Consolidated Financial Statements and Supplementary Information

The Cleveland Clinic Foundation
d.b.a. Cleveland Clinic Health System
Years Ended December 31, 2014 and 2013
With Report of Independent Auditors

Ernst & Young LLP

Building a better
working world

Cleveland Clinic Health System

Consolidated Financial Statements
and Supplementary Information

Years Ended December 31, 2014 and 2013

Contents

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Report of Independent Auditors

The Board of Directors
The Cleveland Clinic Foundation

We have audited the accompanying consolidated financial statements of The Cleveland Clinic Foundation and controlled affiliates, d.b.a. Cleveland Clinic Health System, which comprise the consolidated balance sheets as of December 31, 2014 and 2013, and the related consolidated statements of operations and 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 financial statements in conformity 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 financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Cleveland Clinic Foundation and controlled affiliates, d.b.a. Cleveland Clinic Health System, at December 31, 2014 and 2013, and the consolidated results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

March 6, 2015

Cleveland Clinic Health System

Consolidated Balance Sheets
(In Thousands)

	December 31	
	2014	**2013**
Assets		
Current assets:		
Cash and cash equivalents	**$ 70,322**	$ 70,900
Patient receivables, net of allowances for uncollectible accounts of $211,391 in 2014 and $182,405 in 2013	**819,074**	779,676
Investments for current use	**144,838**	139,129
Other current assets	**332,075**	295,059
Total current assets	**1,366,309**	1,284,764
Investments:		
Long-term investments	**5,950,076**	5,057,251
Funds held by trustees	**119,388**	70,627
Assets held by captive insurance subsidiary	**106,317**	95,666
Donor-restricted assets	**474,227**	428,722
	6,650,008	5,652,266
Property, plant, and equipment, net	**3,599,607**	3,539,781
Other assets:		
Pledges receivable, net	**161,757**	135,457
Trusts and interests in foundations	**122,498**	118,274
Other noncurrent assets	**367,381**	221,257
	651,636	474,988
Total assets	**$ 12,267,560**	$ 10,951,799

	December 31	
	2014	**2013**
Liabilities and net assets		
Current liabilities:		
Accounts payable	**$ 335,475**	$ 325,014
Compensation and amounts withheld from payroll	**238,938**	256,149
Current portion of long-term debt	**55,778**	52,498
Variable rate debt classified as current	**386,875**	488,230
Other current liabilities	**434,815**	381,549
Total current liabilities	**1,451,881**	1,503,440
Long-term debt:		
Hospital revenue bonds	**2,798,062**	2,343,380
Notes payable and capital leases	**175,548**	86,626
	2,973,610	2,430,006
Other liabilities:		
Professional and general liability insurance reserves	**143,240**	133,176
Accrued retirement benefits	**452,897**	263,259
Other noncurrent liabilities	**443,437**	413,512
	1,039,574	809,947
Total liabilities	**5,465,065**	4,743,393
Net assets:		
Unrestricted	**5,998,053**	5,478,927
Temporarily restricted	**519,730**	461,110
Permanently restricted	**284,712**	268,369
Total net assets	**6,802,495**	6,208,406
Total liabilities and net assets	**$ 12,267,560**	$ 10,951,799

See accompanying notes.

Cleveland Clinic Health System

Consolidated Statements of Operations
and Changes in Net Assets
(In Thousands)

Operations

	Year Ended December 31	
	2014	**2013**
Unrestricted revenues		
Net patient service revenue	**$ 6,428,938**	$ 6,284,527
Provision for uncollectible accounts	**(358,821)**	(410,945)
Net patient service revenue less provision for uncollectible accounts	**6,070,117**	5,873,582
Other	**617,262**	576,577
Total unrestricted revenues	**6,687,379**	6,450,159
Expenses		
Salaries, wages, and benefits	**3,635,964**	3,637,198
Supplies	**627,535**	639,807
Pharmaceuticals	**558,984**	494,477
Purchased services and other fees	**382,549**	392,119
Administrative services	**167,587**	163,778
Facilities	**281,898**	303,532
Insurance	**66,943**	65,464
	5,721,460	5,696,375
Operating income before interest, depreciation, and amortization expenses	**965,919**	753,784
Interest	**110,393**	106,692
Depreciation and amortization	**387,983**	353,097
Operating income	**467,543**	293,995
Nonoperating gains and losses		
Investment return	**316,217**	546,398
Derivative (losses) gains	**(79,786)**	60,945
Other, net	**(352)**	(1,239)
Net nonoperating gains	**236,079**	606,104
Excess of revenues over expenses	**703,622**	900,099

(continued on next page)

Changes in Net Assets

	Net Assets			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Balances at January 1, 2013	$ 4,332,388	$ 425,234	$ 244,758	$ 5,002,380
Excess of revenues over expenses	900,099	–	–	900,099
Donated capital and assets released from restrictions for capital purposes	17,510	(16,298)	–	1,212
Gifts and bequests	–	56,091	19,092	75,183
Transfer of net assets	1,684	(1,684)	–	–
Net investment income	–	30,555	–	30,555
Net assets released from restrictions used for operations included in other unrestricted revenues	–	(36,726)	–	(36,726)
Retirement benefits adjustment	225,977	–	–	225,977
Change in interests in foundations	–	3,938	1,838	5,776
Change in value of perpetual trusts	–	–	2,681	2,681
Net change in unrealized losses on nontrading investments	(93)	–	–	(93)
Other	1,362	–	–	1,362
Increase in net assets	1,146,539	35,876	23,611	1,206,026
Balances at December 31, 2013	5,478,927	461,110	268,369	6,208,406
Excess of revenues over expenses	**703,622**	**–**	**–**	**703,622**
Donated capital and assets released from restrictions for capital purposes	**5,894**	**(5,824)**	**–**	**70**
Gifts and bequests	**–**	**83,935**	**12,152**	**96,087**
Transfer of net assets	**(708)**	**(292)**	**1,000**	**–**
Net investment income	**–**	**18,079**	**–**	**18,079**
Net assets released from restrictions used for operations included in other unrestricted revenues	**–**	**(36,190)**	**–**	**(36,190)**
Retirement benefits adjustment	**(193,150)**	**–**	**–**	**(193,150)**
Change in interests in foundations	**–**	**(1,088)**	**955**	**(133)**
Change in value of perpetual trusts	**–**	**–**	**2,236**	**2,236**
Net change in unrealized gains on nontrading investments	**3,163**	**–**	**–**	**3,163**
Other	**305**	**–**	**–**	**305**
Increase in net assets	**519,126**	**58,620**	**16,343**	**594,089**
Balances at December 31, 2014	**$ 5,998,053**	**$ 519,730**	**$ 284,712**	**$ 6,802,495**

See accompanying notes.

Cleveland Clinic Health System

Consolidated Statements of Cash Flows
(In Thousands)

	Year Ended December 31	
	2014	**2013**
Operating activities and net nonoperating gains and losses		
Increase in net assets	**$ 594,089**	$ 1,206,026
Adjustments to reconcile increase in net assets to net cash provided by operating activities and net nonoperating gains and losses:		
Loss on extinguishment of debt	**–**	687
Retirement benefits adjustment	**193,150**	(225,977)
Net realized and unrealized gains on investments	**(296,905)**	(534,657)
Depreciation and amortization	**387,983**	353,097
Provision for uncollectible accounts	**358,821**	410,945
Donated capital	**(70)**	(1,212)
Restricted gifts, bequests, investment income, and other	**(116,269)**	(114,195)
Accreted interest and amortization of bond premiums	**(2,533)**	(2,678)
Net loss (gain) in value of derivatives	**53,993**	(87,044)
Changes in operating assets and liabilities:		
Patient receivables	**(398,219)**	(437,673)
Other current assets	**(38,214)**	54,160
Other noncurrent assets	**(42,035)**	(52,528)
Accounts payable and other current liabilities	**53,878**	(44,010)
Accrued retirement benefits	**(3,512)**	(136,896)
Other liabilities	**(14,004)**	58,085
Net cash provided by operating activities and net nonoperating gains and losses	**730,153**	446,130
Financing activities		
Proceeds from long-term borrowings	**400,000**	382,835
Payments for advance refunding of long-term debt	**–**	(363,851)
Principal payments on long-term debt	**(55,356)**	(53,738)
Debt issuance costs	**(5,471)**	(2,473)
Change in pledges receivable, trusts and interests in foundations	**(29,326)**	(3,013)
Restricted gifts, bequests, investment income and other	**116,269**	114,195
Net cash provided by financing activities	**426,116**	73,955
Investing activities		
Expenditures for property and equipment	**(440,642)**	(402,796)
Proceeds from sale of property and equipment	**341**	10,179
Investment in Akron General	**(10,000)**	–
Net change in cash equivalents reported in long-term investments	**(409,139)**	66,536
Purchases of investments	**(1,822,328)**	(1,944,973)
Sales of investments	**1,524,921**	1,739,076
Net cash used in investing activities	**(1,156,847)**	(531,978)
Decrease in cash and cash equivalents	**(578)**	(11,893)
Cash and cash equivalents at beginning of year	**70,900**	82,793
Cash and cash equivalents at end of year	**$ 70,322**	$ 70,900
Supplemental disclosure of noncash activity		
Assets acquired through notes payable and capital leases	**$ 103,418**	$ 4,594

See accompanying notes.

1. Organization and Consolidation

The Cleveland Clinic Foundation (Foundation) is a nonprofit, tax-exempt, Ohio corporation organized and operated to provide medical and hospital care, medical research, and education. The accompanying consolidated financial statements include the accounts of the Foundation and its controlled affiliates, d.b.a. Cleveland Clinic Health System (System).

The System is the leading provider of healthcare services in northeast Ohio. The System operates eleven hospitals with approximately 3,600 staffed beds. Ten of the hospitals are operated in the Cleveland metropolitan area, anchored by the Foundation. The System operates eighteen outpatient Family Health Centers, ten ambulatory surgery centers, as well as numerous physician offices, which are located throughout a seven-county area of northeast Ohio, and specialized cancer centers in Sandusky and Mansfield, Ohio. In addition, the System operates a hospital and a clinic in Weston, Florida, health and wellness centers in West Palm Beach, Florida and Toronto, Canada, and a specialized neurological clinical center in Las Vegas, Nevada (Keep Memory Alive). The System is a minority member in Akron General Health System (Akron General), an integrated healthcare delivery system with a 532-bed flagship medical center located in Akron, Ohio. Pursuant to agreements, the System also provides management services for Ashtabula County Medical Center, located in Ashtabula, Ohio, with approximately 180 staffed beds, and in cooperation with Abu Dhabi Health Services Company, the Sheikh Khalifa Medical City (SKMC), a network of healthcare facilities in Abu Dhabi, United Arab Emirates with approximately 760 staffed beds.

All significant intercompany balances and transactions have been eliminated in consolidation.

2. Accounting Policies

Recent Accounting Pronouncement

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers*, which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance, and requires significantly expanded disclosures about revenue recognition. The core principle of the revenue model is 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. The guidance is effective for the System as of January 1, 2017. Early adoption is not permitted. The System is currently evaluating the impact on the consolidated financial statements and the options of adopting using either a full retrospective or a modified approach.

2. Accounting Policies (continued)

In August 2014, the FASB issued ASU 2014-15, *Presentation of Financial Statements-Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern.* This ASU is intended to define management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. The amendments in this ASU are effective for reporting periods beginning after December 15, 2016, with early adoption permitted. The System is currently evaluating the new guidance and will adopt the provisions as required upon the effective date.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States 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. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Net Patient Service Revenue and Patient Receivables

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others, including retroactive adjustments under payment agreements with third-party payors. The System has agreements with third-party payors that generally provide for payments to the System at amounts different from its established rates. For uninsured patients who do not qualify for charity care, the System recognizes revenue based on established rates, subject to certain discounts as determined by the System. An estimated provision for uncollectible accounts is recorded that results in net patient service revenue being reported at the net amount expected to be received. The System has determined, based on an assessment at the consolidated entity level, that patient service revenue is primarily recorded prior to assessing the patient's ability to pay and as such, the entire provision for uncollectible accounts related to patient service revenue is recorded as a deduction from patient service revenue.

2. Accounting Policies (continued)

The System is paid a prospectively determined rate for the majority of inpatient acute care and outpatient, skilled nursing, and rehabilitation services provided (principally Medicare, Medicaid, and certain insurers). These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Medicare payments for capital are received on a prospective basis and on a cost reimbursement methodology for Medicaid. Payments are received on a prospective basis for the System's medical education costs, subject to certain limits. The System is paid for cost reimbursable items at a tentative rate, with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicare Administrative Contractor. Provision for estimated retroactive adjustments, if any, resulting from regulatory matters or other adjustments under payment agreements are estimated in the period the related services are provided. The System recorded an increase in net patient service revenue of $1.4 million and $12.2 million in 2014 and 2013, respectively, related to changes in estimates.

