Partners HealthCare System, Inc. and Affiliates

Consolidated Financial Statements

September 30, 2014 and 2013

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September 30, 2014 and 2013

Independent Auditor's Report

To the Board of Directors of
Partners HealthCare System, Inc. and Affiliates

We have audited the accompanying consolidated financial statements of Partners HealthCare System, Inc. and Affiliates (Partners HealthCare), which comprise the consolidated balance sheets as of September 30, 2014 and 2013 and the related consolidated statements of operations, changes in net assets and of cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to Partners HealthCare's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Partners HealthCare's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Partners HealthCare System, Inc. and Affiliates at September 30, 2014 and 2013, and the results of their operations, their changes in net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

December 12, 2014

PricewaterhouseCoopers LLP, 125 High Street, Boston, MA 02110
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Partners HealthCare System, Inc. and Affiliates
Consolidated Balance Sheets
September 30, 2014 and 2013

(dollars in thousands)	2014	2013
Assets		
Current assets		
Cash and equivalents	$ 457,244	$ 471,322
Investments	1,474,058	1,439,299
Collateral held under securities lending arrangements	-	229,400
Current portion of investments limited as to use	2,120,057	1,813,490
Patient accounts receivable, net of allowance for bad debts (2014 - $117,212; 2013 - $104,044)	876,214	813,384
Research grants receivable	115,786	109,708
Other current assets	381,517	326,751
Receivable for settlements with third-party payers	39,082	68,854
Total current assets	5,463,958	5,272,208
Investments limited as to use, less current portion	2,927,360	2,771,216
Long-term investments	1,026,538	957,100
Pledges receivable, net and contributions receivable from trusts, less current portion	197,975	165,095
Property and equipment, net	4,615,908	4,235,839
Other assets	499,353	499,442
Total assets	$ 14,731,092	$ 13,900,900
Liabilities and Net Assets		
Current liabilities		
Current portion of long-term obligations	$ 238,204	$ 361,249
Accounts payable and accrued expenses	645,999	690,946
Accrued medical claims and related expenses	254,480	121,833
Accrued compensation and benefits	677,957	623,352
Collateral due under securities lending arrangements	-	229,400
Current portion of accrual for settlements with third-party payers	55,918	36,052
Unexpended funds on research grants	183,222	160,668
Total current liabilities	2,055,780	2,223,500
Other liabilities		
Accrual for settlements with third-party payers, less current portion	58,899	87,787
Accrued professional liability	455,463	443,688
Accrued employee benefits	1,066,840	648,128
Interest rate swaps liability	295,656	232,005
Accrued other	157,029	158,468
	2,033,887	1,570,076
Long-term obligations, less current portion	3,697,938	3,097,280
Total liabilities	7,787,605	6,890,856
Commitments and contingencies		
Net assets		
Unrestricted	5,623,759	5,805,066
Temporarily restricted	855,954	792,769
Permanently restricted	463,774	412,209
Total net assets	6,943,487	7,010,044
Total liabilities and net assets	$ 14,731,092	$ 13,900,900

The accompanying notes are an integral part of these consolidated financial statements.

Partners HealthCare System, Inc. and Affiliates
Consolidated Statements of Operations
Years Ended September 30, 2014 and 2013

(dollars in thousands)	2014	2013
Operating revenue		
Net patient service revenue, net of provision for bad debts (2014 - $129,492; 2013 - $102,409)	$ 7,042,558	$ 6,769,743
Premium revenue	1,622,392	1,349,525
Direct academic and research revenue	1,225,782	1,242,819
Indirect academic and research revenue	352,911	351,630
Other revenue	662,410	632,322
Total operating revenue	10,906,053	10,346,039
Operating expenses		
Employee compensation and benefits	5,425,156	5,224,242
Supplies and other expenses	2,229,859	2,108,313
Medical claims and related expenses	1,463,972	1,061,630
Direct academic and research expenses	1,225,782	1,242,819
Depreciation and amortization	463,039	434,725
Interest	119,849	116,671
Total operating expenses	10,927,657	10,188,400
(Loss) income from operations	(21,604)	157,639
Nonoperating gains (expenses)		
Income from investments	227,357	146,631
Change in fair value of nonhedging interest rate swaps	(109,275)	48,522
Gifts and other, net of fundraising and other expenses	(67,242)	(56,194)
Academic and research gifts, net of expenses	90,609	49,206
Contribution income - affiliates	-	254,205
Total nonoperating gains, net	141,449	442,370
Excess of revenues over expenses	119,845	600,009
Other changes in net assets		
Change in net unrealized appreciation on marketable investments	(3,309)	74,522
Change in fair value of hedging interest rate swaps	45,624	117,813
Funds utilized for property and equipment	39,058	57,224
Change in funded status of defined benefit plans	(387,698)	835,651
Other	5,173	(11,590)
(Decrease) increase in unrestricted net assets	$ (181,307)	$ 1,673,629

The accompanying notes are an integral part of these consolidated financial statements.

Partners HealthCare System, Inc. and Affiliates
Consolidated Statements of Changes in Net Assets
Years Ended September 30, 2014 and 2013

(dollars in thousands)	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Net assets at October 1, 2012	$ 4,131,437	$ 777,012	$ 374,230	$ 5,282,679
Increases (decreases)				
Income from operations	157,639	-	-	157,639
Income from investments	146,631	10,158	163	156,952
Gifts and other	(56,194)	9,612	35,009	(11,573)
Academic and research gifts, net of expenses	49,206	-	-	49,206
Contribution income - affiliates	254,205	8,431	510	263,146
Change in net unrealized appreciation on marketable investments	74,522	23,802	802	99,126
Change in fair value of interest rate swaps				
Nonhedging	48,522	-	-	48,522
Hedging	117,813	-	-	117,813
Funds utilized for property and equipment	57,224	(36,246)	-	20,978
Change in funded status of defined benefit plans	835,651	-	-	835,651
Other	(11,590)	-	1,495	(10,095)
Change in net assets	1,673,629	15,757	37,979	1,727,365
Net assets at September 30, 2013	5,805,066	792,769	412,209	7,010,044
Increases (decreases)				
Loss from operations	(21,604)	-	-	(21,604)
Income from investments	227,357	36,897	30	264,284
Gifts and other	(67,242)	51,250	49,877	33,885
Academic and research gifts, net of expenses	90,609	-	-	90,609
Change in net unrealized appreciation on marketable investments	(3,309)	(11,209)	1,706	(12,812)
Change in fair value of interest rate swaps				
Nonhedging	(109,275)	-	-	(109,275)
Hedging	45,624	-	-	45,624
Funds utilized for property and equipment	39,058	(12,814)	-	26,244
Change in funded status of defined benefit plans	(387,698)	-	-	(387,698)
Other	5,173	(939)	(48)	4,186
Change in net assets	(181,307)	63,185	51,565	(66,557)
Net assets at September 30, 2014	$ 5,623,759	$ 855,954	$ 463,774	$ 6,943,487

The accompanying notes are an integral part of these consolidated financial statements.

Partners HealthCare System, Inc. and Affiliates
Consolidated Statements of Cash Flows
Years Ended September 30, 2014 and 2013

(dollars in thousands)	2014	2013
Cash flows from operating activities		
Change in net assets	$ (66,557)	$ 1,727,365
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Contribution income - affiliates	-	(263,146)
Change in funded status of defined benefit plans	387,698	(835,651)
Loss on refunding of debt	1,002	-
Change in fair value of interest rate swaps	63,651	(166,335)
Depreciation and amortization	463,039	434,725
Provision for bad debts	129,492	102,409
Gain on disposal of property	(13,275)	(848)
Net realized and change in unrealized appreciation on investments	(342,608)	(344,585)
Restricted contributions and investment income	(102,660)	(88,289)
Cash premium upon issuance of bonds	14,337	-
Increase (decrease) in cash resulting from a change in		
Patient accounts receivable	(192,322)	(119,412)
Research grants receivable	(6,078)	12,050
Other current assets	(51,716)	(9,251)
Pledges receivable and contributions receivable from trusts	(35,930)	21,486
Other assets	(6,433)	45,892
Accounts payable and accrued expenses	(44,947)	46,244
Accrued medical claims and related expenses	132,647	917
Accrued compensation and benefits	53,005	(3,010)
Settlements with third-party payers	20,750	38,999
Unexpended funds on research grants	22,554	(10,468)
Accrued employee benefits and other	42,902	(208,806)
Net cash provided by operating activities	468,551	380,286
Cash flows from investing activities		
Purchase of property and equipment	(835,019)	(703,083)
Proceeds from sale of property	13,713	4,954
Purchase of investments	(3,145,588)	(2,314,810)
Proceeds from sales of investments	2,921,288	2,247,631
Cash acquired through affiliations	-	17,668
Net cash used for investing activities	(1,045,606)	(747,640)
Cash flows from financing activities		
Borrowings under line of credit	45,000	-
Repayments under line of credit	(45,000)	-
Payments on long-term obligations	(60,031)	(112,715)
Proceeds from long-term obligations, net of financing costs	783,348	400,000
Decrease (increase) in auction rate securities holdings	23,830	(23,830)
Deposits into refunding trusts	(286,830)	-
Restricted contributions and investment income	102,660	88,289
Net cash provided by financing activities	562,977	351,744
Net decrease in cash and equivalents	(14,078)	(15,610)
Cash and equivalents		
Beginning of year	471,322	486,932
End of year	$ 457,244	$ 471,322

The accompanying notes are an integral part of these consolidated financial statements.

(dollars in thousands)

1. Organization and Community Benefit Commitments

Partners HealthCare System, Inc. (PHS) is the sole member of The Massachusetts General Hospital (MGH), Brigham and Women's Health Care, Inc. (BWHC), NSMC HealthCare, Inc. (NSMC), Newton-Wellesley Health Care System, Inc. (NWHCS), Partners Continuing Care, Inc. (PCC), Partners HealthCare International, LLC (PHI) and Neighborhood Health Plan, Incorporated (NHP). PHS appoints the two physicians who are the members of Partners Community HealthCare, Inc. (PCHI). The individual serving as the PHS President and Chief Executive Officer is the sole member of Partners Medical International, Inc. (PMI). PHS, together with all of its affiliates, is referred to as "Partners HealthCare."

Partners HealthCare currently operates two tertiary and seven community acute care hospitals in Massachusetts, one facility providing inpatient and outpatient mental health services and four facilities providing inpatient and outpatient services in rehabilitation medicine and long-term care. Partners HealthCare also operates physician organizations and practices, a home health agency, nursing homes, and a graduate level program for health professions. Partners HealthCare provides services to patients primarily from the Greater Boston area as well as New England and beyond. In addition, Partners HealthCare is a nonuniversity-based nonprofit private medical research enterprise and is a principal teaching affiliate of the medical and dental schools of Harvard University. Partners HealthCare also operates a licensed, not-for-profit managed care organization that provides health insurance products to the Medical Assistance Program (Medicaid), Commonwealth Care (a series of health insurance plans for adults who meet income and other eligibility requirements) and commercial populations.

