THE FULTON-DEKALB HOSPITAL AUTHORITY
d/b/a GRADY HEALTH SYSTEM

Information Required Under the Single Audit Act and
Office of Management and Budget's Circular A-133
For the Year Ended December 31, 2014
Together with Independent Auditors' Reports Thereon

THE FULTON-DEKALB HOSPITAL AUTHORITY
d/b/a GRADY HEALTH SYSTEM

December 31, 2014

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THE FULTON-DEKALB HOSPITAL AUTHORITY
d/b/a GRADY HEALTH SYSTEM

Schedule of Findings and Questioned Costs
Year Ended December 31, 2014

Section I – Summary of Auditors' Results

On May 20, 2008, The Fulton-DeKalb Hospital Authority (the "Authority") entered into a lease and transfer agreement with the Grady Memorial Hospital Corporation (GMHC), a non-profit corporation organized under the laws of the State of Georgia, to lease the Authority's health system facilities. The agreement transfers the operating assets and existing operations, as well as the performance and discharge of all other obligations for consideration of annual rent of $2,500,000. The Authority assigns, transfers, and conveys right, title, and interest in and to all assets to the GMHC. The entities are collectively referred to in this report as the "Hospital".

This report has been previously submitted under the name The Fulton-DeKalb Hospital Authority; however, pursuant to the above paragraph, it is now submitted under the name Grady Memorial Hospital Corporation.

Financial Statements

The audits of the basic financial statements of the GMHC were performed by other auditors. The report by the auditor of the GMHC on financial statements as of and for the year then ended December 31, 2014, dated April 30, 2015, expressed an unmodified opinion on those statements.

In connection with the audit of the basic financial statements of the GMHC, the other auditors did not disclosed any significant deficiencies and no material weaknesses which are disclosed in their report issued under separate cover and dated April 30, 2015.

Federal Awards

We issued an unmodified opinion on the compliance for major programs for the Hospital for the year ended December 31, 2014.

We noted no significant deficiencies or material weaknesses involving the internal control over major programs.

We noted no findings that we are required to report in accordance with Circular A-133, Section .510.

Identification of Major Programs:

The following programs were audited as major programs:

Name of Federal Program or Cluster	*CFDA Number*
Ryan White	93.917
Maternal and Infant Care	93.994
Neonatal Intensive Infant Care	93.994
Sickle Cell Legislative	93.994

We used a threshold of $915,642 expended to distinguish between Type A and Type B programs.

The Hospital is considered a low-risk auditee.

BANKS, FINLEY, WHITE & CO.
CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Trustees
The Fulton-DeKalb Hospital Authority

The Board of Directors
Grady Memorial Hospital Corporation:

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Report on Compliance for Each Major Federal Program

We have audited The Fulton-DeKalb Hospital Authority d/b/a Grady Health System (the "Hospital") 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 the Hospital's major federal programs for the year ended December 31, 2014. The Hospital's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Hospital'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 the Hospital'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 the Hospital's compliance.

Opinion on Each Major Federal Program

In our opinion, the Hospital 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.

To the Board of Trustees
The Fulton-DeKalb Hospital Authority

The Board of Directors
Grady Memorial Hospital Corporation

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Report on Internal Control Over Compliance

Management of the Hospital 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 the Hospital'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 the Hospital'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

Banks, Finley, White & Co.

May 1, 2015
College Park, Georgia

THE FULTON-DEKALB HOSPITAL AUTHORITY
d/b/a GRADY HEALTH SYSTEM

Schedule of Findings and Questioned Costs
For the Year Ended December 31, 2014

Section II - Schedule of Findings and Questioned Costs

No current year findings

BANKS, FINLEY, WHITE & CO.
CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Trustees
The Fulton-DeKalb Hospital Authority

The Board of Directors
Grady Memorial Hospital Corporation

INDEPENDENT AUDITOR'S REPORT ON
SCHEDULE OF FEDERAL AND STATE CONTRACTUAL ASSISTANCE

We have audited the accompanying Schedule of Federal and State Contractual Assistance of The Fulton-DeKalb Hospital Authority d/b/a Grady Health System for the year ended December 31, 2014, and the related notes (the "Schedule").

Management's Responsibility

Management is responsible for the preparation and fair presentation of this Schedule 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 a financial statement that is free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on this Schedule based on our audit. We conducted our audit 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* and the "Standards for Audits of DHR Agencies and Programs Conducted by Independent Auditors Under Contract". Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether the Schedule is free from material misstatement.

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

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

To the Board of Trustees
The Fulton-DeKalb Hospital Authority

The Board of Directors
Grady Memorial Hospital Corporation

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Opinion

In our opinion, the Schedule referred to above presents fairly, in all material respects, the expenditures of federal and state awards of The Fulton-DeKalb Hospital Authority d/b/a Grady Health System for the year ended December 31, 2014 in accordance with accounting principles generally accepted in the United States of America.

Banks, Finley, White & Co.

May 1, 2015
College Park, Georgia

THE FULTON-DEKALB HOSPITAL AUTHORITY
d/b/a GRADY HEALTH SYSTEM

Schedule of Federal and State Contractual Assistance
as of December 31, 2014

Federal Grantor/Pass-Through Grantor/Program Title	CFDA Number	Grantor's Number	Award or Amount	Program Revenues	Total Expenditures
U.S. Department of Health and Human Services					
Passed through the Georgia Department of Behavioral Health:					
and Developmental Disabilities					
*Mental Health and Addictive Diseases Adult Core					
Services Block Grant:					
Fiscal 2014	**93.150/93.958/93.959**	441-93-1433AAX	$ 6,394,121	$ 3,497,064	$ 3,497,064
Fiscal 2015	**93.150/93.958/93.959**	441-93-1533046	6,438,846	3,197,046	3,197,046
Subtotal			12,832,967	6,694,110	6,694,110
U.S. Department of Health and Human Services					
HIV Care and Emergency Relief Formula Grants					
Passed through the Georgia Department of Community Health					
AIDS State Clinic:					
Fiscal 2014	**93.914**	40500-044-14110275	3,709,174	2,007,906	2,007,906
Fiscal 2015	**93.914**	40500-044-15110275	3,804,653	1,777,063	1,777,063
Subtotal			7,513,827	3,784,969	3,784,969
U.S. Department of Health and Human Services					
Ryan White Care Act					
Direct Program					
Ryan White (Part D):					
Fiscal 2014	**93.153**	5 HI2HA24799-02-00	676,774	326,962	326,962
Fiscal 2015	**93.153**	4 H12HA24799-03-01	742,116	264,536	264,536
Subtotal			1,418,890	591,499	591,499
U.S. Department of Health and Human Services					
*Ryan White Care Act:					
Passed through Fulton County:					
Ryan White Part A Non-MAI :		`			
Fiscal 2014	**93.917**	PO-118-13SC88896B-TR	8,014,323	3,107,023	3,107,023
Fiscal 2015	**93.917**	PO-118-14SC94086B	7,212,556	5,354,125	5,354,125
Ryan White Children (Part B):					
Fiscal 2014	**93.917**	40500-044-13100179	164,567	28,986	28,986
Fiscal 2014	**93.917**	40500-044-14100179	164,567	139,932	139,932
Heallth Insurnace Navigator					
Fiscal 2014	**93.750**	CA-NAV-13-001	184,464	108,344	108,344
		1NSVCA130083-01-00	184,464	46,342	46,342
Subtotal			15,924,941	8,784,751	8,784,751
Maternal and Child Health Services Block Grants:					
Passed through the Georgia Department of Community Health					
Sickle Cell Legislative:					
Fiscal 2014	**93.994**	40500-039-14110255	1,478,779	997,627	997,627
Fiscal 2015	**93.994**	40500-039-15110255	1,478,779	555,300	555,300
Neonatal Intensive Infant Care:					
Fiscal 2013	**93.994**	40500-042-14141130	507,701	220,525	220,525
Fiscal 2014	**93.994**	40500-039-15151243	544,002	511,806	511,806
Maternal and Infant Care:					
Fiscal 2014	**93.994**	40500-042-14141129	891,030	347,817	347,817
Fiscal 2015	**93.994**	40500-039-1515244	899,239	561,148	561,148
Subtotal			5,799,531	3,194,223	3,194,223
Poison Control Stabilization and Enhancement **(Federal)**					
Fiscal 2014	**93.253**	5H4BHS15495-05-00	511,475	334,225	334,225
Fiscal 2015	**93.253**	2H4BHS15495-08-00	536,050	138,621	138,621
Subtotal			1,047,525	472,846	472,846
Poison Control Center **(State)**:					
Fiscal 2014	**93.253**	40500-036-13110286	3,486,315	1,351,535	1,351,535
Fiscal 2015	**93.253**	40500-036-15110286	2,991,650	2,129,980	2,129,980