In 2014, the Provider Reimbursement Review Board provided a favorable decision to the System regarding the graduate medical education program for Weston Hospital. The decision requires the Centers for Medicare and Medicaid Services (CMS) to reimburse Weston Hospital on its annual cost reports for graduate medical education under new program regulations, which includes all years since the hospital opened in 2001. As a result, the System recorded a change in estimate that resulted in an increase in net patient service revenue of $29.4 million in 2014.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation as well as significant regulatory action, and, in the normal course of business, the System is subject to contractual reviews and audits, including audits initiated by the Medicare Recovery Audit Contractor program. As a result, there is at least a reasonable possibility that recorded estimates will change in the near term. The System believes it is in compliance with applicable laws and regulations governing the Medicare and Medicaid programs and that adequate provisions have been made for any adjustments that may result from final settlements.

2. Accounting Policies (continued)

Patient receivables are reduced by an allowance for uncollectible accounts. The allowance for uncollectible accounts is based upon management's assessment of historical and expected net collections considering historical business and economic conditions, trends in healthcare coverage, major payor sources and other collection indicators. Periodically throughout the year, management assesses the adequacy of the allowance for uncollectible accounts based upon historical write-off experience by payor category. The results of this review are then used to make modifications to the provision for uncollectible accounts to establish an appropriate allowance for uncollectible receivables. After satisfaction of amounts due from insurance, the System follows established guidelines for placing certain past-due patient balances with collection agencies, subject to the terms of certain restrictions on collection efforts as determined by the System.

Electronic Health Record Incentive Program

CMS implemented provisions of the American Recovery and Reinvestment Act of 2009 that provide annual incentive payments for the meaningful use of certified electronic health record (EHR) technology. CMS has defined meaningful use as meeting certain objectives and clinical quality measures based on current and updated technology capabilities over predetermined reporting periods as established by CMS. The objectives and clinical quality measures are implemented in three stages with increasing requirements for participation. The Medicare EHR incentive program provides annual incentive payments to eligible professionals and eligible hospitals, as defined, that are meaningful users of certified EHR technology. The Medicaid EHR incentive program provides annual incentive payments to eligible professionals and hospitals for efforts to adopt, implement, and meaningfully use certified EHR technology in the first year of participation and successfully demonstrating meaningful use of certified EHR technology in subsequent participation years. Incentive payments are subject to retrospective adjustments after the submission of the annual cost reports by the System and audits thereof by the Medicare administrative contractor.

2. Accounting Policies (continued)

The System utilizes a grant accounting model to recognize EHR incentive revenues. The System records EHR incentive revenue ratably throughout the incentive reporting period when it is reasonably assured that it will meet the meaningful use objectives for the required reporting period and that the grants will be received. The EHR reporting period for hospitals is based on the federal fiscal year, which runs from October 1 through September 30. CMS announced Stage 2 EHR meaningful use requirements, which added new objectives and increased the threshold for many of the objectives in Stage 1. System hospitals were required to meet Stage 2 EHR meaningful use requirements in the 2014 federal fiscal year. All of the System's eligible hospitals attested Stage 2 meaningful use standards to Medicare and Medicaid in the 2014 federal fiscal year. The System believes that the hospitals that met meaningful use objectives for the federal fiscal year ended September 30, 2014, and that are eligible for EHR incentive payments in the federal fiscal year ending September 30, 2015, will continue to meet these objectives for the federal fiscal year ending September 30, 2015. Therefore, for the year ended December 31, 2014, the System has accrued a portion of EHR revenues related to the federal fiscal year ending September 30, 2015. In 2014, the System recorded EHR incentive revenues of $22.0 million, comprised of $18.8 million of Medicare revenues and $3.2 million of Medicaid revenues. In 2013, the System recorded EHR incentive revenues of $23.7 million, comprised of $21.6 million of Medicare revenues and $2.1 million of Medicaid revenues. EHR incentive revenues are included in other unrestricted revenues in the consolidated statements of operations and changes in net assets.

Charity Care

The System provides care to patients who do not have the ability to pay and who qualify for charity care pursuant to established policies of the System. Charity care is defined as services for which patients have the obligation and willingness to pay but do not have the ability to do so. The System does not report charity care as net patient service revenue. The cost of charity care provided in 2014 and 2013 approximated $101 million and $171 million, respectively. The System estimated these costs by calculating a ratio of cost to gross charges and then multiplying that ratio by the gross uncompensated charges associated with providing care to charity patients. The decrease in charity care is primarily attributable to the increase in Medicaid patients due to the expansion of Medicaid eligibility in the State of Ohio and the resulting decrease in the number of charity patients.

2. Accounting Policies (continued)

The System participates in the Hospital Care Assurance Program (HCAP). Ohio created HCAP to financially support those hospitals that service a disproportionate share of low-income patients unable to pay for care. HCAP funds basic, medically necessary hospital services for patients whose family income is at or below the federal poverty level, which includes Medicaid patients and patients without health insurance. The System recorded HCAP revenues of $9.1 million and $17.7 million for the years ended December 31, 2014 and 2013, respectively, which are included in net patient service revenue.

International Contract Revenue Recognition

The System has management agreements with international organizations to provide consulting services for various healthcare ventures. The scope of these services ranges from managing current healthcare operations to managing the construction, training, organizational infrastructure, and operational management of future foreign healthcare entities. The management fees are received in advance and recorded as deferred revenue until the services have been provided. The System has recorded deferred revenue related to international management agreements, included in other current liabilities, of $7.5 million and $9.9 million at December 31, 2014 and 2013, respectively. Revenue related to international management agreements for 2014 and 2013 was $30.5 million and $32.9 million, respectively, and is included in other unrestricted revenues.

Clinical and Innovation Agreements

The System has various agreements with national and regional partners to provide consulting services that are designed to improve clinical quality, innovation, patient care, medical education and research at other healthcare organizations and educational institutions. Clinical agreements consist of consulting services that include support, expansion and development of integrated patient care strategies, medical education and research. Services related to innovation agreements include assisting partners in the commercial application of scientific and clinical innovation by creating new companies, mentoring inventors and licensing technology. The System recognizes revenues related to clinical and innovation agreements on a pro rata basis over the term of the agreements. The System recorded revenues related to clinical and innovation agreements of $26.5 million and $26.1 million in 2014 and 2013, respectively, which are included in other unrestricted revenues.

2. Accounting Policies (continued)

Cash and Cash Equivalents

The System considers all highly liquid investments with original maturities of three months or less when purchased to be cash equivalents. Cash equivalents are recorded at fair value in the consolidated balance sheets and exclude amounts included in long-term investments and investments for current use.

Inventories

Inventories (primarily supplies and pharmaceuticals) are stated at an average cost or the lower of cost (first-in, first-out method) or market and are recorded in other current assets.

Property, Plant, and Equipment

Property, plant, and equipment purchased by the System are recorded at cost. Donated property, plant, and equipment are recorded at fair value at the date of donation. Expenditures that substantially increase the useful lives of existing assets are capitalized. Routine maintenance and repairs are expensed as incurred. Depreciation, including amortization of capital leased assets, is computed by the straight-line method using the estimated useful lives of individual assets. Buildings and building components are assigned useful lives ranging from five years to forty years. Equipment is assigned a useful life ranging from three to twenty years. Interest cost incurred on borrowed funds during the period of construction of capital assets and interest income on unexpended project funds are capitalized as a component of the cost of acquiring those assets. The System records costs and legal obligations associated with long-lived asset retirements. Assets acquired though capital lease arrangements are excluded from the consolidated statements of cash flows.

Impairment of Long-Lived Assets

The System evaluates the recoverability of long-lived assets and the related estimated remaining lives when indicators of impairment are present. For purposes of impairment analysis, assets are grouped with other assets and liabilities at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities. The System records an impairment charge or changes the useful life if events or changes in circumstances indicate that the carrying amount may not be recoverable or the useful life has changed.

2. Accounting Policies (continued)

Investments and Investment Income

Investments in equity securities with readily determinable fair values and all investments in debt securities are recorded at fair value in the consolidated balance sheets. Investments, excluding alternative investments, are primarily classified as trading. Investment transactions are recorded on a settlement date basis. Realized gains and losses are determined using the average cost method.

Investments in alternative investments, which include hedge funds, private equity/venture funds and real estate funds, are primarily limited partnerships that invest in marketable securities, privately held securities, real estate, and derivative products and are reported using the equity method of accounting based on net asset value information provided by the respective partnership or third-party fund administrators. Investments held by the partnerships consist of marketable securities as well as securities that do not have readily determinable values. The values of the securities held by the limited partnerships that do not have readily determinable values are determined by the general partner and are based on historical cost, appraisals, or other valuation estimates that require varying degrees of judgment. There is inherent uncertainty in such valuations, and the estimated fair values may differ from the values that would have been used had a ready market for the securities existed. Generally, the equity method investment balance of the System's holdings in alternative investments reflects net contributions to the partnerships and the System's share of realized and unrealized investment income and expenses. The investments may individually expose the System to securities lending, short sales, and trading in futures and forward contract options and other derivative products. The System's risk is limited to its carrying value. The financial statements of the limited partnerships are audited annually.

Alternative investments can be divested only at specified times in accordance with terms of the partnership agreements. Hedge fund redemptions typically contain restrictions that allow for a portion of the withdrawal proceeds to be held back from distribution while the underlying investments are liquidated. These redemptions are subject to lock-up provisions that are generally imposed upon initial investment in the fund. Private equity/venture funds and real estate funds are generally closed-end funds and have significant redemption restrictions that prohibit redemptions during the fund's life.

2. Accounting Policies (continued)

Investment return, including equity method income on alternative investments, is reported as nonoperating gains and losses, except for earnings on funds held by bond trustees and interest and dividends earned on assets held by the captive insurance subsidiary, which are included in other unrestricted revenues. Donor-restricted investment return on temporarily and permanently restricted investments is included in temporarily restricted net assets.

Certain of the System's assets and liabilities are exposed to various risks, such as interest rate, market, and credit risks.

Fair Value Measurements

Fair value measurements are defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Authoritative guidance provides an option to elect fair value as an alternative measurement for selected financial assets and liabilities not previously recorded at fair value. The System did not elect fair value accounting for any assets or liabilities that are not currently required to be measured at fair value.

The framework for measuring fair value is comprised of a three-level hierarchy based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

- Level 2 – inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

- Level 3 – inputs to the valuation methodology are unobservable and significant to the fair value measurement.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

2. Accounting Policies (continued)

Goodwill

Goodwill has resulted from business combinations, primarily physician practice acquisitions, and is based on the purchase price in excess of the fair values of assets acquired and liabilities assumed at the acquisition date. Annually, or when indicators of impairment exist, the System evaluates goodwill for impairment to determine whether there are events or circumstances that indicate it is more likely than not that the fair value of a reporting unit is less than its carrying amount. The System determined that there was no goodwill impairment for the years ended December 31, 2014 and 2013. Goodwill is recorded in other noncurrent assets in the consolidated balance sheets.

Derivatives and Hedging Activities

The System's derivative financial instruments consist of interest rate swaps (Note 11), which are recognized as assets or liabilities in the consolidated balance sheets at fair value.

The System accounts for changes in the fair value of derivative instruments depending on whether they are designated and qualified as part of a hedging relationship and further, on the type of hedging relationship. The System has not designated any derivative instruments as hedges. Accordingly, the changes in fair value of derivative instruments and the related cash payments are recorded in derivative (losses) gains in the consolidated statements of operations and changes in net assets.

Bond Financing Costs

Bond financing costs are amortized over the period the obligation is outstanding using the straight-line method, which approximates the interest method.

2. Accounting Policies (continued)

Contributions

Unconditional donor pledges to give cash, marketable securities, and other assets are reported at fair value at the date the pledge is made to the extent estimated to be collectible by the System. Conditional donor promises to give and indications of intentions to give are not recognized until the condition is satisfied. Pledges received with donor restrictions that limit the use of the donated assets are reported as either temporarily or permanently restricted support. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are transferred to unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as other unrestricted revenues if the purpose relates to operations or reported as a change in unrestricted net assets if the purpose relates to capital.

No amounts have been reflected in the consolidated financial statements for donated services. The System pays for most services requiring specific expertise. However, many individuals volunteer their time and perform a variety of tasks that assist the System with various programs.

Grants

Grant revenue is recognized in the period it is earned based on when the applicable project expenses are incurred and project milestones are achieved. Grant payments received in advance of related project expenses are deferred until the expenditure has been incurred and recorded as deferred revenue and included in other current liabilities. The System recorded research grant revenue, included in other unrestricted revenues, of $179.8 million and $170.8 million in 2014 and 2013, respectively.

2. Accounting Policies (continued)

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are used to differentiate resources, the use of which is restricted by donors or grantors to a specific time period or purpose, from resources on which no restrictions have been placed or that arise from the general operations of the System. Temporarily restricted gifts and bequests are recorded as an addition to temporarily restricted net assets in the period received. Permanently restricted net assets consist of amounts held in perpetuity or for terms designated by donors, including the fair value of several perpetual trusts for which the System is an income beneficiary or the beneficial interest in the fair value of underlying trust assets. Earnings on permanently restricted net assets are recorded as investment income in temporarily restricted net assets and subsequently used in accordance with the donor's designation. Temporarily and permanently restricted net assets are primarily restricted for research, education, and strategic capital projects.

