employees who have attained the age of 20-1/2, are paid for 1,000 hours or more, and are employed on December 31 of that plan year. Employer-matching contributions shall be made at a rate equal to 50% of the elective deferrals of each employee, up to 4% of annual compensation, for a total possible matching contribution of 2% of compensation.

The plan administrator is the Retirement Committee. Employer contributions for the FutureSaver 403(b) Retirement Plan for the years ended December 31, 2014 and 2013, were approximately \$11,224,000 and \$10,241,000, respectively, and are included in salaries and employee benefits in the accompanying consolidated statements of operations.

14. CONCENTRATION OF CREDIT RISK

Roper Hospital, St. Francis Hospital, and Mount Pleasant Hospital provide services primarily to the residents of the greater Charleston, South Carolina, area without collateral or other proof of ability to pay, most of whom are insured by third-party payor agreements.

The mix of receivables from patients and third-party payors as of December 31, 2014 and 2013, is as follows:

	2014	2013
Medicare	33 %	34 %
Medicaid	15	12
Commercial and others	33	31
Patients	<u>19</u>	<u>23</u>
Total	<u>100 %</u>	<u>100 %</u>

15. FAIR VALUE OF FINANCIAL INSTRUMENTS

In accordance with GAAP, certain assets and liabilities are required to be measured at fair value on a recurring basis. For CareAlliance, the assets and liabilities that are adjusted at fair value on a recurring basis are short- and long-term investments, assets whose use is limited, and interest rate swaps.

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. Additionally, the inputs used

to measure fair value are prioritized based on a three-level hierarchy. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

Level 1—Valuations based on unadjusted quoted prices for identical instruments in active markets that are available as of the measurement date

Level 2—Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly

Level 3—Valuations based on inputs that are unobservable and significant to the overall fair value measurement

There were no transfers of investments between levels for the years ended December 31, 2014 and 2013.

The fair value hierarchy of investments and assets limited as to use as of December 31, 2014 and 2013, is as follows:

Fair Value Measurement at Reporting Date Using				
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of December 31, 2014				
Marketable equity securities	\$ 18,539,000	\$ 18,539,000	\$ -	\$ -
Debt securities	23,159,000	2,203,000	20,956,000	
Bond trustee held funds—short-term investments	10,478,000		10,478,000	
Investments in common collective trust funds	97,020,000		97,020,000	
Investments in limited partnerships	57,046,000			57,046,000
Total	<u>\$ 206,242,000</u>	<u>\$ 20,742,000</u>	<u>\$128,454,000</u>	<u>\$ 57,046,000</u>

Fair Value Measurement at Reporting Date Using				
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of December 31, 2013				
Marketable equity securities	\$ 21,166,000	\$21,166,000	\$ -	\$ -
Debt securities	18,090,000	1,981,000	16,109,000	
Bond trustee held funds—short-term investments	31,148,000		31,148,000	
Investments in common collective trust funds	110,447,000		110,447,000	
Investments in limited partnerships	54,328,000			54,328,000
Total	<u>\$235,179,000</u>	<u>\$23,147,000</u>	<u>\$157,704,000</u>	<u>\$54,328,000</u>

CareAlliance estimates the fair value of investments in common collective trust funds, which do not have readily determinable fair values, using the reported net asset value as a practical expedient for fair value. The use of net asset value as a practical expedient for fair value is permitted under GAAP for investments in entities that meet the description of an investment company and whose underlying investments are measured at fair value. The common collective trust funds held by CareAlliance invest primarily in marketable debt and equity securities with readily determinable fair values.

CareAlliance estimates the fair value of its investments in limited partnerships based on information provided by the fund managers. Because CareAlliance's investments in limited partnerships are not readily marketable and do not transact frequently, their estimated fair value is subject to uncertainty and, therefore, may differ from the fair value that would have been used had a ready market for such investments existed. Such differences could be material.

A reconciliation of changes in beginning and ending balances for investments measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended December 31, 2014 and 2013, is as follows:

	Fair Value Measurements Using Significant Unobservable Inputs Level 3—Limited Partnerships	
	2014	2013
Beginning balance—January 1	\$ 54,328,000	\$ 46,984,000
Purchases	535,000	1,398,000
Net change in unrealized gains in limited partnerships	<u>2,183,000</u>	<u>5,946,000</u>
Ending balance—December 31	<u>\$ 57,046,000</u>	<u>\$ 54,328,000</u>
The amount of total gains or losses for the period included in changes in net assets attributable to the change in unrealized gains or losses relating to assets still held at the reporting date		
	<u>\$ 2,183,000</u>	<u>\$ 5,946,000</u>

The redemption frequency and redemption notice period for investments in common collective trust funds and limited partnerships as of December 31, 2014 and 2013, is as follows:

	2014	Redemption Frequency	Redemption Notice Period
Investments in common collective trust funds:			
Marketable debt and domestic equity securities	\$ 73,853,000	Daily	1 day
Marketable international equity securities	23,167,000	Daily	1 day
Private real estate fund	17,553,000	Quarterly	60 days
Private hedge fund	24,720,000	Quarterly	70 days
Private hedge fund	<u>14,773,000</u>	Committed through 1/1/2015 with rolling 2 year commitments thereafter	
	<u>\$ 154,066,000</u>		
	2013	Redemption Frequency	Redemption Notice Period
Investments in common collective trust funds:			
Marketable debt and domestic equity securities	\$ 80,656,000	Daily	1 day
Marketable international equity securities	29,791,000	Daily	1 day
Private real estate fund	16,108,000	Quarterly	60 days
Private hedge fund	23,872,000	Quarterly	70 days
Private hedge fund	<u>14,348,000</u>	Committed through 1/1/2015 with rolling 2 year commitments thereafter	
	<u>\$ 164,775,000</u>		

Management estimates the fair value of interest rate hedges using standard valuation models based primarily on Level 2 inputs, including interest rate indices. Management also considers the creditworthiness of CareAlliance and its counterparties in estimating the fair value of interest rate hedges; however, the effect of credit valuation adjustments was not significant to the fair value measurements as of December 31, 2014 or 2013.

As of December 31, 2014 and 2013, the carrying amounts reported in CareAlliance's consolidated balance sheets for cash equivalents, receivables, accounts payable, and accrued expenses approximate fair value. At December 31, 2014 and 2013, the fair value of CareAlliance's long-term debt was approximately \$318,947,000 and \$314,999,000, respectively. Management estimates the fair value of long-term debt based primarily on Level 2 inputs, including consideration of discounted cash flow analyses and CareAlliance's current incremental borrowing rates for similar types of borrowing arrangements.

16. COMMITMENTS AND CONTINGENCIES

CareAlliance is self-insured for professional malpractice claims exposures. The laws of the State currently limit the amount that can be received from certain nonprofit medical facilities for damages for medical services rendered by the facility or the facility's employees to \$300,000 per claim and an aggregate of \$600,000 per occurrence. CareAlliance's provision for estimated medical malpractice claims includes estimates of the ultimate costs for reported claims and claims incurred but not reported. CareAlliance's liability for professional malpractice is based on actuarially projected estimates discounted to present value at a rate of 4% at December 31, 2014.

CareAlliance is also self-insured for employee health insurance claims and employee workers' compensation claims. Liabilities for asserted and unasserted claims under each of these self-insurance programs have been recorded and included in accrued expenses in the consolidated balance sheets.

CareAlliance is involved in litigation arising in the ordinary course of business. It is the opinion of management, based on consultation with legal counsel, that these cases will be resolved without material adverse effect on CareAlliance's financial position, results from operations, or cash flows.

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers.

Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that CareAlliance is in compliance with fraud and abuse statutes and regulations, as well as other applicable government laws and regulations.

CareAlliance has entered into an agreement with MSSC which grants CareAlliance the unilateral option, through October 25, 2017, to purchase approximately 66 acres of land in Berkeley County, South Carolina, at an amount equal to the initial purchase price paid by MSSC of \$8,902,700, plus increases of 6% cumulatively on each subsequent anniversary of the purchase date (the "Estimated Projected Value of the Property"). If CareAlliance does not purchase the property by October 25, 2017, MSSC shall have the right to retain or sell the property at its own cost and expense, provided that CareAlliance shall pay

MSSC a termination payment equal to the difference between the actual sales price and the Estimated Projected Value of the Property. Management has estimated the value of the termination payment to be approximately \$4,400,000 and \$3,625,000 as of December 31, 2014 and 2013, respectively.

17. FUNCTIONAL EXPENSES

CareAlliance provides general health care services to residents within its geographic location. Expenses related to providing these services for the years ended December 31, 2014 and 2013, are as follows:

	2014	2013
Health care services	\$ 687,977,000	\$ 657,620,000
Supporting services	<u>86,770,000</u>	<u>81,659,000</u>
Total expenses	<u>\$ 774,747,000</u>	<u>\$ 739,279,000</u>

18. RELATED-PARTY TRANSACTIONS

Payments to the Founding Members for management fees and services were approximately \$15,585,000 and \$11,632,000 for the years ended December 31, 2014 and 2013, respectively.

At December 31, 2014, CareAlliance had other receivables of \$291,000 due from MSSC reflecting unpaid member contributions for reimbursement of expenses. In addition, CareAlliance received \$2,382,000 from MSSC for acquisition of property and equipment during the year ended December 31, 2014.