PHS is a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code (IRC). All affiliates of PHS, except for PCHI, PHI, NHP and Newton-Wellesley Physician Hospital Organization, Inc. (NWPHO), are also tax-exempt organizations under Section 501(c)(3) of the IRC. NHP is a tax-exempt organization under Section 501(c)(4) of the IRC. Accordingly, no provision for income taxes related to these tax-exempt entities has been made. PCHI and NWPHO are taxable entities and PHI is a single member LLC that is disregarded for income tax purposes. As of September 30, 2014, PCHI and NWPHO have available net operating loss carryforwards of approximately $35,000 for income tax purposes, expiring in 2018 through 2034.

Community Benefit

Partners HealthCare's community benefit programs include working with communities to address a number of public health issues including racial disparities, alcohol and substance abuse among young people, infant mortality, domestic violence and cancer. Partners HealthCare provides economic opportunity for low income Boston residents by helping people advance into nursing and other healthcare careers through its public school partnerships and workforce development programs. In addition, twenty-one community health centers are licensed by or affiliated with Partners HealthCare entities and provide high quality, culturally competent primary care and access to Partners HealthCare's hospitals. Partners HealthCare invests in these health centers' infrastructure, programming and operation and also helps with relocation, renovation and other capital requirements.

(dollars in thousands)

The Massachusetts Attorney General's Community Benefits Guidelines direct nonprofit acute care hospitals and health maintenance organizations to prepare annual reports documenting the status and level of their community benefit programs and initiatives. These annual reports serve the important purpose of providing the public with access to useful information about these programs and initiatives. Partners HealthCare files its report annually with the Massachusetts Attorney General. The report summarizes community benefit activities on a system-wide basis. In addition, each of the acute care hospitals within Partners HealthCare has a community benefit planning and service delivery structure and files separate community benefit reports. Partners HealthCare's nonacute care hospitals and NHP also file community benefit reports annually.

Uncompensated Care
Partners HealthCare provides care to all patients regardless of their ability to pay. The cost of providing that care is reflected in the statements of operations. The cost related to those patients for which Partners HealthCare receives either partial or no reimbursement for healthcare services provided is summarized as follows:

State Programs
Uncompensated Care
Charity care services are partially reimbursed to acute care hospitals through the statewide Health Safety Net Trust Fund (HSN) established by the Massachusetts Health Care Reform Law (Chapter 58 of the Acts of 2006 or Chapter 58). A portion of the funding for the HSN is paid by hospitals through a statewide hospital assessment levied each year by the Massachusetts Legislature. All acute care hospitals in the state are assessed their share of this total statewide hospital assessment amount ($164,708 in 2014 and $160,000 in 2013) based on each hospital's charges for private sector payers. Partners HealthCare's hospitals report this assessment as a deduction from net patient service revenue.

Hospitals are reimbursed for charity care based on claims for eligible patients and eligible services that are submitted to and adjudicated by the HSN. Rates of payment are based on Medicare rates and payment policies. The HSN is projected to be under-funded by approximately $86,836 and $78,118 in 2014 and 2013, respectively, with approximately $25,571 and $21,924 in 2014 and 2013, respectively, allocated to Partners HealthCare's hospitals. This shortfall is allocated to hospitals based on their share of total statewide patient care costs. Each hospital's share of the overall state shortfall cannot exceed its total charity care reimbursement. Hospitals with a high proportion of charity care and government funding receive more favorable reimbursement, including limiting their shortfall allocation to no more than 15% of their payments for charity care. In aggregate, Partners HealthCare's acute care hospitals received uncompensated care funding covering 47% of the estimated cost of charity care provided in 2014 and 54% of the estimated cost in 2013, excluding the assessment.

Medicaid
Medicaid is a means-tested health insurance program jointly funded by state and federal governments. States administer the program and set rules for eligibility, benefits and provider payments within broad federal guidelines. The program provides health care coverage to low-income children and families, pregnant women, long-term unemployed adults, seniors and persons with disabilities. Eligibility is determined by a variety of factors, which include income relative to the federal poverty line, age, immigrant status and assets.

(dollars in thousands)

Medicaid payments to Partners HealthCare providers do not cover the full cost of services provided. In aggregate, reimbursement from Medicaid covered 61% and 59% of the estimated cost of services provided in 2014 and 2013, respectively. In addition, Medicaid premium revenue paid to NHP for the care of Medicaid patients enrolled in NHP did not cover the medical expense and administrative costs of care for these enrollees. In aggregate, the premium revenue paid to NHP by Medicaid, excluding the impact of premium deficiency reserves, was $108,655, or 8.6%, less than the cost of care in 2014, and $4,339, or 0.5%, less than the cost of care in 2013.

Federal Program

Medicare

Medicare is a federally sponsored health insurance program for people age 65 or older, under age 65 with certain disabilities and any age with End-Stage Renal Disease. For many years, Medicare payments have not kept pace with increases in the cost of care provided at many hospitals. Additionally, payments to physicians have seen little or no increases over the past several years. Compounding this shortfall in payments is the shift of care from higher paying inpatient services to lower paying outpatient services.

Consequently, Medicare payments to Partners HealthCare do not cover the full cost of services provided. In aggregate, reimbursement from Medicare covered approximately 74% of the estimated cost of services provided in 2014 and 2013.

(dollars in thousands)

For charity care, Medicaid and Medicare, the total estimated cost of services provided by Partners HealthCare exceeded the net reimbursement received under these programs by $1,148,200 and $1,085,938 for the years ended September 30, 2014 and 2013, respectively. The estimated cost of services provided is either obtained directly from a costing system or based on an entity specific ratio of cost to gross charges. In the latter case, cost is derived by applying this ratio to gross charges associated with providing care to charity care, Medicaid and Medicare patients. The following summarizes, by program, the cost of services provided, net reimbursement and cost of services in excess of reimbursement for each year:

	Years Ended September 30, 2014	2013
Cost of services provided		
Charity care, including assessment payments to HSN of $60,372 and $56,028 in 2014 and 2013, respectively	$ 140,641	$ 163,326
Medicaid	886,706	755,114
Medicare	2,634,533	2,477,719
	$ 3,661,880	$ 3,396,159
Net reimbursement		
Charity care	$ 29,808	$ 45,069
Medicaid	542,078	441,939
Medicare	1,941,794	1,823,213
	$ 2,513,680	$ 2,310,221
Cost of services in excess of reimbursement		
Charity care	$ 110,833	$ 118,257
Medicaid	344,628	313,175
Medicare	692,739	654,506
	$ 1,148,200	$ 1,085,938

Bad Debts

In addition to charity care and inadequate funding from the Medicaid and Medicare programs, there are significant losses related to self-pay patients who fail to make payment for services rendered or insured patients who fail to remit co-payments and deductibles as required under the applicable health insurance arrangement. The provision for bad debts represents charges for services provided that are deemed to be uncollectible and was $129,492 and $102,409 in 2014 and 2013, respectively. The estimated cost of providing these services was approximately $48,699 and $38,205 for 2014 and 2013, respectively.

2. Summary of Significant Accounting Policies

Basis of Accounting

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting and include the accounts of PHS and its affiliates. Significant interaffiliate accounts and transactions have been eliminated.

(dollars in thousands)

Use of Estimates
The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates are made in the areas of patient accounts receivable, research grants receivable, investments, receivables and accruals for settlements with third-party payers, accrued medical claims and related expenses, accrued professional liability, accrued compensation and employee benefits, interest rate swaps and accrued other.

Fair Value of Financial Instruments
The fair value of financial instruments approximates the carrying amount reported in the consolidated balance sheets for cash and equivalents, certain investments and investments limited as to use, collateral held and due under securities lending arrangements, patient accounts receivable, research grants receivable, accounts payable and interest rate swaps. More information can be found in Note 6, Fair Value Measurements.

Cash and Equivalents
Cash and equivalents represent money market and highly liquid debt instruments with a maturity at the date of purchase of three months or less. Most of Partners HealthCare's banking activity, including cash and equivalents, is maintained with several national banks and from time to time cash deposits exceed federal insurance limits. It is Partners HealthCare's policy to monitor these banks' financial strength on an ongoing basis and no losses have been experienced to date.

Investments
Investments in equity securities with readily determinable fair values and all investments in debt securities (marketable investments) are measured at fair value based on quoted market prices. The change in net unrealized appreciation on these marketable investments is excluded from excess of revenues over expenses.

Alternative investments, including hedge funds and private equities, do not have readily ascertainable market values. Investments in securities sold short or traded on a national securities exchange are valued based on quoted market prices. Investments in securities that are not traded and restricted securities of public companies are valued based on amounts reported by the fund manager and evaluated by management. The reported value of these investments represents the amount Partners HealthCare would expect to receive if it liquidated its investments at the balance sheet date on a nondistressed basis. Investments in hedge funds, private equity, private debt and other private partnerships (collectively, private partnerships) for which Partners HealthCare owns more than 5% of the overall investment are generally recorded as equity method investments. The change in value of equity method investments is included in excess of revenues over expenses as a component of income from investments. All other investments, including alternative investments, are recorded at cost.

Income from investments (including realized gains and losses, change in value of equity method investments, interest, dividends and endowment income distributions) is included in excess of revenues over expenses unless the income or loss is restricted by donor or law. Income from investments is reported net of investment-related expenses.

(dollars in thousands)

Investments whose cost exceeds fair value are reviewed each quarter to determine whether these investments are other-than-temporarily impaired. Externally managed marketable investments with fair value below cost are considered to be other-than-temporarily impaired and, accordingly, the unrealized depreciation is recognized as realized losses through a write-down in the cost basis of these investments. All other investments are subject to a further review, which considers factors including the anticipated holding period for the investment and the extent and duration of below cost valuation. A similar write-down is recorded when the impairment on these investments has been judged to be other-than-temporary.

Depending on any donor-imposed restrictions on the underlying investments, the amount of the write-down is reported as a realized loss in either temporarily restricted net assets or in excess of revenues over expenses as a component of income from investments, with no adjustment in the cost basis for subsequent recoveries.

Partners HealthCare has an endowment spending policy for pooled endowment funds. A fixed distribution rate for spending is determined each year which will come from either income and/or net accumulated appreciation.

Investments Limited as to Use
Investments limited as to use primarily includes assets whose use is contractually limited by external parties as well as assets set aside by the boards (or management) for identified purposes and over which the boards (or management) retain control such that the boards (or management) may, at their discretion, subsequently use such assets for other purposes. Certain investments corresponding to deferred compensation are accounted for such that all income and appreciation (depreciation) is recorded as a direct addition (reduction) to the asset and corresponding liability.

Securities Loaned
Investments that have been loaned to another institution are reported as pledged assets within investments in the consolidated financial statements. Investments held by the custodian on behalf of Partners HealthCare as collateral on the securities lending transaction are also reported as assets on the balance sheet. Because the collateral must be returned in the future, a corresponding liability is also reported in the consolidated financial statements. In 2014, Partners HealthCare ceased participating in securities lending activities.