The System returned $0.3 million and $1.7 million in 2014 and 2013, respectively, from temporarily restricted net assets to unrestricted net assets that had been transferred in prior years for the purpose of maintaining donor-restricted endowment funds at the level required by donor stipulations or law.

Excess of Revenues Over Expenses

The consolidated statements of operations and changes in net assets include excess of revenues over expenses. Changes in unrestricted net assets, which are excluded from excess of revenues over expenses, consistent with industry practice, include unrealized gains and losses on investments classified as nontrading, retirement benefits adjustments, contributions of long-lived assets (including assets acquired using grants or contributions that by donor restriction were to be used for the purpose of acquiring such assets), and transfers of net assets to maintain donor-restricted endowment funds at the level required by donor stipulations or law.

3. Net Patient Service Revenue and Patient Receivables

Net patient service revenue before the provision for uncollectible accounts by major payor source for the years ended December 31, 2014 and 2013, are as follows (in thousands):

	2014		2013	
Medicare	**$ 1,885,973**	**29%**	$ 1,812,579	29%
Medicaid	**260,724**	**4**	199,471	3
Managed care and commercial	**3,943,338**	**62**	3,804,656	61
Self-pay	**338,903**	**5**	467,821	7
	$ 6,428,938	**100%**	$ 6,284,527	100%

The System has experienced a decrease in self-pay revenue resulting from expansion of Medicaid eligibility in the State of Ohio, which has increased enrollment in the Medicaid program in 2014 and decreased the number of self-pay patients. The System records an estimated provision for uncollectible accounts in the year of service for patient receivables associated with self-pay patients, including patients with deductible and copayment balances for which third-party coverage provides for a portion of the services provided. The System does not maintain a material allowance for uncollectible accounts from third-party payors.

The System's allowance for doubtful accounts was 21% and 19% of accounts receivable at December 31, 2014 and 2013, respectively. The increase in the allowance for uncollectible accounts was primarily due to growth in patient deductibles and co-payment balances as a result of the Affordable Care Act and other industry trends. Write-offs on self-pay accounts receivable decreased $70.9 million in 2014 compared to 2013.

The System's concentration of credit risk relating to patient receivables is limited due to the diversity of patients and payors. Patient receivables consist of amounts due from government programs, commercial insurance companies, other group insurance programs, and private pay patients. Patient receivables due from Medicare, Medicaid, and one commercial payor account for approximately 22%, 7%, and 23% at December 31, 2014, and 21%, 5%, and 24% at December 31, 2013, respectively, of the System's total patient receivables. Revenues from the Medicare and Medicaid programs and one commercial payor account for approximately 29%, 4%, and 17% for 2014, and 29%, 3%, and 17% for 2013, respectively, of the System's net patient service revenue. Excluding these payors, no one payor represents more than 10% of the System's patient receivables or net patient service revenue.

4. Cash, Cash Equivalents, and Investments

The composition of cash, cash equivalents, and investments at December 31, 2014 and 2013 is as follows (in thousands):

	2014	2013
Cash and cash equivalents	**$ 661,610**	$ 253,041
Fixed income securities:		
U.S. treasuries	**629,321**	622,899
U.S. government agencies	**20,416**	23,563
U.S. corporate	**172,947**	174,152
U.S. government agencies asset-backed securities	**21,582**	7,449
Corporate asset-backed securities	**8,802**	6,924
Foreign	**47,115**	30,247
Fixed income mutual funds	**53,235**	15,052
Commingled fixed income funds	**779,183**	758,376
Common and preferred stocks:		
U.S.	**611,748**	612,891
Foreign	**237,609**	246,930
Equity mutual funds	**238,320**	239,906
Commingled equity funds	**1,165,477**	955,515
Alternative investments:		
Hedge funds	**1,275,549**	1,246,624
Private equity/venture funds	**434,798**	418,677
Real estate	**357,456**	250,049
Pending purchases of investments	**150,000**	–
Total cash, cash equivalents, and investments	**$ 6,865,168**	$ 5,862,295

Pending purchases of investments of $150 million at December 31, 2014 were invested as $50 million in commingled equity funds and $100 million in hedge funds on January 1, 2015.

4. Cash, Cash Equivalents, and Investments (continued)

Investments are primarily maintained in a master trust fund administered using a bank as trustee. The management of the majority of the System's investments is conducted by numerous external investment management organizations that are monitored by management and an external third-party advisor. Of these investment managers, 19 managers focus on equity investments, 15 managers focus on fixed income investments, and 106 managers focus on alternative investments. The alternative investments have separate administrators and custodian arrangements. Alternative investments also include three holdings in which the System invests directly.

Total investment return is comprised of the following for the years ended December 31, 2014 and 2013 (in thousands):

	2014	2013
Other unrestricted revenues:		
Interest income and dividends	**$ 1,425**	$ 1,413
Nonoperating gains, net:		
Interest income and dividends	**52,357**	51,744
Net realized gains on sales of investments	**150,550**	186,598
Net change in unrealized gains/losses on investments	**24,850**	163,927
Equity method income on alternative investments	**104,540**	157,949
Investment management fees	**(16,080)**	(13,820)
	316,217	546,398
Other changes in net assets:		
Net change in unrealized gains (losses) on nontrading investments	**3,163**	(93)
Investment income on restricted investments	**18,079**	30,555
Total investment return	**$ 338,884**	$ 578,273

5. Other Current Assets and Liabilities and Other Noncurrent Assets and Liabilities

Other current and noncurrent assets at December 31, 2014 and 2013 consist of the following (in thousands):

	2014	2013
Current:		
Inventories	**$ 110,873**	$ 101,424
Estimated amounts due from third-party payors	**67,409**	45,269
Pledges receivable current *(see Note 8)*	**43,698**	44,896
Prepaid expenses	**35,531**	34,566
Research receivables	**27,868**	32,324
Other	**46,696**	36,580
Total other current assets	**$ 332,075**	$ 295,059

	2014	2013
Noncurrent:		
Deferred compensation plan assets	**$ 140,239**	$ 122,288
Investments in affiliates	**132,755**	34,797
Goodwill	**35,056**	19,202
Unamortized bond financing costs	**24,078**	19,148
Other	**35,253**	25,822
Total other noncurrent assets	**$ 367,381**	$ 221,257

In September 2014, the Foundation and Akron General entered into an affiliation agreement to make the Foundation a minority member of Akron General with limited reserve powers. Akron General is an integrated healthcare delivery system located in Northeast Ohio. The investment in Akron General was $100 million, comprised of $10 million cash and $90 million note payable, and is included in investments in affiliates in other noncurrent assets on the consolidated balance sheet. As a result of this investment, the Foundation acquired a 35% special membership interest in Akron General and has determined that the Foundation has significant influence over the operations of Akron General but lacks control. Accordingly, the Foundation records its investment under the equity method of accounting. The Foundation recorded $3.5 million in equity earnings for the year ended December 31, 2014, which is recorded in other unrestricted revenues in the accompanying consolidated statements of operations and changes in net assets.

5. Other Current Assets and Liabilities and Other Noncurrent Assets and Liabilities (continued)

Other current and noncurrent liabilities at December 31, 2014 and 2013 consist of the following (in thousands):

	2014	2013
Current:		
Research deferred revenue	**$ 67,186**	$ 59,274
Estimated amounts due to third-party payors	**66,522**	42,314
Interest payable	**56,534**	51,629
Current portion of professional and general liability insurance reserves *(see Note 12)*	**46,828**	47,306
Employee benefit related liabilities	**37,700**	32,543
State assessment liabilities	**35,847**	31,370
International contracts and other deferred revenue	**31,174**	33,079
Other	**93,024**	84,034
Total other current liabilities	**$ 434,815**	$ 381,549

	2014	2013
Noncurrent:		
Employee benefit related liabilities	**$ 183,749**	$ 176,037
Interest rate swap liability *(see Note 11)*	**152,395**	98,402
Estimated amounts due to third-party payors	**16,677**	15,710
Accrued income tax liabilities *(see Note 14)*	**9,664**	10,763
Gift annuity liabilities	**10,811**	10,636
Other	**70,141**	101,964
Total other noncurrent liabilities	**$ 443,437**	$ 413,512

6. Fair Value Measurements

The carrying values of accounts receivable and accounts payable are reasonable estimates of fair value due to the short-term nature of these financial instruments. Investments, other than alternative investments, are recorded at their fair value. Other current and noncurrent assets and liabilities have carrying values that approximate fair value.

The fair value of the System's pledges receivable is based on discounted cash flow analysis using treasury yield curve interest rates consistent with the maturities of the pledges receivable and adjusted for consideration of the donor's credit. The fair value of pledges receivable was $213.3 million and $179.3 million (see carrying value at Note 8) at December 31, 2014 and 2013, respectively. Pledges receivable would be classified as Level 3 in the fair value hierarchy.

The fair value of the System's long-term debt is estimated by discounted cash flow analyses using current borrowing rates for similar types of borrowing arrangements and adjusted for the System's credit. Inputs, which include reported/comparable trades, broker/dealer quotes, bids and offerings, are obtained from various sources, including market participants, dealers, brokers and various news media/market information. The fair value of long-term debt was $3.3 billion and $2.9 billion (see carrying value at Note 10) at December 31, 2014 and 2013, respectively. Long-term debt would be classified as Level 2 in the fair value hierarchy.

6. Fair Value Measurements (continued)

The following tables present the financial instruments measured at fair value on a recurring basis as of December 31, 2014 and 2013, based on the valuation hierarchy (in thousands):

December 31, 2014	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets				
Cash and investments:				
Cash and cash equivalents	**$ 661,598**	**$ 12**	**$ –**	**$ 661,610**
Fixed income securities:				
U.S. treasuries	**629,321**	**–**	**–**	**629,321**
U.S. government agencies	**–**	**20,416**	**–**	**20,416**
U.S. corporate	**–**	**172,947**	**–**	**172,947**
U.S. government agencies asset-backed securities	**–**	**21,582**	**–**	**21,582**
Corporate asset-backed securities	**–**	**8,802**	**–**	**8,802**
Foreign	**–**	**47,115**	**–**	**47,115**
Fixed income mutual funds	**53,235**	**–**	**–**	**53,235**
Commingled fixed income funds	**–**	**779,183**	**–**	**779,183**
Common and preferred stocks:				
U.S.	**609,133**	**2,615**	**–**	**611,748**
Foreign	**235,907**	**1,702**	**–**	**237,609**
Equity mutual funds	**238,320**	**–**	**–**	**238,320**
Commingled equity funds	**–**	**1,165,477**	**–**	**1,165,477**
Total cash and investments	**2,427,514**	**2,219,851**	**–**	**4,647,365**
Perpetual and charitable trusts	**–**	**66,231**	**–**	**66,231**
Total assets at fair value	**$ 2,427,514**	**$ 2,286,082**	**$ –**	**$ 4,713,596**
Liabilities				
Interest rate swaps	**$ –**	**$ 152,395**	**$ –**	**$ 152,395**
Total liabilities at fair value	**$ –**	**$ 152,395**	**$ –**	**$ 152,395**

6. Fair Value Measurements (continued)

December 31, 2013	Level 1	Level 2	Level 3	Total
Assets				
Cash and investments:				
Cash and cash equivalents	$ 252,398	$ 643	$ –	$ 253,041
Fixed income securities:				
U.S. treasuries	622,899	–	–	622,899
U.S. government agencies	–	23,563	–	23,563
U.S. corporate	–	174,152	–	174,152
U.S. government agencies asset-backed securities	–	7,449	–	7,449
Corporate asset-backed securities	–	6,924	–	6,924
Foreign	–	30,247	–	30,247
Fixed income mutual fund	15,052	–	–	15,052
Commingled fixed income funds	–	758,376	–	758,376
Common and preferred stocks:				
U.S.	611,943	948	–	612,891
Foreign	246,930	–	–	246,930
Equity mutual funds	239,906	–	–	239,906
Commingled equity funds	–	955,515	–	955,515
Total cash and investments	1,989,128	1,957,817	–	3,946,945
Perpetual and charitable trusts	–	61,874	–	61,874
Total assets at fair value	$ 1,989,128	$ 2,019,691	$ –	$ 4,008,819
Liabilities				
Interest rate swaps	$ –	$ 98,402	$ –	$ 98,402
Total liabilities at fair value	$ –	$ 98,402	$ –	$ 98,402

6. Fair Value Measurements (continued)

Financial instruments at December 31, 2014 and 2013 are reflected in the consolidated balance sheets as follows (in thousands):

	2014	2013
Cash, cash equivalents, and investments measured at fair value	**$ 4,647,365**	$ 3,946,945
Alternative investments accounted for under the equity method	**2,067,803**	1,915,350
Pending purchases of investments	**150,000**	–
Total cash, cash equivalents, and investments	**$ 6,865,168**	$ 5,862,295
Perpetual and charitable trusts measured at fair value	**$ 66,231**	$ 61,874
Interests in foundations	**56,267**	56,400
Trusts and interests in foundations	**$ 122,498**	$ 118,274

Interest rate swaps (Note 11) are reported in other noncurrent liabilities in the consolidated balance sheets.

