BON SECOURS HEALTH SYSTEM, INC.
AND SUBSIDIARIES

Consolidated Financial Statements

August 31, 2015 and 2014

(With Independent Auditors' Report Thereon)

KPMG LLP
1 East Pratt Street
Baltimore, MD 21202-1128

Independent Auditors' Report

The Board of Directors
Bon Secours Health System, Inc. and Subsidiaries:

We have audited the accompanying consolidated financial statements of Bon Secours Health System, Inc. and its subsidiaries (the System), which comprise the consolidated balance sheets as of August 31, 2015 and 2014, and the related consolidated statements of operations and changes in unrestricted net assets, changes in net assets and cash flows for the years then ended and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

KPMG LLP is a Delaware limited liability partnership, the U.S. member firm of KPMG International Cooperative ("KPMG International"), a Swiss entity.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Bon Secours Health System, Inc. and its subsidiaries as of August 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

KPMG LLP

October 27, 2015

BON SECOURS HEALTH SYSTEM, INC.
AND SUBSIDIARIES

Consolidated Balance Sheets

August 31, 2015 and 2014

(In thousands)

Assets		2015	2014
Current assets:			
Cash and cash equivalents	$	184,901	143,625
Accounts receivable, net:			
Patient and third-party payors		407,566	463,345
Other		34,510	35,645
Total accounts receivable, net		442,076	498,990
Assets limited or restricted as to use		79,951	61,433
Inventories		55,262	59,090
Prepaid expenses and other current assets		26,616	40,679
Total current assets		788,806	803,817
Assets limited or restricted as to use, less current portion		1,182,371	1,089,334
Property, plant, and equipment, net		1,030,259	1,159,977
Goodwill and other assets, net		390,861	336,053
Total assets	$	3,392,297	3,389,181
Liabilities and Net Assets			
Current liabilities:			
Current portion of long-term debt	$	36,016	28,602
Accounts payable		166,669	199,878
Accrued salaries, wages, and benefits		156,453	159,647
Other accrued expenses		110,721	111,822
Total current liabilities		469,859	499,949
Long-term debt, less current portion		938,887	957,512
Other long-term liabilities and deferred credits		660,649	607,946
Total liabilities		2,069,395	2,065,407
Net assets:			
Unrestricted-controlling interest		1,016,540	1,028,084
Unrestricted-noncontrolling interest		259,591	241,773
Total unrestricted		1,276,131	1,269,857
Temporarily restricted		39,008	46,088
Permanently restricted		7,763	7,829
Total net assets		1,322,902	1,323,774
Total liabilities and net assets	$	3,392,297	3,389,181

See accompanying notes to consolidated financial statements.

BON SECOURS HEALTH SYSTEM, INC.
AND SUBSIDIARIES

Consolidated Statements of Operations and Changes in Unrestricted Net Assets

Years ended August 31, 2015 and 2014

(In thousands)

		2015	2014
Revenues:			
Net patient service revenue before bad debts	$	3,551,875	3,584,441
Provision for patient bad debts		(193,593)	(255,931)
Net patient service revenue		3,358,282	3,328,510
Other revenue		118,218	133,335
Total revenues		3,476,500	3,461,845
Expenses:			
Salaries, wages, and benefits		1,825,233	1,790,641
Supplies		577,496	576,569
Purchased services and other		775,648	804,786
Depreciation and amortization		148,934	131,723
Interest		33,232	34,553
Total expenses		3,360,543	3,338,272
Operating income from continuing operations		115,957	123,573
Nonoperating gains (losses), net:			
Nonoperating investment (losses) gains, net		(7,540)	85,702
Loss on early retirement of debt		(399)	(194)
Inherent contribution, net		6,185	—
Other nonoperating activities, net		(35,415)	(34,234)
Excess of continuing revenues over expenses		78,788	174,847
Loss on discontinued operations, net		—	(1,105)
Excess of revenues over expenses		78,788	173,742
Other changes in unrestricted net assets:			
Grants for capital		393	4,005
Net change in unrealized gains and losses on other-than-trading securities		(784)	(598)
Net assets released from restrictions used for purchase of property, plant, and equipment		6,700	6,980
Net change in equity of joint ventures		3,284	778
Distributions to noncontrolling interest owners		(5,478)	(7,679)
Pension and other postretirement adjustments		(68,214)	(21,208)
Transfers to affiliates and other changes, net		(8,415)	(9,834)
Increase in unrestricted net assets		6,274	146,186
Unrestricted net assets, beginning of year		1,269,857	1,123,671
Unrestricted net assets, end of year	$	1,276,131	1,269,857

See accompanying notes to consolidated financial statements.

BON SECOURS HEALTH SYSTEM, INC.
AND SUBSIDIARIES

Consolidated Statements of Changes in Net Assets

Years ended August 31, 2015 and 2014

(In thousands)

	Unrestricted net assets	Temporarily restricted net assets	Permanently restricted net assets	Total
Balance at August 31, 2013	$ 1,123,671	48,872	7,710	1,180,253
Excess of revenues over expenses	173,742	—	—	173,742
Grants and restricted contributions	—	10,853	156	11,009
Grants for capital	4,005	—	—	4,005
Net change in unrealized gains (losses) on other-than-trading securities	(598)	1,296	4	702
Investment income	—	152	—	152
Net assets released from restrictions used for purchase of property, plant, and equipment	6,980	(6,980)	—	—
Net assets released from restrictions used for operations	—	(7,869)	—	(7,869)
Net change in equity of joint ventures	778	—	—	778
Distributions to noncontrolling interest owners	(7,679)	—	—	(7,679)
Pension and other postretirement adjustments	(21,208)	—	—	(21,208)
Transfers to affiliates and other changes, net	(9,834)	(236)	(41)	(10,111)
Increase (decrease) in net assets	146,186	(2,784)	119	143,521
Balance at August 31, 2014	1,269,857	46,088	7,829	1,323,774
Excess of revenues over expenses	78,788	—	—	78,788
Grants and restricted contributions	—	11,074	702	11,776
Grants for capital	393	—	—	393
Net change in unrealized gains and losses on other-than-trading securities	(784)	(490)	(3)	(1,277)
Investment income	—	125	—	125
Net assets released from restrictions used for purchase of property, plant, and equipment	6,700	(6,700)	—	—
Net assets released from restrictions used for operations	—	(8,659)	(150)	(8,809)
Net change in equity of joint ventures	3,284	—	—	3,284
Distributions to noncontrolling interest owners	(5,478)	—	—	(5,478)
Pension and other postretirement adjustments	(68,214)	—	—	(68,214)
Inherent contribution – restricted	—	1,035	—	1,035
Deconsolidation of subsidiary	—	(3,390)	(615)	(4,005)
Transfers to affiliates and other changes, net	(8,415)	(75)	—	(8,490)
Increase (decrease) in net assets	6,274	(7,080)	(66)	(872)
Balance at August 31, 2015	$ 1,276,131	39,008	7,763	1,322,902

See accompanying notes to consolidated financial statements.

BON SECOURS HEALTH SYSTEM, INC.
AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended August 31, 2015 and 2014

(In thousands)

	2015	2014
Cash flows from operating activities:		
(Decrease) increase in net assets	$ (872)	143,521
Adjustments to reconcile (decrease) increase in net assets to net cash provided by operating activities:		
Loss on discontinued operations, net	—	1,105
Provision for bad debts	193,593	255,931
Depreciation and amortization, including $4,885 and $6,135 reported in nonoperating activities, net in 2015 and 2014, respectively	153,819	137,858
Amortization of deferred financing costs and bond premium/discount, net	(852)	(831)
Equity in income of joint ventures	(19,677)	(31,097)
Loss on deconsolidation of subsidiary	6,083	—
Distributions received from investments in joint ventures	16,664	45,386
Inherent contribution	(7,220)	—
Net realized/unrealized gains on certain investments and derivative instruments	14,817	(93,558)
Loss on early retirement of debt	399	194
Gain on sale of assets	(882)	(324)
Gain on sales of joint ventures	—	(12,046)
Unrealized gains on investment in joint venture	(9,975)	(7,071)
Pension and other postretirement adjustments	68,214	21,208
Grants received for capital expenditures	(393)	(4,005)
Contributions restricted by donor	(11,776)	(11,009)
Cash distributions to noncontrolling interest owners and affiliates	11,830	13,818
Cash (used in) provided by changes in assets and liabilities:		
Increase in accounts receivable	(200,691)	(270,119)
Decrease (increase) in inventories, prepaid expenses and other current assets	3,582	(8,284)
Decrease (increase) in goodwill and other assets, net	8,710	(1,589)
Increase in accounts payable and other current liabilities	13,977	11,851
Increase (decrease) in other long-term liabilities and deferred credits	3,013	(519)
Net cash provided by operating activities	242,363	190,420
Cash flows from investing activities:		
Investment in joint ventures	—	(13,490)
Cash assumed through RGH acquisition	1,148	—
Proceeds from sales of joint ventures	—	13,725
Cash disposed in Charity transaction	(12,224)	—
(Purchases) proceeds from sales of securities, net	(56,635)	33,499
Purchases of alternative investments and equity and fixed income commingled funds	(158,425)	(71,644)
Proceeds from sale of equity and fixed income commingled funds	88,850	43,700
Property, plant, and equipment additions, net of disposals	(154,781)	(202,567)
Payments related to interest rate swaps	(11,730)	(12,533)
Net cash used in investing activities	(303,797)	(209,310)
Cash flows from financing activities:		
Proceeds from issuance of long-term debt	80,500	26,900
Payments of long-term debt	(28,394)	(29,736)
Retirements of long-term debt	(68,664)	(30,320)
Payment of deferred financing fees	(1,071)	(413)
Grants received for capital expenditures	393	4,005
Proceeds from repayment of note receivable	120,000	—
Proceeds from contributions restricted by donors	11,776	11,009
Cash distributions to noncontrolling interest owners and affiliates	(11,830)	(13,818)
Net cash provided by (used in) financing activities	102,710	(32,373)
Net increase (decrease) in cash and cash equivalents	41,276	(51,263)
Cash and cash equivalents, beginning of year	143,625	194,888
Cash and cash equivalents, end of year	$ 184,901	143,625

Supplemental disclosures:
(a) Cash paid for taxes was $70 and $773 for 2015 and 2014, respectively.
(b) Entered into a capital lease of $5,540 in 2015 (none in 2014).

See accompanying notes to consolidated financial statements.

(1) Organization and Mission

(a) Organizational Structure

Bon Secours Health System, Inc., a Maryland nonprofit, nonstock membership corporation (BSHSI or the System), and all of the other entities that are controlled directly or indirectly by Bon Secours, Inc., a Maryland nonprofit, nonstock membership corporation (BSI) are described collectively as the System. BSI, which is the sole corporate member of BSHSI, has no healthcare operations. The System was organized in June 1983 to fulfill the healthcare mission of the United States Province of the Congregation of the Sisters of Bon Secours of Paris (Sisters of Bon Secours), a congregation of religious women of the Roman Catholic Church founded in France in 1824.

The Sisters of Bon Secours have ministered to the healthcare needs of people in the United States since 1881. To ensure the sustainability of the ministry into the future as well as to broaden their collaboration with the laity in areas of influence, the Sisters of Bon Secours petitioned the Vatican to establish Bon Secours Ministries, an entity comprised of both laypersons and Sisters of Bon Secours to oversee the Catholic healthcare ministry of BSHSI. Bon Secours Ministries, which is referred to as a "public juridic person" in the Catholic Church's *Code of Canon Law*, was established by the Vatican on May 31, 2006 with the specific responsibility to oversee (and, as appropriate, initiate) the healthcare ministries within the System and, in particular, BSHSI's Catholic identity and mission. This formal relationship with the Catholic Church and the specific ministry is commonly referred to as "sponsorship." The Sisters of Bon Secours formally transferred the responsibility of sponsorship of the System to Bon Secours Ministries on November 1, 2006. Since then, Bon Secours Ministries (of which the majority of its members are Sisters of Bon Secours) has provided an active presence of leadership and direction for BSHSI to ensure its operations and use of resources are aligned with the mission, values and fundamentals of Catholic social teaching.

The System's principal activities comprise health and nursing care services in the states of New York, Maryland, Virginia, Kentucky, South Carolina, and Florida.

(b) Acquisitions and Disposals

Bon Secours Charity Health System, Inc.

In May 2015, BSHSI entered into an Affiliation agreement with the Sisters of Charity and Westchester Medical Center (Westchester), which resulted in Westchester holding a 60% holding interest in Bon Secours Charity Health System (Charity) and BSHSI holding the remaining 40% interest in Charity. Prior to the transaction, Charity was a wholly owned subsidiary of BSHSI.