Derivative Instruments
Derivatives are recognized on the balance sheet at fair value. As of September 30, 2014, Partners HealthCare elected to stop applying hedge accounting treatment for interest rate swap contracts (swap contracts). As a result of the election to stop applying hedge accounting treatment, changes in the fair value are recorded in excess of revenue over expenses. Previously, Partners HealthCare designated at inception whether the swap contracts were considered hedging or nonhedging for accounting purposes. For hedges, Partners HealthCare formally documented at inception all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategies for undertaking various accounting hedges. Partners HealthCare used its swap contracts which were designated as hedging for accounting purposes as cash flow hedges. Changes in the fair value of swap contracts designated for hedging activities that were highly effective as hedges were excluded from excess of revenues over expenses. Hedge ineffectiveness, if any, was recorded in excess of revenues over expenses.

(dollars in thousands)

Patient Accounts Receivable

Partners HealthCare receives payments for services rendered from federal and state agencies (under the Medicare and Medicaid programs), managed care payers, commercial insurance companies and patients. Patient accounts receivable are reported net of contractual allowances and reserves for denials, uncompensated care and doubtful accounts. The level of reserves is based upon management's assessment of historical and expected net collections, business and economic conditions, trends in federal and state governmental and private employer health care coverage and other collection indicators.

Research Grants Receivable

Partners HealthCare receives research funding from departments and agencies of the U.S. Government, industry and other foundation sponsors. Research grants receivable include amounts due from these sponsors of externally funded research. These amounts have been billed or are billable to the sponsor, or in limited circumstances, represent accelerated spending in anticipation of future funding. Research grants receivable are reported net of reserves for uncollectible accounts.

Other Current Assets

Other current assets include prepaids, nonpatient and research receivables, premiums receivable, and reinsurance recoveries.

Property and Equipment

Property and equipment is reported on the basis of cost less accumulated depreciation. Donated items are recorded at fair value at the date of contribution. All research grants received for capital are recorded in the year of expenditure as a change in unrestricted net assets. Property and equipment is reviewed for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. Depreciation of property and equipment is calculated by use of the straight-line method at rates intended to depreciate the cost of assets over their estimated useful lives, which generally range from three to forty years. Interest costs incurred on borrowed funds during the period of construction of capital assets are capitalized, net of any interest earned, as a component of the cost of acquiring those assets.

Asset Retirement Obligations

Asset retirement obligations, reported in accrued other, are legal obligations associated with the retirement of long-lived assets. These liabilities are initially recorded at fair value and the related asset retirement costs are capitalized by increasing the carrying amount of the related assets by the same amount as the liability. Asset retirement costs are subsequently depreciated over the useful lives of the related assets. Partners HealthCare records changes in the liability resulting from the passage of time and revisions to either the timing or the amount of the original liability estimate. Partners HealthCare reduces these liabilities when the related obligations are settled.

Other Assets

Other assets consist of long-term receivables, deferred financing costs, intangible assets, prepaid ground rent, malpractice insurance receivables (Note 14), investments in healthcare related limited partnerships and benefit assets for over-funded defined benefit plans. Deferred financing costs are amortized over the terms of the related obligations. The carrying value of other assets is reviewed if the facts and circumstances suggest that it may be impaired.

(dollars in thousands)

Compensated Absences
In accordance with formal policies concerning vacation and other compensated absences, accruals of $234,572 and $225,967 were recorded as of September 30, 2014 and 2013, respectively.

Unexpended Funds on Research Grants
Research grants received in advance of corresponding grant expenditures are accounted for as a direct addition to investments limited as to use and unexpended funds on research grants.

Self-Insurance Reserves
Partners HealthCare is generally self-insured for employee healthcare, disability, workers' compensation and certain other employee benefits. These costs are accounted for on an accrual basis to include estimates of future payments for claims incurred prior to year end.

Net Assets
Permanently restricted net assets include the historical dollar amounts of gifts and the income and gains on such gifts which are required by donors to be permanently retained. Temporarily restricted net assets include gifts and the income and gains on permanently restricted net assets which can be expended but for which restrictions have not yet been met. Such restrictions include purpose restrictions where donors have specified the purpose for which the net assets are to be spent, or time restrictions imposed by donors or implied by the nature of the gift (capital projects, pledges to be paid in the future, life income funds) or by interpretations of law (gains available for appropriation but not appropriated in the current period). Unrestricted net assets include all of the remaining net assets of Partners HealthCare. More information can be found in Note 16, Net Assets.

Realized gains and losses are classified as unrestricted net assets unless they are restricted by the donor or law. Unless permanently restricted by the donor, realized gains and net unrealized appreciation on permanently restricted gifts are classified as temporarily restricted until appropriated for spending by Partners HealthCare in accordance with policies established by Partners HealthCare and the Massachusetts Uniform Prudent Management of Institutional Funds Act (UPMIFA). Net losses on permanently restricted endowment funds are classified as a reduction to unrestricted net assets until such time as the fair value of these funds exceeds historical cost.

Gifts
Unconditional promises to give cash and other assets to Partners HealthCare are reported at fair value at the date the promise is received. Conditional promises to give are recognized when the conditions are substantially met. Gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted gifts in the accompanying financial statements.

Gifts of long-lived assets with explicit restrictions that specify use of assets and gifts of cash or other assets that must be used to acquire long-lived assets are reported as additions to temporarily restricted net assets if the assets are not placed in service during the year.

(dollars in thousands)

Grants

Grants and contracts normally provide for the recovery of direct and indirect costs, subject to audit. Partners HealthCare recognizes revenue associated with direct and indirect costs as direct costs are incurred. The recovery of indirect costs is based on predetermined rates for U.S. Government grants and contracts and negotiated rates for other grants and contracts.

Contributed Securities

Partners HealthCare's policy is to sell securities contributed by donors upon receipt, unless prevented from doing so by donor request. For the years ended September 30, 2014 and 2013, contributed securities of $45,058 and $29,017, respectively, were received and liquidated. Donors restricted the proceeds received from the sale of these contributed securities of $8,737 and $4,553 for long-term purpose for the years ended September 30, 2014 and 2013, respectively.

Statement of Operations

All activities of Partners HealthCare deemed by management to be ongoing, major and central to the provision of healthcare services, teaching, research activities and health insurance are reported as operating revenue and expenses. Other activities are deemed to be nonoperating and include unrestricted gifts (net of fundraising expenses), net change in unexpended academic and research gifts, change in fair value of nonhedging interest rate swaps, contribution income from affiliates (Note 3) and substantially all income (loss) from investments. Academic and research gifts largely consist of donor contributions (and the related investment income including realized gains and losses) designated to support the clinical, teaching or research efforts of a physician or department as directed by the donor. These gifts are reported as unrestricted, net of related support expenses, when donor restrictions are of a general nature that are inherent in the normal activities of the organization.

Partners HealthCare recognizes changes in third-party payer settlements and other estimates in the year of the change in estimate. For the years ended September 30, 2014 and 2013, adjustments to prior year estimates resulted in an increase (decrease) to income from operations of $14,642 and ($17,503), respectively. The ($17,503) decrease in income from operations for the year ended September 30, 2013 includes $79,020 recorded as deferred revenue and more fully described below.

Effective October 1, 2007, the Centers for Medicare and Medicaid Services (CMS) adopted the MS-DRG patient classification system (MS-DRGs) for inpatient services to better recognize severity of illness in Medicare payment rates for acute care hospitals. The adoption of MS-DRGs resulted in the expansion of the number of diagnosis related groups (DRGs), a system of classifying patients for purposes of inpatient reimbursement. By increasing the number of DRGs and more fully taking into account patients' severity of illness in Medicare payment rates for acute care hospitals, the use of MS-DRGs encourages hospitals to improve their documentation and coding of patient diagnoses. CMS has determined that the adoption of the MS-DRGs has increased aggregate payments to hospitals due to additional documentation and coding without a corresponding increase in actual patient severity of illness.

(dollars in thousands)

CMS is required by its enabling statute to maintain budget neutrality by prospectively adjusting the Medicare payment rate to eliminate the effect of changes in DRG classification that do not reflect real changes in case-mix. CMS requires Congressional authority, however, to recoup any overpayments made in prior years. In 2007, Congress granted CMS the authority to recoup overpayments made to hospitals in 2008 and 2009 resulting from increased coding and documentation, which CMS did through rate reductions in 2011 and 2012. Under the American Taxpayer Relief Act of 2012, Congress granted CMS the authority to recoup overpayments made to hospitals in 2010 through 2012 through rate reductions in 2014 through 2017.

In 2013, Partners HealthCare recorded the estimated overpayment amounts received in 2010 through 2012 of $79,020 as deferred revenue to be amortized into net patient service revenue in 2014 through 2017 to offset the rate reductions. Management believes this accounting treatment better reflects the financial impact of this rate methodology and more accurately presents the recognition of revenue. For the years ended September 30, 2014 and 2013, amortization of these overpayments amounted to $6,893 and $0, respectively. Partners HealthCare anticipates amortizing the remaining overpayments as follows: 2015 - $15,192; 2016 - $23,900; and 2017 - $33,035.

The statement of operations includes excess of revenues over expenses. Changes in unrestricted net assets, which are excluded from excess of revenues over expenses, include change in net unrealized appreciation on marketable investments, change in fair value of effective hedging interest rate swaps (prior to the change in accounting policy), contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for acquisition of such assets) and change in funded status of defined benefit plans.

Net Patient Service Revenue

Partners HealthCare maintains agreements with CMS of the United States Department of Health and Human Services under the Medicare program, the Commonwealth of Massachusetts (the Commonwealth) under the Medicaid program and various managed care payers that govern payment for services rendered to patients covered by these agreements. The agreements generally provide for per case or per diem rates or payments based on discounted charges for inpatient care and discounted charges or fee schedules for outpatient care. Certain contracts also provide for payments that are contingent upon meeting agreed upon quality and efficiency measures.

(dollars in thousands)

Partners HealthCare recognizes patient service revenue associated with services provided to patients who have third-party payer coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, Partners HealthCare recognizes revenue on the basis of its standard rates (subject to discounts) for services provided. On the basis of historical experience, a significant portion of Partners HealthCare's uninsured patients are unable or fail to pay for the services provided. Consequently, Partners HealthCare records a provision for bad debts related to uninsured patients in the period the services are provided. For the years ended September 30, 2014 and 2013, patient service revenue net of contractual allowances and discounts (before the provision for bad debts) is as follows:

	2014	2013
Patient service revenue (net of contractual allowances and discounts)		
Third-party payers	$ 6,906,051	$ 6,638,603
Uninsured patients	265,999	233,549
Total all payers	$ 7,172,050	$ 6,872,152

Net patient service revenue includes estimated retroactive revenue adjustments due to future audits, reviews and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews and investigations. Contracts, laws and regulations governing the Medicare, Medicaid and uncompensated care programs (Note 1) and managed care payer arrangements are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. A portion of the accrual for settlements with third-party payers has been classified as long-term because such amounts, by their nature or by virtue of regulation or legislation, will not be paid within one year.

Partners HealthCare provides either full or partial uncompensated care to patients who cannot afford to pay for their medical services based on income and family size. Uncompensated care is generally available to qualifying patients for medically necessary services. Partners HealthCare reports certain bad debts related to emergency services as uncompensated care. Uncompensated care is reported at gross charges with an offsetting allowance, as there is no expectation of collection. Accordingly, there is no net patient service revenue related to uncompensated care.