The following is a description of the System's valuation methodologies for assets and liabilities measured at fair value. Fair value for Level 1 is based upon quoted market prices. Fair value for Level 2 is determined as follows:

Investments classified as Level 2 are primarily determined using techniques that are consistent with the market approach. Valuations are based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Inputs, which include broker/dealer quotes, reported/comparable trades, and benchmark yields, are obtained from various sources, including market participants, dealers, and brokers. Commingled investment funds are valued using, as a practical expedient, the net asset value as provided by the respective investment companies and partnerships. There are no significant redemption restrictions on the commingled investment funds.

6. Fair Value Measurements (continued)

The fair value of perpetual and charitable trusts in which the System receives periodic payments from the trust is determined based on the present value of expected cash flows to be received from the trust using discount rates ranging from 3.8% to 5.0%, which are based on Treasury yield curve interest rates or the assumed yield of the trust assets. The fair value of charitable trusts in which the System is a remainder beneficiary is based on the System's beneficial interest in the investments held in the trust, which are measured at fair value.

The fair value of interest rate swaps is determined based on the present value of expected future cash flows using discount rates appropriate with the risks involved. The valuations include a credit spread adjustment to market interest rate curves to appropriately reflect nonperformance risk. The credit spread adjustment is derived from other comparably rated entities' bonds recently priced in the market. The System manages credit risk based on the net portfolio exposure with each counterparty.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the System believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

7. Property, Plant, and Equipment

Property, plant, and equipment at December 31, 2014 and 2013 consist of the following (in thousands):

	2014	2013
Land and improvements	**$ 355,503**	$ 348,165
Buildings	**4,428,136**	4,269,866
Leasehold improvements	**29,360**	29,164
Equipment	**1,409,358**	1,437,438
Computer hardware and software	**740,051**	625,252
Construction-in-progress	**261,979**	198,709
Leased facilities and equipment	**92,883**	92,144
	7,317,270	7,000,738
Accumulated depreciation and amortization	**(3,717,663)**	(3,460,957)
	$ 3,599,607	$ 3,539,781

7. Property, Plant, and Equipment (continued)

Included in the preceding table is unamortized computer software of $83.4 million and $68.5 million at December 31, 2014 and 2013, respectively. Amortization of computer software totaled $26.3 million and $27.2 million in 2014 and 2013, respectively. Amortization of computer software for the five years subsequent to December 31, 2014, is as follows (in thousands): 2015 – $25,224; 2016 – $19,889; 2017 – $13,042; 2018 – $8,293; and 2019 – $5,547.

Accumulated amortization of leased facilities and equipment was $28.7 million and $29.9 million at December 31, 2014 and 2013, respectively.

8. Pledges

Outstanding pledges receivable from various corporations, foundations, and individuals at December 31, 2014 and 2013, are as follows (in thousands):

	2014	2013
Pledges due:		
In less than one year	**$ 62,699**	$ 55,675
In one to five years	**103,391**	90,431
In more than five years	**103,946**	70,812
	270,036	216,918
Allowance for uncollectible pledges and discounting	**(64,581)**	(36,565)
Current portion (net of allowance for uncollectible pledges of $19.0 million in 2014 and $10.8 million in 2013)	**(43,698)**	(44,896)
	$ 161,757	$ 135,457

9. Notes Payable and Capital Leases

Notes payable and capital leases at December 31, 2014 and 2013 consist of the following (in thousands):

	2014	2013
Installments and mortgage notes with interest rates up to 6.0%	**$ 106,908**	$ 20,512
Capital leases for facilities and equipment	**70,144**	65,107
City of Lakewood lease	**10,134**	10,640
	187,186	96,259
Less current portion	**(11,638)**	(9,633)
Total notes payable and capital leases	**$ 175,548**	$ 86,626

In 2014, the Foundation executed a $90.0 million promissory note in connection with the investment in Akron General. Payments on the promissory note will be made to Akron General in accordance with the affiliation agreement. The promissory note is excluded from the consolidated statement of cash flows.

In October 2013, Lakewood Hospital Association (Lakewood) executed a $4.8 million taxable term loan with a financial institution. The proceeds of the term loan were used to pay a portion of the refunding of the Lakewood Series 2003 Bonds.

Maturities of the installment and mortgage notes for the five years subsequent to December 31, 2014, are as follows (in thousands): 2015 – $3,114; 2016 – $8,898; 2017 – $4,788; 2018 – $82; and 2019 – $26.

Future minimum capital lease payments, including total interest of $25.0 million, are as follows (in thousands): 2015 – $12,942; 2016 – $19,794; 2017 – $9,727; 2018 – $7,809; 2019 – $9,217; and thereafter – $35,639. Assets acquired through capital lease arrangements are included in property, plant, and equipment.

9. Notes Payable and Capital Leases (continued)

The City of Lakewood, Ohio (the City) leases real and personal property to Lakewood for the purpose of operating Lakewood. In connection with executing an Amended Lease with the City, Lakewood has agreed to make additional payments to the City. The additional payments commenced in 1997 and range in annual amounts from $1.0 million to $1.2 million through 2026. The net present value of the additional payments is $10.1 million and $10.6 million at December 31, 2014 and 2013, respectively (discounted at an interest rate of 6%). In connection with the Amended Lease, Lakewood has approximately $96 million of net assets, included in the System's unrestricted net assets at December 31, 2014, available for Lakewood's use but unavailable to other members of the System.

10. Bonds

Bonds at December 31, 2014 and 2013 consist of the following (in thousands):

	Interest Rate(s)	Final Maturity	Amount Outstanding at December 31 2014	2013
Series 2014	4.86%	2114	**$ 400,000**	$ –
Series 2013A	3.62% to 4.04%	2042	**89,380**	105,445
Series 2013B	Variable rate	2039	**201,160**	201,160
Series 2013, Keep Memory Alive	Variable rate	2037	**66,850**	68,600
Series 2012A	0.97% to 4.07%	2039	**469,485**	469,485
Series 2011A	1.69% to 4.83%	2032	**190,085**	191,010
Series 2011B	2.94%	2031	**33,270**	35,190
Series 2011C	2.73% to 4.72%	2032	**170,995**	170,995
Series 2009A	5.58%	2039	**305,400**	305,400
Series 2009B	3.20% to 5.58%	2039	**395,165**	408,215
Series 2008A	3.93% to 5.55%	2043	**429,500**	438,395
Series 2008B	Variable rate	2043	**369,250**	369,250
Series 2003C	Variable rate	2035	**41,905**	41,905
Series 2002	Variable rate	2032	**10,225**	10,485
			3,172,670	2,815,535
Net unamortized premium			**56,407**	58,940
Current portion			**(44,140)**	(42,865)
Long-term variable rate debt classified as current			**(386,875)**	(488,230)
			$ 2,798,062	$ 2,343,380

The majority of the System's outstanding revenue bonds are limited obligations of various issuing authorities payable solely by the System pursuant to loan agreements between the borrowing entities and the issuing authorities. Under various financing agreements, the System must meet certain operating and financial performance covenants. The Series 2014 bonds and the Keep Memory Alive Series 2013 bonds are issued directly by the Foundation and Keep Memory Alive, respectively.

10. Bonds (continued)

In September 2014, the System issued $400.0 million of Taxable Bonds (the Series 2014 Bonds). The System used the proceeds of the Series 2014 Bonds for authorized corporate purposes, which purposes may include, without limitation, payment of capital expenditures, current operating expenses and costs related to the issuance of the Series 2014 Bonds. The Series 2014 Bonds are century bonds with a single bullet principal maturity date in 2114. The System capitalized $5.0 million of bond financing costs in connection with the issuance of the Series 2014 Bonds.

In November 2014, pursuant to certain agreements between the System and the State of Ohio (State) acting by and through the Ohio Higher Education Facility Commission, the System established the Cleveland Clinic Health System Obligated Group Commercial Paper Program, which provides for the issuance of Taxable Hospital Revenue Commercial Paper Notes (the Series 2014A CP Notes) for the benefit of the System. The Series 2014A CP Notes may be issued from time to time in a maximum outstanding face amount of $100.0 million. As of December 31, 2014, there were no amounts outstanding on the Series 2014A CP Notes. Proceeds from the sale of the Series 2014A CP Notes will be used to pay or reimburse costs of acquiring, constructing, reconstructing, renovating, equipping, furnishing and improving healthcare facilities of certain System entities in the State of Ohio. The System capitalized $0.5 million of bond financing costs in connection with the establishment of the Cleveland Clinic Health System Obligated Group Commercial Paper Program.

In May 2013, pursuant to certain agreements between the System and the State acting by and through the Ohio Higher Education Facility Commission, the State issued $105.4 million of Hospital Revenue Bonds (the Series 2013A Bonds), comprised of $62.6 million of fixed-rate bonds and $42.8 million of index-rate bonds, and $201.2 million of variable-rate Hospital Revenue Bonds (the Series 2013B Bonds) for the benefit of the System. Proceeds from the sale of the Series 2013A Bonds were used to refund all of the outstanding fixed-rate Series 2003A Bonds, and proceeds from the sale of the Series 2013B Bonds were used to refund all of the outstanding variable-rate Series 2004B Bonds. The balance of the proceeds was used to finance certain capital expenditures of the System and pay the costs of issuance. The Series 2013A Bonds were sold at a net premium of $2.8 million. The System recorded a gain on extinguishment of debt of $0.4 million in 2013 related to this transaction, which is recorded in other nonoperating gains and losses in the consolidated statements of operations and changes in net assets, and includes an offset of $1.2 million of previously unamortized bond financing costs related to the refunded bonds. The System capitalized $2.1 million of bond financing costs in connection with the issuance of the Series 2013A Bonds and Series 2013B Bonds.

10. Bonds (continued)

In October 2013, the Lakewood Series 2003 Bonds were refunded. The System recorded a gain on extinguishment of debt of $0.1 million in 2013 related to this transaction, which is recorded in other nonoperating gains and losses in the consolidated statements of operations and changes in net assets, and includes an offset of $0.1 million of previously unamortized bond financing costs related to the refunded bonds.

In November 2013, Keep Memory Alive issued $68.6 million of taxable variable rate demand bonds (the Series 2013 KMA Bonds). Proceeds from the sale of the Series 2013 KMA Bonds were used to refund all of the outstanding variable rate Series 2007A Bonds. The System recorded a loss on extinguishment of debt of $1.2 million in 2013 related to this transaction, which is recorded in other nonoperating gains and losses in the consolidated statements of operations and changes in net assets, and represents previously unamortized bond financing costs related to the refunded bonds. The System capitalized $0.3 million of bond financing costs in connection with the issuance of the Series 2013 KMA Bonds.

Certain of the System's current outstanding bonds bear interest at a variable rate. During 2014 and 2013, the rates for the System's variable rate bonds ranged from 0.01% to 0.15% (average rate 0.08%) and 0.01% to 0.25% (average rate 0.11%), respectively.

Certain variable rate revenue bonds are secured by irrevocable direct pay letters of credit and standby bond purchase agreements totaling $381.8 million at December 31, 2014. The letter-of-credit agreement for the Series 2002 Bonds requires repayment of a remarketing draw within one year, and as such, these bonds are classified as current in the consolidated balance sheets. The letter-of-credit agreement for the Series 2013 KMA Bonds contains a subjective clause that, if declared by the lender, could cause immediate repayment of the bonds. As a result, these bonds are classified as current in the consolidated balance sheets.

The System provides self-liquidity on the Series 2003C Bonds and certain sub-series of the Series 2008B Bonds. These bonds are classified as current liabilities in the consolidated balance sheets. In November 2014, certain sub-series of the 2008B Bonds totaling $99.3 million were substituted with a liquidity facility providing support through a standby bond purchase agreement that qualifies for long-term classification of the bonds. Previously, the bonds were supported by the System's self-liquidity program.

10. Bonds (continued)

During the term of agreements with the issuing authorities, the System is required to make specified deposits with trustees to fund principal and interest payments when due. Also, unexpended bond proceeds are held by the trustee and released to the System for approved requisition requests for capital projects. There were no unexpended bond proceeds at December 31, 2014 and 2013. The current portion of the funds held by trustees, which consist of deposits with the trustees to fund current principal and interest payments were $98.0 million and $91.8 million at December 31, 2014 and 2013, respectively, and is included in investments for current use.

The System is subject to certain restrictive covenants, including provisions relating to certain debt ratios, days cash on hand, and other matters. The System was in compliance with these covenants at December 31, 2014 and 2013.

Combined current aggregate scheduled maturities, assuming the remarketing of the variable rate demand bonds, for the five years subsequent to December 31, 2014, are as follows (in thousands): 2015 – $44,140; 2016 – $55,150; 2017 – $58,670; and 2018 – $60,920; and 2019 – $64,040.

Total interest paid approximated $108.4 million and $112.6 million in 2014 and 2013, respectively. Capitalized interest cost approximated $2.9 million and $3.9 million in 2014 and 2013, respectively.