THE FULTON-DEKALB HOSPITAL AUTHORITY
d/b/a GRADY HEALTH SYSTEM

Schedule of Federal and State Contractual Assistance
as of December 31, 2014

Federal Grantor/Pass-Through Grantor/Program Title	CFDA Number	Grantor's Number	Award or Amount	Program Revenues	Total Expenditures
Provide Training Courses for Georgia Healthcare Providers					
Fiscal 2014	**93.889**	40500-033-14110436	231,800	178,750	178,750
Fiscal 2015	**93.889**	40500-033-15110436	158,700	52,498	52,498
Poison Control **(State)** - BT Hotline					
Fiscal 2014	**93.069**	40500-033-14091314	263,081	67,950	67,950
Fiscal 2015	**93.069**	40500-033-1515254	190,000	76,000	76,000
Dual Protection	**93.946**	5U01DP003894-02	206,852	125,706	125,706
Family Planning Program:					
Fiscal 2014	**93.558**	40500-041-14110272	723,943	246,002	246,002
Pass through the 'Family Health Centers of Georgia					
Family Planning Title X					
Fiscal 2015	**93.558**	None	795,342	588,167	588,167
Strong Start for Mothers and Newborns	**93.611**	1D1CMS331150-01-02	243,207	168,017	168,017
Preventive Health and Health Services Block Grant:					
Rape Crisis Center - VAWA Victim Services:					
Fiscal 2014	**16.575**	W13-8-011	69,122	69,122	69,122
Sexual Violence Prevention Education II					
Fiscal 2013	**93.991**	40500-032-13130950 A3	106,470	94,970	94,970
Grady Rape Crisis Center					
Fiscal 2014	**93.991**	SA14-007	33,630	15,489	15,489
Fiscal 2015	**93.991**	X15-8-026	28,478	10,743	10,743
Passed through the Georgia Department of Community Health					
Tuberculosis Detection:					
Fiscal 2013	**93.116**	40500-044-13100209	77,576	19,394	19,394
Fiscal 2014	**93.116**	40500-044-14100209	77,576	58,182	58,182
Test, Educate, Support, Treat - T.E.S.T Georgia Expanded Access HIV Testing Grant (ARTAS)					
Fiscal 2011	**93.940**	40500-044-14141141	162,500	88,403	88,403
Cancer Control					
Fiscal 2014	**93.283**	40500-032-14110312	87,550	45,240	45,240
Fiscal 2015	**93.283**	40500-032-15110344	87,550	33,961	33,961
Subtotal			10,021,342	5,420,109	5,420,109
Passed through the Georgia Department of Community Health:					
Special Supplemental Food Program for Women, Infants,					
and Children:					
WIC Supplemental Nutrition Program:					
Fiscal 2014	**10.572**	40500-041-14110409	397,757	285,634	285,634
Fiscal 2015	**10.572**	40500-041-15110409	397,757	99,341	99,341
Subtotal			795,514	384,975	384,975
WIC Supplemental Nutrition Program:(Non-Cash Vouchers)					
Fiscal 2014	**10.572**	40500-041-14110409	1,090,307	1,090,307	1,090,307
Subtotal			1,090,307	1,090,307	1,090,307
U.S. Department of Education					
Student Financial Assistance Programs:					
Pell Grants Radiologic Technology:					
Fiscal 2015	**84.063**	91259159	98,833	93,638	93,638
			98,833	93,638	93,638

Federal Grantor/Pass-Through Grantor/Program Title	CFDA Number	Grantor's Number	Award or Amount	Program Revenues	Total Expenditures
US Department of Labor					
Workforce Investment Act (WIA)					
Atlanta Regional Commision - WIA	**17.259**	Unknown	2,500	2,500	2,500
DeKalb Workforce Development Center	**17.259**	Unknown	1,666	1,666	1,666
NE Georgia Regional Commission - WIA	**17.259**	Unknown	2,800	2,800	2,800
Atlanta Workforce Development Center	**17.259**	Unknown	3,000	3,000	3,000
Subtotal			56,553,643	30,521,392	30,521,392
Consumer Product Safety Commission					
NEISS Surveillance Report and Special Survey	**NA**	CFSC-N-12-0033	297,838	99,399	99,399
Georgia Department of Community Health					
Statewide Tuberculosis:					
Fiscal 2014	**NA**	40500-044-14110261	216,242	108,121	108,121
Fiscal 2015	**NA**	40500-044-15110261	216,242	108,121	108,121
Forensics Psychiatric Evaluation:					
Fiscal 2014	**NA**	44100-016-0000036108	139,900	69,950	69,950
Fiscal 2015	**NA**	44100-016-000054488	170,000	69,950	69,950
Assertive Community Treatment (ACT)					
Fiscal 2014	**NA**	441-93-11110321-02	1,560,000	780,000	780,000
Fiscal 2015	**NA**	44100-026-0000027801	780,000	33,235	33,235
Fiscal 2015	**NA**	44100-93-11103212	1,560,000	789,844	789,844
Case Management					
Fiscal 2014	**NA**	44100-263-0000037527	32,000	15,775	15,775
Fiscal 2015	**NA**	44100-263-0000051850	32,000	19,721	19,721
Fiscal 2016	**NA**	44100-263-00000	153,045	47,014	47,014
SAMHSA Atlanta Collaborative HIV/AIDS Network for Growth	**NA**	40500-044-12120593	471,374	347,935	347,935
New or Expanded Collection Hospital Development for Public Cord Blood Collection	**????**	383-9595	142,320	128,730	128,730
HIV-EMR IDP					
Fiscal 2014	**NA**	40500-044-14130927	44,000	7,500	7,500
Fiscal 2015	**NA**	40500-044-15130927	44,000	-	-
Trauma Readiness Services					
Fiscal 2014	**NA**	GTC_Grady2014.1/GTC_Grady2014.2.	1,634,424	339,584	339,584
Fiscal 2015	**NA**	GTC_Grady2015.1	1,653,781	1,232,700	1,232,700
Trauma Readiness Services (Burn)					
Fiscal 2014	**NA**	GTC_GradyBurn2014.2	206,319	126,883	126,883
Fiscal 2015	**NA**	GTC_GradyBurn 2015.1	453,150	242,609	242,609
D Regional Coordinating Hospital					
Fiscal 2014	**NA**	4500-034-14130839	150,748	150,748	150,748
Subtotal			9,957,383	4,717,819	4,717,819
Georgia Board for Physician Workforce					
Residency Capitation					
Fiscal 2014	**Unknown**	Unknown	1,545,349	1,545,349	1,545,349
Fiscal 2015	**Unknown**	Unknown	1,642,778	1,642,778	1,642,778
			3,188,127	3,188,127	3,188,127
Total			13,145,510	7,905,946	7,905,946
Grand Total			$ 69,699,152	$ 38,427,337	$ 38,427,337

THE FULTON DEKALB HOSPITAL AUTHORITY
d/b/a GRADY HEALTH SYSTEM

Notes to the Schedule of Federal and State
Contractual Assistance
December 31, 2014

1. **General:**

On May 20, 2008, The Fulton-DeKalb Hospital Authority (the "Authority") entered into a lease and transfer agreement with the Grady Memorial Hospital Corporation (GMHC), a non-profit corporation organized under the laws of the State of Georgia, to lease the Authority's health system facilities. The agreement transfers the operating assets and existing operations, as well as the performance and discharge of all other obligations for consideration of annual rent of $2,500,000. The Authority assigned, transferred, and conveyed right, title, and interest in and to all assets to the GMHC.

The accompanying Schedule of Federal and State Contractual Assistance presents the combined activity of Federal and State assistance programs of the Authority and GMHC. Contractual assistance received directly from Federal grantor agencies, as well as contractual assistance passed through other government agencies, and direct state of Georgia contractual assistance are included on the accompanying schedule.

2. **Accounting Principles:**

a. The accompanying Schedule of Federal and State Contractual Assistance are presented using the accrual basis of accounting.

b. All Federal and State Contractual Assistance Programs are accounted for on the reimbursement basis.

Indirect costs charged to federal programs were as follows:

Sickle Cell	$131,744
Poison Control	406,780
Total	$538,524

THE FULTON DEKALB HOSPITAL AUTHORITY
d/b/a GRADY HEALTH SYSTEM

Notes to the Schedule of Federal and State
Contractual Assistance
December 31, 2014

3. Voucher Distributions

The Authority is the pass-through recipient of federal grant funds from the U. S. Department of Agriculture's Special Supplemental Food for Women, Infants and Children (WIC) Program through Georgia Department of Community Health (the "State"). The Authority identifies eligible program participants and the State issues non-cash food vouchers. According to the State's records, the Authority's WIC program participants received 67,402 vouchers for program year 2014 and redeemed 51,455 vouchers valued at $ 1,090,307 for program year 2014.

4. Relationship to Basic Financial Statements and Federal Financial Reports:

Federal and State Contractual Assistance revenues are reported in the GMHC's basic financial statements as follows:

Federal Contractual assistance	$30,521,391
State Contractual assistance	7,905,946
Total per Schedule of Federal and State Contractual Assistance	38,427,337
Non-federal and state grant revenues	7,523,510
Restricted fund and other revenues, net of WIC Vouchers and Pell Grants	(1,193,911)
Total revenues in GMHC's basic financial statements	$44,756,936

5. Pass Through Cost:

Sickle Cell Foundation, which is included with Sickle Cell Legislative Service, is the only program with (pass-through) cost of $186,521.