In connection with the transaction, Charity issued $122,324 of taxable bonds (the Charity bonds), of which approximately $120,000 of the proceeds were used by Charity to repay BSHSI a portion of the outstanding principal amount of certain intercompany loans previously made by BSHSI to Charity. An additional portion of the outstanding principal amount of such intercompany loans in the amount of $80,000 was deemed a capital contribution by BSHSI to Charity (the BSHSI capital contribution), and the remaining outstanding principal amount of such loans was forgiven by BSHSI. Westchester is the guarantor of the Charity bonds and BSHSI does not have any obligation with respect to the debt service on the Charity Bonds.

(In thousands)

After the transaction was completed, Westchester bears full responsibility for meeting all cash, working capital and other capital needs of Charity, including any operating losses determined on a cash basis, debt service obligations on all debt of Charity and all obligations of the Charity subsidiaries relating to the Archdiocese Plan. Any amounts contributed by Westchester to or on behalf of Charity shall be considered unsecured, subordinated loans from Westchester to Charity and shall not be considered equity contributions to Charity. In the event of a dissolution and liquidation of Charity, the distribution of net proceeds (if any, after payment of all of the liabilities of Charity, including amounts owed to Westchester) from such event shall be made first to repay the BSHSI capital contribution, and then remainder will be based on the respective ownership percentages.

As a result of the transaction, BSHSI deconsolidated the financial position and excluded the operating results of Charity in the consolidated statement of operations and changes in unrestricted net assets for the period of June 1, 2015 through August 31, 2015. BSHSI did not record a gain or loss in connection with the transaction. The assets, liabilities and net assets of Charity at the time of the deconsolidation, including the $120,000 proceeds of the Charity Bonds, were as follows:

Current assets	$	93,171
Property, plant and equipment, net		151,424
Other assets		6,729
Current liabilities		60,778
Long-term liabilities		134,232
Net assets		56,314

After the transaction date, BSHSI accounts for its interest in Charity under the equity method and includes its interest in Charity's excess of revenue over expenses in its consolidated statements of operations and changes in unrestricted net assets as other operating revenues. In addition, BSHSI is continuing to provide corporate services to Charity through December 31, 2015 with an option to extend on an annual basis. The System recorded other operating revenues of approximately $5,400 during the year ended August 31, 2015 related to the corporate services agreement.

Rappahannock General Hospital

In December 2011, BSHSI entered into an affiliation agreement with Chesapeake Health Services (CHS or RGH), pursuant to which BSHSI became a minority member of RGH. From 2011 to 2014, BSHSI made various capital contributions to RGH ($2,005 in 2014). As a result of these transactions, BSHSI's minority membership in RGH was 41% and its investment in RGH was $7,056 at August 31, 2014.

On December 31, 2014 (acquisition date), BSHSI acquired the remaining 59% interest in RGH and BSHSI did not transfer any consideration as part of this transaction. BSHSI accounted for this business combination under the acquisition method and recorded an inherent contribution of $6,185 since the fair value of the assets assumed exceeded the liabilities acquired. The results of RGH's operations have been included in the statement of operations and changes in unrestricted net assets commencing on the acquisition date. The assets, liabilities, and net assets of RGH on the acquisition date were as follows:

(In thousands)

Current assets	$	5,469
Property, plant and equipment, net		18,134
Other assets		8,873
Current liabilities		17,906
Long-term liabilities		640
Net assets		13,930

The following table represents the proforma financial information, assuming the deconsolidation of Charity and acquisition of RGH had taken place on September 1, 2013. The proforma financial information is not necessarily indicative of the results of operations as they would have been had the transactions been effective on September 1, 2013.

		Year ended August 31,	
		2015	**2014**
		(Unaudited)	
Revenues	$	3,126,762	3,026,724
Expenses		3,003,356	2,898,344
Operating income		123,406	128,380
Nonoperating (losses) gains		(37,484)	53,509
Excess of revenue over expenses		85,922	181,889

(c) Mission

The Mission of the System is to bring compassion to healthcare and to be good help to those in need, especially those who are poor and dying. As a system of caregivers, the System is committed to helping to bring people and communities to health and wholeness as part of the healing ministry of Jesus Christ and the Catholic Church.

The ministry of BSHSI aids those in need, particularly those who are sick and dying, by offering a wide variety of services, including acute inpatient, outpatient, pastoral, palliative, home health, nursing home, rehabilitative, primary and secondary care and assisted living, in Florida, Kentucky, Maryland, New York, South Carolina, and Virginia without regard to race, religion, color, gender, age, marital status, national origin, sexual orientation, veteran status, genetic information, disability or any other characteristic protected by applicable federal, state or local employment laws and/or regulations. Activities directly associated with this purpose are considered operating activities. Operating activities also include other incidental services that are closely related to healthcare.

(d) Community Benefits

The System exists to benefit the people in the communities it serves. In pursuing its mission, the System advocates for and provides services to help meet healthcare and related socioeconomic needs of poor and disadvantaged individuals and the broader community. The System provides services in the communities served by holistically ministering to its patients with respect and without regard to their ability to pay.

Programs and services for the uninsured and underinsured represent the financial commitment of the System to everyone in the community. The System's financial assistance policy ensures that all members of the community receive this basic human right to access healthcare.

The categories included as programs and services for the poor and disadvantaged are as follows:

(i) Charitable Services – Financially Disadvantaged Persons

The System provides care to patients regardless of their ability to pay for all or a portion of the charges incurred. This care is classified as charity care based upon the System's established policies. In accordance with the Catholic Health Association (CHA) guidelines, charity care represents the unpaid costs of free or discounted health services provided to persons who cannot afford to pay and who meet the organization's criteria for financial assistance.

In assessing a patient's ability to pay, the System utilizes generally recognized poverty income levels, financially supporting 100% of the healthcare services provided to patients with annual family income at or below 200% of the federal poverty guidelines. Additional assistance is provided by a reduction in charges for medically necessary services through a community service adjustment.

(ii) Charitable Services – State Programs

The System provides services to indigent patients under various state programs, including state Medicaid, that generally pay healthcare providers amounts that are less than the cost of the services provided to the recipients. Estimated unreimbursed costs of the care provided to these disadvantaged patients are also reported as charitable services.

(iii) Other Community Benefits

Other community benefits include community services for the poor and disadvantaged as well as the broader community. The programs cover a broad spectrum of services and are financially supported by the System:

- Primary care access – providing free community-based preventive and primary care services through free-standing clinics and mobile health vehicles;

(In thousands)

- Health screenings and immunizations – provision of free health screenings and immunizations for a variety of health conditions for women, children, and senior residents;
- Child programs – providing oral healthcare, asthma and childhood obesity interventions;
- Caregiver and senior programs – focused on support, health screenings, and services to assist older adult populations;
- Education – providing medical and other health professional programs;
- Leadership activities – a full-time community health leader is provided in each community served who works to expand community capacity, identify community health needs and address social health conditions.

The cost of charitable services and community benefits provided by the System is determined in accordance with the System's accounting policies. These costs are estimated by using the cost to charge ratio applied by Medicaid and other state programs as well as specific patient visits identified under the System's charity care policies. The estimated cost of these services is as follows for the years ended August 31, 2015 and 2014:

		2015	2014
Charitable services and other community benefits:			
Cost of services to financially disadvantaged persons	$	119,710	156,932
Unpaid cost of state programs (e.g., Medicaid) to financially disadvantaged persons		81,835	86,795
Cost of other community benefits		58,746	57,656
Total community benefits, at cost	$	260,291	301,383

(2) Significant Accounting Policies

(a) Principles of Consolidation

The consolidated financial statements include the accounts of all members of the corporate group controlled by BSHSI. Members of the corporate group include all entities that BSHSI directly or indirectly controls, even if the System has less than 50% of the ownership or membership interest in the entity. Investments in entities where the System holds 50% or less of an entity's operations and does not have operational control are recorded under the equity or cost method of accounting. The System has included its equity share of income or losses and changes in net assets from investments in unconsolidated affiliates in other revenue and changes in unrestricted net assets, respectively, in the accompanying consolidated statements of operations and changes in unrestricted net assets. All material intercompany transactions and account balances have been eliminated in consolidation.

(In thousands)

(b) Use of Estimates

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

In the years ended August 31, 2015 and 2014, the System recorded income of $10,448 and $9,878, respectively, related to expense reductions and increases in net patient service revenue as a result of the reassessment of various third-party payor settlement issues and changes in estimates associated with other operating assets and liabilities.

(c) Cash and Cash Equivalents

For purposes of the consolidated financial statements, cash and cash equivalents include investments in highly liquid debt instruments with original maturities of three months or less, excluding investments limited or restricted as to use.

(d) Accounts Receivable, net

Accounts receivable is presented net of allowances for uncollectible accounts. The System grants credits to patients and generally does not require collateral or other security. However, it routinely obtains assignment of patients' benefits under their health insurance policies. Most of the System's net patient service revenue is derived from third-party payment programs. Medicare, Medicaid, and Managed Care contracts comprise approximately 75% of the System's consolidated third-party payor revenue.

The respective percentages of amounts due from patients and third-party payors at August 31, 2015 and 2014 are as follows:

	2015	2014
Medicare	22%	25%
Medicaid	8	10
Commercial and managed care	43	43
Other, including self-pay	27	22
	100%	100%

In evaluating the collectibility of accounts receivable, the System analyzes historical collections and write-offs and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for bad debts and provision for uncollectible accounts. Management regularly reviews its estimate and evaluates the sufficiency of the allowance for bad debts. The System analyzes contractual amounts due from patients who have third-party coverage and provides an allowance for

(Continued)

(In thousands)

doubtful accounts and a provision for bad debts. For patient accounts receivable associated with self-pay patients, which includes those patients without existing insurance coverage for a portion of the bill, the Company records a significant provision for bad debts for patients that are unable or unwilling to pay for the portion of the bill representing their financial responsibility. Account balances are charged off against the allowance for doubtful accounts after all means of collection have been exhausted.

(e) Assets Limited or Restricted as to Use and Investment Income

Assets limited or restricted as to use include assets held by trustees under indentures, self-insurance trust arrangements, assets related to donor-restricted net assets, and assets designated by the board of directors over which it retains control and may, at its discretion, use for other purposes. The fair value of investments, with the exception of alternative investments, is based upon quoted market prices or other observable market inputs. The System elected to fair value its investments in its equity and fixed income commingled funds. Alternative investments are recorded under the equity method.

Unrealized gains or losses on trading securities are included in nonoperating investment gains, net. As of August 31, 2015 and 2014, all investments and assets limited or restricted as to use are designated as trading securities, except for certain foundation investments and trustee held funds, which are designated as other than trading securities.

Investment income on donor-restricted funds is recorded as an addition to donor-restricted net assets provided the income has been restricted by the donor. Investment income on trustee-held funds, professional/general liability, workers' compensation, and health benefit self-insurance funds is reported in other revenue for the years ended August 31, 2015 and 2014, respectively. All other investment income is reported within nonoperating investment gains, net.

(f) Inventories

Inventories, consisting primarily of pharmaceuticals and medical supplies, are stated at the lower of cost or market, principally on a first-in, first-out basis.

(g) Property, Plant, and Equipment, net

Property, plant, and equipment, net are recorded at cost or, if donated, at fair value on the date of receipt. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the accompanying consolidated financial statements. Estimated useful lives of the assets are as follows:

Buildings	20 to 50 years
Fixed equipment	10 to 20 years
Major movable equipment	5 to 10 years
Software	3 to 7 years

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support and are excluded from the excess of revenues over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit donor 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.

Interest cost is capitalized as part of the cost of constructing capital assets, net of any interest income earned on unexpended bond proceeds borrowed for a specific project, during the construction period. The System capitalizes the direct costs, including internal costs, associated with the implementation of new information systems for internal use. Capitalized amounts are amortized over the estimated lives of the software.

(h) Asset Impairment

The System regularly evaluates whether events or changes in circumstances have occurred that could indicate an impairment in the value of long-lived assets. In accordance with the provisions of the Accounting Standards Codification (ASC) Topic 360-10, *Impairment or Disposal of Long-Lived Assets*, if events or changes in circumstances indicate that the carrying value of an asset is not recoverable, the System's management estimates the projected undiscounted cash flows, excluding interest and taxes, of the related individual facilities to determine if an impairment loss should be recognized. The amount of impairment loss is determined by comparing the historical carrying value of the asset to its estimated fair value. Estimated fair value is determined through an evaluation of recent and projected financial performance of facilities using standard industry valuation techniques.