11. Interest Rate Swaps

The System's objective with respect to interest rate risk is to manage the risk of rising interest rates on the System's variable rate debt and certain variable rate operating lease payments. Consistent with its interest rate risk management objective, the System entered into various interest rate swap agreements with a total outstanding notional amount of $612.6 million and $625.4 million at December 31, 2014 and 2013, respectively. During the term of these transactions, the System pays interest at a fixed rate and receives interest at a variable rate based on the London Interbank Offered Rate (LIBOR) or the Securities Industry and Financial Markets Association Index (SIFMA). The swap agreements are not designated as hedging instruments. Net interest paid or received under the swap agreements is included in derivative (losses) gains in the consolidated statements of operations and changes in net assets.

The following table summarizes the System's interest rate swap agreements (in thousands):

Swap Type	Expiration Date	System Pays	System Receives	Notional Amount at December 31 2014	Notional Amount at December 31 2013
Fixed	2016	5.28%	100% of SIFMA	**$ 8,080**	$ 11,810
Fixed	2021	3.21%	68% of LIBOR	**36,240**	37,670
Fixed	2024	3.42%	68% of LIBOR	**28,800**	29,300
Fixed	2027	3.56%	68% of LIBOR	**135,939**	139,525
Fixed	2028	5.12%	100% of LIBOR	**40,785**	41,710
Fixed	2028	3.51%	68% of LIBOR	**31,495**	32,085
Fixed	2030	5.07%	100% of LIBOR	**62,500**	62,500
Fixed	2030	5.06%	100% of LIBOR	**62,500**	62,500
Fixed	2032	4.32%	79% of LIBOR	**2,509**	2,574
Fixed	2032	4.33%	70% of LIBOR	**5,017**	5,147
Fixed	2032	3.78%	70% of LIBOR	**2,509**	2,574
Fixed	2036	4.90%	100% of LIBOR	**50,000**	50,000
Fixed	2036	4.90%	100% of LIBOR	**79,375**	79,375
Fixed	2037	4.62%	100% of SIFMA	**66,850**	68,600
				$ 612,599	$ 625,370

11. Interest Rate Swaps (continued)

The following table summarizes the location and fair value for the System's interest rate swap agreements (in thousands):

	Derivatives Liability			
	December 31, 2014		December 31, 2013	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives not designated as hedging instruments				
Interest rate swap agreements	Other noncurrent liabilities	**$ 152,395**	Other noncurrent liabilities	$ 98,402

The following table summarizes the location and amounts of derivative (losses) gains on the System's interest rate swap agreements (in thousands):

	Location of (Loss) Gain Recognized	Year Ended December 31 2014	2013
Derivatives not designated as hedging instruments			
Interest rate swap agreements	Derivative (losses) gains	**$ (79,786)**	$ 60,945

The System has used various derivative contracts in connection with certain prior obligations and investments. Although minimum credit ratings are required for counterparties, this does not eliminate the risk that a counterparty may fail to honor its obligations. Derivative contracts are subject to periodic "mark-to-market" valuations. A derivative contract may, at any time, have a positive or negative value to the System. In the event that the negative value reaches certain thresholds established in the derivative contracts, the System is required to post collateral, which could adversely affect its liquidity. At December 31, 2014 and 2013, the System posted $88.2 million and $41.9 million, respectively, of collateral with counterparties that is included in funds held by trustees in the consolidated balance sheets. In addition, if the System were to choose to terminate a derivative contract or if a derivative contract were terminated pursuant to an event of default or a termination event as described in the derivative contract, the System could be required to pay a termination payment to the counterparty.

12. Professional and General Liability Insurance

The System manages its professional and general liability insurance program through a captive insurance arrangement.

In the ordinary course of business, professional and general liability claims have been asserted against the System by various claimants. These claims are in various stages of processing or, in certain instances, are in litigation. In addition, there are known incidents, and there also may be unknown incidents, which may result in the assertion of additional claims. The System has accrued its best estimate of both asserted and unasserted claims based on actuarially determined amounts. These estimates are subject to the effects of trends in loss severity and frequency, and ultimate settlement of professional and general liability claims may vary significantly from the estimated amounts.

The System's professional and general liability insurance reserves of $190.1 million and $180.5 million at December 31, 2014 and 2013, respectively, are recorded as current and noncurrent liabilities and include discounted estimates of the ultimate costs for both asserted claims and unasserted claims. Asserted claims were discounted at 1.25% and 0.75% at December 31, 2014 and 2013, respectively. Unasserted claims were discounted at 1.75% at both December 31, 2014 and 2013. Through the captive insurance subsidiary, the System has set aside investments of $153.1 million ($46.8 million included in investments for current use) and $143.0 million ($47.3 million included in investments for current use) at December 31, 2014 and 2013, respectively, of which $36.1 million and $35.1 million at December 31, 2014 and 2013, respectively, are restricted in accordance with reinsurance trust agreements related to coverage of the Florida operations and other reinsurance programs provided by the captive insurance subsidiary.

12. Professional and General Liability Insurance (continued)

Activity in the professional and general liability insurance reserves is summarized as follows (in thousands):

	2014	2013
Balance at beginning of year	**$ 180,482**	$ 172,356
Incurred related to:		
Current period	**57,476**	54,626
Prior period	**(29)**	(2,730)
Total incurred	**57,447**	51,896
Paid related to:		
Current period	**1,666**	1,774
Prior period	**45,526**	45,607
Total paid	**47,192**	47,381
	10,255	4,515
(Decrease) increase in unasserted claims	**(236)**	3,789
Decrease in reinsurance recoverable	**(433)**	(178)
Balance at end of year	**$ 190,068**	$ 180,482

The foregoing reconciliation shows $29 thousand and $2.7 million of favorable development in 2014 and 2013, respectively, due to changes in the actuarial estimates as a result of lower claim activity, closed claims, and settlement amounts lower than expected due to risk management initiatives and the impact of a series of tort reforms passed by the Ohio General Assembly beginning in 2003. The System utilizes a combination of actual and industry statistics to estimate loss and loss adjustment expense reserves.

13. Pensions and Other Postretirement Benefits

The System has two defined benefit pension plans, including the CCHS Retirement Plan, which covers substantially all of the System's employees. The benefits provided are based on age, years of service, and compensation. The System's policy is to fund at least the minimum amounts required by the Employee Retirement Income Security Act. The CCHS Retirement Plan ceased benefit accruals as of December 31, 2009 for substantially all employees. Benefit accruals for remaining employees ceased at various intervals through December 31, 2012. The System also maintains a nonqualified defined benefit supplemental retirement plan, which covers certain of its employees.

In 2014, the System amended the CCHS Retirement Plan to allow deferred vested participants to commence benefits prior to age 55, effective January 1, 2015. As a result of this amendment, the System recorded a credit of $11.4 million for the year ended December 31, 2014, which is included in retirement benefits adjustment in the accompanying consolidated statement of operations and changes in net assets.

In 2014, approximately 3,600 deferred vested participants in the CCHS Retirement Plan elected to receive a one-time enhanced distribution from the CCHS Retirement Plan. Elections for eligible participants expired in 2014 and all of the distributions occurred prior to the end of 2014. As a result of this transaction, along with additional lump-sum payments made in 2014 according to plan terms, the System recorded a settlement charge of $14.0 million for the year ended December 31, 2014, which is recorded in salaries, wages, and benefits in the accompanying consolidated statement of operations and changes in net assets. Total settlement payments for the System were $140.3 million for the year ended December 31, 2014.

In 2013, a voluntary retirement program was offered to select active participants in the CCHS Retirement Plan and the postretirement health benefit plan. Participants that enrolled in the voluntary retirement program were offered enhanced benefits that commenced in the first quarter of 2014, including an increase in pension benefits from the CCHS Retirement Plan and two years of premium-free retiree medical coverage from the postretirement health benefit plan. The System recorded additional benefit expense of $9.7 million and $5.7 million for the enhanced benefits in the CCHS Retirement Plan and the postretirement health benefit plan, respectively, for the year ended December 31, 2013.

13. Pensions and Other Postretirement Benefits (continued)

The System sponsors two noncontributory, defined contribution plans, and a contributory, defined contribution plan. The Cleveland Clinic Investment Pension Plan (IPP) is a noncontributory, defined contribution plan, which covers substantially all of the System's employees. The System's contribution for the IPP is based upon a percentage of employee compensation and years of service. The System sponsors an additional noncontributory, defined contribution plan, which covers certain of its employees. The System's contribution to the plan is based upon a percentage of employee compensation, as defined, determined according to age. The System also sponsors a contributory, defined contribution plan, which covers substantially all employees. The System's contribution to the contributory plan is determined based on employee contributions.

The System provides healthcare benefits upon retirement for substantially all of its employees. The System's healthcare plans generally provide for cost sharing, in the form of retiree contributions, deductibles, and coinsurance. The System's policy is to fund the annual cost of healthcare benefits from the general assets of the System. The estimated cost of these postretirement benefits is actuarially determined and accrued over the employees' service periods.

The System committed to change certain provisions in its postretirement health benefit plan in 2013. Changes to the plan, which were implemented in 2014 and impacted certain participants in the plan, included increases in co-payments, deductibles and co-insurance limits to better align benefit provisions for all participants in the plan. As a result of these benefit changes, the System recorded a credit of $14.3 million for the year ended December 31, 2013, which is included in retirement benefits adjustment in the consolidated statements of operations and changes in net assets.

In 2014, the mortality tables used to calculate the benefit obligation for the System's defined benefit pension plans and postretirement health benefit plan were updated to separate mortality rates for non-annuitants (based on RP-2014 "Employees" table unadjusted, with generational projection) and annuitants (based on RP-2014 "Healthy Annuitants" table unadjusted, with generational projection). The System believes that the updated mortality rates are the best estimate of future experience.

The System expects to make contributions of $7.8 million to the defined benefit pension plans in 2015. Pension benefit payments over the next ten years are estimated as follows: 2015 – $74.3 million; 2016 – $79.4 million; 2017 – $82.5 million; 2018 – $87.1 million; 2019 – $90.7 million; and in the aggregate for the five years thereafter – $472.3 million.

13. Pensions and Other Postretirement Benefits (continued)

The System expects to make contributions of $8.3 million to other postretirement benefit plans in 2015. Other postretirement benefit payments over the next ten years, net of the average annual Medicare Part D subsidy of approximately $4.4 million, are estimated as follows: 2015 – $8.3 million; 2016 – $5.5 million; 2017 – $5.6 million; 2018 – $5.5 million; 2019 – $9.6 million; and in the aggregate for the five years thereafter – $21.0 million.

No plan assets are expected to be returned to the employer during 2015.

The System is required to recognize the funded status, which is the difference between the fair value of plan assets and the projected benefit obligations, of its pension and other postretirement benefit plans in the consolidated balance sheets, with a corresponding adjustment to unrestricted net assets. Amounts recorded in unrestricted net assets consist of actuarial gains and losses and prior service credits and costs. Actuarial gains and losses recorded in unrestricted net assets outside of the corridor, which is 10% of the greater of the projected benefit obligation or the fair value of the plan assets, will be recognized as a component of net periodic benefit cost immediately in the current period. Prior service credits and costs will be amortized over future periods, pursuant to the System's accounting policy.

Unrecognized prior service credits and costs are amortized on a straight-line basis over the estimated life of the plan participants. In 2015, the System is expected to amortize $3.0 million of unrecognized prior service credits in net periodic benefit costs.

Included in unrestricted net assets at December 31, 2014 and 2013 are the following amounts that have not yet been recognized in net periodic benefit cost (in thousands):

	Defined Benefit Pension Plans		Other Postretirement Benefits	
	2014	**2013**	**2014**	**2013**
Unrecognized actuarial losses (gains)	**$ 155,566**	$ (39,512)	**$ 7,730**	$ 1,336
Unrecognized prior service credit	**(16,125)**	(5,404)	**(6,475)**	(8,874)
Total	**$ 139,441**	$ (44,916)	**$ 1,255**	$ (7,538)

Unrecognized actuarial losses (gains) included in unrestricted net assets represent amounts within the corridor that do not require recognition in net periodic benefit cost for each respective year.