THE FULTON-DEKALB HOSPITAL AUTHORITY
d/b/a GRADY HEALTH SYSTEM

Status of Prior Audit Findings and Questioned Costs
For the Year Ended December 31, 2014

Schedule of Findings and Questioned Costs

No prior year audit findings.

KPMG

GRADY MEMORIAL HOSPITAL CORPORATION AND AFFILIATE

Combined Financial Statements

December 31, 2014 and 2013

(With Independent Auditors' Report Thereon)

KPMG LLP
Suite 2000
303 Peachtree Street, N.E.
Atlanta, GA 30308-3210

Independent Auditors' Report

The Board of Directors
Grady Memorial Hospital Corporation:

Report on the Combined Financial Statements

We have audited the accompanying combined financial statements of Grady Memorial Hospital Corporation and affiliate (the System), which comprise the combined balance sheets as of December 31, 2014 and 2013, and the related combined statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the combined financial statements.

Management's Responsibility for the Combined Financial Statements

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

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

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

Opinion

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Grady Memorial Hospital Corporation and affiliate as of December 31, 2014 and 2013, and the results of their operations, changes in net assets, and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

KPMG

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 30, 2015 on our consideration of the System'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 the System's internal control over financial reporting and compliance.

KPMG LLP

Atlanta, Georgia
April 30, 2015

GRADY MEMORIAL HOSPITAL CORPORATION AND AFFILIATE

Combined Balance Sheets

December 31, 2014 and 2013

(In thousands)

Assets		2014	2013
Current assets:			
Cash and cash equivalents	$	74,043	75,809
Patient accounts receivable, net of allowance for uncollectible accounts of $133,277 and $95,864 at December 31, 2014 and 2013, respectively		81,259	70,941
Grants receivable		10,453	12,150
Current portion of pledges receivable, net		38,720	28,676
Other current assets		64,181	72,031
Total current assets		268,656	259,607
Assets limited as to use		80,344	55,437
Property and equipment, net		311,759	318,011
Beneficial interest in net assets held by others		17,258	16,948
Pledges receivable, net, excluding current portion		14,197	34,543
Other assets		3,743	3,843
Total assets	$	695,957	688,389
Liabilities and Net Assets			
Current liabilities:			
Current portion of capital lease obligations	$	873	820
Current portion of notes payable		5,073	3,864
Accounts payable		16,572	15,625
Current portion of self-insurance reserves		14,742	13,462
Due to third-party payors, net		17,868	22,030
Due to medical schools		25,692	20,157
Other accrued expenses		65,135	76,151
Total current liabilities		145,955	152,109
Capital lease obligations, excluding current portion		34,386	35,259
Notes payable, excluding current portion		3,113	8,317
Self-insurance reserves, excluding current portion		45,847	48,148
Accrued postretirement benefit cost		4,910	10,251
Other long-term liabilities		9,671	5,093
Total liabilities		243,882	259,177
Net assets:			
Unrestricted		344,118	305,209
Temporarily restricted		92,608	108,964
Permanently restricted		15,349	15,039
Total net assets		452,075	429,212
Commitments and contingencies			
Total liabilities and net assets	$	695,957	688,389

See accompanying notes to combined financial statements.

GRADY MEMORIAL HOSPITAL CORPORATION AND AFFILIATE

Combined Statements of Operations

Years ended December 31, 2014 and 2013

(In thousands)

		2014	2013
Revenue, gains, and other support:			
Net patient service revenue (net of provision for uncollectible accounts of $368,502 in 2014 and $268,698 in 2013)	$	710,767	625,427
Contributions from Fulton and DeKalb Counties		56,240	61,232
Other revenue		95,744	88,657
Total revenue, gains, and other support		862,751	775,316
Expenses:			
Salaries and benefits		369,324	346,731
Supplies and other expenses		422,395	372,363
Net periodic postretirement benefit credit		(11,997)	(7,977)
Interest		3,642	4,462
Depreciation and amortization		45,248	44,963
Total expenses		828,612	760,542
Operating income		34,139	14,774
Nonoperating gains, net:			
Investment income, net		91	242
Other		129	3,883
Total nonoperating gains, net		220	4,125
Revenue, gains, and other support in excess of expenses and losses		34,359	18,899
Accrued postretirement benefit cost adjustments		(6,828)	31,780
Net assets released from restriction used for the purchase of property and equipment		12,679	50,095
Contributions and other		(1,301)	(22)
Change in unrestricted net assets	$	38,909	100,752

See accompanying notes to combined financial statements.

GRADY MEMORIAL HOSPITAL CORPORATION AND AFFILIATE

Combined Statements of Changes in Net Assets

Years ended December 31, 2014 and 2013

(In thousands)

		Unrestricted	Temporarily restricted	Permanently restricted	Total
Net assets, December 31, 2012	$	204,457	153,849	13,974	372,280
Revenue, gains, and other support in excess of expenses and losses		18,899	—	—	18,899
Accrued postretirement benefit cost adjustments		31,780	—	—	31,780
Net assets released from restriction used for purchase of property and equipment		50,095	(50,095)	—	—
Net assets released from restriction used for operations		—	(2,720)	—	(2,720)
Net change in beneficial interest in net assets held by others		—	—	1,065	1,065
Contributions and other		(22)	7,930	—	7,908
Change in net assets		100,752	(44,885)	1,065	56,932
Net assets, December 31, 2013		305,209	108,964	15,039	429,212
Revenue, gains, and other support in excess of expenses and losses		34,359	—	—	34,359
Accrued postretirement benefit cost adjustments		(6,828)	—	—	(6,828)
Net assets released from restriction used for purchase of property and equipment		12,679	(12,679)	—	—
Net assets released from restriction used for operations		—	(5,221)	—	(5,221)
Net change in beneficial interest in net assets held by others		—	—	310	310
Contributions and other		(1,301)	1,544	—	243
Change in net assets		38,909	(16,356)	310	22,863
Net assets, December 31, 2014	$	344,118	92,608	15,349	452,075

See accompanying notes to combined financial statements.

GRADY MEMORIAL HOSPITAL CORPORATION AND AFFILIATE

Combined Statements of Cash Flows

Years ended December 31, 2014 and 2013

(In thousands)

		2014	2013
Cash flows from operating activities:			
Change in net assets	$	22,863	56,932
Adjustments to reconcile change in net assets to net cash provided by operating activities:			
Depreciation and amortization		45,248	44,963
Loss (gain) on asset disposal		35	(8)
Accrued postretirement benefit cost adjustments		6,828	(31,780)
Net change in beneficial interest in net assets held by others		(310)	(1,857)
Provision for uncollectible accounts		368,502	268,698
Contributions used for the purchase of property and equipment		(12,679)	(50,095)
Changes in operating assets and liabilities:			
Patient accounts receivable		(378,820)	(279,579)
Grants and pledges receivable		11,999	57,481
Other current assets		7,850	1,195
Other assets		(736)	298
Accounts payable, due to medical schools, and other accrued expenses		(836)	(10,207)
Due to third-party payors, net		(4,162)	(7,731)
Accrued postretirement benefit cost		(12,496)	(8,731)
Self-insurance reserves		(1,021)	1,186
Net cash provided by operating activities		52,265	40,765
Cash flows from investing activities:			
Purchase of property and equipment		(36,988)	(49,801)
Change in assets limited as to use		(24,907)	(8,114)
Net cash used in investing activities		(61,895)	(57,915)
Cash flows from financing activities:			
Principal repayments under capital lease obligations		(820)	(1,314)
Principal repayments under notes payable		(3,995)	(3,187)
Contributions used for the purchase of property and equipment		12,679	50,095
Net cash provided by financing activities		7,864	45,594
Net change in cash and cash equivalents		(1,766)	28,444
Cash and cash equivalents, beginning of year		75,809	47,365
Cash and cash equivalents, end of year	$	74,043	75,809
Supplemental disclosure of cash flow information:			
Cash paid for interest	$	3,237	3,600
Supplemental disclosure of noncash investing activity:			
Liabilities assumed for additions to property and equipment	$	8,043	6,836

See accompanying notes to combined financial statements.

(1) Organization, Business, and Summary of Significant Accounting Policies

Grady Memorial Hospital Corporation (the System) is a 501(c)(3) not-for-profit health system formed on March 17, 2008, which subsequently entered into a Lease and Transfer Agreement (the Agreement) effective June 1, 2008 with The Fulton-DeKalb Hospital Authority (the Authority). The System, located in Atlanta, Georgia, comprises Grady Memorial Hospital (one of the largest teaching hospitals in the state, licensed with over 900 beds), Hughes Spalding Children's Hospital, six free-standing primary care clinics, and other significant healthcare facilities and services consistent with an integrated healthcare delivery and medical education system serving a major metropolitan area. The System is the principal safety-net healthcare provider for the Atlanta metropolitan area, and maintains the primary Level I trauma center for the region.