Medical Claims and Related Expenses
NHP contracts with various community health centers, hospital-based primary care physician practices and other health care providers for the delivery of services to its members and compensates these providers on a capitated, fee-for-service, or per diem basis.

(dollars in thousands)

The cost of contracted health care services is accrued in the period in which services are provided and include certain estimated amounts. The estimated liability for medical claims and related expenses is actuarially determined based on analysis of historical claims-paid experience, modified for changes in enrollment, inflation and benefit coverage. The liability for medical claims and related expenses represents the anticipated cost of claims incurred but unpaid at the balance sheet date. The estimates for claims expense may be more or less than the amounts ultimately paid when claims are settled. Such changes in estimates are reflected in the current period in the consolidated statements of operations.

In the normal course of business, NHP identifies and recoups overpayments through reductions in future payments made to providers and hospitals. Such overpayments are the result of, among other things, coordination of benefits and provider claim audits. For the years ended September 30, 2014 and 2013, NHP identified approximately $44,100 and $34,500, respectively, of recoveries related to claim overpayments made for both current-year and prior-year paid claims, which are reflected as a reduction to medical claims and related expenses in the consolidated statements of operations. As of September 30, 2014 and 2013, NHP's accounts receivable include $2,049 and $2,270, respectively, relating to such overpayments.

Premium Revenue

Premiums are due monthly and recorded as earned during the period in which members are eligible to receive services. Premiums received prior to the first day of the coverage period are recorded as unearned premiums in accounts payable and accrued expenses.

Reinsurance

Reinsurance premiums are reported in medical claims and related expenses and reinsurance recoveries are reported as reductions in medical claims and related expenses.

Settlements

NHP contracts with the Executive Office of Health and Human Services (EOHHS) and certain providers based on historical and anticipated experience. These methods of reimbursement result in settlements based on actual versus anticipated experience which could result in either payments due from (to) these providers. Settlements receivable of $21,197 and $16,174 were recorded as of September 30, 2014 and 2013, respectively. Settlements payable of $14,654 and $15,989 were recorded as of September 30, 2014 and 2013, respectively. The settlements are intended to include both reported and unreported incurred claims as of September 30, 2014 and 2013.

Premium Deficiency Reserve

NHP recognizes premium deficiency reserves based upon expected premium revenue, medical expense and administrative expense levels, and remaining contractual obligations using historical experience. Anticipated investment income is not included in the determination of premium deficiency reserves since its effect is deemed to be immaterial. As of September 30, 2014 and 2013, premium deficiency reserves total approximately $91,555 and $6,494, respectively, and are included in accrued medical claims and related expenses in the accompanying consolidated financial statements.

(dollars in thousands)

Claims Adjustment Expenses
Claims adjustment expenses (CAE) are those costs expected to be incurred in connection with the adjustment and recording of health claims. NHP has recorded an estimate of unpaid CAE associated with incurred but unpaid claims, which is included in medical claims and related expenses in the accompanying consolidated statements of operations. Management believes the amount of the liability for unpaid CAE as of September 30, 2014, is adequate to cover NHP's cost for the adjustment and recording of unpaid claims; however, actual expenses may differ from those established estimates. Adjustments to the estimates for unpaid CAE are reflected in operating results in the period in which the change in estimate is identified (Note 9).

Other Revenue
Other revenue includes institutional revenue (for example, billing for services provided to other healthcare providers), royalties and management services.

3. Acquisitions

NHP and Cooley Dickinson Health Care Corporation and Subsidiaries (CDHCC) contributed their net assets to Partners HealthCare on October 1, 2012 and July 1, 2013, respectively. As a result, Partners HealthCare recorded contribution income of $263,146 reflecting the fair value of the contributed net assets of NHP of $152,461 and of CDHCC of $110,685 on their respective transaction dates. Of this amount, $254,205 represents unrestricted net assets and is included as a nonoperating gain in the accompanying consolidated statements of operations and changes in net assets. Restricted contribution income of $8,431 and $510 was recorded within temporarily restricted net assets and permanently restricted net assets, respectively, in the accompanying consolidated statement of changes in net assets.

(dollars in thousands)

Assets, liabilities, and net assets assumed as of the acquisition dates are as follows:

	NHP	CDHCC	Total
Assets			
Cash and cash equivalents	$ 12,461	$ 5,207	$ 17,668
Assets limited as to use and investments	230,551	131,057	361,608
Patient accounts receivable, net	-	20,463	20,463
Property plant and equipment	4,224	76,514	80,738
Other assets	56,202	7,056	63,258
Total assets acquired	$ 303,438	$ 240,297	$ 543,735
Liabilities			
Accounts payable and accrued expenses	$ 25,616	$ 16,073	$ 41,689
Accrued medical claims and related expenses	120,916	-	120,916
Accrual for settlements with third-party payers	-	11,631	11,631
Long-term debt	-	61,812	61,812
Accrued pension and post retirement benefits	-	25,205	25,205
Other liabilities	4,445	14,891	19,336
Total liabilities assumed	150,977	129,612	280,589
Net Assets			
Unrestricted	152,461	101,744	254,205
Temporarily restricted	-	8,431	8,431
Permanently restricted	-	510	510
Total net assets	152,461	110,685	263,146
Total liabilities and net assets	$ 303,438	$ 240,297	$ 543,735

A summary of the financial results of NHP from the period October 1, 2012 through September 30, 2013 and of CDHCC from the period July 1, 2013 through September 30, 2013 that is included in the consolidated statements of operations and changes in net assets is as follows:

	NHP	CDHCC	Total
Total operating revenue	$ 1,351,361	$ 47,006	$ 1,398,367
Total operating expenses	1,332,641	50,385	1,383,026
Income (loss) from operations	18,720	(3,379)	15,341
Nonoperating gains (expenses), net	1,245	(12,802)	(11,557)
Excess (deficit) of revenues over expenses	19,965	(16,181)	3,784
Pension related changes	-	2,255	2,255
Other changes	7,825	6,765	14,590
Increase (decrease) in unrestricted net assets	$ 27,790	$ (7,161)	$ 20,629

(dollars in thousands)

A summary of the consolidated financial results of Partners HealthCare for the year ended September 30, 2013, as if the transactions had occurred on October 1, 2012 is as follows (unaudited):

	2013
Total operating revenue	$ 10,501,763
Total operating expenses	10,331,840
Income from operations	169,923
Nonoperating gains	445,658
Excess of revenues over expenses	615,581
Pension related changes	851,141
Other changes	239,551
Increase in unrestricted net assets	$ 1,706,273

4. Levels of Capital and Surplus

Risk-based capital (RBC) is a methodology adopted by the National Association of Insurance Commissioners (NAIC) for determining the minimum level of capital and surplus deemed necessary for an insurer based upon the types of assets held and business written. Pursuant to a guaranty entered into by PHS when it acquired NHP in 2012 (the RBC Guaranty), PHS has committed to maintain NHP' s capital and surplus at a specified minimum level, measured quarterly in accordance with an RBC methodology permitted by the Massachusetts Division of Insurance (DOI). The RBC Guaranty may be enforced by the DOI.

Due to significant incurred and anticipated losses under NHP's MassHealth and CommCare contracts, PHS transferred $86,000 to NHP in June 2014 pursuant to the RBC Guaranty.

In accordance with accounting guidance, NHP recognized premium deficiency reserves of $91,555, related to its MassHealth and CommCare contracts, for anticipated losses in fiscal 2015. In order to comply with its obligations under the RBC Guaranty PHS transferred $60,000 to NHP in December 2014.

NHP's current contract with EOHHS requires NHP to maintain a minimum net worth and/or financial insolvency insurance in an amount equal to the Minimum Net Worth calculation as defined in Massachusetts General Law 176G, Section 25. At December 31, 2013 and 2012 (NHP's fiscal and statutory year end), the minimum net worth requirement, as determined in accordance with EOHHS guidelines, was $78,800 and $75,300, respectively. NHP's statutory net worth was $97,200 and $160,300 at December 31, 2013 and 2012, respectively, and thus exceeded the EOHHS requirements by $18,400 and $85,000, respectively.

(dollars in thousands)

5. Investments and Investments Limited as to Use

Investments are either separately invested or included in pooled investment funds. The Partners HealthCare System Pooled Investment Accounts (Partnership) is structured as a single general partnership composed of three investment pools, with PHS and substantially all of its affiliates participating in the pools as partners. Each partner's interest in the Partnership is based on its underlying investments in one or more of the three separate pools. Amounts included in the investment pools are accounted for using the fair value method whereby each partner is assigned a number of units based on the fair value of the assets of a pool at the time of entry of the funds into the pool. Current fair value is used to determine the number of units allocated to additional amounts placed in a pool and to value withdrawals from a pool. Income from investments of the pools, including realized gains and losses, is allocated on a unitized basis to a partner based on the partner's share of units in a pool.

Among other investments, the Partnership invests in private partnerships whose assets include equity, fixed income and other investments. As of September 30, 2014, the Partnership has unfunded commitments of approximately $451,980 which will be drawn down by the various general partners over the next several years. The maximum annual drawdown is expected to be less than 2% of investments and investments limited as to use.

Investments and investments limited as to use are recorded in the balance sheet as follows:

	September 30, 2014	September 30, 2013
Current assets		
Investments	$ 1,474,058	$ 1,439,299
Current portion of investments limited as to use	2,120,057	1,813,490
	3,594,115	3,252,789
Long-term assets		
Investments limited as to use, less current portion	2,927,360	2,771,216
Long-term investments	1,026,538	957,100
	$ 7,548,013	$ 6,981,105

(dollars in thousands)

Investments limited as to use consist of the following:

	September 30, 2014		September 30, 2013	
	Current Portion	Long-Term Portion	Current Portion	Long-Term Portion
Internally designated funds				
Reserved for capital expenditures	$ 1,010,371	$ -	$ 854,265	$ -
Unexpended academic and research gifts	-	2,449,470	-	2,331,946
Deferred compensation	-	216,553	-	191,726
Other	863,371	224,310	771,482	207,902
	1,873,742	2,890,333	1,625,747	2,731,574
Externally limited funds				
Unexpended funds on research	183,222	-	160,668	-
Contributions held for others	3,991	-	4,272	-
Professional liability trust fund	-	37,027	-	39,642
Held by trustees under debt and other agreements	59,102	-	22,803	-
	246,315	37,027	187,743	39,642
	$ 2,120,057	$ 2,927,360	$ 1,813,490	$ 2,771,216

Investments and investments limited as to use are reported at either fair value or on the equity or cost methods of accounting. The composition of these investments, segregated between pooled investments and those that are separately invested, is as follows:

	September 30, 2014			
	At Fair Value	On Equity Method	On Cost Method	Total
Pooled investments				
Invested cash equivalents	$ 43,396	$ -	$ -	$ 43,396
Separately managed investments	2,301,880	-	-	2,301,880
Mutual funds	549,948	-	-	549,948
Commingled funds	1,151,708	-	-	1,151,708
Private partnerships	-	804,445	2,013,552	2,817,997
	4,046,932	804,445	2,013,552	6,864,929
Separately invested				
Invested cash equivalents	127,785	-	741	128,526
Equities	14,062	-	23,937	37,999
U.S. Government and domestic fixed income securities	32,427	-	-	32,427
Mutual funds	360,417	-	-	360,417
Other	47,018	-	76,697	123,715
	581,709	-	101,375	683,084
	$ 4,628,641	$ 804,445	$ 2,114,927	$ 7,548,013

(dollars in thousands)

Separately managed investments include cash and equivalents of $193,406, equities of $930,884 and fixed income securities of $1,177,590 as of September 30, 2014.