13. Pensions and Other Postretirement Benefits (continued)

Changes in plan assets and benefit obligations recognized in unrestricted net assets during 2014 and 2013 are as follows (in thousands):

	Defined Benefit Pension Plans		Other Postretirement Benefits	
	2014	**2013**	**2014**	**2013**
Current year actuarial (loss) gain	**$ (226,589)**	$ 200,257	**$ (6,394)**	$ 12,284
Recognition of actuarial loss in excess of corridor	**17,489**	–	–	–
Recognition of actuarial loss for settlement charge	**14,022**	–	–	–
Current year prior service credit	**11,380**	–	–	14,332
Amortization of prior service credit	**(659)**	(656)	**(2,399)**	(240)
Total	**$ (184,357)**	$ 199,601	**$ (8,793)**	$ 26,376

13. Pensions and Other Postretirement Benefits (continued)

The following table sets forth the funded status of the System's pensions and other postretirement benefit plans and the amounts recognized in the System's December 31, 2014 and 2013 consolidated balance sheets (in thousands):

	Defined Benefit Pension Plans		Other Postretirement Benefits	
	2014	**2013**	**2014**	**2013**
Change in projected benefit obligation:				
Projected benefit obligation at beginning of year	**$ 1,468,578**	$ 1,607,443	**$ 118,782**	$ 136,205
Service cost	**2,324**	1,458	**1,032**	2,146
Interest cost	**71,870**	65,719	**6,129**	5,902
Actuarial loss (gain)	**192,301**	(132,939)	**6,394**	(12,284)
Participant contributions	**–**	–	**7,760**	6,572
Plan amendments and benefit changes	**(11,380)**	–	**–**	(14,332)
Settlement payments	**(140,285)**	–	**–**	–
Special termination benefits	**–**	9,681	**–**	5,688
Benefits paid	**(27,104)**	(82,784)	**(15,146)**	(12,492)
Federal subsidy	**–**	–	**1,140**	1,377
Projected benefit obligation at end of year	**1,556,304**	1,468,578	**126,091**	118,782
Change in plan assets:				
Fair value of plan assets at beginning of year	**1,309,251**	1,106,528	**–**	–
Actual return on plan assets	**66,432**	155,895	**–**	–
Participant contributions	**–**	–	**7,760**	6,572
System contributions	**5,108**	129,612	**7,386**	5,920
Settlement payments	**(140,285)**	–	**–**	–
Benefits paid	**(27,104)**	(82,784)	**(15,146)**	(12,492)
Fair value of plan assets at end of year	**1,213,402**	1,309,251	**–**	–
Accrued retirement benefits	**$ (342,902)**	$ (159,327)	**$ (126,091)**	$ (118,782)
Current liabilities	**$ (7,832)**	$ (6,839)	**$ (8,264)**	$ (8,011)
Noncurrent liabilities	**(335,070)**	(152,488)	**(117,827)**	(110,771)
Net liability recognized in consolidated balance sheets	**$ (342,902)**	$ (159,327)	**$ (126,091)**	$ (118,782)

The accumulated benefit obligation for all defined benefit pension plans was $1.5 billion at both December 31, 2014 and 2013.

13. Pensions and Other Postretirement Benefits (continued)

The components of net periodic benefit cost (income) are as follows (in thousands):

	Defined Benefit Pension Plans		Other Postretirement Benefits	
	2014	**2013**	**2014**	**2013**
Components of net periodic benefit cost (income):				
Service cost	**$ 2,324**	$ 1,458	**$ 1,032**	$ 2,146
Interest cost	**71,870**	65,719	**6,129**	5,902
Expected return on plan assets	**(100,720)**	(88,577)	–	–
Recognition of actuarial loss in excess of corridor	**17,489**	–	–	–
Amortization of unrecognized prior service credit	**(659)**	(656)	**(2,399)**	(240)
Settlement charge	**14,022**	–	**–**	–
Special termination benefits	–	9,681	**–**	5,688
Net periodic benefit cost (income)	**4,326**	(12,375)	**4,762**	13,496
Defined contribution plans	**187,580**	181,468	–	–
Total included in operations	**$191,906**	$169,093	**$ 4,762**	$ 13,496

Weighted-average assumptions used to determine pension and postretirement benefit obligations and net periodic benefit cost (income) are as follows:

	Defined Benefit Pension Plans		Other Postretirement Benefits	
	2014	**2013**	**2014**	**2013**
Weighted-average assumptions:				
Discount rates:				
Used for benefit obligations	**4.23%**	5.07%	**4.41%**	5.29%
Used for net periodic benefit cost (income)	**5.07%**	4.18%	**5.29%**	4.34%
Expected rate of return on plan assets	**8.00%**	8.00%	–	–
Rate of compensation increase:				
Used for benefit obligations	**2.50%**	3.00%	–	–
Used for net periodic benefit cost (income)	**3.00%**	3.00%	–	–

13. Pensions and Other Postretirement Benefits (continued)

The System uses a direct cost approach to estimate its postretirement benefit obligation for healthcare services provided by the System (internally provided services). Healthcare services provided by non-System entities (externally provided services) are based on the System's historical cost experience.

The annual assumed healthcare cost trend rates for the next year and the assumed trend thereafter is as follows:

	2014	2013
Internally provided services:		
Initial rate	**6.00%**	6.25%
Ultimate rate	**4.50%**	4.50%
Year ultimate reached	**2021**	2021
Externally provided services:		
Initial rate	**7.00%**	7.25%
Ultimate rate	**5.50%**	5.50%
Year ultimate reached	**2021**	2021

A one-percentage-point increase or decrease in the healthcare cost trend rate would have increased or decreased the December 31, 2014 service and interest costs in total by $2.4 million and $1.7 million, respectively, and the December 31, 2013 service and interest costs in total by $2.9 million and $2.0 million, respectively.

The System's weighted-average asset allocation of pension plan assets at December 31, 2014 and 2013, by asset category, are as follows:

	Percentage of Plan Assets		
	December 31 2014	Target Allocation	December 31 2013
Asset category			
Interest-bearing cash	**2.8%**	0%–10%	7.0%
Fixed income securities	**47.9**	40%–80%	22.6
Common and preferred stocks	**29.9**	17%–37%	51.1
Alternative investments	**19.4**	3%–23%	19.3
Total	**100.0%**		100.0%

13. Pensions and Other Postretirement Benefits (continued)

The System's investment strategy for its pension assets balances the liquidity needs of the pension plans with the long-term return goals necessary to satisfy future pension obligations. The target allocation ranges of the investment pool to various asset classes are designed to diversify the portfolio in a way that achieves an efficient trade-off between long-term return and risk while providing adequate liquidity to meet near-term expenses and obligations.

The System's pension portfolio return assumption of 8.0% in 2013 and 2014 is based on the targeted assumed rate of return through its asset mix at the beginning of each year, which is designed to mitigate short-term return volatility and achieve an efficient trade-off between return and risk. Expected returns and risk for each asset class are formed using a global capital asset pricing model framework in which the expected return is the compensation earned from taking risk. Forward-looking adjustments are made to expected return, volatility, and correlation estimates as well. Additionally, constraints such as permissible asset classes, portfolio guidelines, and liquidity considerations are included in the model.

In 2014, the System updated its investment strategy and modified the target allocations of pension plan assets based on the current funded status of the pension plans. Coincident with this update, the System reduced the asset allocation for common and preferred stocks with a corresponding increase in fixed income securities. The updated investment strategy was implemented because of the funded status of the pension plans and the anticipation that such changes in investment strategy will result in lower volatility of future changes in funded status. As a result of these changes, the System estimates an expected rate of return on plan assets of 7.0%. Once the new investment strategy is fully implemented, it is anticipated that the duration of the investment assets will match the liabilities of the pension plans over time. Additional revisions in asset allocations may occur based on future changes in the funded status of the pension plans.

13. Pensions and Other Postretirement Benefits (continued)

The following tables present the financial instruments in the System's defined benefit pension plans measured at fair value on a recurring basis as of December 31, 2014 and 2013, based on the valuation hierarchy (in thousands):

December 31, 2014	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets				
Cash and investments:				
Cash and cash equivalents	**$ 33,685**	**$ 6**	**$ –**	**$ 33,691**
Fixed income securities:				
U.S. treasuries	**293,543**	**–**	**–**	**293,543**
U.S. government agencies	**–**	**6,065**	**–**	**6,065**
U.S. corporate	**–**	**53,201**	**–**	**53,201**
Foreign	**–**	**11,893**	**–**	**11,893**
Fixed income mutual funds	**49,477**	**–**	**–**	**49,477**
Commingled fixed income funds	**–**	**167,000**	**–**	**167,000**
Common and preferred stocks:				
U.S.	**120,825**	**652**	**–**	**121,477**
Foreign	**24,070**	**424**	**–**	**24,494**
Equity mutual funds	**19,030**	**–**	**–**	**19,030**
Commingled equity funds	**–**	**198,205**	**–**	**198,205**
Hedge funds	**–**	**–**	**206,277**	**206,277**
Private equity	**–**	**–**	**29,049**	**29,049**
Total assets at fair value	**$540,630**	**$437,446**	**$235,326**	**$ 1,213,402**

13. Pensions and Other Postretirement Benefits (continued)

December 31, 2013	Level 1	Level 2	Level 3	Total
Assets				
Cash and investments:				
Cash and cash equivalents	$ 92,222	$ 8	$ –	$ 92,230
Fixed income securities:				
U.S. treasuries	106,420	–	–	106,420
U.S. government agencies	–	6,455	–	6,455
U.S. corporate	–	37,597	–	37,597
Foreign	–	5,052	–	5,052
Fixed income mutual fund	47,219	–	–	47,219
Commingled fixed income funds	–	93,185	–	93,185
Common and preferred stocks:				
U.S.	228,523	489	–	229,012
Foreign	52,241	–	–	52,241
Equity mutual funds	75,245	–	–	75,245
Commingled equity funds	–	311,861	–	311,861
Hedge funds	–	–	212,646	212,646
Private equity	–	–	40,088	40,088
Less securities under lending agreement	(507)	–	–	(507)
Total cash and investments	601,363	454,647	252,734	1,308,744
Investments under securities lending agreement	507	–	–	507
Total assets at fair value	$ 601,870	$ 454,647	$ 252,734	$ 1,309,251

13. Pensions and Other Postretirement Benefits (continued)

Level 3 Rollforward	Hedge Funds	Private Equity	Total
Fair value as of January 1, 2013	$ 180,353	$ 33,305	$ 213,658
Unrealized gains, net	17,559	4,764	22,323
Purchases	18,000	8,317	26,317
Sales and redemptions	(3,266)	(6,298)	(9,564)
Fair value as of December 31, 2013	212,646	40,088	252,734
Unrealized gains, net	**11,558**	**4,698**	**16,256**
Purchases	**–**	**3,729**	**3,729**
Sales and redemptions	**(17,927)**	**(19,466)**	**(37,393)**
Fair value as of December 31, 2014	**$ 206,277**	**$ 29,049**	**$ 235,326**

Fair value methodologies for Level 1 and Level 2 are consistent with the inputs described in Note 6. Fair value for Level 3 represents the System's ownership interest in the net asset value of the respective partnership as a practical expedient to measure fair value.

Fixed income securities include debt obligations of the U.S. government and various agencies, U.S. corporations, and other fixed income instruments such as mortgage-backed and asset-backed securities. The composition of these securities represents an expected return and risk profile that is commensurate with broadly defined fixed income indexes such as the Barclays Capital U.S. Aggregate Index. Additionally, investments include mutual funds and commingled fixed-income funds that may also invest in opportunistic as well as non-U.S. and high-yield debt instruments.

Common and preferred stocks include investments of publicly traded common stocks of both U.S. and international corporations, the majority of which represent actively traded and liquid securities that are traded on many of the world's major exchanges and include large-, mid-, and small-capitalization securities. The composition of these securities represents an expected return and risk profile that is commensurate with broadly defined equity indexes such as the Russell 3000 Index and the Morgan Stanley Capital International (MSCI) All Country World ex-U.S. Index. Investments also include equity mutual funds and commingled equity funds whose underlying assets may include publicly traded equity securities.

13. Pensions and Other Postretirement Benefits (continued)

Alternative investments include hedge funds that are meant to provide returns between those expected from stocks and fixed income investments with commensurate levels of risk and lower correlation relative to traditional investments. Included in this category are investments that are well diversified across various strategies and may consist of absolute return funds, long/short funds, and other opportunistic/multi-strategy funds. The underlying investments in such funds may include publicly traded and privately held equity and debt instruments issued by U.S. and international corporations as well as various derivatives based on these securities. Hedge fund redemptions typically contain restrictions that allow for a portion of the withdrawal proceeds to be held back from distribution while the underlying investments are liquidated. Private equity investments make up a smaller portion of the alternative investments and generally consist of limited partnerships formed to invest in equity and debt investments in operating companies that are not publicly traded. Investment strategies in this category may include buyouts, distressed debt, and venture capital. Private equity funds are closed-end funds and have significant redemption restrictions that prohibit redemptions during the fund's life.

14. Income Taxes

The Foundation and most of its controlled affiliates are tax-exempt organizations as described in Section 501(c)(3) of the Internal Revenue Code. These organizations are subject to income tax on any income from unrelated business activities. The System also owns or controls certain taxable affiliates.

The System files income tax returns in the U.S. federal jurisdiction and in various state and foreign jurisdictions. With few exceptions, the System is no longer subject to U.S. federal, state, and local or non-U.S. income tax examinations by tax authorities for years before 2011.

At December 31, 2014 and 2013, the liability for uncertainty in income taxes was $9.7 million and $10.8 million, respectively. The System does not expect a significant increase or decrease in unrecognized tax benefits within the next 12 months. The System recognizes interest and penalties accrued related to the liability for unrecognized tax benefits in the consolidated statements of operations and changes in net assets.

At December 31, 2014 and 2013, the System has net operating losses available for federal income tax purposes of $114.3 million and $110.3 million, respectively. These losses expire in varying amounts from 2018 through 2034. A valuation allowance has been recorded for the full amount of the deferred tax asset related to the net operating loss carryforwards due to the uncertainty regarding their use.