In addition to consideration of impairment upon the events or changes in circumstances described above, management regularly evaluates the remaining lives of its long-lived assets. If estimates are changed, the carrying value of affected assets is allocated over the remaining lives. In estimating the future cash flows for determining whether an asset is impaired and if expected future cash flows used in measuring assets are impaired, the System groups their assets at the lowest level for which there are identifiable cash flows independent of other groups of assets. No impairment charges were recorded during the years ended August 31, 2015 and 2014, respectively.

(i) Goodwill and Other Assets, Net

Goodwill represents the excess of the aggregate purchase price over the fair value of the net assets acquired in a business combination. ASC Topic 350, *Intangibles – Goodwill and Other*, requires that tangible and indefinite-lived assets, as well as goodwill, must be analyzed in order to determine whether their value has been impaired.

Goodwill is assessed annually for impairment at the reporting unit. The System first assesses qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two step goodwill impairment tests as described in Topic 350. The more–likely–than–not threshold is defined as having a likelihood of more than 50%. The System determined that it was not more likely than not that the fair value of its reporting unit was less than its carrying amount. Accordingly, the System concluded that goodwill was not impaired as of August 31, 2015 and 2014 without having to perform the two-step impairment test.

(In thousands)

Goodwill and other assets, net, consist of the following at August 31, 2015 and 2014:

		2015	2014
Goodwill, net	$	93,478	98,359
Investment in joint ventures (note 12)		224,678	158,953
Self insurance receivable		20,941	20,876
Other assets		15,005	18,538
Pledges and notes receivable		27,067	29,038
Deferred financing costs, net		9,692	10,289
Total goodwill and other assets, net	$	390,861	336,053

(j) Deferred Financing Costs, Net

Financing costs incurred in connection with the issuance of long-term debt have been capitalized and included in other assets. These costs are being amortized using the effective-interest method over the term of the related obligations. Accumulated amortization of long-term debt issuance costs amounted to $8,037 and $7,138 at August 31, 2015 and 2014, respectively.

(k) Leases

Lease arrangements, including assets under construction, are capitalized when such leases convey substantially all the risks and benefits incidental to ownership. Capital leases are amortized over either the lease term or the life of the related assets, depending upon available purchase options and lease renewal features. Amortization related to capital leases is included in the consolidated statements of operations and changes in unrestricted net assets within depreciation and amortization expense.

(In thousands)

(l) Other Long-Term Liabilities and Deferred Credits

Other long-term liabilities and deferred credits consist of the following at August 31, 2015 and 2014:

		2015	2014
Accrued pension liability (note 9)	$	390,094	314,225
Self-insurance liabilities		140,928	146,254
Environmental liabilities		10,968	14,657
Derivative instrument valuations (note 7)		54,050	62,986
Medical office building liabilities (note 13(e))		31,000	35,321
Other long-term liabilities		33,609	34,503
	$	660,649	607,946

(m) Donor-Restricted Gifts

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 gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction is satisfied, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the accompanying consolidated statements of operations and changes in unrestricted net assets as net assets released from restrictions. Such amounts are classified as other revenue or transfers for additions to property, plant, and equipment. Donor-restricted contributions whose restrictions are satisfied within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

(n) Net Assets

The System classifies net assets based on the existence or absence of donor-imposed restrictions. Unrestricted net assets represent contributions, gifts, and grants that have no donor-imposed restrictions or that arise as a result of operations. Temporarily restricted net assets are subject to donor-imposed restrictions that must or will be met either by satisfying a specific purpose and/or passage of time. Temporarily restricted net assets of $39,008 and $46,088 at August 31, 2015 and 2014, respectively, primarily consisted of pledges and funds received for capital projects, various healthcare programs, and community outreach programs. Approximately 75% of the temporarily restricted net assets will be expended for capital with the remaining 25% for operating purposes. Permanently restricted net assets are subject to donor-imposed restrictions that must be maintained in perpetuity. Generally, the donors of these assets permit the use of all or part of the income earned on related investments for specific purposes.

(o) Fair Values

The carrying values of financial instruments classified as current assets and current liabilities approximate fair values. The fair values of assets limited or restricted as to use, with the exception of

(Continued)

alternative investments, are based on quoted market prices or other observable inputs. Alternative investments are recorded under the equity method but approximate fair value. The System elected to record its investments in equity and fixed income commingled funds at fair value. See note 4 for additional disclosures of assets limited or restricted as to use. The carrying values of other long-term liabilities approximate fair values. See note 6 for the fair value of long-term debt.

(p) Net Patient Service Revenue

The System has agreements with third-party payors that provide for payments to the System at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at estimated net realizable amounts from patients, third-party payors, and others for services rendered, including retroactive adjustments under reimbursement agreements with third-party payors. Retroactive reimbursement adjustments are estimated in the period in which the related services are rendered and adjusted in future periods as final settlements are determined.

(q) Other Revenue

Other revenue includes income from equity investments in joint ventures (note 12), gains on sales of operating activities, grant revenues (including Meaningful Use-Health Information Technology for Economic and Clinical Health Act (HITECH) Stimulus Grants) (note 11), assisted living, capitated payments from insurance companies, earnings on funds held by bond trustees and cafeteria and meal sales.

(r) Other Nonoperating Activities, Net

Other activities, which are largely unrelated to the System’s primary mission, are recorded as other nonoperating gains (losses), include rental activities of medical office buildings, school of nursing, general donations, and fund-raising activities.

(s) Performance Indicator

The accompanying consolidated statements of operations and changes in unrestricted net assets include a performance indicator, excess of continuing revenues over expenses. Changes in unrestricted net assets that are excluded from the performance indicator, consistent with industry practice, include discontinued operations, net change in unrealized gains and losses on other-than-trading securities, permanent transfers of assets to and from unconsolidated affiliates for other than goods and services, pension and other postretirement adjustments, the System’s allocated share of joint ventures’ change in equity, distributions to noncontrolling interest owners, and contributions of long-lived assets (including assets acquired using contributions, which by donor restriction were to be used for the purpose of acquiring such assets).

(t) Discontinued Operations

The System accounts for discontinued operations under relevant accounting guidance, which requires that a component of an entity that has been disposed of or is classified as held-for-sale and has operations and cash flows that can be clearly distinguished from the rest of the entity be reported as discontinued operations. In the period that a component of an entity has been disposed of or classified as held-for-sale, the results of operations for prior periods are reclassified to discontinued operations in the accompanying consolidated statements of operations and changes in unrestricted net assets. The System recognized loss on discontinued operations of $1,105 for the year ended August 31, 2014, as the result of adjustments to certain liabilities for final settlements associated with the System's formerly discontinued operations.

(u) Income Taxes

The System and most of its subsidiaries (including certain joint venture entities) are exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended. The system accounts for uncertain tax positions in accordance with ASC Topic 740. The System's taxable subsidiaries have approximately $84,748 and $61,513 of net operating loss carryforwards as of August 31, 2015 and 2014, respectively, which expire in varying periods through 2035 and are available to offset future taxable income. The System's deferred tax assets are fully reserved at August 31, 2015 and 2014 as the System considers it more likely than not that these amounts will not be recognized. Any changes to the valuation allowance on the deferred tax asset are reflected in the year of the change.

(v) Derivative Instruments

ASC Topic 815, *Derivatives and Hedging*, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives) and for hedging activities. An entity is required to recognize all derivatives as either assets or liabilities in the consolidated balance sheets and measure those instruments at fair value. In addition, for those derivative instruments that meet the criteria of an effective hedge, the hedged item must also be recorded at its fair value, with the changes in fair value reflected in other changes in unrestricted net assets.

Derivative instruments, specifically interest rate swaps, are recorded on the consolidated balance sheets at their respective fair values and are included in other long-term liabilities and deferred credits. The System's current derivative instruments do not qualify for hedge accounting, and the changes in fair value of such derivative instruments are reflected in nonoperating investment gains, net in the accompanying consolidated statements of operations and changes in unrestricted net assets in the period of change. Net settlement payments made or received on nonqualifying derivatives are recorded as a component of nonoperating investment gains, net.

(w) Self-Insurance

Under the System's self-insurance programs (professional/general liability, workers' compensation, and employee health benefits), claims are reflected as based upon actuarial estimation, including both reported and incurred but not reported claims, taking into consideration the severity of incidents and the expected timing of claim payments. BSHSI shares certain insurance risks it has underwritten through the use of reinsurance contracts. Amounts that can be claimed from BSHSI's reinsurers are valued by an independent actuary and are included in other assets. Should BSHSI's reinsurers be unable to reimburse BSHSI for recoverable claims, BSHSI would still be liable to pay the claims; however, BSHSI contracts with various highly rated insurance carriers to mitigate this risk.

(x) Recently Issued Accounting Pronouncements

The Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This ASU establishes principles for reporting useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. Particularly, that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 is effective for fiscal year 2019. The System expects to record a decrease in net patient service revenue and a corresponding decrease in bad debt expense upon adoption of the standard.

In April 2015, the FASB issued ASU 2015-03, *Interest-Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs*. ASU 2015-03 requires companies to present debt issuance costs as a direct deduction from the carrying value of that debt liability. ASU 2015-03 is effective for BSHSI beginning September 1, 2016. Entities would apply the new guidance retrospectively to all prior periods (i.e., the balance sheet for each period is adjusted). The System is currently evaluating the effect of this standard on the System's consolidated financial statements.

In May 2015, the FASB issued ASU 2015-07, *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, which removes the requirement to categorize within the fair value hierarchy all investments whose fair values are measured at net asset value (NAV) under the practical expedient and also removes the requirement to make certain disclosures for these investments from the FASB's fair value measurement guidance. This ASU is effective beginning September 1, 2016 and the System is currently evaluating the effect of this standard on the System's consolidated financial statements and disclosures.

(y) Reclassifications

Certain reclassifications were made to 2014 amounts to conform to the 2015 presentation.

(In thousands)

(3) Property, Plant, and Equipment, Net

Property, plant, and equipment, net consist of the following at August 31, 2015 and 2014:

	2015	2014
Land	$ 78,802	80,984
Land improvements	38,445	47,496
Buildings	942,998	1,043,696
Fixed equipment	79,732	80,255
Major movable equipment	1,276,738	1,332,717
Leasehold improvements	111,409	88,250
Construction in progress	38,642	56,847
	2,566,766	2,730,245
Less accumulated depreciation	1,536,507	1,570,268
	$ 1,030,259	1,159,977

Included in construction in progress at August 31, 2015 and 2014 are costs mainly associated with new facility construction, and other facility renovations and expansion. The System anticipates expending an additional $82,445 in future periods to complete strategic capital projects. Depreciation expense for the System was $152,759 and $136,167 for the years ended August 31, 2015 and 2014, respectively.

(In thousands)

(4) Assets Limited or Restricted as to Use

The composition of assets limited or restricted as to use consists of the following at August 31, 2015 and 2014:

	2015	2014
Board-designated funds:		
Cash and cash equivalents	$ 93,181	59,740
Equity mutual funds	49,918	58,501
Equity commingled funds	51,143	50,951
Common and preferred stocks	237,420	221,496
Fixed income mutual funds	105,249	111,359
Fixed income commingled funds	169,238	122,375
U.S. government and agency securities	15,249	17,374
Corporate obligations	18,706	15,966
Alternative investments	375,372	338,914
Land and other investments, at cost	39	39
	1,115,515	996,715
Donor-restricted funds:		
Cash and cash equivalents	11,044	14,807
Equity mutual funds	2,074	2,387
Equity commingled funds	606	658
Common and preferred stocks	6,717	7,935
Fixed income mutual funds	2,007	2,142
Fixed income commingled funds	2,005	1,580
U.S. government and agency securities	737	812
Corporate obligations	1,021	1,337
Alternative investments	4,447	4,377
Land and other investments, at cost	23	24
	30,681	36,059
Funds held by indenture trustees:		
Cash and cash equivalents	5,421	7,456
Government and agency bonds	5,350	7,067
Corporate obligations	3,028	1,348
	13,799	15,871

(In thousands)

		2015	2014
Self-insurance funds:			
Cash and cash equivalents	$	8,346	7,375
Equity commingled funds		22,183	23,139
Common and preferred stocks		11,211	11,448
Fixed income mutual funds		—	24,778
Fixed income commingled funds		49,001	24,286
Alternative investments		11,586	11,096
		102,327	102,122
Assets limited or restricted as to use		1,262,322	1,150,767
Available for current liabilities		(79,951)	(61,433)
Long-term assets limited or restricted as to use	$	1,182,371	1,089,334

The portion of the System’s assets limited or restricted as to use available for current liabilities consists of the following at August 31, 2015 and 2014:

		2015	2014
Self-insurance programs	$	49,420	43,965
Foundation programs		10,686	12,877
Board-designated		19,845	4,591
	$	79,951	61,433

The System’s consolidated total return on assets limited or restricted as to use consists of the following for the years ended August 31, 2015 and 2014:

		2015	2014
Dividends and interest	$	7,560	7,663
Net realized gains on securities		24,492	36,088
Change in net unrealized gains and losses on securities		(36,498)	70,541
		(4,446)	114,292
Realized and unrealized losses on derivative instruments		(2,811)	(13,071)
	$	(7,257)	101,221

(In thousands)

Total return on assets limited or restricted as to use is classified in the accompanying consolidated financial statements as follows for the years ended August 31, 2015 and 2014:

		2015	2014
Nonoperating investment (losses) gains, net	$	(7,540)	85,702
Investment income, net on self insurance and trustee-held funds recorded as other revenue		1,435	14,665
Investment income and net change in unrealized gains and losses on other than trading securities in restricted net assets		(368)	1,452
Net change in unrealized gains and losses on other-than-trading securities		(784)	(598)
Total return on assets limited or restricted as to use	$	(7,257)	101,221

The System's ability to generate investment income is dependent in large measure on market conditions. The market value of the System's investment portfolio, as well as the System's investment income, have fluctuated significantly in the past and are likely to continue to fluctuate in the future. The System's investment portfolio assets are designated as trading securities as discussed in ASC Topic 320, *Investments – Debt and Equity Securities*. The System's entire portfolio is actively managed by third-party investment managers. Trading generally reflects active and frequent buying and selling, and trading securities are generally used with the objective of generating profits on short-term differences in price. As required by U.S. GAAP, realized and unrealized gains and losses on an investment portfolio designated as a trading portfolio are accounted for as nonoperating investment income and are included in excess of continuing revenues over expenses. Because of this designation as a trading portfolio, management anticipates fluctuations in excess of revenues over expenses.

At August 31, 2015 and 2014, the System had invested approximately $391,405 and $354,387, or 31.0% and 30.8%, respectively, of the portfolio in alternative investments, which are allocated between hedge funds of funds, real estate investment funds and long/short equity funds.

The hedge funds include two multi-strategy and two dedicated equity long/short hedge funds of funds. The investment objective of the multi-strategy funds is to achieve positive absolute returns with low volatility, achieved through investments with multiple underlying managers who are investing across various strategies. Strategies used within the multi-strategy hedge funds include, but are not limited to:

Equity Long/Short: Investment companies that maintain long and short positions in publicly traded equities in order to capture opportunities driven by the perception of securities or industries being over-or undervalued.

Credit/Distressed: Investment companies that focus mainly on opportunities in corporate fixed income securities that are in financial distress, or perceived distress, or are going through a restructuring or reorganization.

Event Driven: Investment companies that focus on identifying securities that would benefit from the occurrence of a major corporate event.

Global Macro: Investment companies that employ broad mandates to invest globally across all asset classes, including interest rates, currencies, commodities and equities, in order to benefit from market movements within various countries.

Relative Value: Investment companies that seek to identify valuation discrepancies between related securities, utilizing fundamental and quantitative techniques to establish equity, fixed income and derivative positions.

The objective of the dedicated long/short equity fund strategy is to achieve long-term equity market-like returns at a lower level of risk, achieved through investments solely in equity long/short managers.

(5) Fair Value of Financial Instruments

The System determines the fair values of its financial instruments based on the fair value hierarchy established in ASC Topic 820, *Fair Value Measurement*, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include cash and cash equivalents, debt and equity securities and mutual funds that are traded in an active exchange market, as well as government and agency securities.

Level 2: Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include debt securities with quoted market prices that are traded less frequently than exchange-traded instruments. This category generally includes certain equity mutual funds, corporate-debt securities, equity commingled funds, fixed income commingled funds, and interest rate swaps.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. This category generally includes certain private debt and equity instruments.

The following discussion describes the valuation methodologies used for financial assets and liabilities measured at fair value. The techniques utilized in estimating the fair values are affected by the assumptions used, including discount rates and estimates of the amount and timing of future cash flows. Care should be exercised in deriving conclusions about the System’s business, its value or consolidated financial position based on the fair value information of financial assets presented below.

Fair value estimates are made at a specific point in time, based on available market information and judgments about the financial asset, including estimates of timing, amount of expected future cash flows, and the credit standing of the issuer. In some cases, the fair value estimates cannot be substantiated by comparison to independent markets. In addition, the disclosed fair value may not be realized in the immediate settlement of the financial asset. In addition, the disclosed fair values do not reflect any premium or discount that could result from offering for sale at one time an entire holding of a particular financial asset. Potential taxes and other expenses that would be incurred in an actual sale or settlement are not reflected in amounts disclosed.

Fair values for the System's fixed maturity securities are based on prices provided by its investment managers and its custodian bank. Both the investment managers and the custodian bank use a variety of pricing sources to determine market valuations. Each designate specific pricing services or indexes for each sector of the market based upon the provider's expertise. The System's fixed maturity securities portfolio is highly liquid, which allows for a high percentage of the portfolio to be priced through pricing services.

Fair values of equity securities have been determined by the System from observable market quotations, when available. Private placement securities and other equity securities where a public quotation is not available are valued by using broker quotes.

Fair values for the System's interest rate swaps have been determined using pricing models developed based on the LIBOR swap rate and other observable market data. The values were determined after considering the potential impact of collateralization and netting agreements, adjusted to reflect nonperformance risk of both the counterparty and the System.

BSHSI elected to record equity and fixed income commingled funds using the fair value option contained within FASB ASC Topic 825, *Financial Instruments*, in prior years and continues to account for these investments at fair value.

(In thousands)

The following table presents the System's fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of August 31, 2015:

	Fair value	Fair value measurements at August 31, 2015 using Level 1	Level 2	Level 3
Assets limited or restricted as to use:				
Cash and cash equivalents	$ 117,992	117,992	—	—
Equity mutual funds	51,992	51,992	—	—
Equity commingled funds	73,932	—	73,932	—
Common and preferred stocks	255,348	255,348	—	—
Fixed income mutual funds	107,256	107,256	—	—
Fixed income commingled funds	220,244	—	220,244	—
Government and agency bonds	21,336	18,898	2,438	—
Corporate obligations	22,755	3,757	18,998	—
Assets limited or restricted as to use	$ 870,855	555,243	315,612	—
Liabilities:				
Interest rate swaps	$ 54,050	—	54,050	—
Total liabilities	$ 54,050	—	54,050	—

 (Continued)

(In thousands)

The following table presents the System's fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of August 31, 2014:

		Fair value	Fair value measurements at August 31, 2014 using		
			Level 1	**Level 2**	**Level 3**
Assets limited or restricted as to use:					
Cash and cash equivalents	$	89,378	89,378	—	—
Equity mutual funds		60,888	60,888	—	—
Equity commingled funds		74,748	—	74,748	—
Common and preferred stocks		240,879	240,879	—	—
Fixed income mutual funds		138,279	138,279	—	—
Fixed income commingled funds		148,241	—	148,241	—
Government and agency bonds		25,253	22,169	3,084	—
Corporate obligations		18,651	1,763	16,888	—
Assets limited or restricted as to use	$	796,317	553,356	242,961	—
Liabilities:					
Interest rate swaps	$	62,986	—	62,986	—
Total liabilities	$	62,986	—	62,986	—

During the year ended August 31, 2015, the System transferred $49,675 of Level 1 fixed income assets to Level 2 fixed income assets, due to a change in investment strategy for the System's investment portfolio. There were no significant transfers between Levels 1, 2 and 3 during the year ended August 31, 2014.

The System had no activity in Level 3 assets during the year ended August 31, 2015 and 2014.

The System has incorporated an Investment Policy Statement (IPS) into its investment program. The IPS, which has been formally adopted by the Board of Directors, contains numerous standards designed to ensure adequate diversification by asset category and geography. The IPS also limits investments by manager and position size, and limits fixed-income positions based on credit ratings, which serves to further mitigate the risks associated with the investment program. At August 31, 2015 and 2014, management believes that its investment positions are in accordance with the guidelines in the IPS.

(In thousands)

(6) Long-Term Debt

Long-term debt consists of the following at August 31, 2015 and 2014:

		2015	2014
Master Trust Notes and Hospital Revenue Bonds:			
Series 1992B and 1992C Virginia fixed rate term bonds payable in installments through August 2027; interest at 5.93%	$	56,743	61,043
Series 1995 Memorial Regional Medical Center fixed rate serial and term bonds payable in installments through August 2018; interest at 6.38% to 6.50%		12,400	16,050
Series 1996 Virginia fixed rate serial and term bonds payable in installments through August 2020; interest at 5.40% to 6.25%		7,895	9,210
Series 2002B Florida variable rate demand bond payable in installments beginning November 2017 through November 2026 subject to a fifteen day put provision; interest at 0.10% and 0.07% at August 31, 2015 and 2014, set at prevailing rates		4,250	4,250
Series 2002B Kentucky variable rate demand bond payable in installments through November 2026 subject to a fifteen day put provision; interest at 0.10% and 0.05% at August 31, 2015 and 2014, set at prevailing rates		11,225	11,975
Series 2008B-C Virginia fixed rate serial and term bond payable in installments through November 2042; interest at 4.50 to 5.25% at August 31, 2015 and 2014.		173,355	173,355
Series 2008A South Carolina variable rate demand bonds subject to a seven day put provision payable in installments beginning November 2032 through November 2042; interest at 0.01% and 0.05% at August 31, 2015 and 2014, set at prevailing rates		69,925	69,925
Series 2008D Virginia variable rate demand bonds subject to a seven day put provision payable in installments through November 2025; interest at 0.02% and 0.05% at August 31, 2015 and 2014, set at prevailing rates		102,875	106,955

(In thousands)

	2015	2014
Series 2008D South Carolina variable rate demand bonds subject to a seven day put provision payable in installments through November 2025; interest at 0.02% and 0.07% at August 31, 2015 and 2014, set at prevailing rates	$ 20,570	22,105
Series 2011 variable rate direct placement bonds payable in installments through November 2025; interest at 1.4% at August 31, 2014, set at prevailing rates	—	62,900
Series 2013 Kentucky fixed rate serial and term bonds payable in installments beginning November 2015 through November 2026; interest at 4.0% to 5.0%	39,075	39,075
Series 2013 South Carolina fixed rate serial bonds payable in installments beginning November 2015 through November 2029; interest at 3.75% to 5.0%	184,870	184,870
Series 2013 Virginia fixed rate serial bonds payable in installments beginning November 2016 through November 2030; interest at 4.0% to 5.0%	78,245	78,245
Series 2013B variable rate direct placement bonds payable in installments through November 2043; interest at 1.2% to 1.3% at August 31, 2015 and 1.1% to 1.3% at August 31, 2014, set at prevailing rates	58,455	59,420
Series 2013 New York variable rate term loan payable in installments beginning November 2016 through November 2020; interest at 1.0% at August 31, 2015 and 2014	23,900	26,900
Series 2014 Virginia variable rate term loan payable in installments beginning November 2016 through November 2026; interest at 1.28% at August 31, 2015, set at prevailing rates	58,260	—
Total Master Trust Notes and Hospital Revenue Bonds	902,043	926,278

(In thousands)

		2015	2014
Other debt secured by certain property, plant, and equipment:			
9.25% note payable to HUD, due April 2025	$	—	5,931
3.27% mortgage note payable due April 2050		22,126	—
3.00% note payable to Wells Fargo		575	900
Capital leases obligations (interest at 5.00-6.00%)		7,090	5,587
Notes payable		21,744	24,179
Other debt		97	97
Total other debt		51,632	36,694
Total debt		953,675	962,972
Add bond premium, net of accumulated amortization		21,228	23,142
		974,903	986,114
Less current portion		36,016	28,602
Long-term debt, less current portion	$	938,887	957,512

Master Notes have been issued by BSHSI on behalf of itself and certain affiliates who collectively constitute the Members of an Obligated Group created by a Second Amended and Restated Master Trust Indenture dated as of March 12, 2014, as restated, supplemented, and amended. Master Notes secure payment of principal and interest on various series of serial and term indebtedness issued for the benefit of the Members of the Obligated Group by various governmental issuers as well as the performance of certain agreements entered into with credit enhancers, liquidity providers, swap counterparties and certain banks, which have purchased indebtedness issued for the benefit of the Obligated Group. Each Master Note is a joint and several obligation of each Member of the Obligated Group and is secured by a pledge of such Member's unrestricted receivables. Approximately, 37.2% and 37.3% of the indebtedness secured by Master Notes was supported, as to payments of principal and interest, by bond insurance policies as of August 31, 2015 and 2014, respectively. Approximately, 22.8% and 30.0% of the indebtedness secured by the Master Notes was supported by letters of credit as of August 31, 2015 and 2014, respectively. Certain amounts of the indebtedness supported by letters of credit are also supported by bond insurance policies.