	September 30, 2013			
	At Fair Value	On Equity Method	On Cost Method	Total
Pooled investments				
Invested cash equivalents	$ 63,146	$ -	$ -	$ 63,146
Separately managed investments	2,297,413	-	-	2,297,413
Mutual funds	607,991	-	-	607,991
Commingled funds	959,607	-	-	959,607
Private partnerships	-	722,516	1,628,480	2,350,996
	3,928,157	722,516	1,628,480	6,279,153
Separately invested				
Invested cash equivalents	145,057	-	488	145,545
Equities	12,273	-	14,247	26,520
U.S. Government and domestic fixed income securities	33,653	-	-	33,653
Mutual funds	359,306	-	327	359,633
Other	59,380	-	77,221	136,601
	609,669	-	92,283	701,952
	$ 4,537,826	$ 722,516	$ 1,720,763	$ 6,981,105

Separately managed investments include cash and equivalents of $284,815, equities of $660,847 and fixed income securities of $1,351,751 as of September 30, 2013.

For the private partnerships reflected in the balance sheet at cost, the difference (unrecorded net unrealized appreciation) between the value reported by the investment managers and the cost for these investments was $883,174 and $745,013 as of September 30, 2014 and 2013, respectively.

(dollars in thousands)

The fair value and gross unrealized depreciation of investments and investments limited as to use, with a fair value less than cost, that are not deemed to be other-than-temporarily impaired as of September 30, 2014 are as follows:

	Less than 12 Months		12 Months or Greater	
	Fair Value	**Gross Unrealized Depreciation**	**Fair Value**	**Gross Unrealized Depreciation**
Pooled investments				
Separately managed investments	$ 29,206	$ (878)	$ 196	$ (2)
Mutual funds	247,707	(3,342)	112,054	(3,691)
Commingled funds	105,325	(7,761)	72,888	(3,074)
	382,238	(11,981)	185,138	(6,767)
Separately invested				
Equities	-	-	756	(97)
Fixed income securities	-	-	1,168	(866)
Mutual funds	-	-	27,949	(69)
External trusts	-	-	5,865	(1,945)
	-	-	35,738	(2,977)
	$ 382,238	$ (11,981)	$ 220,876	$ (9,744)

In addition, for certain private partnerships recorded at cost, gross unrealized depreciation amounted to $31,375 as of September 30, 2014, with $11,228 of that amount unrealized for 12 months or greater.

Based on management's quantitative and qualitative assessment, investments whose cost exceeds fair value are not considered to be other-than-temporarily impaired as of September 30, 2014. Management believes these investments will recover their values and there is no intention to liquidate these positions.

(dollars in thousands)

Investment income and gains (losses) from cash and equivalents, investments and investments limited as to use are comprised of the following:

	Years Ended September 30, 2014	Years Ended September 30, 2013
Unrestricted		
Dividends, interest and other income	$ 62,576	$ 54,710
Endowment income distributions, net of reinvested gains	35,564	32,272
Net realized gains (losses) on investments		
Realized gains	313,244	267,110
Other-than-temporary impairment	(55,636)	(85,879)
Change in value of equity method investments	33,832	19,971
Recovery on endowment funds	91	893
Total investment activity included in excess of revenues over expenses	389,671	289,077
Change in net unrealized appreciation on marketable investments	(3,309)	74,522
Total unrestricted investment activity	386,362	363,599
Temporarily restricted		
Dividends and interest income	14,857	5,146
Endowment income distributions	(41,823)	(38,182)
Net realized gains (losses) on investments		
Realized gains	63,595	53,844
Other-than-temporary impairment	(10,468)	(15,351)
	26,161	5,457
Change in value of equity method investments	10,736	4,701
Change in net unrealized appreciation on marketable investments	(11,118)	24,695
Recovery on endowment funds	(91)	(893)
	(473)	28,503
Total temporarily restricted investment activity	25,688	33,960
Permanently restricted		
Dividends and interest income	4	(7)
Net realized gains on investments	26	170
Change in net unrealized appreciation on marketable investments	1,706	802
Total permanently restricted investment activity	1,736	965
	$ 413,786	$ 398,524

(dollars in thousands)

Investment income included in operating results and excess of revenues over expenses is comprised of the following:

	Years Ended September 30, 2014	Years Ended September 30, 2013
Investment income included in operations and reported in other revenue	$ 13,692	$ 11,816
Investment income included in nonoperating gains and reported in		
Income from investments	227,357	146,631
Academic and research gifts, net of expenses	148,622	130,630
Total investment activity included in excess of revenues over expenses	$ 389,671	$ 289,077

Securities Lending
In 2014, Partners HealthCare ceased participation in lending securities. The fair value of loaned securities and related collateral as of September 30, 2014 and 2013 is as follows:

	2014		2013	
	Loaned Securities	Collateral	Loaned Securities	Collateral
Equities, U.S. government, domestic and foreign fixed income securities	$ -	$ -	$ 223,389	$ 229,400

Income generated by the Partnership from securities lending arrangements was $157 and $561 for the years ended September 30, 2014 and 2013, respectively.

6. Fair Value Measurements

Fair value is 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 (also referred to as exit price). Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. In determining fair value, the use of various valuation approaches, including market, income and cost approaches, is permitted.

Fair Value Hierarchy
A fair value hierarchy has been established based on whether the inputs to valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the reporting entity's assumptions about the inputs market participants would use. The fair value hierarchy requires the reporting entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. In addition, for hierarchy classification purposes, the reporting entity should not look through the form of an investment to the nature of the underlying securities held by an investee.

(dollars in thousands)

The hierarchy is described below.

Level 1 Valuations using quoted prices in active markets for identical assets or liabilities. Valuations of these products do not require a significant degree of judgment. Level 1 assets and liabilities primarily include debt and equity securities that are traded in an active exchange market.

Level 2 Valuations using observable inputs other than Level 1 prices such as quoted prices in active markets for similar assets or liabilities; quoted prices for identical or similar assets or liabilities in markets that are not active; broker or dealer quotations; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities primarily include debt securities with quoted prices that are traded less frequently than exchange-traded instruments as well as debt securities and derivative contracts whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.

Level 3 Valuations using unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities. Level 3 includes assets and liabilities whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques reflecting the reporting entity’s assumptions about the assumptions market participants would use as well as those requiring significant management judgment.

Valuation Techniques
Pooled investments (except for private partnerships, which are reported on either the equity method or cost method of accounting), separately invested cash equivalents, debt and equity securities, and collateral held under securities lending arrangements are classified within Level 1 or Level 2 of the fair value hierarchy as they are valued using quoted market prices, broker or dealer quotations, or other observable pricing sources. Certain types of investments are classified within Level 3 of the fair value hierarchy because they have little or no market activity and therefore have little or no observable inputs with which to measure fair value.

The valuation of interest rate swaps is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves and implied volatilities.

(dollars in thousands)

The following tables summarize fair value measurements as of September 30, 2014 and 2013 for financial assets and liabilities measured at fair value on a recurring basis:

	Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value at September 30, 2014
Assets				
Pooled investments				
Invested cash equivalents	$ 9,702	$ 33,694	$ -	$ 43,396
Separately managed investments	1,700,305	601,575	-	2,301,880
Mutual funds	549,948	-	-	549,948
Commingled funds	-	1,151,708	-	1,151,708
	2,259,955	1,786,977	-	4,046,932
Separately invested				
Invested cash equivalents	127,785	-	-	127,785
Equities	9,708	4,354	-	14,062
U.S. Government and domestic fixed income securities	17,224	15,203	-	32,427
Mutual funds	360,417	-	-	360,417
Other	-	36,280	10,738	47,018
	515,134	55,837	10,738	581,709
	$ 2,775,089	$ 1,842,814	$ 10,738	$ 4,628,641
Liabilities				
Interest rate swaps		$ 295,656		$ 295,656

(dollars in thousands)

	Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Items (Level 1)	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Fair Value at September 30, 2013**
Assets				
Pooled investments				
Invested cash equivalents	$ 13,988	$ 49,158	$ -	$ 63,146
Separately managed investments	1,483,585	813,828	-	2,297,413
Mutual funds	607,991	-	-	607,991
Commingled funds	-	959,607	-	959,607
	2,105,564	1,822,593	-	3,928,157
Separately invested				
Invested cash equivalents	145,048	9	-	145,057
Equities	9,760	2,513	-	12,273
U.S. Government and domestic fixed income securities	18,773	14,880	-	33,653
Mutual funds	359,306	-	-	359,306
Other	108	49,591	9,681	59,380
	532,995	66,993	9,681	609,669
	$ 2,638,559	$ 1,889,586	$ 9,681	$ 4,537,826
Collateral held under securities lending arrangements		$ 229,400		$ 229,400
Liabilities				
Interest rate swaps		$ 232,005		$ 232,005

For the years ended September 30, 2014 and 2013, the changes in the fair value of the assets measured using significant unobservable inputs (Level 3) were comprised of the following:

	2014	**2013**
Balances at beginning of year	$ 9,681	$ 9,073
Total gains (losses)		
Dividends and interest income	33	43
Realized gains on investments	198	463
Realized loss on investments	(182)	(8)
Change in net unrealized appreciation on investments	724	115
Purchases	541	170
Sales	(365)	(175)
Transfer into Level 3	108	-
Balances at end of year	$ 10,738	$ 9,681

The net unrealized gain on Level 3 investments held as of September 30, 2014 was $1,236.

(dollars in thousands)

7. Pledges Receivable and Contributions Receivable From Trusts

Pledges receivable represent unconditional promises to give and are net of allowances for uncollectible amounts. Pledges are recorded at the present value of their estimated future cash flows. Pledges collectible within one year are classified as other current assets, net of allowances, and total $94,331 and $91,281 as of September 30, 2014 and 2013, respectively. Estimated cash flows due after one year are discounted using published treasury bond and note yields that are commensurate with estimated collection risks. The blended discount rate was 0.8% for 2014 and 2013. Pledges are expected to be collected as follows:

	September 30, 2014	September 30, 2013
Amounts due		
Within one year	$ 110,668	$ 111,141
In one to five years	161,764	140,842
In more than five years	19,300	11,084
Total pledges receivable	291,732	263,067
Less: Unamortized discount	5,348	4,715
	286,384	258,352
Less: Allowance for uncollectibles	23,460	29,857
Net pledges receivable	262,924	228,495
Contributions receivable from trusts	29,382	27,881
	$ 292,306	$ 256,376

8. Property and Equipment

Property and equipment consists of the following:

	September 30, 2014	September 30, 2013
Land and land improvements	$ 172,924	$ 172,530
Buildings and building improvements	5,558,974	5,348,349
Equipment	1,427,800	1,348,621
Construction in progress	900,180	591,763
	8,059,878	7,461,263
Accumulated depreciation	(3,443,970)	(3,225,424)
Property and equipment, net	$ 4,615,908	$ 4,235,839

Depreciation expense for the years ended September 30, 2014 and 2013 was $454,512 and $429,734, respectively. Interest costs, net of interest earned, aggregating $30,744 and $20,771 were capitalized in 2014 and 2013, respectively.