15. Commitments and Contingent Liabilities

The System leases various equipment and facilities under operating lease arrangements. Total rental expense in 2014 and 2013 was $64.9 million and $70.9 million, respectively. Minimum operating lease payments over the next five years are as follows (in millions): 2015 – $47.7; 2016 – $39.2; 2017 –$35.1; 2018 – $29.5; and 2019 – $14.6.

Included in the System's operating lease payments are the following off-balance-sheet financing agreements:

> In 2003, the System entered into an operating lease agreement for the purpose of leasing a genetics and stem cell research building (Stem Cell Building Lease). Under the terms of the Stem Cell Building Lease, the System began to lease the facility upon the issuance of the certificate of occupancy in December 2004 and is required to lease the facility for 29 years. At December 31, 2014, total remaining minimum operating lease payments were $28.8 million.
>
> In 2006, the System entered into an operating lease agreement for the purpose of leasing a parking garage and service center building (Service Center Lease). Under the terms of the Service Center Lease, the System began to lease the facility upon issuance of a certificate of occupancy in October 2008 and is required to lease the facility for 21 years with an option (by the System) to extend the lease an additional five years. At December 31, 2014, total remaining minimum operating lease payments were $83.3 million.
>
> In 2007, the System entered into two operating lease agreements to lease an office complex comprised of four office buildings and a day care center facility, totaling approximately 707,000 square feet. The System is required to lease the facilities for 22 years with an option (by the System) to extend the leases an additional five years. At December 31, 2014, total remaining minimum operating lease payments were $42.8 million.

At December 31, 2014, the System has commitments for construction and other related capital contracts of $288.5 million and letters of credit of $0.5 million. Guarantees of mortgage loans made by banks to certain staff members are $14.1 million at December 31, 2014. In addition, the System has remaining commitments to invest approximately $603.3 million in alternative and direct investments at December 31, 2014. The largest commitment at December 31, 2014, to any one alternative strategy manager is $50.0 million. These investments are expected to occur over the next three to five years. No amounts have been recorded in the consolidated balance sheets for these commitments and guarantees.

16. Endowment

The System's endowment consists of approximately 261 individual donor-restricted funds established for a variety of purposes. Net assets associated with endowment funds are classified and reported based on donor-imposed restrictions.

Interpretation of Relevant Law

In 2009, the Uniform Prudent Management of Institutional Funds Act (UPMIFA) was enacted to update and replace Ohio's previous law, the Uniform Management of Institutional Funds Act. The System has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds, absent explicit donor stipulations to the contrary. As a result of this interpretation, the System classifies as permanently restricted net assets (1) the original value of gifts donated to the permanent endowment, (2) the original value of subsequent gifts to the permanent endowment, and (3) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the System in a manner consistent with the standard for expenditure prescribed by UPMIFA. In accordance with UPMIFA, the System considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund.
2. The purposes of the System and the donor-restricted endowment fund.
3. General economic conditions.
4. The possible effect of inflation and deflation.
5. The expected total return from income and the appreciation of investments.
6. Other resources of the System.
7. The investment policies of the System.

Funds With Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the System to retain as a fund of perpetual duration. Deficiencies of this nature that are reported in unrestricted net assets were $0.5 million and $0.8 million as of December 31, 2014 and 2013, respectively.

16. Endowment (continued)

Return Objectives and Risk Parameters

The System has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity. Under this policy, the endowment assets are invested in a highly diversified portfolio of U.S. and non-U.S. publicly traded equities, alternative investments, and fixed income securities structured to achieve an optimal balance between return and risk. The System expects its endowment funds, over time, to provide an average rate of return of approximately 7.5% annually. Actual returns in any given year may vary from this amount.

Strategies Employed for Achieving Objectives

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 current yield (interest and dividends). The System targets a diversified asset allocation to achieve its long-term return objective within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

The System has a policy of appropriating for distribution each year up to 5% of its endowment fund's average fair value over the prior three years through the calendar year-end preceding the fiscal year in which the distribution is planned. In establishing this policy, the System considered the long-term expected return on its endowment. Accordingly, over the long term, the System expects the current spending policy to allow its endowment to grow at an average of 2.5% annually. This is consistent with the System's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

16. Endowment (continued)

Changes in Endowment Net Assets (in thousands)

	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, January 1, 2013	$ 20,145	$ 201,620	$ 221,765
Investment return	1,487	–	1,487
Net appreciation	24,671	–	24,671
Contributions	–	18,890	18,890
Appropriation of endowment assets for expenditure	(6,434)	–	(6,434)
Endowment net assets, December 31, 2013	39,869	220,510	260,379
Investment return	**2,088**	–	**2,088**
Net appreciation	**13,735**	–	**13,735**
Contributions	–	**11,533**	**11,533**
Appropriation of endowment assets for expenditure	**(8,126)**	–	**(8,126)**
Endowment net assets, December 31, 2014	**$ 47,566**	**$ 232,043**	**$ 279,609**

17. Functional Expenses

The System provides healthcare services and education and performs research. Expenses related to these functions were as follows (in thousands):

	2014	2013
Healthcare services	**$ 4,917,538**	$ 4,874,530
Research	**215,006**	207,987
Medical education	**279,365**	263,337
General and administrative	**733,709**	733,559
Non-healthcare services	**74,218**	76,751
	$ 6,219,836	$ 6,156,164

18. Subsequent Events

The System evaluated events and transactions occurring subsequent to December 31, 2014 through March 6, 2015, the date the consolidated financial statements were issued. During this period, there were no subsequent events requiring recognition in the consolidated financial statements, and there were no nonrecognized subsequent events requiring disclosure.

Supplementary Information

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Report of Independent Auditors on Supplementary Information

The Board of Directors
The Cleveland Clinic Foundation

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The following consolidating balance sheets, statements of operations and changes in net assets, and statements of cash flows are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Ernst & Young LLP

March 6, 2015

Cleveland Clinic Health System

Consolidating Balance Sheet

December 31, 2014
(In Thousands)

	Obligated Group	Non-Obligated Group	Consolidating Adjustments and Eliminations	Consolidated
Assets				
Current assets:				
Cash and cash equivalents	$ 2,952	$ 67,370	$ –	$ 70,322
Patient receivables, net	807,085	36,257	(24,268)	819,074
Due from affiliates	1,466	119	(1,585)	–
Investments for current use	98,010	46,828	–	144,838
Other current assets	305,379	27,794	(1,098)	332,075
Total current assets	1,214,892	178,368	(26,951)	1,366,309
Investments:				
Long-term investments	5,739,503	210,573	–	5,950,076
Funds held by trustees	119,388	–	–	119,388
Assets held by captive insurance subsidiary	–	106,317	–	106,317
Donor-restricted assets	459,401	14,826	–	474,227
	6,318,292	331,716	–	6,650,008
Property, plant, and equipment, net	3,329,725	269,882	–	3,599,607
Other assets:				
Pledges receivable, net	160,774	983	–	161,757
Trusts and interests in foundations	80,971	41,527	–	122,498
Other noncurrent assets	378,275	3,242	(14,136)	367,381
	620,020	45,752	(14,136)	651,636
Total assets	$ 11,482,929	$ 825,718	$ (41,087)	$ 12,267,560

	Obligated Group	Non-Obligated Group	Consolidating Adjustments and Eliminations	Consolidated
Liabilities and net assets				
Current liabilities:				
Accounts payable	**$ 307,962**	**$ 28,611**	**$ (1,098)**	**$ 335,475**
Compensation and amounts withheld from payroll	**233,438**	**5,500**	**–**	**238,938**
Current portion of long-term debt	**50,763**	**5,015**	**–**	**55,778**
Variable rate debt classified as current	**321,845**	**65,030**	**–**	**386,875**
Due to affiliates	**22**	**1,563**	**(1,585)**	**–**
Other current liabilities	**387,019**	**72,064**	**(24,268)**	**434,815**
Total current liabilities	**1,301,049**	**177,783**	**(26,951)**	**1,451,881**
Long-term debt:				
Hospital revenue bonds	**2,798,062**	**–**	**–**	**2,798,062**
Notes payable and capital leases	**165,875**	**20,361**	**(10,688)**	**175,548**
	2,963,937	**20,361**	**(10,688)**	**2,973,610**
Other liabilities:				
Professional and general liability insurance reserves	**54,760**	**88,480**	**–**	**143,240**
Accrued retirement benefits	**452,897**	**–**	**–**	**452,897**
Other noncurrent liabilities	**436,676**	**6,761**	**–**	**443,437**
	944,333	**95,241**	**–**	**1,039,574**
Total liabilities	**5,209,319**	**293,385**	**(37,639)**	**5,465,065**
Net assets:				
Unrestricted	**5,533,572**	**467,929**	**(3,448)**	**5,998,053**
Temporarily restricted	**486,218**	**33,512**	**–**	**519,730**
Permanently restricted	**253,820**	**30,892**	**–**	**284,712**
Total net assets	**6,273,610**	**532,333**	**(3,448)**	**6,802,495**
Total liabilities and net assets	**$ 11,482,929**	**$ 825,718**	**$ (41,087)**	**$ 12,267,560**

See accompanying note.

Cleveland Clinic Health System

Consolidating Balance Sheet

December 31, 2013
(In Thousands)

	Obligated Group	Non-Obligated Group	Consolidating Adjustments and Eliminations	Consolidated
Assets				
Current assets:				
Cash and cash equivalents	$ –	$ 70,900	$ –	$ 70,900
Patient receivables, net	767,742	32,725	(20,791)	779,676
Due from affiliates	2,387	3	(2,390)	–
Investments for current use	91,823	47,306	–	139,129
Other current assets	270,502	25,745	(1,188)	295,059
Total current assets	1,132,454	176,679	(24,369)	1,284,764
Investments:				
Long-term investments	4,849,078	208,173	–	5,057,251
Funds held by trustees	70,627	–	–	70,627
Assets held by captive insurance subsidiary	–	95,666	–	95,666
Donor-restricted assets	416,634	12,088	–	428,722
	5,336,339	315,927	–	5,652,266
Property, plant, and equipment, net	3,262,478	277,303	–	3,539,781
Other assets:				
Pledges receivable, net	131,118	4,339	–	135,457
Trusts and interests in foundations	78,806	39,468	–	118,274
Other noncurrent assets	227,219	3,412	(9,374)	221,257
	437,143	47,219	(9,374)	474,988
Total assets	$ 10,168,414	$ 817,128	$ (33,743)	$ 10,951,799

	Obligated Group	Non-Obligated Group	Consolidating Adjustments and Eliminations	Consolidated
Liabilities and net assets				
Current liabilities:				
Accounts payable	$ 297,322	$ 28,880	$ (1,188)	$ 325,014
Compensation and amounts withheld from payroll	248,667	7,482	–	256,149
Current portion of long-term debt	47,546	4,952	–	52,498
Variable rate debt classified as current	421,380	66,850	–	488,230
Due to affiliates	–	2,390	(2,390)	–
Other current liabilities	329,074	73,266	(20,791)	381,549
Total current liabilities	1,343,989	183,820	(24,369)	1,503,440
Long-term debt:				
Hospital revenue bonds	2,343,380	–	–	2,343,380
Notes payable and capital leases	73,759	18,793	(5,926)	86,626
	2,417,139	18,793	(5,926)	2,430,006
Other liabilities:				
Professional and general liability insurance reserves	55,794	77,382	–	133,176
Accrued retirement benefits	263,259	–	–	263,259
Other noncurrent liabilities	406,414	7,098	–	413,512
	725,467	84,480	–	809,947
Total liabilities	4,486,595	287,093	(30,295)	4,743,393
Net assets:				
Unrestricted	5,012,344	470,031	(3,448)	5,478,927
Temporarily restricted	426,843	34,267	–	461,110
Permanently restricted	242,632	25,737	–	268,369
Total net assets	5,681,819	530,035	(3,448)	6,208,406
Total liabilities and net assets	$ 10,168,414	$ 817,128	$ (33,743)	$ 10,951,799

See accompanying note.