The key terms and conditions associated with the Agreement are as follows:

- The System makes monthly lease payments to the Authority, totaling $2.5 million in the initial year of the Agreement, and increasing each year by an amount generally measured by inflation in the published Consumer Price Index (CPI), not to exceed 3%, for an initial term of 40 years.
- The System assumed the liabilities of the Authority related to its previous operation of the former Grady Memorial Hospital and related facilities.
- In exchange for the lease payments and assumption of liabilities, the Authority transferred to the System all of the Authority's right, title, and interest in the operating assets of Grady Memorial Hospital and provided to the System the right to use its related facilities.
- The System is the agent for the Authority with respect to preexisting Operating Agreements among the Authority, Fulton County, and DeKalb County. The Operating Agreements define the obligations of the Authority with respect to (principally) the provision of indigent care to the citizens of Fulton and DeKalb Counties (the Counties), in exchange for related ongoing funding that the Counties provide. The Authority is obligated to remit directly to the System all such funds the Authority receives from the Counties.

Certain assets and obligations of the Authority were excluded from the Agreement. In particular, the Authority retained certain assets and obligations related to (a) its sponsorship of The Fulton-DeKalb Hospital Authority Employee Pension Plan (the Plan – a frozen plan effective May 19, 2008) and (b) preexisting Authority hospital revenue bond issues.

The Authority has defined obligations within the Agreement related to how it will apply the lease payments to its own obligations. A portion of the lease payments is to be applied to the Authority's ongoing funding of the Plan, and the Agreement requires that the System fund any shortfall between required Plan funding and available funds from the lease payments. Should there be an excess of lease payments over the Authority's bona fide operating costs and pension obligations, such excess must be returned to the System. The Authority may not carry over excess funds from year to year.

The System's acquisition of assets and assumption of liabilities under the Agreement was accounted for as a purchase. The System has recognized a capital lease obligation for the lease payments (excluding any future CPI adjustments), which were discounted at 7.24%, representing management's best estimate of a fair value rate that might be available to the System on an unenhanced credit basis. Other acquired assets and assumed liabilities were recognized at their respective estimated fair values.

(Continued)

Because any future funding obligations of the System for the Plan are currently indeterminable, those payments (if any) are accounted for on a "pay-as-you-go" basis and recognized currently in expense as invoiced from the Authority. During the years ended December 31, 2014 and 2013, the System recognized approximately \$3.5 million and \$4.9 million, respectively, in expense associated with its pension funding obligation as described herein. At December 31, 2014 and 2013, all such pension funding amounts were fully settled.

The Agreement subjects the System to a number of commercially typical covenants, principally related to continuance of mission as a safety-net hospital system, maintenance of facilities, and financial and other reporting, including the System's obligation to deliver audited financial statements within 120 days of year-end.

The significant accounting policies used by the System in preparing and presenting its combined financial statements are as follows:

(a) Principles of Combination

The accompanying combined financial statements include the accounts of the System and the Henry W. Grady Memorial Foundation, Inc. (the Foundation). All significant intercompany accounts and transactions are eliminated in combination.

(b) Use of Estimates

The preparation of combined financial statements in conformity with U.S. generally accepted accounting principles (U.S. GAAP) requires that management make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the combined financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Significant items subject to such estimates and assumptions include the determination of the allowances for uncollectible patient accounts and contractual adjustments, reserves for general and professional liability claims, reserves for workers' compensation claims, third-party payor settlements, and the actuarially determined benefit liability related to the System's postretirement benefit plan. In addition, 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 related to these programs will change by a material amount in the near term.

(c) Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand, deposits with banks, and investments in highly liquid debt instruments with original maturities of three months or less, excluding amounts limited as to use.

(d) Assets Limited as to Use and Investment Income

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the accompanying combined balance sheets. Investment income items (including unrealized gains and losses on trading investments, realized gains and losses on sales of investments, interest, and dividends) are included in revenue, gains, and other support in excess of expenses and losses unless the investment income is temporarily or permanently restricted by donor or law.

Assets limited as to use include assets internally designated for capital acquisition and other uses, assets held by trustee under escrow agreements, an insurance guaranty trust fund, and funds limited by donors for specific purposes.

(e) Inventories

Inventories, consisting principally of medical supplies and pharmaceuticals, are stated at the lower of cost (first-in, first-out method) or market.

(f) Property and Equipment, Net

Property and equipment transferred to the System under the terms of the Agreement are stated at fair value at the date of transfer. Property and equipment acquired subsequently are stated at cost, with the exception of donated items, which are stated at fair value at the date of donation. Equipment held under capital lease obligations is initially recorded at the lower of estimated fair value or the present value of minimum lease payments. Provisions for depreciation are computed using the straight-line method based on the estimated useful lives of the assets. Equipment held under capital lease obligations is amortized using the straight-line method over the shorter of the estimated useful life or the lease term, and such amortization is included in depreciation and amortization in the accompanying combined statements of operations.

A summary of asset classes and related depreciable lives is as follows:

Land improvements	3–8 years
Buildings and improvements	5–40 years
Machinery, equipment, and vehicles	3–20 years
Computer hardware and software	3–10 years

(g) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the System is restricted by the donor to a specific time period or purpose. Permanently restricted net assets are those that have been restricted by donors to be maintained in perpetuity. Permanently restricted net assets consist primarily of the System's beneficial interest in indigent care and nursing scholarship funds held by the Authority. All of the earnings of the trust are donor-restricted for the System's use in providing indigent and charity care.

(h) 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 revenue adjustments (if necessary) due to audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations.

(i) Charity Care

The System provides care to patients who meet certain criteria under its financial assistance policies at amounts less than its established rates. Because the System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

(j) Revenue, Gains, and Other Support in Excess of Expenses and Losses

The combined statements of operations include revenue, gains, and other support in excess of expenses and losses. Changes in unrestricted net assets, which are excluded from revenue, gains, and other support in excess of expenses and losses (to the extent applicable in any particular year), include certain postretirement benefit plan accounting adjustments, donor-restricted contributions and net assets released from restrictions used for purchase of property and equipment.

For purposes of presentation, transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are reported as revenue and expenses. Peripheral or incidental transactions are reported as nonoperating gains and losses.

(k) Contributions

Unconditional promises to give cash and other assets to the System 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 underlying condition is satisfied by the System or the date the donor's intention to give becomes a promise to give. Gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the combined statements of operations as net assets released from restrictions.

Gifts of long-lived assets such as property and equipment are excluded from revenue, gains, and other support in excess of expenses and losses and are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

(l) Asset Retirement Obligations

The System recognizes a liability for legal obligations associated with asset retirements in the period in which it is incurred, if a reasonable estimate of the fair value of the obligation can be made. When the liability is initially recorded, the System capitalizes the cost of the asset retirement obligation by increasing the carrying amount of the related long-lived asset. Over time, the liability (a component of long-term liabilities in the accompanying combined balance sheets) is accreted to its present value each period, and the capitalized cost associated with the retirement obligation is depreciated over the useful life of the related asset. Upon settlement of the obligation, any difference between the cost to settle the asset retirement obligation and the recorded liability is recognized as a gain or loss in the combined statements of operations.

(m) Long-lived Assets

Long-lived assets, such as property and equipment and purchased intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If circumstances require a long-lived asset or asset group to be tested for possible impairment, the System first compares undiscounted future cash flows expected to be generated by that asset or asset group to its carrying amount. If the carrying amount of the long-lived asset is not recoverable on an undiscounted cash flow basis, an impairment is recognized to the extent that the carrying amount exceeds its fair value. Fair value is determined through various valuation techniques including discounted cash flow models, quoted market values, and third-party independent appraisals, as considered necessary. Assets to be disposed of are separately presented in the combined balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposal group classified as held-for-sale are presented separately in the appropriate asset and liability sections of the combined balance sheet. In the period in which the disposal group is sold or classified as held-for-sale, the results of its operations are classified as discontinued operations in the combined statement of operations.

(n) Income Taxes

The System has been recognized by the Internal Revenue Service as exempt from federal income tax under Internal Revenue Code Section 501(a) as an organization described in Section 501(c)(3), and therefore, related income is generally not subject to federal or state income taxes. The Foundation has been similarly recognized.

The System applies FASB Accounting Standards Codification (ASC) 740, *Income Taxes* (ASC 740), which addresses the accounting for uncertain income tax positions. ASC 740 provides guidance on when tax positions are recognized in an entity's financial statements and how the values of these positions are determined. There is no impact on the System's combined financial statements as of a result of applying ASC 740.

(o) Postretirement Benefit Plan

The System applies the recognition and disclosure provisions of FASB ASC Topic 715, *Compensation – Retirement Benefits* (ASC 715). ASC 715 requires that the System recognize the unfunded status of its postretirement benefit plan in its combined balance sheets. ASC 715 also requires measurement of plan assets and benefit obligations as of the System's fiscal year-end.