(dollars in thousands)

For the years ended September 30, 2014 and 2013, fully depreciated assets with an original cost of $235,966 and $241,091, respectively, were written off.

9. Accrued Medical Claims and Related Expenses

These liabilities include estimates of expected trends in claims severity, frequency, and other factors, which could vary as the claims are ultimately settled and are based principally upon historical experience. As a result of changes in estimates of insured events in prior years and recoveries, the liability on claims existing on October 1, 2013 and 2012, increased (decreased) $13,332 and ($26,081), respectively, in the years ended September 30, 2014 and 2013, respectively. Increases (decreases) of this nature occur as the result of claim settlements and recoveries during the current year and as additional information is received regarding individual claims, causing changes from the original estimates of the cost of these claims. Ongoing analysis of the recent loss development trends is also taken into account in evaluating the overall adequacy of the reserves.

	2014	2013
Balance at beginning of year	$ 121,833	$ 120,916
Less:		
Premium deficiency reserve	(6,494)	(9,552)
Medical loss ratio rebate payable	(4,701)	(202)
Accrual for claims adjustment expenses	(2,855)	(2,759)
Claim recoveries	(1,991)	(4,484)
Plus: Settlements payable, net	23,555	19,559
Net balance at beginning of year	129,347	123,478
Incurred related to		
Current year	1,597,866	1,242,333
Prior years	13,332	(26,081)
Total incurred	1,611,198	1,216,252
Paid related to		
Current year	1,431,205	1,103,374
Prior years	136,954	107,009
Total paid	1,568,159	1,210,383
Net balance at end of year	172,386	129,347
Plus:		
Premium deficiency reserve	91,555	6,494
Medical loss ratio rebate payable	611	4,701
Accrual for claims adjustment expenses	4,381	2,855
Claims recoveries	7,567	1,991
Less: Settlements payable, net	(22,020)	(23,555)
Balance at end of year	$ 254,480	$ 121,833

(dollars in thousands)

Medical claims and related expenses in the accompanying consolidated statements of operations include these amounts along with other nonclaims related costs. These nonclaims related expenses were for directly delivered services and medical cost risk sharing and incentives, totaling approximately $14,792 and $13,181 for the years ended September 30, 2014 and 2013, respectively.

10. Long-Term Obligations

Long-term obligations issued by PHS and its affiliates consist of the following:

	September 30, 2014	September 30, 2013
Massachusetts Health and Educational Facilities Authority (Authority) Revenue Bonds		
Partners HealthCare System Series D, variable interest rate of 0.02% and 0.05% at September 30, 2014 and 2013, respectively, final maturity in 2017	$ 11,490	$ 92,005
Partners HealthCare System Series E, average fixed interest rate of 5.00%, final maturity in 2023	-	4,475
Partners HealthCare System Series F, issued in multiple subseries, average fixed interest rate of 5.00%, variable interest rate of 0.24% and 0.17% at September 30, 2014 and 2013, respectively, final maturity in 2040	273,458	371,618
Partners HealthCare System Series G, issued in multiple subseries, average fixed interest rate of 4.92%, variable interest rate of 0.24% and 0.19% at September 30, 2014 and 2013, respectively, final maturity in 2047	438,054	446,252
Partners HealthCare System Series H, variable interest rate of 0.08% and 0.11% at September 30, 2014 and 2013, respectively, final maturity in 2042	171,165	171,159
Partners HealthCare System Series I, issued in multiple subseries, average fixed interest rate of 4.79%, variable interest rate of 0.03% and 0.06%, at September 30, 2014 and 2013, respectively, final maturity in 2044	171,996	226,002
Partners HealthCare System Series J, average fixed interest rate of 5.00%, final maturity in 2039	456,746	473,742
Partners HealthCare System Series P, variable interest rate of 0.04% and 0.06% at September 30, 2014 and 2013, respectively, final maturity in 2027	150,000	150,000
Massachusetts Development Finance Agency (Agency) Revenue Bonds		
Partners HealthCare System Series K, issued in multiple subseries, average fixed interest rate of 4.74%, variable interest rate of 0.04% and 0.34% at September 30, 2014 and 2013, respectively, final maturity in 2046	352,836	434,063
Partners HealthCare System Series L, average fixed interest rate of 4.93%, final maturity in 2041	351,264	352,185
Partners HealthCare System Series M, issued in multiple subseries, average fixed interest rate of 4.95%, variable interest rate of 0.36% at September 30, 2014, final maturity in 2048	509,100	-
Partners HealthCare System Series N, issued in multiple subseries, variable interest rate of 0.62% at September 30, 2014, final maturity in 2044	141,350	-
Partners HealthCare System Series 2007 taxable bonds, fixed interest rate of 6.26%, final maturity in 2037	100,000	100,000
Partners HealthCare System Series 2011 taxable bonds, fixed interest rate of 3.44%, final maturity in 2021	250,000	250,000
Partners HealthCare System 2012 Taxable Senior Notes, fixed interest rate of 4.11%, final maturity in 2052	400,000	400,000
Partners HealthCare System 2014 Taxable Senior Notes, fixed interest rate of 4.73%, final maturity in 2044	150,000	-
Other obligations	6,454	6,798
Capital lease obligations	2,229	4,060
Total long-term obligations net of premiums and discounts	3,936,142	3,482,359
Less:		
Current portion	238,204	361,249
Auction rate securities held	-	23,830
	$ 3,697,938	$ 3,097,280

(dollars in thousands)

Aggregate maturities and payments of long-term obligations during the next five years and thereafter, and other amounts classified as current liabilities, are as follows:

	Scheduled Maturities	Bonds Supported by Partners HealthCare Liquidity	Total
2015	$ 64,944	$ 173,260	$ 238,204
2016	63,576	-	63,576
2017	64,419	-	64,419
2018	70,755	-	70,755
2019	71,687	-	71,687
Thereafter	3,427,501	-	3,427,501
	$ 3,762,882	$ 173,260	$ 3,936,142

The scheduled maturities represent annual payments as required under debt repayment schedules. The current portion of long-term obligations includes the payments scheduled to be made in 2015 along with bonds supported by Partners HealthCare liquidity. The variable rate bonds supported by self liquidity provide the bondholder with an option to tender the bonds to Partners HealthCare. Accordingly, these bonds are classified as a current liability.

The fair value of long-term obligations was $4,152,828 and $3,559,469 as of September 30, 2014 and 2013, respectively, and would be classified as Level 2. The carrying amount of the variable rate debt is a reasonable estimate of its fair value. The fair value of the fixed rate debt is estimated based on quoted market prices for the same or similar issues.

Interest expense approximates interest paid, net of capitalized interest, during the years ended September 30, 2014 and 2013.

Taxable Bonds and Notes
In November 2012, PHS issued $400,000 of Partners HealthCare System Taxable Senior Notes. Proceeds from the notes were used to make a voluntary contribution to Partners HealthCare's defined benefit pension plans ($200,000) and to finance certain capital projects ($200,000).

In March 2014, PHS issued $150,000 of Partners HealthCare System Taxable Senior Notes. Proceeds from the notes were used to finance certain capital projects.

Revenue Bonds
In January 2014, PHS issued $496,040 of Partners HealthCare System Series M Revenue Bonds, plus bond premium of $14,337. The bond proceeds, net of issuance costs of $4,042, were used to refund portions of Series D Bonds ($71,665) and Series K Bonds ($73,815) and to finance certain capital projects ($360,855).

(dollars in thousands)

In August 2014, PHS issued $141,350 of Partners HealthCare System Series N Revenue Bonds. The Series N Bonds were privately placed with two banks. The bond proceeds were used to refund portions of Series F Bonds ($91,350) and Series I Bonds ($50,000).

Partners HealthCare bonds are general obligations of PHS supported by guarantees from BWHC, The Brigham and Women's Hospital, Inc. (BWH), MGH and The General Hospital Corporation (the General) which may be suspended under certain conditions.

PHS bond agreements contain certain covenants, including a minimum debt service coverage ratio and limitations on additional indebtedness and asset transfers.

Credit Agreement

Partners HealthCare maintains a $150,000 Credit Agreement (the Agreement) that provides access to same day funds. Advances under the Agreement bear a variable rate of interest based on the London Interbank Offered Rate (LIBOR). As of September 30, 2014, there were no amounts outstanding under the Agreement. The Agreement expires in June 2017.

11. Derivatives

Interest Rate Swaps

Partners HealthCare utilizes swap contracts to manage fluctuations in cash flows resulting from interest rate risk on certain of its variable rate bonds. These bonds expose Partners HealthCare to variability in interest payments due to changes in interest rates. Management believes that it is prudent to limit the variability of its interest payments. To meet this objective and to take advantage of low interest rates, Partners HealthCare entered into various swap contracts involving the exchange of fixed rate payments by Partners HealthCare for variable rate payments from several counterparties based on a percentage of LIBOR.

By using swap contracts to manage the risk of changes in interest rates, Partners HealthCare exposes itself to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the swap contracts. When the fair value of a swap contract is positive, the counterparty has a liability to Partners HealthCare, which creates credit risk. Partners HealthCare minimizes its credit risk by entering into swap contracts with several counterparties and requiring the counterparty to post collateral for the benefit of Partners HealthCare based on the credit rating of the counterparty and the fair value of the swap contract. When the fair value of a swap contract is negative, Partners HealthCare has a liability to the counterparty and, therefore, it does not possess credit risk. Under certain circumstances, Partners HealthCare may be required to post collateral for the benefit of the counterparty and the counterparty may be required to post collateral for the benefit of Partners HealthCare. Market risk is the adverse effect on the value of a financial instrument that results from a change in interest rates. The market risk associated with interest rate changes is managed by establishing and monitoring parameters that limit the types and degree of market risk that may be undertaken.

(dollars in thousands)

The following is a summary of the outstanding positions under these swap contracts as of September 30, 2014:

Effective Date	Notional Amount	Maturity	Rate Paid	Rate Received
5/1/03	$ 150,000	7/1/35	4.40%	67% 1-month LIBOR
7/1/03	8,700	7/1/15	5.11%	67% 6-month LIBOR
7/1/05	150,000	7/1/40	3.63%	67% 1-month LIBOR
7/1/05	42,500	7/1/25	5.11%	67% 6-month LIBOR
7/1/07	150,000	7/1/42	3.46%	67% 1-month LIBOR
7/1/09	100,000	7/1/44	3.71%	67% 1-month LIBOR
7/1/11	100,000	7/1/46	3.74%	67% 1-month LIBOR
7/1/13	100,000	7/1/48	3.80%	67% 1-month LIBOR
7/1/15	100,000	7/1/50	3.80%	67% 1-month LIBOR
7/1/17	100,000	7/1/52	3.74%	67% 1-month LIBOR

As of September 30, 2014, Partners HealthCare elected to stop applying hedge accounting treatment for its swap contracts; accordingly, changes in the fair value of interest rate swaps are recognized as nonoperating gains (expenses). As a result of this election and in accordance with accounting guidance for derivative instruments, losses of $81,600 which were previously recognized as a change in unrestricted net assets were reclassed to nonoperating gains (expenses) in the consolidated statement of operations.