The Master Trust Indenture and certain other agreements require the Obligated Group to maintain minimum financial ratios, place restrictions on the disposition of assets, the incurrence of additional indebtedness and changes in members of the Obligated Group, and provide for the maintenance of certain trustee-held funds, among other things.

The Series 2002 Bonds, the Series 2008A Bonds and the Series 2008D Bonds are subject to optional tender by the bondholders, and in certain events, mandatory tender. Tendered bonds which are net remarketed will be purchased by a bank pursuant to a related letter of credit. No principal payments are due the bank with respect to such purchased Bonds until at least 367 days after the purchase date.

The Obligated Group has delivered letters of credit as additional security for the Series 2002 and 2008A Bonds. Pursuant to each letter of credit, the bank covenants to pay principal of and interest on the related series of Bonds. An existing bond insurance policy with respect to each series of such bonds will only pay principal of and interest on the related series of Bonds if the bank fails to pay pursuant to the letter of credit. The bank can, under certain circumstances, cause the cancellation of each bond insurance policy. The Obligated Group must repay the principal amount of the purchased Series 2002 Bonds and Series 2008A Bonds beginning on the 367th day after the purchase date in ten substantially equal semiannual installments (or if the bond insurance policy has been canceled, in six substantially equal semiannual installments). The Obligated Group must repay the principal amount of the purchased Series 2008D Bonds (x) pursuant to one of the letter of credit agreements, in eight substantially equal semiannual installments commencing on the first business day following the 367th day after the purchase date and (y) pursuant to two of the letter of credit agreements, in eight substantially equal quarterly installments commencing on the first March 31, June 30, September 30 or December 31 occurring at least eighteen months following the date the bank purchases the related bonds.

BSHSI issued separate Master Notes to secure its obligations to reimburse the various letter of credit banks. The letters of credit which secure the Series 2002 Bonds, the Series 2008A Bonds and the Series 2008D Bonds have stated expiration dates, which range from November 2017 to November 2019. BSHSI has historically been able to request and receive extensions of the stated expiration dates.

The Series 2013B Bonds (as hereinafter defined) were purchased by a financial institution for a stated term less than the maturity of such bonds.

On January 11, 2013, the South Carolina Jobs-Economic Development Authority, the City of Russell, Kentucky, the Economic Development Authority of Henrico County, Virginia and the Economic Development Authority of the City of Norfolk, respectively, issued their revenue bonds (referred to as the Series 2013 Bonds) in the aggregate principal amount of $302,190 and loaned the proceeds thereof to BSHSI. The proceeds were used to (i) pay or reimburse, or refinance certain indebtedness the proceeds of which were used by one or more of St. Mary's Hospital, located in Henrico County, Virginia, Memorial Regional Medical Center, located in Hanover County, Virginia, Maryview Hospital, located in Portsmouth, Virginia, DePaul Medical Center, Norfolk, located in Virginia, Mary Immaculate Hospital, located in Newport News, Virginia, Our Lady of Bellefonte Hospital, located in Russell, Kentucky, and St. Francis Hospital and St. Francis Women's & Family Hospital, both located in Greenville, South Carolina, for the payment of the costs of acquiring, constructing, equipping, expanding, enlarging and improving certain of their healthcare facilities and (ii) refinance, in current refunding transactions, four series of revenue bonds that were issued for the benefit of BSHSI and other Members of the Obligated Group, and that were outstanding in the aggregate principal amount of $326,025.

On July 11, 2013, the Virginia Small Business Financing Authority and the Economic Development Authority of Henrico County, Virginia issued $67,245 principal amount of its revenue bonds (referred to as the Series 2013B Bonds) and loaned the proceeds thereof to BSHSI and certain other Members of the Obligated Group. The proceeds were used to refinance, in current refunding transactions, two series of revenue bonds that were issued for the benefit of BSHSI and other Members of the Obligated Group, and

 (Continued)

that were outstanding in the aggregate principal amount of $67,245. The two series of Series 2013B Bonds have final maturities of November 1, 2025 and 2042, respectively, and were purchased by a financial institution (referred to as the Series 2013B Direct Purchase Bank) for an initial term of twelve years. During the initial term, the Series 2013B Bonds will bear interest based on a percentage of LIBOR plus an agreed–upon spread. With respect to the series maturing on November 1, 2042, following the expiration of the initial term, BSHSI may determine to seek an extension of the initial term, convert the interest rate mode on such Series 2013B Bonds or otherwise refinance such Series 2013B Bonds. Payment of the Series 2013B Bonds is secured by Master Notes issued under the Master Indenture. In connection with the issuance of the Series 2013B Bonds, the Obligated Group entered into separate covenant agreements with the Series 2013B Direct Purchase Bank, which contain various covenants that can be enforced or waived solely by the Series 2013B Direct Purchase Bank. Those covenants are similar to covenants BSHSI has provided to various other banks and insurance companies, which have provided credit enhancement with respect to BSHSI's other outstanding indebtedness. The obligations of the Obligated Group under the covenant agreement are secured by a Master Note.

Frances Schervier Home and Hospital (Schervier) is located in the Bronx, New York and directly controlled by BSHSI, but is not a member of the BSHSI Obligated Group. On November 21, 2013, Schervier borrowed $26,900 (referred to as the 2013 Term Loan) from a financial institution through a taxable term loan. The proceeds of the 2013 Term Loan, together with $4,500 of existing debt service reserve funds, were used to defease certain Series 1997 fixed rate bonds (referred to as the Schervier Bonds) issued by the Dormitory Authority of the State of New York (referred to as DASNY) that were outstanding in the principal amount $30,320. Schervier's scheduled payment obligations under the Schervier Bonds were secured by a Master Note. Schervier's scheduled payment obligations under the 2013 Term Loan are guaranteed by the Members of the Obligated Group pursuant to a guaranty agreement with U.S. Bank (the Schervier Guaranty). The Schervier Guaranty does not guarantee payment of principal or interest on the 2013 Term Loan upon an acceleration of the due date thereof by reason of an event of default under the agreement governing the 2013 Term Loan. In the event of any such acceleration, payments under the Schervier Guaranty will be required to be made only in such amounts and at such times as such payments would have been due had there been no acceleration of the 2013 Term Loan. The Schervier Guaranty is secured by a Master Note. In connection with the defeasance, BSHSI incurred a loss on extinguishment of debt of approximately $200 for the year ended August 31, 2014.

On October 31, 2014, BSHSI borrowed from the Economic Development Authority of the City of Norfolk the proceeds of a series of revenue bonds (referred to as the Series 2014 Bonds) issued by the Norfolk EDA in the principal amount of $58,260. The Series 2014 Bonds bear interest at a variable rate equal to the sum of a percentage of LIBOR plus an agreed-upon spread. The proceeds of the Series 2014 Bonds were used to refinance, in a current refunding transaction, the Series 2011 Bonds. BSHSI contributed equity in the amount of $4,700 to pay the November 15, 2014 principal payment as well as accrued interest on the Series 2011 Bonds. In connection with the issuance of the Series 2014 Bonds, BSHSI, as Credit Group Representative, entered into a Continuing Covenant Agreement with a financial institution (referred to as the Series 2014 Direct Purchase Bank), which purchased the Series 2014 Bonds. The Series 2014 Direct Purchase Bank has agreed to hold the Series 2014 Bonds until the maturity date, November 1, 2025, subject to the right of BSHSI to redeem the Series 2014 Bonds or to convert the Series 2014 Bonds to another interest rate mode.

(In thousands)

The covenants contained in the Continuing Covenant Agreement are similar to covenants BSHSI has provided to various financial institutions and insurance companies which have provided credit enhancement with respect to BSHSI's other outstanding indebtedness or have directly purchased revenue bonds issued for the benefit of the Obligated Group. The obligation of BSHSI to repay the Series 2014 Bonds and obligations of the Obligated Group under the Continuing Covenant Agreement are secured by separate Obligations issued under the Master Trust Indenture.

On March 19, 2015, Schervier Apartments, LLC (a BSHSI subsidiary) borrowed $22,240 under a 35-year 3.27% fixed rate nonrecourse Mortgage Note, with interest and principal payable in monthly installments. The Mortgage Note is insured by HUD pursuant to Section 223(f) of the National Housing Act, as amended, and is collateralized by land, buildings and equipment of Schervier Apartments, LLC. The proceeds of the Mortgage Note were used to 1) pay all debts and liabilities of Frances Schervier Housing Development Fund Corporation including a Mortgage Note in the amount of $5,763 and accounts payable to Schervier for past operating subsidies of $1,331; 2) pay all associated transactions fees and costs of issuance; and 3) fund escrow and replacement reserve accounts. The remaining proceeds of the Mortgage Note are to be used by Bon Secours New York Health System to develop additional services for seniors.

Scheduled principal repayments on long-term debt are as follows:

2016	$	35,998
2017		40,058
2018		35,379
2019		42,322
2020		37,396
Thereafter		762,522
Total	$	953,675

In May 2014, BSHSI executed a $100,000 revolving credit agreement with a five year term with a commercial bank (the Credit Agreement). Pursuant to the Credit Agreement, BSHSI, as Credit Group Representative, may either request loans or request that the bank issue letters of credit for the benefit of the Obligated Group. The proceeds of any such loan and any such letter of credit are available for general corporate purposes. As of August 31, 2015 and 2014, no loans have been made under the Credit Agreement. The obligations of the Obligated Group under the Credit Agreement are secured by a Master Note.

The System has entered into four leases maturing from 2019-2028 that are classified as capital leases for building and equipment. In addition, the System consolidates two limited liability corporations that own medical office buildings with notes payable outstanding of $21,744 and $23,919 as of August 31, 2015 and 2014, respectively. Such notes have an interest rate of 7.75% and maturity dates in 2021.

Total interest expense was $33,232 and $34,553 for the years ended August 31, 2015 and 2014, respectively. Cash paid for interest was $34,937 and $36,516 for the years ended August 31, 2015 and 2014, respectively, and includes capitalized interest for construction projects of $204 and $1,798, net of investment income, for the years ended August 31, 2015 and 2014, respectively.

(Continued)

(In thousands)

(7) Interest Rate Risk Management

The System uses fixed and variable-rate debt to finance capital needs and develop an appropriate debt structure. Variable-rate debt exposes the System to variability in interest expense due to changes in interest rates. Conversely, fixed-rate debt obligations can be more expensive to the System in times of declining interest rates. The System manages and monitors its cost of capital on a regular basis and from time to time enters into derivative instruments with financial institutions to help manage interest rate risk.

At August 31, 2015 and 2014, the System had eleven instruments, respectively, which did not qualify for hedge accounting treatment under ASC Topic 815. Fair value changes of these instruments were reported under nonoperating investment gains, net. The following is a summary of the derivative instruments in place at August 31, 2015:

Description	Number	Outstanding notional amount	Pay rates	Maturity dates	Collateral posted at August 31, 2015	Counterparties	Mark to market	Collateral thresholds
Fixed payer	1	$ 36,030	3.448%	Nov-2025	$ —	Goldman Sachs	$ (4,178)	10,000
Fixed payer	1	54,045	3.491%	Nov-2025	—	Deutsche Bank	(6,387)	20,000
Fixed payer	2	103,350	4.460%/3.420%	Aug-2026/Nov-2028	—	Merrill Lynch	(16,662)	*
Fixed payer	2	108,550	4.485%/3.384%	Oct-2025/Oct-2026	3,824	JP Morgan	(18,301)	15,000
Fixed payer	1	69,925	3.454%	Nov-2042	—	PNC Bank	(18,649)	*
	7	371,900			3,824		(64,177)	
Fixed basis	1	200,000	SIFMA	Jan-2029	—	Citigroup	6,358	20,000
Variable basis	3	444,750	SIFMA	Nov-2029	—	Merrill Lynch	694	*
Total derivatives	11	$ 1,016,650			$ 3,824		(57,125)	65,000
						Valuation adjustments	3,075	
							$ (54,050)	

* Derivative instrument does not provide for the posting of collateral.