The System records annual amounts relating to its postretirement benefit plan based on calculations that incorporate various actuarial and other assumptions, including discount rates, mortality, assumed rates of return, compensation increases, turnover rates, and healthcare cost trend rates. The System reviews its assumptions on an annual basis and makes modifications to the assumptions based on current rates and trends when it is appropriate to do so. The effect of modifications to those assumptions is recorded as a change in unrestricted net assets and amortized to net periodic cost over future periods using the corridor method. The System believes that the assumptions utilized in recording its obligations under its plan are reasonable based on its experience and market conditions.

The net periodic costs are recognized as employees render the services necessary to earn the postretirement benefits.

(p) Commitments and Contingencies

Liabilities for loss contingencies arising from claims, assessments, litigation, fines, and penalties and other sources are recorded when it is probable that a liability has been incurred and the amount can be reasonably estimated. Legal costs incurred in connection with loss contingencies are expensed as incurred.

(q) Subsequent Events

On April 8, 2015, the System entered into a transaction with a bank and certain lenders to obtain financing through the New Markets Tax Credit (NMTC) program sponsored by the U.S. Department of Treasury. The NMTC program permits certain taxpayers to receive a credit against federal income taxes for making qualified equity investments in community development entities. Total financing provided to the System as a part of the transaction totaled $12.4 million in the form of a term loan (interest paid monthly at one-month LIBOR plus 250 basis points with total principal due no later than October 2015). The estimated net benefit related to proceeds from the transaction is approximately $7.1 million. The financing will be used by the System for certain construction projects.

The System has evaluated subsequent events through April 30, 2015, the date the combined financial statements were available to be issued, and determined that there are no other items to disclose.

(r) Current Operating Environment

Management of the System continually monitors current economic conditions closely, both with respect to potential impacts on the healthcare provider industry and from a more general business perspective. Management recognizes that economic conditions will continue to impact the System in a number of ways, including uncertainties associated with U.S. healthcare system reform and rising self-pay/emerging high-deductible health funded patient volumes and corresponding increases in uncompensated care and decreasing reimbursement rates relative to governmental payors.

(2) Principal Safety Net Healthcare Provider – Implications for the System

The System's formation was driven by the strategic vision of local business and community leaders who recognized the overriding importance of Grady Memorial Hospital in providing appropriately accessible healthcare for the indigent and other potentially under-served populations in the region. In short, the vision is founded on a deep desire to ensure that the System can both survive and thrive in an increasingly competitive and challenging healthcare industry environment. The System's ability to continue its mission on a long-term sustainable basis is a critical benefit to the citizens of both metropolitan Atlanta and the State of Georgia.

As indicated in note 1, the System is the principal safety-net healthcare provider for the Atlanta metropolitan area. Additionally, because the System is the primary Level I trauma center for the region (and for other reasons unique to the System), it also has some patient volumes from outside of the metropolitan area. Finally, the System is one of the largest medical education platforms in Georgia. Given all of those factors, the System's payor mix is heavily influenced by care to the uninsured and underinsured. The financing of the System's care for this critical population is provided through two key sources:

- Funding from the Counties, as described in note 1, which totaled approximately \$56.2 million and \$61.2 million for the 2014 and 2013 fiscal years, respectively, included in contributions from Fulton and DeKalb Counties in the accompanying combined statements of operations.
- Funding from the combined state/federal Medicaid disproportionate share program (referred to in Georgia as the Indigent Care Trust Fund, or ICTF), which totaled approximately \$78.1 million and \$85.9 million for the 2014 and 2013 fiscal years, respectively, included in net patient service revenue in the accompanying combined statements of operations.

The System is largely dependent on the two financing sources described above to provide net cash from operations at levels sufficient to fund the System's operating activities in a fashion consistent with its mission. Any material reduction in funds from these two financing sources would have a materially adverse impact on the System's financial results. Management recognizes the risks inherent in the System's dependence on these financing sources.

As previously noted, the System is the legal agent for the Authority's obligations to the Counties regarding the provision of indigent care to the Counties' citizens, under the terms of continuing Operating Agreements that obligate the Counties to fund the cost of that care according to certain defined criteria. To further clarify Fulton County's obligations (which have historically represented the significant majority of related funding), the Authority and Fulton County entered into a Memorandum of Understanding (the MOU), which effectively further memorializes the financial obligation of Fulton County under the Operating Agreements. System management views the MOU as an important additional level of confirmation ensuring that funding it receives from the Counties will continue at levels reasonably consistent with the services the System provides to the Counties' citizens. Nevertheless, funding under the Operating Agreements (as supplemented by the MOU) is necessarily subject to political and related implications arising from the Counties' budgeting and related processes, and therefore, there are no guarantees regarding future funding amounts beyond the commitments evidenced in the Operating Agreements.

Under the provisions of the ICTF program, the System contributes funds to be used by the state in the Medicaid program that are then supplemented by federal funds, the aggregate of which are often referred to as combination dollars. The combination dollars are returned to the System as additional Medicaid inpatient reimbursement. The state Medicaid program is funded on a state fiscal year basis (the state maintains a June 30 fiscal year-end). As of December 31, 2014 and 2013, the System has been approved to participate in the state fiscal 2014 ICTF program; the state fiscal 2015 ICTF program plan terms have not been finalized. Because of the importance of ICTF funding to the System, management maintains routine contact with state Medicaid officials and has no reason to believe that the System's participation in the state fiscal 2015 ICTF program will be meaningfully different from the System's historical participation. Nevertheless, there can be no assurance that the specific funding levels associated with the System's future participation in this program will be maintained at or near historical levels, or that the program will not ultimately be discontinued or materially modified. Distributions of the annual ICTF funding are generally disbursed in semiannual lump sums, the timing of which varies from year to year. Amounts outstanding for fiscal year 2014 totaled $41.0 million and are included in other current assets in the accompanying combined balance sheets. The fiscal year 2014 outstanding amount was received by the System in January 2015.

Significant operational improvements have been achieved since the formation of the System and management remains focused on continuing to improve operational efficiencies and growing revenue.

An important goal in the creation of the System was the solicitation of contributions from community donors who had previously not significantly supported Grady Memorial Hospital. To that end, the System has received multiple commitments totaling approximately $315 million through December 31, 2014 for contributions to support the System's significant need to improve its capital asset base. In particular, The Woodruff Foundation previously committed $200 million to the System for capital improvements to be used over an indefinite period as needed. These funds have been, and will be, directed to a number of important capital asset needs, including major clinical equipment upgrades, new information technology systems, and a new emergency department expansion and tower construction. These capital asset additions support the System's important strategic goals of improving clinical quality, attracting commercial and other insured patients, providing physicians and other clinicians clinical equipment that is consistent with current standards of care, and creating support systems that optimize effectiveness and efficiency in both clinical and nonclinical information reporting.

The System's ability to continue to pursue its safety net mission in a fashion consistent with otherwise-comparable institutions serving major metropolitan areas is dependent on a number of factors, the most important of which have been described above. A reasonably assured funds flow from the Counties, continued participation in the ICTF program at legacy levels (assuming no Medicaid expansion), achievement of continued operational improvement strategies, and enhanced community fund-raising support are all vital to the System's mission. Management believes that the System is well-positioned against the critical dependencies previously described, but also notes that any material variance from the System's expectations in any of these areas would have an associated material adverse effect on its financial condition and its results of operations.

(3) Other Current Assets

The composition of other current assets is as follows:

		December 31	
		2014	2013
		(In thousands)	
Prepaid expenses	$	10,169	12,045
Inventories		10,614	12,879
Due from state reimbursement programs		40,966	43,527
Other current assets		2,432	3,580
	$	64,181	72,031

(4) Assets Limited as to Use and Investment Income

The composition of assets limited as to use is as follows:

	Fair value hierarchy level (note 15)		December 31	
			2014	2013
			(In thousands)	
Internally designated for capital acquisition and other uses:				
Cash and cash equivalents	Level 1	$	31,428	1,441
Mutual funds	Level 1		1,135	484
			32,563	1,925
Held by trustee under escrow agreements:				
Cash and cash equivalents	Level 1		1,016	776
Insurance guaranty trust fund:				
Cash and cash equivalents	Level 1		8,040	7,824
Limited by donors for specific purposes:				
Cash and cash equivalents	Level 1		35,968	42,233
High yield mutual funds	Level 1		280	275
Common collective trust funds	Level 1		2,477	2,404
			38,725	44,912
		$	80,344	55,437

There were no transfers among Level 1, Level 2 and Level 3 during the years ended December 31, 2014 and 2013.

Investment income, net (of investment fees) represents interest and dividends and was $91,000 and $242,000 for the years ended December 31, 2014 and 2013, respectively.