Previously, for swap contracts designated as cash flow hedges, the change in fair value of the effective portion of the hedge was reflected as a change in unrestricted net assets and the ineffective portion of the hedge was reflected as a component of nonoperating gains (expenses) in the consolidated statements of operations. For nonhedging swap contracts, the change in fair value was recorded as a component of nonoperating gains (expenses) in the consolidated statements of operations.

The fair value of swap contracts is as follows:

	September 30, 2014	September 30, 2013
Balance sheet location		
Swap contracts designated as hedging instruments		
Interest rate swaps liability	$ -	$ 99,868
Swap contracts not designated as hedging instruments		
Interest rate swaps liability	295,656	132,137
	$ 295,656	$ 232,005

(dollars in thousands)

The effects of swap contracts on the consolidated statements of operations are as follows:

	Amount of Gain (Loss) Recognized in Changes in Unrestricted Net Assets Years Ended September 30,		Amount of Gain (Loss) Recognized in Excess of Revenues Over Expenses Years Ended September 30,	
	2014	**2013**	**2014**	**2013**
Statement of operations location				
Swap contracts designated as hedging instruments				
Change in fair value of hedging interest rate swaps	$ 44,806	$ 116,995	$ -	$ -
Amortization of swaption premiums	-	-	1,112	1,386
Hedge ineffectiveness	-	-	771	5,539
Swap contracts not designated as hedging instruments				
Change in fair value of nonhedging interest rate swaps	-	-	(110,340)	42,415
Amortization of net asset balance upon hedge de-designation	818	818	(818)	(818)
	$ 45,624	$ 117,813	$ (109,275)	$ 48,522

Partners HealthCare's swap contracts contain provisions that require collateral to be posted if the fair value of the swap exceeds certain thresholds. The collateral thresholds reflect the current credit ratings issued by major credit rating agencies on Partners HealthCare's and the counterparty's debt. Declines in Partners HealthCare's or the counterparty's credit ratings would result in lower collateral thresholds and, consequently, the potential for additional collateral postings by Partners HealthCare or the counterparty. As of September 30, 2014 and 2013, Partners HealthCare had posted collateral of $58,944 and $22,663, respectively. Partners HealthCare has established procedures to ensure that liquidity and securities are available to meet collateral posting requirements.

Upon the occurrence of certain events of default or termination events identified in the swap contracts, either Partners HealthCare or the counterparty could terminate the contracts in accordance with their terms. Termination results in the payment of a termination amount by one party that attempts to compensate the other party for its economic losses. If interest rates at the time of termination are lower than those specified in the swap contract, Partners HealthCare would make a payment to the counterparty. Conversely, if interest rates at such time are higher, the counterparty would make a payment to Partners HealthCare.

Derivatives - Other

Partners HealthCare also enters into options and futures primarily as hedges on securities and indices primarily related to foreign currency. Forward contracts are used as currency hedges. These agreements are limited in use and generally do not exceed one year and are included in separately invested investments.

(dollars in thousands)

12. Commitments

Leases

Partners HealthCare has capital and noncancelable operating leases for certain buildings and equipment. Minimum future lease commitments under noncancelable leases for the next five years and thereafter are as follows:

	Capital Leases	Operating Leases
2015	$ 1,149	$ 197,393
2016	437	217,268
2017	437	150,630
2018	359	126,961
2019	-	86,867
Thereafter	-	462,325
Total lease payments	2,382	$ 1,241,444
Less: Amount representing interest	153	
Capital lease obligations at September 30, 2014	$ 2,229	

Rental expense under operating leases approximated $190,827 in 2014 and $177,554 in 2013.

Construction Projects

BWH is constructing a building (the Brigham Building for the Future or BBF) and a parking garage (the Brigham Patient Parking project or BPP). The BBF will expand research and clinical space on the BWH campus, with a focus on the Neuroscience and Musculoskeletal programs, and increase flexibility for future campus redevelopment while allowing for lease consolidation. The associated land is leased to BWH by the Commonwealth through 2105. Phase 1 of the project, which involved the construction of two smaller facilities to be used by the Commonwealth, was completed in 2012. Phase 2 of the project, which involves the site preparation and construction of BBF, is ongoing. As of September 30, 2014, accumulated costs incurred related to the BBF approximated $91,652 with approximately $90,178 in outstanding construction contracts. Phase 2 costs are expected to be approximately $499,000, with occupancy scheduled for late 2016.

BPP locates a 400 space parking facility under BWH's 15 Francis Street entrance. BPP mitigates a parking shortage on campus and also satisfies commitments to the community and regulators. BPP includes a "greening" landscaped park over the garage as required by the City of Boston. BPP's total project cost is expected to be approximately $63,500. As of September 30, 2014 the project had accumulated costs of approximately $50,552 and outstanding construction contracts of approximately $6,450. The garage opened in October 2014.

Partners HealthCare is constructing a building and parking garage as part of the mixed-use development project at Assembly Row in Somerville, MA. This building will primarily be administrative space and allow for consolidation of multiple locations into a single cost- effective location. As of September 30, 2014, accumulated costs incurred related to the new administrative project are approximately $8,300 with approximately $15,500 in outstanding commitments. The total cost of the project is expected to be approximately $467,000.

(dollars in thousands)

13. Pension and Postretirement Healthcare Benefit Plans

Substantially all employees of Partners HealthCare are covered under various noncontributory defined benefit pension plans and various defined contribution pension plans. In addition, certain affiliates provide subsidized healthcare benefits for retired employees on a self-insured basis, with the benefit obligation being partially funded. These retiree healthcare benefits are administered through an insurance company and are accounted for on the accrual basis, which includes an estimate of future payments for claims incurred.

Total expense for these plans consists of the following:

	Years Ended September 30, 2014	Years Ended September 30, 2013
Defined benefit plans	$ 181,748	$ 275,096
Defined contribution plans	144,747	139,973
Postretirement healthcare benefit plans	7,029	9,683
	$ 333,524	$ 424,752

Information regarding benefit obligations, plan assets, funded status, expected cash flows and net periodic benefit cost follows within this footnote.

Benefit Obligations

	Defined Benefit Pension Plans		Postretirement Healthcare Benefit Plans	
	2014	2013	2014	2013
Change in benefit obligations				
Benefit obligations at beginning of year	$ 4,260,555	$ 4,441,164	$ 138,329	$ 140,344
Service cost	221,631	245,002	5,373	6,293
Interest cost	221,702	191,652	5,777	5,036
Plan amendments	1,825	-	-	-
Actuarial (gain) loss	507,350	(610,840)	(15,438)	(15,268)
Benefits paid	(105,475)	(85,811)	(5,077)	(5,025)
Expenses paid	(5,672)	(4,019)	-	-
Employee contributions	201	52	7,538	6,949
Affiliation	-	83,355	-	-
Benefit obligations at end of year	$ 5,102,117	$ 4,260,555	$ 136,502	$ 138,329

The accumulated benefit obligation for all defined benefit pension plans at the end of 2014 and 2013 was $4,806,399 and $4,025,049, respectively.

(dollars in thousands)

	Defined Benefit Pension Plans		Postretirement Healthcare Benefit Plans	
	2014	2013	2014	2013
Weighted-average assumptions used to determine end of year benefit obligation				
Discount rate	4.40%	5.05%	3.05% - 4.40%	3.15% - 5.05%
Rate of compensation increase				
Professional staff	4.45%	4.45%	N/A	N/A
Other than professional staff	3.00% - 4.00%	3.00% - 4.00%	N/A	N/A
Healthcare cost trend rate for next year	N/A	N/A	7.00%	6.50%
Rate to which the cost trend rate is to decline	N/A	N/A	5.00%	5.00%
Year that rate reaches the ultimate trend rate	N/A	N/A	2020	2017

Assumed healthcare cost trend rates have a significant effect on the amounts reported for the healthcare plans. A one-percentage-point change in assumed healthcare cost trend rates would have the following effect:

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on postretirement benefit obligation	$ 940	$ (871)

Plan Assets

	Defined Benefit Pension Plans		Postretirement Healthcare Benefit Plans	
	2014	2013	2014	2013
Change in plan assets				
Fair value of plan assets at beginning of year	$ 3,925,818	$ 3,114,884	$ 56,761	$ 45,982
Actual return on plan assets	366,240	367,705	5,212	5,041
Employer contributions	184,454	474,857	4,004	3,814
Employee contributions	201	52	7,538	6,949
Benefits paid	(105,475)	(85,811)	(5,077)	(5,025)
Expenses paid	(5,672)	(4,019)	-	-
Affiliation	-	58,150	-	-
Fair value of plan assets at end of year	$ 4,365,566	$ 3,925,818	$ 68,438	$ 56,761

The assets of the defined benefit pension plans are aggregated in a single master trust (Master Trust) and managed as one asset pool. The investment objective for the Master Trust is to achieve the highest reasonable total return after considering (i) plan liabilities, (ii) funding status and projected cash flows, (iii) projected market returns, valuations and correlations for various asset classes and (iv) Partners HealthCare's ability and willingness to incur market risk.

Oversight of the management of Partners HealthCare's investable assets, including the Master Trust, is provided by the Investment Committee of the PHS Board of Directors. The Committee seeks to add incremental returns by manager selection and asset allocation (increasing/decreasing allocations within allowable ranges based on current and projected valuations). The Committee is supported by a professional staff, an outside investment consultant and a pension actuarial consultant.

(dollars in thousands)

Partners HealthCare utilizes a target allocation policy that balances projected returns, correlations and volatility of various asset classes within the overall risk tolerance. Asset allocations are managed based on relative valuations among and within asset classes and the perceived ability of managers to outperform passive benchmarks. Exposure by asset class is the sum of the net exposures reported by each manager. Asset allocation can and will deviate from target exposures and is regularly monitored for rebalancing opportunities.

The following table presents the capital allocations, reported exposures of the allocations and policy benchmarks by manager mandate within the Master Trust. Some managers, particularly real assets and less market sensitive managers, invest allocated capital among multiple policy benchmark asset classes.

	September 30, 2014			September 30, 2013		
	Dollars	Reported Exposures	Policy Benchmark	Dollars	Reported Exposures	Policy Benchmark
Global equity	$ 204,952	4 %	4 %	$ 177,304	4 %	3 %
Traditional U.S. equity	610,856	14	13	549,170	14	12
Traditional foreign developed equity	601,744	14	13	500,323	13	12
Traditional emerging markets equity	571,868	13	13	494,358	13	12
Private equity	329,329	8	8	240,657	6	8
Real assets	334,631	8	8	343,265	9	9
Less market sensitive managers	1,404,996	32	31	1,271,823	32	33
Fixed income managers	307,190	7	10	348,918	9	11
	$ 4,365,566	100 %	100 %	$ 3,925,818	100 %	100 %

Inflation defensive strategies include investments in real estate assets, commodities, timber and inflation protection bonds. Other exposures include currency and volatility based strategies.