(In thousands)

The following is a summary of the derivative instruments in place at August 31, 2014:

Description	Number	Outstanding notional amount	Pay rates	Maturity dates	Collateral posted at August 31, 2014	Counterparties	Mark to market	Collateral thresholds
Fixed payer	1	$ 38,580	3.448%	Nov-2025	$ —	Goldman Sachs	$ (4,542)	10,000
Fixed payer	1	57,870	3.491%	Nov-2025	—	Deutsche Bank	(6,952)	20,000
Fixed payer	2	109,775	4.460%/3.420%	Aug-2026/Nov-2028	—	Merrill Lynch	(17,723)	*
Fixed payer	2	113,000	4.485%/3.384%	Oct-2025/Oct-2026	4,698	JP Morgan	(19,626)	15,000
Fixed payer	1	69,925	3.454%	Nov-2042	—	PNC Bank	(15,924)	*
	7	389,150			4,698		(64,767)	
Fixed basis	1	200,000	SIFMA	Jan-2029	—	Citigroup	1,806	20,000
Variable basis	3	460,500	SIFMA	Nov-2029	—	Merrill Lynch	(4,828)	*
Total derivatives	11	$ 1,049,650			$ 4,698		(67,789)	65,000
						Valuation adjustments	4,803	
							$ (62,986)	

* Derivative instrument does not provide for the posting of collateral.

The unrealized gains of $8,919 and losses of $538 for the years ended August 31, 2015 and 2014, respectively, relating to these nonqualifying derivative activities are recorded within nonoperating investment gains, net in the accompanying consolidated statements of operations and changes in unrestricted net assets.

(In thousands)

The System utilizes a diversified group of swap counterparties and has sought to limit its obligations to post collateral in the agreements governing its derivative instruments. In addition, the System routinely evaluates its derivative portfolio and may decide at any time to terminate certain of the derivative instruments discussed above and/or enter into new derivative instruments. Should the System decide to terminate any of such instruments, it may be required to make termination or breakage payments under the terms of those instruments.

(8) Noncontrolling Interest

The following table presents a reconciliation of the changes in consolidated unrestricted net assets attributable to the System's controlling interest and noncontrolling interest, including amounts such as the performance indicator, change in pension and other postretirement adjustments and other changes in unrestricted net assets as of and for the years ended August 31, 2015 and 2014:

	Unrestricted net assets-controlling interest	Unrestricted net assets-non controlling interest	Total unrestricted net assets
Balance as of August 31, 2013	$ 901,618	222,053	1,123,671
Excess of continuing revenues over expenses	146,504	27,238	173,742
Grants for capital	4,005	—	4,005
Net change in unrealized gains and losses on other than trading securities	(598)	—	(598)
Net assets released from restrictions used for purchase of property, plant, and equipment	6,980	—	6,980
Net change in equity of joint ventures	778	—	778
Distributions to noncontrolling interest owners	—	(7,679)	(7,679)
Pension and other postretirement adjustments	(21,208)	—	(21,208)
Transfers to affiliates and other changes, net	(9,995)	161	(9,834)
Increase in net assets	126,466	19,720	146,186
Balance as of August 31, 2014	1,028,084	241,773	1,269,857

(In thousands)

		Unrestricted net assets-controlling interest	Unrestricted net assets-non controlling interest	Total unrestricted net assets
Excess of continuing revenues over expenses	$	56,607	22,181	78,788
Grants for capital		393	—	393
Net change in unrealized gains and losses on other than trading securities		(784)	—	(784)
Net assets released from restrictions used for purchase of property, plant, and equipment		6,700	—	6,700
Net change in equity of joint ventures		3,284	—	3,284
Distributions to noncontrolling interest owners		—	(5,478)	(5,478)
Pension and other postretirement adjustments		(68,214)	—	(68,214)
Transfers to affiliates and other changes, net		(9,530)	1,115	(8,415)
(Decrease) increase in net assets		(11,544)	17,818	6,274
Balance as of August 31, 2015	$	1,016,540	259,591	1,276,131

(9) Pension Plan

The System’s employees are covered either by one of the System’s noncontributory defined benefit pension plans, or are covered by defined contribution retirement plans. The System’s noncontributory defined benefit pension plans provide benefits based upon age at retirement, years of credited services, and average earnings. Seven of the System’s eight defined benefit plans are deemed church plans under the Internal Revenue Code. For defined benefit pension plans deemed to be church plans under the Internal Revenue Code, the System’s funding policy is to make contributions to fund the annual service cost of the plans plus a 15 year amortization of the unfunded Accumulated Benefit Obligation. The defined benefit pension plan that is subject to the Employee Retirement Income Security Act of 1974 guidelines is funded in accordance with those guidelines. The service cost and projected benefit obligation is based upon the projected unit credit actuarial method.

In July 2011, the System announced the closure of the defined benefit pension plans to all new employees. Existing defined benefit plan participants were given a choice option. This choice option allowed a one time election to maintain participation in the defined benefit pension plan or move to a defined contribution retirement plan.

(In thousands)

The investment policy and objectives for defined benefit plan assets are established by BSHSI and are based on a long-term perspective. An investment advisory firm engaged by BSHSI reviews asset performance and allocation on a periodic basis throughout the fiscal year. The percentage allocation to each asset class may vary depending upon market conditions and is adjusted when it falls outside the established ranges set for each asset class.

The following are deferred pension costs, which have not yet been recognized in periodic pension expense but are accrued in unrestricted net assets, as of August 31, 2015 and 2014. Unrecognized actuarial losses represent unexpected changes in the projected benefit obligation and plan assets over time, primarily due to changes in assumed discount rates and investment experience. Unrecognized prior service cost is the impact of changes in plan benefits applied retrospectively to employee service previously rendered. Deferred pension costs are amortized into annual pension expense over the expected average remaining assumed service period for active employees.

		Amounts in unrestricted net assets at August 31, 2015	Amounts in unrestricted net assets at August 31, 2014	Amounts in unrestricted net assets to be recognized in fiscal year 2016
Net prior service cost	$	58	48	(16)
Net actuarial losses		285,186	216,084	14,598
Total	$	285,244	216,132	14,582

(In thousands)

The components of the funded status, net periodic benefit costs, and actuarial assumptions used in accounting for defined benefit pension plans as of and for the years ended August 31, 2015 and 2014 are as follows:

		2015	2014
Change in projected benefit obligation:			
Net projected benefit obligation at beginning of year	$	979,940	850,444
Service cost		20,388	18,553
Interest cost		41,970	43,154
Actuarial loss		31,559	100,359
Gross benefits paid		(36,736)	(32,570)
Projected benefit obligation at end of year		1,037,121	979,940
Change in plan assets:			
Fair value of plan assets at beginning of year		665,715	560,217
Actual return on plan assets		(11,025)	108,710
Employer contributions		29,073	29,358
Gross benefits paid		(36,736)	(32,570)
Fair value of plan assets at end of year		647,027	665,715
Net amount recognized at end of year	$	390,094	314,225

		2015	2014
Accumulated benefit obligation at end of year	$	994,315	933,159
Amounts recognized in the consolidated balance sheets consist of:			
Accrued benefit costs – long term	$	(390,094)	(314,225)
Components of net periodic benefit cost:			
Service cost	$	20,388	18,553
Interest cost		41,970	43,154
Expected return on plan assets		(45,050)	(41,041)
Amortization of:			
Actuarial loss		17,299	11,146
Prior service cost		(10)	105
Transition asset		—	(7)
Total net periodic benefit costs	$	34,597	31,910

(Continued)

(In thousands)

	2015	2014
Weighted average assumptions used to determine benefit obligations at August 31:		
Discount rate	4.55%	4.30%
Rate of compensation increase	3.00	3.00
Weighted average assumptions used to determine net periodic benefit cost at August 31:		
Discount rate	4.30%	5.10%
Expected return on plan assets	7.80	7.80
Rate of compensation increase	3.00	3.00

Net pension expense is included as a component of fringe benefits recorded as salaries, wages, and benefits in the accompanying consolidated statements of operations and changes in unrestricted net assets.

The expected long-term rate of return of the pension plan assets used for determining pension expense was 7.80% and was determined based upon a review of the System's long-term rate of return experienced in the capital markets for the target asset allocation employed to invest pension assets.

As of August 31, 2015, BSHSI adopted the new RP-2014 Mortality Table with generational improvements using projection scale BB-2D. As a result of the adoption, the projected benefit obligation increased approximately $66,100.

As of August 31, 2015, BSHSI changed its methodology used to estimate the interest and service cost components of net periodic benefit costs to a spot rate approach for all defined benefit pension plans. Historically, BSHSI estimated the service and interest cost components using a single weighted average discount rate derived from a hypothetical portfolio of bonds used to measure the benefit obligation at the beginning of the period. BSHSI made this change to improve the correlation between projected benefit cash flows and the corresponding yield curve spot rates and to provide a more precise measurement of service and interest costs. This change did not impact the projected benefit obligation nor the net periodic benefit costs as of and for the year ended August 31, 2015. BSHSI accounted for this change as a change in estimate and, accordingly, will account for it prospectively starting with the year ending August 31, 2016. This change is expected to reduce the net periodic benefit costs during the year ending August 31, 2016 by approximately $7,500. This change does not affect the measurement of the projected benefit obligation as the change in the service cost and interest cost is completely offset in the actuarial (gain) loss reported.

In order to apply the spot rate approach, BSHSI also changed its methodology for determining the discount rate for its projected benefit obligation as of August 31, 2015 from a bond model approach to a yield curve approach because the bond model approach is not compatible with the spot rate approach. The change to the yield curve approach resulted in an increase of the projected benefit obligation at August 31, 2015 and a reduction of other changes in unrestricted net assets of approximately $5,640.

(In thousands)

The System's pension plan asset allocation is planned to include approximately 65% equities, 25% fixed income/cash, and 10% alternatives. Equity investments are balanced between type and size of investment and investment managers are monitored against benchmarks. As of August 31, 2015 and 2014, the pension plan assets were allocated by asset category as follows:

		2015	2014
Asset category:			
Equity mutual and commingled funds and securities	$	62%	63%
Fixed income mutual and commingled funds and securities		25	25
Alternative investments		10	9
Cash		3	3
Total	$	100%	100%

The following table presents the System's fair value hierarchy for the pension plan assets measured at fair value on a recurring basis as of August 31, 2015:

		Fair value	Fair value measurements		
			Level 1	Level 2	Level 3
Investments:					
Cash and cash equivalents	$	22,384	22,384	—	—
Equity mutual funds		4,145	4,145	—	—
Equity commingled funds		70,255	—	70,255	—
Common and preferred stocks		327,488	325,944	1,544	—
Fixed income commingled funds		50,616	—	50,616	—
Government and agency bonds		13,627	1,019	12,608	—
Corporate obligations		96,882	—	96,882	—
Alternative investments		61,630	—	—	61,630
Total investments	$	647,027	353,492	231,905	61,630

(In thousands)

The following table presents the System's fair value hierarchy for the pension plan assets measured at fair value on a recurring basis as of August 31, 2014:

		Fair value	Fair value measurements		
			Level 1	**Level 2**	**Level 3**
Investments:					
Cash and cash equivalents	$	23,258	23,258	—	—
Equity mutual funds		7,447	7,447	—	—
Equity commingled funds		75,491	—	75,491	—
Common and preferred stocks		335,016	333,862	1,154	—
Fixed income mutual funds		56,584	56,584	—	—
Government and agency bonds		18,026	43	17,983	—
Corporate obligations		90,954	—	90,954	—
Alternative investments		58,939	—	—	58,939
Total investments	$	665,715	421,194	185,582	58,939

During the year ended August 31, 2015 and 2014, the System transferred approximately $55,000 and $30,000, respectively of Level 1 fixed income assets to Level 2 due to a change in investment strategy in the pension assets.

The change in the fair value for the pension assets valued using significant unobservable inputs (Level 3) was due to the following:

		Alternative investments
Ending balance August 31, 2013	$	48,217
Total net gains realized		442
Total net gains unrealized		3,080
Purchases		7,200
Ending balance August 31, 2014		58,939
Total net gains realized		—
Total net gains unrealized		2,691
Purchases		—
Ending balance August 31, 2015	$	61,630

The System applies ASU No. 2009-12, *Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities That Calculate Net Asset per Share (or Its Equivalent)*, to its pension plan asset portfolio. The guidance amends ASC Topic 820 and permits, as a practical expedient, fair value of investments within its scope to be estimated using net asset value or its equivalent. The alternative investments classified within Level 3 of the fair value hierarchy have been recorded using Net Asset Value (NAV).