(Continued)

(5) Property and Equipment, Net

A summary of property and equipment, net is as follows:

	December 31	
	2014	2013
	(In thousands)	
Land and land improvements	$ 2,765	2,765
Buildings, leasehold improvements, and fixtures	254,030	246,680
Equipment	187,269	175,775
Computer hardware and software	92,539	80,455
	536,603	505,675
Less accumulated depreciation and amortization	(252,154)	(207,965)
	284,449	297,710
Construction in progress	27,310	20,301
	$ 311,759	318,011

Depreciation expense for the years ended December 31, 2014 and 2013 totaled approximately $44.4 million and $44.3 million, respectively. Construction in progress at December 31, 2014 and 2013 principally consists of expenditures related to new construction and renovation of existing facilities. Current projects in process at December 31, 2014 are planned for completion at various dates through fiscal year 2016 at an estimated total remaining cost to complete of approximately $68.8 million.

Equipment under capital lease obligations at both December 31, 2014 and 2013, exclusive of amounts held under the Agreement, is approximately $7.8 million. Related accumulated amortization at December 31, 2014 and 2013 is $5.1 million and $4.3 million, respectively.

(6) Pledges Receivable, Net

A summary of pledges receivable, net is as follows:

		December 31 2014	December 31 2013
		(In thousands)	
Less than one year	$	38,720	28,676
One to five years		16,942	37,871
		55,662	66,547
Less:			
Unamortized discounts using a discount rate of 3.3% and 3.5% at December 31, 2014 and 2013, respectively		(775)	(1,288)
Allowance for doubtful pledges		(1,970)	(2,040)
	$	52,917	63,219

(7) Other Accrued Expenses

The composition of other accrued expenses is as follows:

		December 31 2014	December 31 2013
		(In thousands)	
Accrued salaries and benefits	$	31,364	36,438
Current portion of accrued postretirement benefit cost		705	1,032
Due to related party (note 17(a))		4,964	7,370
Other accrued expenses		28,102	31,311
	$	65,135	76,151

(Continued)

(8) Notes Payable

During 2009, the System entered into separate agreements with Emory University and Morehouse School of Medicine to convert certain accounts payable then due under healthcare services contracts (as described further in note 16) to long-term debt. Amounts outstanding are reflected as notes payable in the accompanying combined balance sheets and are as follows:

		December 31	
		2014	2013
		(In thousands)	
Note payable to Emory University, payable in monthly installments of $268,000, including imputed interest at approximately 6.3% per annum. Final payment is due on December 31, 2016.	$	6,591	9,663
Note payable to the Morehouse School of Medicine, payable in monthly installments of $95,000, including imputed interest at approximately 6.3% per annum. Final payment is due on December 31, 2016.		2,000	3,410
		8,591	13,073
Less:			
Allowance for interest		(405)	(892)
Current installments		(5,073)	(3,864)
Notes payable, less current installments	$	3,113	8,317

On January 23, 2015, outstanding amounts under the note payable to Morehouse School of Medicine were fully repaid.

(9) Insurance Programs

The System is self-insured for its general and professional liability insurance coverages. The System's self-insured retention is $5 million per claim. Commercial insurance has been obtained to provide for coverage in excess of the System's self-insured retention limits on a claims-made basis.

The general and professional self-insurance reserves included in the accompanying combined balance sheets, totaling $58.2 million and $58.6 million at December 31, 2014 and 2013, respectively, include estimates of the ultimate costs for both reported claims and claims incurred but not reported. The System has employed independent actuaries to estimate the ultimate costs of the settlement of such claims. Accrued general and professional liability costs have been discounted at 1.0% at both December 31, 2014 and 2013.

The System is self-insured for its workers' compensation liability exposures up to limits of $350,000 per claim. Commercial insurance has been obtained to provide for excess workers' compensation liability coverage. The related amounts recorded by the System in the accompanying combined balance sheets totaled $2.4 million (discounted at 1.0%) and $3.0 million (discounted at 1.0%) at December 31, 2014 and 2013, respectively.

(Continued)

The System sponsors a self-insured program for its employee health benefits up to limits of $250,000 per claim. The System recognized related reserves of approximately $2.6 million and $2.0 million in accrued medical benefits (included in other accrued expenses in the accompanying combined balance sheets), at December 31, 2014 and 2013, respectively. The reserves include estimates of the ultimate cost for claims incurred but not reported.

In the opinion of management, adequate provision has been made for losses that may occur from the asserted and unasserted claims for each of these self-insurance programs.

(10) Net Patient Service Revenue

The System has agreements with governmental and other third-party payors that provide for reimbursement to Grady Memorial Hospital at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between billings at established rates for services and amounts reimbursed by third-party payors. A summary of payment arrangements with major third-party payors is as follows:

Medicare – Substantially all acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to patient classification systems that are based on clinical, diagnostic, and other factors. Certain types of exempt services and other defined payments related to Medicare beneficiaries are paid based upon cost reimbursement or other retroactive-determination methodologies. Payments for cost reimbursable items are made at tentative rates, with final settlement determined after submission of annual cost reports by Grady Memorial Hospital and audits by the Medicare administrative contractors. Grady Memorial Hospital's cost reports have been audited and settled for all fiscal years through 2010. Revenue from the Medicare program accounted for approximately 29% and 31% of the System's net patient service revenue for the years ended December 31, 2014 and 2013, respectively.

Medicaid – Inpatient services rendered to Medicaid program beneficiaries are generally paid based upon prospective reimbursement methodologies established by the State of Georgia. Certain types of exempt services and outpatient services related to Medicaid beneficiaries are paid based upon cost reimbursement or other retroactive-determination methodologies. Payments for cost reimbursable items are made at tentative rates, with final settlement determined after submission of annual cost reports by the System and audits by the Medicaid fiscal intermediary. Grady Memorial Hospital's cost reports have been audited and settled for all fiscal years through 2011. The System also contracts with certain managed care organizations to receive reimbursement for providing services to Medicaid beneficiaries. Payment arrangements with these managed care organizations consist primarily of prospectively determined rates per discharge, discounts from established charges, or prospectively determined per diem rates. Revenue from the Medicaid program (excluding ICTF revenue) accounted for approximately 46% and 43% of the System's net patient service revenue for the years ended December 31, 2014 and 2013, respectively.

As described in note 2, the System participates in the state ICTF program (which for purposes of disclosure here also includes the System's participation in an ancillary program referred to as the Upper Payment Limit program). Net amounts received from the ICTF program are recognized as additional Medicaid inpatient reimbursement and, therefore, are reflected in net patient service revenue. The related net reimbursement benefit recognized by the System for the years ended December 31, 2014 and 2013 was approximately $88.0 million and $94.9 million, respectively. The fact that the System's fiscal year-end differs from the state fiscal year also drives certain timing differences in terms of ICTF funds received and to be received. The System's ICTF revenue is subject to retrospective adjustment in future periods based upon audits as required by the Centers for Medicare & Medicaid Services (CMS).

The System has also entered into other reimbursement arrangements providing for payment methodologies, which include prospectively determined rates per discharge, prospectively determined per diem amounts, and discounts from established charges.

With respect to reserves for third-party payor cost report audits and anticipated settlements, the System routinely provides such reserves through initial audit and final settlement of the related cost reports. The System has historically provided such reserves in recognition of the complexity of relevant reimbursement regulations and the volatility of related settlement processes. In any event, the System's estimates in this area will differ from actual experience, and those differences may be material.

During fiscal years 2014 and 2013, net patient service revenue increased by approximately $8.8 million and $5.2 million, respectively, due to the adjustment of previously estimated third-party payor reserves that are no longer necessary as a result of final settlements, years that are no longer subject to audits, reviews, and investigations, and new reserves established in accordance with the System's policy.

The composition of net patient service revenue (excluding charity care) is as follows:

	2014	2013
	(In thousands)	
Gross patient service revenue	$ 2,989,809	2,215,841
Less provisions for contractual and other adjustments	(1,910,540)	(1,321,716)
Less provision for uncollectible accounts	(368,502)	(268,698)
Net patient service revenue	$ 710,767	625,427

As further described in both notes 1 and 2, the System is the principal safety net healthcare provider for the Atlanta metropolitan area. As a result, the System provides significant amounts of healthcare services to a large number of uninsured citizens in the region, the majority of whom do not have the means to pay for the cost of services provided. Consistent with the System's mission, all patients are served without regard to ability to pay and charity care is offered to all in accordance with the System's financial assistance policies. While a significant number of uninsured patients apply and qualify for financial assistance, a large population of uninsured patients that are cared for by the System (especially those provided emergency care) does not qualify for financial assistance, and therefore, the System also incurs significant amounts of bad debt expense related to the charges for services provided.