Cleveland Clinic Health System

Consolidating Statements of Operations and Changes in Net Assets

Year Ended December 31, 2014
(In Thousands)

Operations

	Obligated Group	Non-Obligated Group	Consolidating Adjustments and Eliminations	Consolidated
Unrestricted revenues				
Net patient service revenue	$ 6,386,203	$ 253,946	$ (211,211)	$ 6,428,938
Provision for uncollectible accounts	(345,882)	(12,939)	–	(358,821)
Net patient service revenue less provision for uncollectible accounts	6,040,321	241,007	(211,211)	6,070,117
Other	527,332	218,873	(128,943)	617,262
Total unrestricted revenues	6,567,653	459,880	(340,154)	6,687,379
Expenses				
Salaries, wages, and benefits	3,672,795	206,685	(243,516)	3,635,964
Supplies	584,864	43,841	(1,170)	627,535
Pharmaceuticals	543,631	15,353	–	558,984
Purchased services and other fees	362,653	32,442	(12,546)	382,549
Administrative services	128,196	64,716	(25,325)	167,587
Facilities	259,680	28,212	(5,994)	281,898
Insurance	58,419	60,127	(51,603)	66,943
	5,610,238	451,376	(340,154)	5,721,460
Operating income before interest, depreciation, and amortization expenses	957,415	8,504	–	965,919
Interest	108,334	2,059	–	110,393
Depreciation and amortization	367,102	20,881	–	387,983
Operating income (loss)	481,979	(14,436)	–	467,543
Nonoperating gains and losses				
Investment return	300,537	15,680	–	316,217
Derivative losses	(76,694)	(3,092)	–	(79,786)
Other, net	(300)	(52)	–	(352)
Net nonoperating gains	223,543	12,536	–	236,079
Excess (deficiency) of revenues over expenses	705,522	(1,900)	–	703,622

Cleveland Clinic Health System

Consolidating Statements of Operations and Changes in Net Assets

Year Ended December 31, 2013
(In Thousands)

Operations

	Obligated Group	Non-Obligated Group	Consolidating Adjustments and Eliminations	Consolidated
Unrestricted revenues				
Net patient service revenue	$ 6,223,945	$ 263,631	$ (203,049)	$ 6,284,527
Provision for uncollectible accounts	(395,031)	(15,914)	–	(410,945)
Net patient service revenue less provision for uncollectible accounts	5,828,914	247,717	(203,049)	5,873,582
Other	482,809	213,775	(120,007)	576,577
Total unrestricted revenues	6,311,723	461,492	(323,056)	6,450,159
Expenses				
Salaries, wages, and benefits	3,652,825	213,797	(229,424)	3,637,198
Supplies	597,482	43,848	(1,523)	639,807
Pharmaceuticals	479,229	15,248	–	494,477
Purchased services and other fees	376,085	29,529	(13,495)	392,119
Administrative services	123,348	65,061	(24,631)	163,778
Facilities	279,661	29,473	(5,602)	303,532
Insurance	60,610	53,235	(48,381)	65,464
	5,569,240	450,191	(323,056)	5,696,375
Operating income before interest, depreciation, and amortization expenses	742,483	11,301	–	753,784
Interest	104,670	2,022	–	106,692
Depreciation and amortization	332,260	20,837	–	353,097
Operating income (loss)	305,553	(11,558)	–	293,995
Nonoperating gains and losses				
Investment return	520,440	25,958	–	546,398
Derivative gains (losses)	64,077	(3,132)	–	60,945
Other, net	(118)	(1,121)	–	(1,239)
Net nonoperating gains	584,399	21,705	–	606,104
Excess of revenues over expenses	889,952	10,147	–	900,099

Cleveland Clinic Health System

Consolidating Statements of Operations and Changes in Net Assets (continued)

(In Thousands)

	Obligated Group	Non-Obligated Group	Consolidating Adjustments and Eliminations	Consolidated
Total net assets at January 1, 2013	$ 4,493,222	$ 512,604	$ (3,446)	$ 5,002,380
Excess of revenues over expenses	889,952	10,147	–	900,099
Donated capital, excluding assets released from restrictions for capital purposes of $16,298	1,173	39	–	1,212
Restricted gifts and bequests	73,051	2,132	–	75,183
Restricted net investment income	29,398	1,157	–	30,555
Net assets released from restrictions used for operations included in other unrestricted revenues	(34,773)	(1,953)	–	(36,726)
Retirement benefits adjustment	225,977	–	–	225,977
Transfers (to) from affiliates	(68)	68	–	–
Change in restricted net assets related to interest in foundations	1,613	4,163	–	5,776
Change in restricted net assets related to value of perpetual trusts	2,059	622	–	2,681
Net change in unrealized losses on nontrading investments	(93)	–	–	(93)
Other	308	1,056	(2)	1,362
Increase in total net assets	1,188,597	17,431	(2)	1,206,026
Total net assets at December 31, 2013	5,681,819	530,035	(3,448)	6,208,406
Excess (deficiency) of revenues over expenses	**705,522**	**(1,900)**	**–**	**703,622**
Donated capital, excluding assets released from restrictions for capital purposes of $5,824	**70**	**–**	**–**	**70**
Restricted gifts and bequests	**93,139**	**2,948**	**–**	**96,087**
Restricted net investment income	**16,991**	**1,088**	**–**	**18,079**
Net assets released from restrictions used for operations included in other unrestricted revenues	**(32,416)**	**(3,774)**	**–**	**(36,190)**
Retirement benefits adjustment	**(193,150)**	**–**	**–**	**(193,150)**
Transfers (to) from affiliates	**(1,378)**	**1,378**	**–**	**–**
Change in restricted net assets related to interest in foundations	**(1,667)**	**1,534**	**–**	**(133)**
Change in restricted net assets related to value of perpetual trusts	**1,711**	**525**	**–**	**2,236**
Net change in unrealized gains on nontrading investments	**3,163**	**–**	**–**	**3,163**
Other	**(194)**	**499**	**–**	**305**
Increase in total net assets	**591,791**	**2,298**	**–**	**594,089**
Total net assets at December 31, 2014	**$ 6,273,610**	**$ 532,333**	**$ (3,448)**	**$ 6,802,495**

See accompanying note.

Cleveland Clinic Health System

Consolidating Statement of Cash Flows

Year Ended December 31, 2014
(In Thousands)

	Obligated Group	Non-Obligated Group	Consolidating Adjustments and Eliminations	Consolidated
Operating activities and net nonoperating gains and losses				
Increase in total net assets	**$ 591,791**	**$ 2,298**	**$ –**	**$ 594,089**
Adjustments to reconcile increase in total net assets to net cash provided by operating activities and net nonoperating gains and losses:				
Retirement benefits adjustment	**193,150**	**–**	**–**	**193,150**
Net realized and unrealized gains on investments	**(283,175)**	**(13,730)**	**–**	**(296,905)**
Depreciation and amortization	**367,102**	**20,881**	**–**	**387,983**
Provision for uncollectible accounts	**345,882**	**12,939**	**–**	**358,821**
Donated capital	**(70)**	**–**	**–**	**(70)**
Restricted gifts, bequests, investment income, and other	**(110,174)**	**(6,095)**	**–**	**(116,269)**
Transfers to (from) affiliates	**1,378**	**(1,378)**	**–**	**–**
Accreted interest and amortization of bond premiums	**(2,533)**	**–**	**–**	**(2,533)**
Net loss in value of derivatives	**53,993**	**–**	**–**	**53,993**
Changes in operating assets and liabilities:				
Patient receivables	**(385,225)**	**(16,471)**	**3,477**	**(398,219)**
Other current assets	**(38,113)**	**794**	**(895)**	**(38,214)**
Other noncurrent assets	**(46,929)**	**132**	**4,762**	**(42,035)**
Accounts payable and other current liabilities	**56,979**	**(519)**	**(2,582)**	**53,878**
Accrued retirement benefits	**(3,512)**	**–**	**–**	**(3,512)**
Other liabilities	**(24,765)**	**10,761**	**–**	**(14,004)**
Net cash provided by operating activities and net nonoperating gains and losses	**715,779**	**9,612**	**4,762**	**730,153**
Financing activities				
Proceeds from long-term borrowings	**400,000**	**4,762**	**(4,762)**	**400,000**
Principal payments on long-term debt	**(50,405)**	**(4,951)**	**–**	**(55,356)**
Debt issuance costs	**(5,471)**	**–**	**–**	**(5,471)**
Change in pledges receivables, trusts and interests in foundations	**(27,664)**	**(1,662)**	**–**	**(29,326)**
Restricted gifts, bequests, investment income, and other	**110,174**	**6,095**	**–**	**116,269**
Net cash provided by financing activities	**426,634**	**4,244**	**(4,762)**	**426,116**
Investing activities				
Expenditures for property and equipment	**(423,459)**	**(17,183)**	**–**	**(440,642)**
Proceeds from sale of property and equipment	**341**	**–**	**–**	**341**
Investment in Akron General	**(10,000)**	**–**	**–**	**(10,000)**
Net change in cash equivalents reported in long-term investments	**(424,814)**	**15,675**	**–**	**(409,139)**
Purchases of investments	**(1,709,536)**	**(112,792)**	**–**	**(1,822,328)**
Sales of investments	**1,429,385**	**95,536**	**–**	**1,524,921**
Transfers (to) from affiliates	**(1,378)**	**1,378**	**–**	**–**
Net cash used in investing activities	**(1,139,461)**	**(17,386)**	**–**	**(1,156,847)**
Increase (decrease) in cash and cash equivalents	**2,952**	**(3,530)**	**–**	**(578)**
Cash and cash equivalents at beginning of year	**–**	**70,900**	**–**	**70,900**
Cash and cash equivalents at end of year	**$ 2,952**	**$ 67,370**	**$ –**	**$ 70,322**

See accompanying note.

Cleveland Clinic Health System

Consolidating Statement of Cash Flows

Year Ended December 31, 2013
(In Thousands)

	Obligated Group	Non-Obligated Group	Consolidating Adjustments and Eliminations	Consolidated
Operating activities and net nonoperating gains and losses				
Increase in total net assets	$ 1,188,597	$ 17,431	$ (2)	$ 1,206,026
Adjustments to reconcile increase (decrease) in total net assets to net cash provided by operating activities and net nonoperating gains and losses:				
(Gain) loss on extinguishment of debt	(383)	1,070	–	687
Retirement benefits adjustment	(225,977)	–	–	(225,977)
Net realized and unrealized gains on investments	(510,416)	(24,241)	–	(534,657)
Depreciation and amortization	332,260	20,837	–	353,097
Provision for uncollectible accounts	395,031	15,914	–	410,945
Donated capital	(1,173)	(39)	–	(1,212)
Restricted gifts, bequests, investment income, and other	(106,121)	(8,074)	–	(114,195)
Transfers to (from) affiliates	68	(68)	–	–
Accreted interest and amortization of bond premiums	(2,535)	(143)	–	(2,678)
Net gain in value of derivatives	(87,044)	–	–	(87,044)
Changes in operating assets and liabilities:				
Patient receivables	(421,615)	(17,896)	1,838	(437,673)
Other current assets	66,248	2,152	(14,240)	54,160
Other noncurrent assets	(56,963)	(275)	4,710	(52,528)
Accounts payable and other current liabilities	(38,205)	(18,206)	12,401	(44,010)
Accrued retirement benefits	(136,896)	–	–	(136,896)
Other liabilities	44,602	13,480	3	58,085
Net cash provided by operating activities and net nonoperating gains and losses	439,478	1,942	4,710	446,130
Financing activities				
Proceeds from long-term borrowings	309,435	78,110	(4,710)	382,835
Payments for advance refunding of long-term debt	(287,306)	(76,545)	–	(363,851)
Principal payments on long-term debt	(48,726)	(5,012)	–	(53,738)
Debt issuance costs	(2,129)	(344)	–	(2,473)
Change in pledges receivables, trusts and interests in foundations	1,855	(4,868)	–	(3,013)
Restricted gifts, bequests, investment income, and other	106,121	8,074	–	114,195
Net cash provided by (used in) financing activities	79,250	(585)	(4,710)	73,955
Investing activities				
Expenditures for property and equipment	(389,785)	(13,011)	–	(402,796)
Proceeds from sale of property and equipment	10,179	–	–	10,179
Net change in cash equivalents reported in long-term investments	56,599	9,937	–	66,536
Purchases of investments	(1,837,185)	(107,788)	–	(1,944,973)
Sales of investments	1,634,776	104,300	–	1,739,076
Transfers (to) from affiliates	(68)	68	–	–
Net cash used in investing activities	(525,484)	(6,494)	–	(531,978)
Decrease in cash and cash equivalents	(6,756)	(5,137)	–	(11,893)
Cash and cash equivalents at beginning of year	6,756	76,037	–	82,793
Cash and cash equivalents at end of year	$ –	$ 70,900	$ –	$ 70,900

See accompanying note.

1. Presentation of Consolidating Financial Statements

The accompanying financial statement information presents consolidating financial statement information for the Obligated Group (as defined herein) and certain controlled affiliates of The Cleveland Clinic Foundation (collectively referred to as the Non-Obligated Group), which have no liability under the Master Trust Indenture (Indenture), amended and restated as of April 1, 2003 (as supplemented, the Indenture), between the Foundation and The Huntington National Bank, as successor Master Trustee. The Foundation, Cleveland Clinic Health System – East Region, Fairview Hospital, Lutheran Hospital, Marymount Hospital, Inc., Medina Hospital, Cleveland Clinic Florida (a nonprofit corporation) and Cleveland Clinic Florida Health System Nonprofit Corporation are the sole members of the Obligated Group under the Indenture.

With respect to the Obligated Group, certain properties and interests are considered to be Excluded Property under the Indenture. In addition, the provisions of the Indenture provide that additional property may be categorized as Excluded Property upon satisfaction of various financial tests. As such, these properties and interests are not subject to the restrictions contained in the Indenture and, under the Indenture, are not subject to the restriction on liens and other encumbrances that may be placed on property of the Obligated Group. Furthermore, the revenues derived from the Excluded Property are not subject to the restrictions contained in the Indenture until they are received and commingled with other revenues of the Obligated Group. The accompanying financial statement information is presented by legal entity and no adjustment has been made for the Excluded Property.

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