(Continued)

The following summarizes the redemption and commitment terms for the alternative investment vehicles held in the pension plan assets as of August 31, 2015:

	Hedge fund 1	Hedge fund 2
Redemption timing:		
Redemption frequency	Monthly	Quarterly
Required notice	70 days	95 days
Audit reserve:		
Percentage held back for audit reserve	10%	10%
Gates:		
Potential gate holdback	—%	—%
Potential gate release timeframe	n/a	n/a
Unfunded commitments	—	—

The hedge funds include two multi-strategy hedge funds of funds. The investment objective of the multi-strategy funds is to achieve positive absolute returns with low volatility, achieved through investments with multiple underlying manager who are investing across various strategies. Strategies used within these hedge funds include, but are not limited to:

Equity Long/Short: Investment companies that maintain long and short positions in publicly traded equities in order to capture opportunities driven by the perception of securities or industries being over-or undervalued.

Credit/Distressed: Investment companies that focus mainly on opportunities in corporate fixed income securities that are in financial distress, or perceived distress, or are going through a restructuring or reorganization.

Event Driven: Investment companies that focus on identifying securities that would benefit from the occurrence of a major corporate event.

Global Macro: Investment companies that employ broad mandates to invest globally across all asset classes, including interest rates, currencies, commodities and equities, in order to benefit from market movements within various countries.

Relative Value: Investment companies that seek to identify valuation discrepancies between related securities, utilizing fundamental and quantitative techniques to establish equity, fixed income and derivative positions.

The System expects to contribute $42,096 to its pension plans during the year ended August 31, 2016.

(In thousands)

Future pension benefit payments, which reflect expected future service, as appropriate, are expected as follows:

2016	$	53,657
2017		40,321
2018		42,577
2019		45,851
2020		48,471
2021–2025		287,278

The System also has various contributory, tax-deferred annuity, and savings plans with participation available to certain employees. The System matches employee contributions up to 6% of compensation under certain defined contribution plans. The System contributed $40,542 and $36,571 towards these plans during the years ended August 31, 2015 and 2014, respectively. Total expense was $40,389 and $40,875 in 2015 and 2014, respectively.

In addition to the retirement plan described above, other postretirement healthcare benefits are provided to certain qualified retirees who meet certain eligibility requirements. The net obligation recognized in the accompanying consolidated balance sheets at August 31, 2015 and 2014 is $1,452 and $3,038, respectively.

Multi-Employer Plans

The system contributes to two multi-employer defined benefit pension plans. These plans include The Archdiocese Pension Plan for the Archdiocese of New York (Archdiocesan Plan) and the 1199 Union Pension Plan.

(a) Archdiocesan Plan

The Archdiocesan Plan is a noncontributory, multi-employer defined benefit plan, which covers substantially all of the System's full-time nonunion employees in the state of New York. The Employer Identification Number is 13-3089351. The Archdiocesan Plan is a Church plan approved by the Internal Revenue Service and is exempt from the provisions of the Employee Retirement Income Security Act of 1974 (ERISA). Contributions to the Archdiocesan Plan are based on actuarial valuations. The contributions of all participating employers are pooled. As of January 1, 2014, the Archdiocesan Plan's market value of assets is $1,033,253 and the present value of accrued plan benefits is $1,388,763 resulting in a funded status of 81.6%. Contributions to the Archdiocesan Plan were $2,569 and $3,419 for the years ended August 31, 2015 and 2014, respectively.

(b) 1199 SEIU Health Care Employees Pension Fund

The System contributes to a multi-employer defined benefit plan under the terms of a collective bargaining agreement for its 1199 SEIU employees. The Employer Identification Number is 13-3604862/001. The most recent available information on the Pension Protection Act (PPA) zone status is for the plan years ended December 31, 2013 and 2012. The zone status is based on information that the System received from the plan sponsor and, as required by the PPA, is certified by the plan's actuary. Among other factors, plans in the red zone are generally less than 65% funded, plans in the yellow zone are less than 80% funded, and plans in the green zone are at least 80% funded. Based on this information, the zone status was green for the plan year ended December 31, 2013 and 2012.

(In thousands)

The expiration date of the collective bargaining agreements requiring contributions to the plan are October 31, 2015 for service and maintenance units and December 31, 2015 for nursing units. The contributions by the System to the union pension fund were $9,992 and $10,504 for the years ended August 31, 2015 and 2014, respectively. There have been no significant changes that affect the comparability of 2015 and 2014 contributions. The System was not listed in the plan's most recent available annual report (Form 5500 for U.S. Plans) for providing more than 5% of the total contributions to the plan for the years ended December 31, 2013 and 2012.

(10) Net Patient Service Revenue

BSHSI has agreements with third-party payors that provide for payments to the System at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at estimated net realizable amounts from patients, third-party payors, and others for services rendered, including retroactive adjustments under reimbursement agreements with third-party payors. Retroactive reimbursement adjustments are estimated in the period in which the related services are rendered and adjusted in future periods as final settlements are determined.

The System estimates the allowance for uncollectible accounts based on the aging of the accounts receivable, historical collection experience, payor mix and other relevant factors. A significant portion of the allowance for uncollectible accounts relates to self-pay patients, as well as co-payments and deductibles owed by patients with insurance. There are various factors that can impact collection trends such as changes in the economy, which in turn have an impact on unemployment rates and the number of uninsured and underinsured patients. Other factors include the volume of patients through the emergency departments and the increased level of co-payments and deductibles due from patients with insurance. These factors continuously change and can have an impact on collection trends and the estimation process.

The activity in the allowance for uncollectible accounts is summarized as follows for the years ended August 31, 2015 and 2014:

		2015	2014
Beginning balance	$	145,138	140,588
Provision for bad debts		193,593	255,931
Divestiture of Charity		(25,754)	—
Write-offs		(181,494)	(251,381)
Ending balance	$	131,483	145,138

(11) Reimbursement Programs

The System participates in the Medicare and Medicaid programs. Payment rates for inpatient services provided to program beneficiaries are governed by the applicable regulations and implementation provisions thereunder, based generally on prospectively determined rates using clinical and diagnostic charges. Capital costs are also generally based upon prospectively determined rates. However, certain services are subject to cost-based reimbursement principles, subject to certain limitations. The System also participates in various managed care programs. Generally, these programs provide for payments based on negotiated rates; however, certain plans utilize cost-based or charge-based payment principles.

Programs utilizing cost-based reimbursement principles are subject to review and final determination by appropriate program representatives. In the opinion of management, adequate provision has been made for any adjustments that may result from such reviews. Due to third-party payors, net is included in other accrued expenses and other long-term liabilities in the accompanying consolidated balance sheets.

Since 2005, the Centers for Medicare and Medicaid Services (CMS) have utilized recovery audit contractors (RACs) as part of the CMS's further efforts to assure accurate patient payments. The project uses the RACs to search for potentially inaccurate Medicare payments that may have been made to healthcare providers and that were not detected through existing CMS program integrity efforts. To date, all System hospitals have had certain Medicare claims denied, and all have a diligent appeal process. While additional RAC assessments against the System are anticipated, the impact of such assessments is still unknown. In December 2014, CMS awarded the Region 5 Recovery Audit contract, the purpose of which will be to support CMS in completing this mission through the identification and correction of improper payments for durable medical equipment, prosthetics, orthotics and supplies (DMEPOS), and home health/hospice (HH/H) claims submitted under Title XVIII of the Social Security Act. This award marks the beginning of the new Recovery Audit contracts and is the start date of the implementation of many improvements to reduce provider burden and increase transparency in the program. Effective June 4, 2015, CMS withdrew the Requests for Quotes for the next round of Recovery Auditor contracts. CMS plans to update the Statement of Work and release new Requests for Proposals shortly. In the meantime, the current Recovery Auditors will continue active recovery auditing through at least December 31, 2015.

In addition to RAC audits, System affiliates may from time to time be subject to other audits by state or federal agencies, including state Medicaid programs. The outcome of these audits is uncertain and the impact cannot be reasonably estimated at this time.

The System's management strives to anticipate factors that affect payment changes and develop plans to address them. Management attempts to address these issues proactively through its policies and practices that focus on areas such as charity and uninsured care as well as effective managed care contracting, accounts receivable and revenue cycle best practices and analysis of potential government payment changes. Nonetheless, future actions by federal, state, and private payors could have a significant adverse effect on the System's operating results, cash flows, and liquidity. In addition, management pursues the highest level of compliance, but state and federal audits by the Offices of the Inspector General do create uncertainty. At this time, the System has audits underway, the outcomes of which are uncertain and the impact cannot be reasonably estimated at this time.

As a result of the federal healthcare reform legislation enacted in 2010, substantial changes are anticipated in the U.S. healthcare system. Such legislation includes numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement of healthcare providers, and the legal obligations of health insurers, providers, and employers. These provisions are currently slated to take effect at specified times over approximately the next decade.

A number of programs were enacted by CMS in 2011 that impacted the reimbursement for the System during the fiscal year ended August 31, 2015 and 2014. The first is value-based purchasing, which affects acute care hospitals paid under the Medicare Inpatient Prospective Payment System. Beginning in federal fiscal year 2013, value-based incentive payments were made based upon achievement of or improvement on a set of clinical and patient experience of care quality measures designed to foster improved clinical outcomes for hospital patients as well as improve how patients experience inpatient care. For Federal fiscal year 2014 and 2015, respectively, 1.25% and 1.50% of a hospital's inpatient Medicare reimbursement was at risk/available in this program for either a penalty or a bonus depending on performance as measured with the rest of the hospitals in the country. Percentages considered at risk will increase an additional 0.25% each Federal fiscal year, with 2% of a hospital's inpatient Medicare reimbursement being at risk by Federal fiscal year 2017. In addition, components of valuable based purchasing are changed and/or expanded each Federal fiscal year and include new measures, performance periods, performance standards, and domain weighting. The System's hospitals are currently measuring quality indicators consistent with the CMS value-based purchasing methodology and creating action plans to continue improvement in future periods in an effort to maximize the System's reimbursement opportunities.

The second program is the readmission reduction program that also began with federal fiscal year 2013 and is a penalty-only based program based on a hospital's actual readmissions for three specific costly diagnoses compared to an expected readmission rate. Effective for discharges beginning on October 1, 2012, the CMS's Hospital Readmissions Reduction Program withheld up to 1% of regular reimbursements for hospitals that had excess patient readmissions within 30 days of discharge for three medical conditions: heart attack, heart failure and pneumonia. As a part of healthcare reform legislation, the maximum penalty increased to 2% for federal fiscal year 2014 and will increase to 3% by 2015 and be expanded to include readmissions for other medical conditions. BSHSI anticipated this reduction in its year ended August 31, 2015 and 2014 results and is monitoring readmission trends to minimize payment reductions.

Another program enacted by CMS is Meaningful Use – HITECH Stimulus Grants. On July 13, 2010, CMS issued rules to implement the Medicare and Medicaid electronic health record (EHR) incentive program established under the Health Information Technology for Economic and Clinical Health Act (HITECH Act). Certain hospitals and eligible healthcare professionals (EPs) that demonstrate "meaningful use" of certified EHR technology can qualify for Medicare payments beginning in 2011. Medicaid requires that hospitals and EPs "adopt, implement or upgrade" certified EHR, which includes purchasing the technology, in order to receive incentive payments. Beginning in federal fiscal year 2015, Medicare payment reduction penalties will be assessed against hospitals and EP's that do not achieve meaningful use of EHR. The System uses the grant model to account for Meaningful Use incentive payments and during the year ended August 31, 2015 and 2014, the System qualified for Medicare EHR incentive payments of approximately $5,900 and $15,000, respectively, and Medicaid EHR incentive payments of $1,600 and $3,600, respectively. BSHSI has made a substantial investment in a qualified EHR. The System expects to qualify providers for Medicaid payments in all states where the State Medicaid Health Information Technology Plan has been submitted to and are approved by CMS.

Beginning April 1, 2013, sequestration was put into effect as part of the spending reductions required by the Budget Control Act of 2011. These budget deficit reductions have resulted in a 2% reduction in all Medicare payments made to all healthcare providers.

On August 2, 2013, CMS published the "Two Midnight" rule. This rule establishes the basis of determining a patient's stay as inpatient or outpatient. If a patient stays more than two midnights from the hour the service began then the stay is classified as inpatient. If the time is less than two midnights then it will be classified as outpatient or observation time. This rule is expected to result in decreased payments to hospitals nation-wide. The rule became effective October 1, 2014 but Recovery Audit Contractors (referred to as RACs) utilized by CMS initially could not begin to audit claims until April 30, 2015. Due to controversy over the implementation of the rule, CMS has extended the moratorium until December 31, 2015.