The System recognizes patient service revenue associated with services provided to patients with third-party payor coverage on the basis of contractual rates for the services rendered. For uninsured patients who do not qualify for community financial aid, the System recognizes revenue on the basis of its discounted rates for services provided. On the basis of historical experience, a significant portion of the System's uninsured patients are unable or unwilling to pay for the services provided. Thus, the System records a significant provision for uncollectible accounts related to uninsured patients in the period the services are provided. Patient service revenue, net of contractual allowances and discounts (but before the provision for uncollectible accounts), recognized during the years ended December 31, 2014 and 2013 from these major payor sources, is as follows:

		2014		
		Third-party payors	Self-pay	Total
			(In thousands)	
Patient service revenue, net of contractual adjustments and discounts	$	693,502	385,767	1,079,269

		2013		
		Third-party payors	Self-pay	Total
			(In thousands)	
Patient service revenue, net of contractual adjustments and discounts	$	611,535	282,590	894,125

The System provides services to patients who do not have the ability to pay and who qualify for charity services pursuant to established policies of the System. Charity services are defined as those for which patients have the obligation and willingness to pay but do not have the financial wherewithal to do so. The System does not include charity care in net patient service revenue. The cost of charity care provided totaled $97.6 million and $117.6 million for the years ended December 31, 2014 and 2013, respectively. The System estimated these costs by applying a ratio of cost to gross charges to the gross uncompensated charges associated with providing care to charity patients.

The System incurred bad debt expense, valued at established charges, of $368.5 million and $268.7 million for the years ended December 31, 2014 and 2013, respectively. In an effort to improve amounts collected from uninsured patients that do not apply and/or qualify for charity assistance, the System offers discounted prices to the uninsured. In addition to charity care and bad debt write-offs, the System provided discounts to the uninsured of $215.0 million and $93.0 million (recorded as discounts in net patient service revenue) for the years ended December 31, 2014 and 2013, respectively.

The Health Information Technology for Economic and Clinical Health (HITECH) Act was enacted as part of the American Recovery and Reinvestment Act of 2009 and signed into law in February 2009. In the context of the HITECH Act, the System must implement a certified Electronic Health Records (EHR) technology in an effort to promote the adoption and "meaningful use" of health information technology (HIT). The HITECH Act includes significant monetary incentives and payment penalties to encourage the adoption of EHR technology. The System anticipates that its current efforts at implementing an enterprise-wide EHR technology will enable its compliance with the meaningful use objectives mandated in the HITECH legislation. During fiscal year 2013, the System recognized approximately $2.0 million in incentive payments under the Georgia Medicaid EHR incentive payment program related to its efforts at

(Continued)

implementing a certified EHR technology. During fiscal years 2014 and 2013, the System recognized approximately $0.9 million and $1.3 million, respectively, in incentive payments under the Medicare EHR incentive payment program. The incentive payments are included as other operating revenue in the accompanying combined statements of operations.

(11) Employee Benefits Plans

(a) Postretirement Medical Plan

The System provides retiree medical benefits covering all employees of the System who previously retired at age 55 or older with at least 10 years of service. In fiscal year 2008, the System amended this plan to limit availability of retiree medical benefits to current employees aged 50 or older on September 4, 2008 and who retire at age 62 or older with at least 10 years of service. The cost of providing most of these benefits is shared with the retirees. The plan is unfunded, and therefore, the System's participation is on a "pay-as-you-go" basis.

The plan was amended effective May 1, 2013, the terms of which generally provide that Medicare-eligible employees are no longer eligible for retiree medical benefits under the postretirement benefit plan. Consequently, during 2013 the System began providing a retiree Health Reimbursement Account (HRA) for each Medicare-eligible individual in the plan. The fiscal year 2013 HRA allocation for each retiree was $650, which was reduced to $325 for fiscal year 2014. The financial impact of the plan amendments was recognized in the System's fiscal year 2014 and 2013 combined financial statements, resulting in a $4.0 million and $40.0 million decrease in accrued postretirement benefit cost at December 31, 2014 and 2013 respectively, and a $12.1 million and $7.5 million increase in 2014 and 2013 operating income, respectively, through a reduction in net periodic benefit cost. The plan amendments had no significant impact on cash flows from operations for the years ended December 31, 2014 and 2013. A discount rate of 3.35% was used to remeasure obligations at the amendment date.

The changes in the accumulated postretirement benefit obligation (APBO) during the years ended December 31, 2014 and 2013 are as follows:

		December 31	
		2014	2013
		(In thousands)	
APBO, beginning of year	$	11,283	51,794
Service cost		254	740
Interest cost		355	751
Plan participant contributions		308	674
Plan amendments		(3,979)	(39,972)
Benefits paid		(921)	(1,260)
Actuarial gain		(1,685)	(1,444)
APBO, end of year	$	5,615	11,283

(Continued)

The APBO amounts recognized in the accompanying combined balance sheets are as follows:

		December 31	
		2014	2013
		(In thousands)	
Current liabilities	$	705	1,032
Long-term liabilities		4,910	10,251
Amount recognized	$	5,615	11,283

The amounts accumulated in unrestricted net assets are as follows:

		December 31	
		2014	2013
		(In thousands)	
Prior service credit	$	(33,749)	(41,901)
Net gain		(2,365)	(1,155)
	$	(36,114)	(43,056)

The total amount of prior service credit and actuarial net gain expected to be amortized into net periodic postretirement benefit cost in 2015 is a net credit of $13.4 million.

Weighted average assumptions used to determine benefit obligations in the accompanying combined balance sheets are as follows:

	December 31	
	2014	2013
Discount rate	2.20%	3.92%
Rate of compensation increases	N/A	N/A

The components of net periodic postretirement benefit (credit) cost are as follows:

		Year ended December 31	
		2014	2013
		(In thousands)	
Service cost	$	254	740
Interest cost		355	751
Amortization of prior service credit		(12,131)	(9,468)
Amortization of net gain		(475)	—
Net periodic postretirement benefit credit	$	(11,997)	(7,977)

(Continued)

Weighted average assumptions used to determine net periodic postretirement benefit credit are as follows:

	Year ended December 31	
	2014	2013
Discount rate	3.92%	3.80%
Expected long-term rate of return on plan assets	N/A	N/A
Rate of compensation increases	N/A	N/A

Assumed healthcare cost trend rates are as follows:

2015	7.10%
2016	7.00
2017	6.80
2018	6.60
2019–2026	Reduce by 0.20% per year
2027	4.90
2028 and thereafter	4.50

Changes in assumed healthcare cost trend rates may impact the amounts reported for postretirement healthcare benefits. A 1% increase in the healthcare cost trend rate would increase the APBO by approximately $223,000 and increase interest and service cost by approximately $15,000. A 1% decrease in the healthcare cost trend rate would decrease the APBO by approximately $214,000 and reduce interest and service cost by approximately $15,000.

Expected Future Benefit Payments

Future benefit payments (in thousands) are expected to be paid as follows.

Payable in fiscal year:		
2015	$	705
2016		836
2017		909
2018		1,007
2019		957
2020–2024		2,170

(b) *Defined Contribution Savings Plan*

The System sponsors a defined contribution savings plan, which covers substantially all of its employees. Total matching contributions made and accrued under the savings plan totaled approximately $6.5 million and $5.2 million for the years ended December 31, 2014 and 2013, respectively.

Beginning January 1, 2009, the deferred retirement savings program changed from the previous 403(b) plan sponsored by the Authority to a 401(k) Plan sponsored by the System. The System matches employee contributions dollar for dollar up to 4% of eligible employees' base compensation after completion of one year of eligible service. Employees are immediately fully vested in matching contributions.

(12) Leases

As previously described in note 1, the Agreement was determined to be a capital lease obligation under relevant accounting literature. Additionally, the System has also entered into certain other noncancelable medical equipment leases, determined to be capital lease obligations under relevant accounting literature, which expire at various dates through 2019. Future minimum payments under these capital lease obligations at December 31, 2014 are as follows (in thousands):

		The Agreement	Other
Payable in fiscal year:			
2015	$	2,500	778
2016		2,500	663
2017		2,500	663
2018		2,500	663
2019		2,500	552
Thereafter		71,042	—
		83,542	3,319
Less:			
Interest cost		(51,169)	(433)
Current portion		(251)	(622)
	$	32,122	2,264

The System has also entered into certain noncancelable leases for office space and office equipment, determined to be operating leases under relevant accounting literature, which expire at various dates through 2025. Total rent expense recognized for the years ended December 31, 2014 and 2013 was approximately $7.3 million and $5.8 million, respectively, principally for building and equipment rentals.

Future minimum payments due under noncancelable operating leases as of December 31, 2014 are as follows (in thousands):

Payable in fiscal year:		
2015	$	3,035
2016		3,232
2017		3,210
2018		2,793
2019		2,705
Thereafter		8,766
	$	23,741

(13) Temporarily Restricted Net Assets

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

		December 31	
		2014	2013
		(In thousands)	
Capital improvements	$	86,323	102,933
Fund-raising and other programs		6,285	6,031
	$	92,608	108,964

(14) Business and Credit Concentrations

The System grants credit to patients, substantially all of whom reside in the System's service area. The System generally does not require collateral or other security in extending credit to patients; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits payable under their health insurance programs, plans, or policies (e.g., Medicare, Medicaid, preferred provider arrangements, and commercial insurance policies).