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FEDERAL AWARDS SUPPLEMENTAL INFORMATION

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

To the Board of Directors of
CareAlliance Health Services
(d/b/a Roper St. Francis Healthcare):

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 CareAlliance Health Services (d/b/a Roper St. Francis Healthcare) ("CareAlliance"), which comprise the consolidated balance sheet as of December 31, 2014, and the related consolidated statement of operations, changes in net assets, and cash flows for the year then ended, and the related notes to the consolidated financial statements, which collectively comprise CareAlliance's basic financial statements, and have issued our report thereon dated May 26, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered CareAlliance's 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 CareAlliance's internal control. Accordingly, we do not express an opinion on the effectiveness of CareAlliance's 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 CareAlliance's 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 consolidated 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 CareAlliance's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Deloitte + Touche LLP

May 26, 2015

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

To the Board of Directors of
CareAlliance Health Services
(d/b/a Roper St. Francis Healthcare):

Report on Compliance for Each Major Federal Program

We have audited CareAlliance Health Services' (d/b/a Roper St. Francis Healthcare) ("CareAlliance") 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 CareAlliance's major federal programs for the year ended December 31, 2014. CareAlliance's major federal programs are identified in the summary of auditors' 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 CareAlliance's 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 CareAlliance's 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 CareAlliance's compliance.

Opinion on Each Major Federal Program

In our opinion, CareAlliance 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 December 31, 2014.

Report on Internal Control Over Compliance

Management of CareAlliance 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 CareAlliance's 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 CareAlliance's 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. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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.

Deloitte + Touche LLP

June 17, 2015

CAREALLIANCE HEALTH SERVICES
(d/b/a Roper St. Francis Healthcare)

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2014

PART I. SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditor's report issued: Unmodified

Internal control over financial reporting:

Material weakness(es) identified? Yes No

Significant deficiency(ies) identified
not considered to be material weakness? Yes None reported

Noncompliance material to consolidated financial
statements noted? Yes No

Federal Awards

Internal control over major programs:

Material weakness(es) identified? Yes No

Significant deficiency(ies) identified
not considered to be material weakness? Yes None reported

Type of auditor's report issued on
compliance for major programs: Unmodified

Any audit findings disclosed that are required to be reported
in accordance with Circular A-133 Section 510(a)? Yes No

Identification of major programs:

Program Name	CFDA #
U.S. Department of Health and Human Services—Ryan White Title III: Early Intervention Services	93.918

(Continued)

CAREALLIANCE HEALTH SERVICES
(d/b/a/ Roper St. Francis Healthcare)

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2014

Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Expenditures
FEDERAL AWARDS:		
U.S. Department of Health and Human Services—		
Direct programs:		
Ryan White Title III: Early Intervention Services	93.918	\$ 627,299
Passed through The Regents of the University of California (“UCSD”) as a subaward to Jacobo Mintzer (Roper Hospital)		
Alzheimer’s Disease Cooperative Study—Clinical Trial—		
ADCS_ADNI2 (ARC-F-0002)—Protocol#ADC-039	93.866	11,760
ADCS_NGF (ARC-F-0001)—Protocol#ADC-033-NGF	93.866	8,895
ADCS_RES (ARC-F_0003)—Protocol#ADC-037-RES	93.866	1,958
ADCS_RES (ARC-F_0006)—Protocol#ADC-040-A4	93.866	5,202
Passed through The Medical University of South Carolina (“MUSC”) as a subaward to Jacobo Mintzer (Roper Hospital)		
Alzheimer’s Disease Cooperative Study—Clinical Trials		
MUSC_CitAD (ARC-F-0004)—Protocol#MUSC14-020	93.866	29,074
Passed through the South Carolina Department of Health and Environmental Control:		
Assistant Secretary for Preparedness and Response (ASPR)—		
HIV Program SVC—ADAP	93.917	308,335
Newborn Hearing	93.251	14,765
Passed through the City of Charleston Department of Housing and Community Development—		
HOPWA Housing Support—Housing Support for HIV Recipients	14.241	133,345
Passed through the Trident Area Agency on Aging		
Authorized Federal Funds passed down through state & area agencies for coordinated system of providing programs for evidenced-base disease and disability prevention and health promotion service (HTH)		
	93.044	<u>25,128</u>
Total Federal Awards		<u>\$1,165,761</u>

See note to schedule of expenditures of federal awards.

CAREALLIANCE HEALTH SERVICES
(d/b/a Roper St. Francis Healthcare)

NOTE TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2014

1. BASIS OF ACCOUNTING

The accompanying schedule of expenditures of federal awards (the “Schedule”) includes the federal grant activity of CareAlliance Health Services (d/b/a Roper St. Francis Healthcare) (“CareAlliance”) during the year ended December 31, 2014. The expenditures on the Schedule are reported on the basis of when CareAlliance has met the qualifications for the incurred expenses according to the grant requirements. The information on this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Therefore, some amounts presented in the Schedule may differ from amounts presented in or used in the consolidated financial statements.

CAREALLIANCE HEALTH SERVICES
(d/b/a Roper St. Francis Healthcare)

SCHEDULE OF STATUS OF PRIOR YEAR FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2013

There were no findings for the year ended December 31, 2013.