Beginning October 1, 2013, the Affordable Care Act (ACA) amended the adjustment provision for hospital Medicare disproportionate share (DSH) payments. Hospitals, which qualified for DSH payments will now receive twenty five percent of what would have been received under the historical statutory formula and will receive an additional payment for uncompensated care. Hospital-specific uncompensated care allotments are announced in the annual rulemaking process, and allotments are expected to decrease annually relative to the growing percentage of newly insured individuals. For both traditional DSH and the uncompensated care component, the System records reserves to account for differences in estimated earned amounts versus actual payments received.

(12) Investments in Joint Ventures

The System has invested in a number of joint ventures, limited liability corporations and other entities to provide specialty healthcare services or engage in other activities. These investments range from minority investments with no control to majority investments or investments with control.

(a) Roper St. Francis Healthcare – South Carolina

BSHSI, The Medical Society of South Carolina, and the Carolinas Health System, Inc. are members of Care Alliance Health Services (d/b/a Roper St. Francis Healthcare). Roper St. Francis Healthcare is the sole member of and operates Bon Secours – St. Francis Xavier Hospital, Roper Hospital, a supporting foundation and physician practices located in Charleston, South Carolina. BSHSI is obligated to provide 27% of any capital contribution to Roper St. Francis Healthcare and is entitled to 27% of any surplus capital. BSHSI accounts for its interest in Roper St. Francis Healthcare under the equity method and includes its interest in Roper St. Francis Healthcare's excess of revenue over expenses in its consolidated statements of operations and changes in unrestricted net assets as other revenue. Roper St. Francis Healthcare, The Medical Society of South Carolina, and the Carolinas Health System, Inc. are not otherwise affiliated with BSHSI and are not Members of the Obligated Group.

(In thousands)

The System recorded income of $5,940 and $5,967 related to its equity interest for the years ended August 31, 2015 and 2014, respectively. Included in these amounts were the System's allocated share of investment gains of $472 and $5,773 for the years ended August 31, 2015 and 2014, respectively. In addition, adjustments of $1,663 and $778 were recorded as net change in equity of joint ventures in 2015 and 2014, respectively, to reflect the System's 27% interest in the net assets of this joint venture. The System received cash distributions of $5,400 and $8,556 related to its equity interest during the years ended August 31, 2015 and 2014, respectively.

The total assets, total liabilities, and net assets as of August 31, 2015 and 2014 and the total revenue, total expenses, investment gains, net, and change in unrestricted net assets for the years then ended for Roper St. Francis Healthcare are as follows:

		2015	2014
Total assets	$	861,843	861,020
Total liabilities		476,975	486,733
Net assets		384,868	374,287
Total revenue		830,595	772,468
Total expenses		805,744	756,442
Investment gains, net		1,828	21,384
Change in unrestricted net assets		(8,161)	(6,699)

In June 2009, Roper St. Francis Healthcare received state approval for the construction of a new 50-bed full service hospital located in Berkeley County, South Carolina. The approval of this project is currently under appeal at the request of a local hospital that also received state approval for a 50-bed facility. These capital construction projects will be financed through Roper St. Francis Healthcare's equity. A portion of the annual distributions are expected to be foregone during the construction period.

(b) Sentara Princess Anne

BSHSI, DePaul Medical Center and Bon Secours Hampton Roads Health System (referred to as Bon Secours Hampton Roads) and Sentara Healthcare (Sentara) are members in a Virginia not-for-profit, nonstock corporation that owns and operates Sentara Princess Anne Hospital located in Virginia Beach, Virginia. Sentara holds a 70% membership interest and DePaul Medical Center holds a 30% membership interest in the corporation.

The joint venture is managed by Sentara and the agreements provide the members with rights to "put" and "call" the Bon Secours Hampton Roads' membership interest at fair market value terms upon the occurrence of certain events and dates.

BSHSI accounts for its interest in Sentara Princess Anne Hospital under the equity method and includes its interest in Sentara Princess Anne Hospital's excess of revenue over expenses in its consolidated statements of operations and changes in unrestricted net assets as other revenue. Sentara Healthcare is not otherwise affiliated with BSHSI and is not a Member of the Obligated Group.

(In thousands)

The System recorded income of $8,830 and $5,014 and received cash distributions of $9,201 and $5,742 related to its equity interest during the years ended August 31, 2015 and 2014, respectively.

The total assets, total liabilities, and net assets as of August 31, 2015 and 2014 and the total revenue, total expenses, and change in unrestricted net assets for the years then ended, for Sentara Princess Anne Hospital are as follows:

		2015	2014
Total assets	$	259,887	263,647
Total liabilities		166,800	168,449
Net assets		93,087	95,198
Total revenue		224,798	203,959
Total expenses		196,544	186,939
Change in unrestricted net assets		(2,112)	(1,666)

(c) Premier Purchasing Partners, LP

BSHSI holds an equity investment in Premier Purchasing Partners, LP (Premier LP), a group purchasing organization, in which BSHSI is a limited partner. The System recorded income of $7,027 in other operating revenue related to its equity interest and revenue share for the year ended August 31, 2014. On October 1, 2013, Premier LP sold 16% of its equity as part of an organizational restructuring and an initial public offering of shares in its affiliate, Premier, Inc. As a result of this restructuring and related public offering, the System received a cash distribution of $9,700, which resulted in a net gain of $9,056 that was recognized in other operating revenue for the year ended August 31, 2014.

BSHSI recorded reductions to operating supply expenses of $9,975 and $7,071 resulting from the unrealized gains related to the System's vesting of its interests in Premier, LP for the years ended August 31, 2015 and 2014, respectively. As of August 31, 2015 and 2014, the System's investment in Premier was $21,722 and $11,096, respectively.

(d) Bon Secours Charity Health System, Inc.

As of May 19, 2015, BSHSI holds a 40% interest in Charity Health System, Inc. (note 1(b)) and accounts for its interest in Charity under the equity method and includes its interest in Charity's excess of revenue over expenses its consolidated statements of operations and changes in unrestricted net assets as other revenue. BSHSI recorded losses of $564 in operating revenue related to its equity interest in Charity for the year ended August 31, 2015. BSHSI's investment in Charity was $56,995 as of August 31, 2015.

(13) Other Commitments and Contingent Liabilities

(a) General and Professional Liability Insurance

The System participates in a self-insurance program for health professional/general liability (HPL/GL Program) by policies issued under a member of the System, Bon Secours Assurance Company, LTD (BSAC). BSAC is incorporated in the Cayman Islands. BSHSI is the sole shareholder of BSAC. Assets are available under the HPL/GL Program to provide specified levels of claims-made coverage for health professional liabilities and occurrence-based coverage for general liabilities, with excess layers reinsured through commercial carriers under policies written on a claims-made basis.

The provision for claims and related funding levels for the HPL/GL Program is established annually based upon the recommendations of consulting actuaries. BSAC has accrued claims including liabilities for incidents incurred but not reported of approximately $107,534 and $111,639 at August 31, 2015 and 2014, respectively. The current portion of such accruals, $19,263 at August 31, 2015 and $17,713 at August 31, 2014, is included in other accrued expenses, and the remainder, $88,271 at August 31, 2015 and $93,926 at August 31, 2014, is reported within other long-term liabilities in the accompanying consolidated balance sheets. Amounts recorded for unpaid claims are based upon the estimated present value of future claim payments and such amounts are undiscounted and based upon an actuarial estimate.

(b) Workers' Compensation Insurance

The System's workers' compensation program primarily consists of self-insurance programs in various states with excess coverage through a commercial insurer. Mary Immaculate Hospital, which is also a participant of the System's workers' compensation program, is insured under a large deductible policy. Accrued workers' compensation claims of $61,907 and $60,428, of which the current portion, $9,250 and $8,100 at August 31, 2015 and 2014, respectively, is reported as other accrued expenses and the remainder, $52,657 and $52,328 at August 31, 2015 and 2014, respectively, is reported within other long-term liabilities in the accompanying consolidated balance sheets, include estimates for incidents incurred but not reported at August 31, 2015 and 2014, respectively. Amounts recorded for unpaid claims are based upon the estimated present value of future claim payments such amounts are undiscounted and based upon an actuarial central estimate. The impact of the change in discount rate was not significant to the consolidated financial statements.

(c) Employee Health Insurance

Employee health benefits of the System are principally provided through the System's self-insurance program. Accrued claims associated with this program, which are reported as other accrued expenses in the accompanying consolidated balance sheets, of approximately $20,975 and $19,621, include estimates for claims incurred but not reported, at August 31, 2015 and 2014, respectively.

(d) Litigation

The healthcare industry is subject to numerous laws and regulations from federal, state, and local governments. The System's compliance with these laws and regulations can be subject to periodic governmental review and interpretation, which can result in regulatory action unknown or unasserted at this time. Management is aware of certain asserted and unasserted legal claims and regulatory matters arising in the ordinary course of business, but cannot reasonably predict any particular outcomes or operational or financial effects from these matters at this time.

(In thousands)

(e) Operating Leases

Leases that do not meet the criteria for capitalization are classified as operating leases with related rentals charged to operations as incurred. Total rental expense was $75,984 and $81,340 in 2015 and 2014, respectively. Future rental payments under noncancelable operating leases with durations in excess of one year are as follows:

2016	$	46,975
2017		35,254
2018		30,156
2019		24,832
2020		19,232
Thereafter		31,516

Certain local systems entered into agreements to lease space in medical office buildings (MOBs) under construction by external development companies. Based on the provisions of ASC Topic 840-40-05-5, *Lessee Involvement with Construction*, local systems were considered the owner of the MOBs during construction. These transactions do not qualify for sale-leaseback accounting and as such are treated as financing transactions. Accordingly, the associated financing obligations, along with their related construction in progress or building assets of $31,000 and $35,321 at August 31, 2015 and 2014 are included in other long-term liabilities and construction in progress or buildings and equipment in the accompanying consolidated balance sheets. The financing obligations associated with these transactions will not result in cash payments in excess of amounts paid under the related operating lease payments. All future cash obligations related to leased space within these MOBs are included as future minimum lease payments in the amounts reported above.

(f) Guaranty Agreements

Affiliates of the System entered into nine limited partnership agreements during the period from 1997 through 2014. The limited partnerships are involved in housing projects in the System's Baltimore market. System affiliates have entered into guaranty agreements with the limited partnerships during 1997 through 2014, whereby they have agreed to advance funds to the partnerships under specified conditions. The termination of each guaranty agreement is predicated on the occurrence of certain events. Seven such guaranty agreements are still in effect as of August 31, 2015. System affiliates have not been obligated to make any guarantee payments under the guaranty agreements to date through August 31, 2015. The maximum potential amount of future payments the System affiliates are obligated to make was $22,787 and $12,864 as of August 31, 2015 and 2014, respectively.

(Continued)

(14) Net Assets

BSHSI's endowments consist of approximately 76 and 83 individual funds established for a variety of purposes as of August 31, 2015 and 2014, respectively. Net assets associated with endowment funds, including board-designated funds, are classified and reported based on the existence or absence of donor or board-imposed restrictions and the nature of the restrictions, if any.

The System's endowment net assets are comprised of permanently restricted funds, which were $7,763 and $7,829 at August 31, 2015 and 2014, respectively. The System does not hold any board-designated endowment funds within unrestricted net assets or temporarily restricted net assets.

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or Uniform Prudent Management of Institutional Funds Act (UPMIFA) requires the System to retain as a fund of perpetual duration. Deficiencies of this nature are reported in unrestricted net assets. There were no deficiencies at August 31, 2015 and 2014.

The System has investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the System must hold in perpetuity or for a donor-specified period as well as board-designated funds. The practice allows the endowment assets to be invested in a manner that is intended to produce investment returns that exceed the price and yield the results of the allocation index while assuming a moderate level of investment risk. The System expects its endowment funds to provide a rate of return that preserves the gift and generates earnings to achieve the endowment purpose.

To satisfy its long-term rate-of-return objectives, the System relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and interest and dividend income. The System uses diversified asset allocation to achieve its long-term return objectives within prudent risk constraints to preserve capital.

BSHSI has a practice of distributing the major portion of current year earnings on the endowment funds, if the restrictions have been met. This is consistent with the System's objective to maintain the purchasing power of the endowment assets held in perpetuity as well as to provide additional real growth through new gifts and investment return.

(In thousands)

(15) Functional Expenses

The functional breakdown of expenses incurred by the System in fulfilling its mission for the years ended August 31, 2015 and 2014 is as follows:

		2015	2014
Healthcare services	$	3,108,788	3,027,535
General and administrative		247,884	305,892
Fundraising		3,871	4,845
Total expenses	$	3,360,543	3,338,272

(16) Subsequent Events

Management evaluated all events and transactions that occurred after August 31, 2015 and through October 27, 2015. The System did not have any material recognizable subsequent events during this period.