The composition of patient accounts receivable, net balance by payor type is as follows:

	December 31	
	2014	2013
Medicare	30%	30%
Medicaid	31	27
Commercial and other third-party payors	33	38
Patients	6	5
	100%	100%

(Continued)

(15) Fair Value of Financial Instruments

The System's estimates of fair value for financial assets and liabilities are based on the framework established in ASC 820, *Fair Value Measurement*, which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This framework is based on the inputs used in valuation and gives the highest priority to quoted prices in active markets and requires observable inputs to be used in the valuations when available. The disclosure of fair value estimates in the ASC 820 hierarchy is based on whether the significant inputs into the valuation are observable. In determining the level of the hierarchy in which the estimate is disclosed, the highest priority is given to unadjusted quoted prices in active markets and the lowest priority to unobservable inputs that reflect the System's significant market assumptions. The three levels of hierarchy are as follows:

Level 1 – Valuations based on unadjusted quotes market prices for identical assets or liabilities in active markets

Level 2 – Valuations based on pricing inputs that are other than quoted prices in active markets, which are either directly or indirectly observable. Examples include quoted prices in active markets for underlying assets, quoted prices for similar asset or liabilities in active markets, quoted prices for identical or similar assets or liabilities in an inactive market, or valuations based on models where significant inputs are observable or can be corroborated by observable market data

Level 3 – Valuations are derived from other valuation methodologies, including pricing models, discounted cash flow models, and similar techniques. Level 3 valuations incorporate certain assumptions and projections that are not observable in the market and require significant professional judgment in determining the fair value assigned to such asset or liabilities.

The hierarchy requires the use of observable market data when available. As required by ASC 820, assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

The fair value hierarchy of the System's assets limited as to use is disclosed at note 4. Fair value disclosures of the System's remaining financial instruments is as follows:

(a) Cash and Cash Equivalents

Cash and cash equivalents include short-term financial instruments whose carrying values approximate fair value, classified as Level 1 within the fair value hierarchy, given short-term maturity of these instruments

(b) Beneficial Interest in Net Assets Held by Others

The carrying value of the System's beneficial interest in funds held by the Authority is adjusted annually for changes in fair value. The fair value of these funds is included in beneficial interest in net assets held by others in the combined balance sheets on December 31, 2014 and 2013 at $15.8 million and $15.5 million, respectively. The majority of the related assets are investments in listed fixed income and equity securities, which are classified as Level 1 within the fair value hierarchy.

(c) Pledges Receivable, Net

Pledges receivable for current year gifts are initially measured at fair value in the year the receivable is recorded based on the present value of future cash flows discounted at a rate commensurate with the risks involved, which is an application of the income approach. Current year gifts included in pledges receivable reflected at fair value at December 31, 2013 totaled approximately $2.0 million, and are classified as Level 3 within the fair value hierarchy. No gifts were received during the year ended December 31, 2014.

(d) Patient Accounts and Grants Receivable, Accounts Payable, Due to Medical Schools, and Other Accrued Expenses

The carrying amounts of patient accounts and grants receivable, accounts payable, due to medical schools and other accrued expenses approximate fair value, classified as Level 1 within the fair value hierarchy, because of the short-term maturity of these instruments.

(e) Capital Lease Obligations

The carrying value of capital lease obligations approximates fair value based on the discount rate and the remaining terms of the leases. The most significant of such inputs are considered to be Level 3 inputs.

(16) Affiliation with Medical Schools

Grady Memorial Hospital serves as one of the largest teaching hospitals in the state of Georgia. In that respect, the System has contracts with both Emory University (Emory) and the Morehouse School of Medicine (Morehouse) (collectively, the Medical Schools), wherein practicing interns and residents of the Medical Schools receive clinical training at Grady Memorial Hospital. The teaching services provided to the interns and residents are provided primarily by faculty members of the Medical Schools in addition to other clinical and administrative services, which they provide to Grady Memorial Hospital. The Medical Schools are compensated for the costs of interns and residents effectively at cost. The Medical Schools are compensated for the faculty teaching, administrative, and clinical services based on certain formulas that consider the number of interns and residents taught, time spent performing administrative services and otherwise unreimbursed clinical services, and consider fair market value of compensation rates by specialty and ranking. Additionally, the System has agreed to fund other costs specifically associated with the ongoing provision of physician services by the Medical Schools, including the cost of professional liability exposures and the funding of intergovernmental transfers to enable the receipt of related Medicaid program supplemental payments for physician services billed by the Medical Schools. A new contract with Emory was entered into on June 1, 2013. This contract expires on May 31, 2018. The Morehouse contract expires on January 15, 2018. Net expenses for direct physician services under these contracts totaled approximately $113.0 million and $96.6 million for the years ended December 31, 2014 and 2013, respectively, and are included in supplies and other expenses in the accompanying combined statements of operations.

(17) Related Party Transactions

(a) HSOC, Inc.

With the execution of the Agreement (note 1), HSOC, Inc. (HSOC) committed to a total of $15 million of donated capital for capital improvements to Hughes Spalding Children's Hospital (Hughes

Spalding). The System has a contract with HSOC, a nonprofit affiliate of Children's Healthcare of Atlanta (CHOA), whereby HSOC provides certain management, administrative, and related services to Hughes Spalding for an initial term of 15 years beginning in February 2006. The contract requires that Hughes Spalding operate under the name "Children's Healthcare of Atlanta at Hughes Spalding." HSOC is responsible for the costs of operating Hughes Spalding. The System has a commitment of $2 million of specific annual support for the operation of Hughes Spalding and CHOA has a matching support commitment of $2 million annually. Additionally, the System is responsible for 50% of the Hughes Spalding "Excess/Deficit" (as defined) up to a total of $2 million annually, not to exceed $4 million in any successive rolling three-year period. The System maintains ownership of Hughes Spalding, including ownership of Hughes Spalding's certificate of need, licensure, and provider agreements. The System provided support for Hughes Spalding totaling $2.6 million during the years ended December 31, 2014 and 2013 in fulfilling its annual support commitment. Hughes Spalding also received $2.6 million from CHOA during the years ended December 31, 2014 and 2013 related to its annual support commitment. Amounts due to HSOC were $5.0 million and $7.4 million as of December 31, 2014 and 2013, respectively, and are included in other accrued expenses in the accompanying combined balance sheets.

The management agreement also gives CHOA the right to acquire Hughes Spalding, subject to a lease/purchase negotiation with the System and other terms and conditions. Any such option, if elected, contemplates a reversionary interest on the part of the System and other System involvement in HSOC's potential ownership of Hughes Spalding, which would be subject to additional negotiation as well. The agreement also contemplates that, given the $15 million in original donations by HSOC and other ongoing consideration under the agreement as described above, there would be no further economic consideration required in the exercise of the HSOC option. Given the significant uncertainties associated with the potential future exercise of the HSOC option, there is no current recognition of the option in the System's combined financial statements.

(b) Fulton-DeKalb Hospital Authority

During both the years ended December 31, 2014 and 2013, $2.5 million of lease payments were provided to the Authority in accordance with the Agreement (note 1). As required by the Agreement, at the conclusion of the "lease years" ended May 31, 2014 and 2013, no excess funds were applied toward the Authority's pension obligation. On August 17, 2012, the System and the Authority entered into an agreement whereby the Authority will fund a minimum of $0.7 million annually towards the pension obligation. As of December 31, 2014, no amounts were due to the Authority under the System's annual funding obligation.

(18) Line of Credit

The System has historically maintained a line-of-credit facility with a commercial bank, which serves as bridge financing when needed for the System's intergovernmental transfer (IGT) funding requirements for the ICTF program (note 10) and as a general revolving working capital facility. The working capital component provides $20 million of non-IGT funding capacity, while the ICTF program component provides $25 million of IGT funding. In total, the facility is currently estimated at $45 million. On November 21, 2014, the System obtained a renewal of this facility which expires on November 30, 2015.

Amounts outstanding under the working capital and ICTF program components accrue interest at one-month LIBOR plus 170 basis points and 145 basis points, respectively. The working capital component carries a 20 basis point commitment fee on the unused line, while the ICTF program component carries a commitment fee of 10 basis points against each associated draw. No amounts were due under the facility at both December 31, 2014 and 2013.

KPMG LLP
Suite 2000
303 Peachtree Street, N.E.
Atlanta, GA 30308-3210

The Audit and Compliance Committee
Grady Memorial Hospital Corporation
Atlanta, Georgia

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 combined financial statements of Grady Memorial Hospital Corporation and affiliate (the System), which comprise the combined balance sheet as of December 31, 2014, and the related combined statements of operations, changes in net assets, and cash flows for the year then ended, and the related notes to the combined financial statements, and have issued our report thereon dated April 30, 2015.

Internal Control over Financial Reporting

In planning and performing our audit of the combined financial statements, we considered the System'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 combined financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System'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 the System's combined 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 combined 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 the System'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 System's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Atlanta, Georgia
April 30, 2015