Within the Master Trust, assets are allocated to managers with investment mandates that may range from a single sub-asset class to very broad mandates; with restrictions that range from long-only to unconstrained; and with management structures ranging from separately managed funds to mutual/commingled funds to private partnerships. Less market sensitive managers employ absolute return, long/short equity and diversified strategies, which in the aggregate are expected to generate positive returns on a consistent basis. Investment risks (concentration, correlation, valuation, liquidity, leverage, mandate compliance, etc.) are measured at the manager level as well as the pool level.

The postretirement healthcare benefit plans assets are commingled funds, with the objective of achieving returns to satisfy plan obligations and with a level of volatility commensurate with Partners HealthCare's overall financial profile.

(dollars in thousands)

The following table presents plan assets, by form of ownership, as of September 30, 2014 and 2013 measured at fair value on a recurring basis using the fair value hierarchy defined in Note 6:

	Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value at September 30, 2014
Defined benefit pension plans				
Invested cash equivalents	$ 2,169	$ -	$ -	$ 2,169
Separately managed investments	536,940	221,807	-	758,747
Mutual funds	419,479	-		419,479
Commingled funds	-	977,778	-	977,778
Private partnerships	-	1,170,043	1,037,350	2,207,393
	958,588	2,369,628	1,037,350	4,365,566
Postretirement healthcare benefit plans				
Commingled funds	671	60,892	6,875	68,438
Total plan assets	$ 959,259	$ 2,430,520	$ 1,044,225	$ 4,434,004

	Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value at September 30, 2013
Defined benefit pension plans				
Invested cash equivalents	$ 59,826	$ -	$ -	$ 59,826
Separately managed investments	452,654	216,796	-	669,450
Mutual funds	472,768	-	-	472,768
Commingled funds	-	863,109	-	863,109
Private partnerships	-	996,926	863,739	1,860,665
	985,248	2,076,831	863,739	3,925,818
Postretirement healthcare benefit plans				
Commingled funds	2,200	49,057	5,504	56,761
Total plan assets	$ 987,448	$ 2,125,888	$ 869,243	$ 3,982,579

In evaluating the Level at which Partners HealthCare's private partnerships have been classified within the fair value hierarchy, management has assessed factors including, but not limited to price transparency, the ability to redeem these investments at net asset value at the measurement date, and the existence or absence of certain restrictions at the measurement date. Investments in private partnerships generally have limited redemption options for investors and, subsequent to final closing, may or may not permit subscriptions by new or existing investors. These entities may also have the ability to impose gates, lockups and other restrictions on an investor's ability to readily redeem out of their investment interest in the fund. As of September 30, 2014 and 2013, certain private partnerships where Partners HealthCare has the ability and the right to redeem interests within the next twelve months have been classified as Level 2 investments in the plan assets fair value table.

(dollars in thousands)

During the years ended September 30, 2014 and 2013, the change in the fair value of the plan assets measured using significant unobservable inputs (Level 3) is comprised of the following:

	2014	2013
Balances at beginning of year	$ 869,243	$ 757,553
Total gains		
Dividends and interest income	6,552	3,787
Realized gains on investments	52,729	60,893
Change in net unrealized appreciation on investments	74,883	27,932
Purchases	116,560	53,630
Sales	(28,779)	(34,552)
Transfers out of Level 3	(46,963)	-
Balances at end of year	$ 1,044,225	$ 869,243

The net unrealized gain on Level 3 investments held as of September 30, 2014 was $307,803.

Funded Status

The funded status of the plans recognized in the balance sheet and the amounts recognized in unrestricted net assets follows:

	Defined Benefit Pension Plans		Postretirement Healthcare Benefit Plans	
	2014	2013	2014	2013
End of year				
Fair value of plan assets at measurement date	$ 4,365,566	$ 3,925,818	$ 68,438	$ 56,761
Benefit obligations at measurement date	(5,102,117)	(4,260,555)	(136,502)	(138,329)
Funded status	$ (736,551)	$ (334,737)	$ (68,064)	$ (81,568)
Amounts recognized in the balance sheet consist of				
Noncurrent assets	$ -	$ -	$ 348	$ 1,001
Current liabilities	(4,272)	(2,493)	(3,299)	(3,477)
Long-term liabilities	(732,279)	(332,244)	(65,113)	(79,092)
	$ (736,551)	$ (334,737)	$ (68,064)	$ (81,568)
Amounts not yet recognized in net periodic benefit cost and included in unrestricted net assets consist of				
Actuarial net loss (gain)	$ 1,227,732	$ 822,034	$ (4,551)	$ 11,816
Prior service cost (credit)	9,360	11,007	-	(20)
	$ 1,237,092	$ 833,041	$ (4,551)	$ 11,796
Amounts recognized in unrestricted net assets consist of				
Current year actuarial (gain) loss	$ 449,880	$ (707,747)	$ (16,404)	$ (16,875)
Amortization of actuarial gain (loss)	(44,183)	(107,057)	33	(1,810)
Current year prior service cost (credit)	1,354	-	-	-
Amortization of prior service (cost) credit	(3,002)	(2,183)	20	21
	$ 404,049	$ (816,987)	$ (16,351)	$ (18,664)

(dollars in thousands)

At the end of 2014 and 2013, the projected benefit obligation, accumulated benefit obligation and fair value of plan assets for pension plans with an accumulated benefit obligation in excess of plan assets were as follows:

	2014	2013
Accumulated benefit obligation in excess of plan assets		
Projected benefit obligation	$ 5,102,117	$ 3,042,196
Accumulated benefit obligation	4,806,399	2,943,202
Fair value of plan assets	4,365,566	2,791,146

Expected Cash Flows

Information about the expected cash flows for the defined benefit and postretirement healthcare benefit plans is as follows:

	Defined Benefit Pension Plans	Postretirement Healthcare Benefit Plans	
Expected employer contributions			
2015	$ 238,971	$ 6,760	
			Medicare Subsidy
Expected benefit payments (receipts)			
2015	$ 198,229	$ 7,021	$ (261)
2016	219,615	7,619	(244)
2017	240,124	8,239	(227)
2018	255,582	8,865	(210)
2019	271,748	9,494	(192)
2020–2024	1,638,827	33,032	(684)

Net Periodic Benefit Cost

	Defined Benefit Pension Plans		Postretirement Healthcare Benefit Plans	
	2014	2013	2014	2013
Service cost	$ 221,631	$ 245,002	$ 5,373	$ 6,293
Interest cost	221,702	191,652	5,777	5,036
Expected return on plan assets	(308,770)	(270,798)	(4,247)	(3,435)
Amortization of				
Prior service cost (credit)	3,002	2,183	(20)	(21)
Actuarial net (gain) loss	44,183	107,057	146	1,810
Net periodic benefit cost	$ 181,748	$ 275,096	$ 7,029	$ 9,683

(dollars in thousands)

Amounts expected to be amortized from unrestricted net assets into net periodic benefit cost during the year ending September 30, 2015 are as follows:

	Defined Benefit Pension Plans	Postretirement Healthcare Benefit Plans
Actuarial net loss (gain)	$ 75,985	$ (533)
Prior service cost (credit)	3,071	-

	Defined Benefit Pension Plans		Postretirement Healthcare Benefit Plans	
	2014	2013	2014	2013
Weighted-average assumptions used to determine net periodic pension and postretirement cost				
Discount rate	5.05 %	3.70 % - 4.15 %	3.15 % - 5.05 %	2.65 % - 4.15 %
Expected return on plan assets	8.00%	7.75 % - 8.00 %	7.50 %	7.50 %
Rate of compensation increase				
Professional staff	4.45 %	4.45 %	N/A	N/A
Other than professional staff	3.00 % - 4.00 %	3.00 % - 4.00 %	N/A	N/A
Healthcare cost trend rate for this year	N/A	N/A	6.50 %	7.00 %
Rate to which the cost trend rate is to decline	N/A	N/A	5.00 %	5.00 %
Year that rate reaches the ultimate trend rate	N/A	N/A	2017	2017

Partners HealthCare uses a long-term return assumption which is validated annually by obtaining long-term asset return, volatility and correlation projections for relevant asset class indexes; modifying volatility and correlations to reflect the actual historical experience of the active managers; calculating the expected return using benchmark weights and indexes; and comparing the return assumption to the sum of the expected return and the historical outperformance of the actual return versus the benchmark. Partners HealthCare regularly monitors the active risk of the Master Trust by a statistical regression of the return series of the actual portfolio to that of the policy benchmark.

Assumed healthcare cost trend rates have a significant effect on the amounts reported for the healthcare plans. A one-percentage-point change in assumed healthcare cost trend rates would have the following effect:

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on service and interest cost	$ 48	$ (44)

(dollars in thousands)

14. Professional Liability Insurance

Partners HealthCare insures substantially all of its professional and general liability risk on a claims-made basis in cooperation with other healthcare organizations in the Greater Boston area through a captive insurance company, Controlled Risk Insurance Company Ltd. (CRICO). PHS owns 10% of CRICO. The investment is accounted for on the cost basis of accounting. The policies cover claims made during their respective terms, but not those occurrences for which claims may be made after expiration of the policy, except for certain tail liabilities which CRICO has assumed on an occurrence basis through December 31, 2014. Management intends to renew its coverage on a claims-made basis and has no reason to believe that it will be prevented from such renewal.

Partners HealthCare follows the accounting policy of establishing reserves to cover the ultimate costs of medical malpractice claims, which include costs associated with litigating or settling claims. The liability also includes an estimated tail liability, established to cover all malpractice claims incurred but not reported to the insurance company as of the end of the year. The total malpractice liability of $455,463 and $443,688 as of September 30, 2014 and 2013, respectively, is presented as an accrued professional liability in the consolidated balance sheets. These reserves have been recorded on a discounted basis using an interest rate of 3.25% and 3.50% as of September 30, 2014 and 2013, respectively.

Partners HealthCare also recognizes an insurance receivable from CRICO, at the same time that it recognizes the liability, measured on the same basis as the liability, subject to the need for a valuation allowance for uncollectible amounts. The insurance receivable of $370,311 and $355,332 as of September 30, 2014 and 2013, respectively, is reported as a component of other assets in the consolidated balance sheets.

Management is not aware of any claims against Partners HealthCare or factors affecting CRICO that would cause the expense for professional liability risks to vary materially from the amount provided.

15. Concentration of Credit Risk

Financial instruments that potentially subject Partners HealthCare to concentration of credit risk consist of patient accounts receivable, research grants receivable, pledges receivable, certain investments and interest rate swaps.

Partners HealthCare receives a significant portion of its payments for services rendered from a limited number of government and commercial third-party payers, including Medicare, Medicaid, Blue Cross and Blue Shield of Massachusetts, Harvard Pilgrim Health Care and Tufts Health Plan. Research funding is provided through many government and private sponsors. NHP receives a significant portion of its premium revenue from the Commonwealth. Pledges receivable are due from multiple donors. Partners HealthCare assesses the credit risk for pledges based on history and the financial wherewithal of donors, most of which are individuals or organizations well known to Partners HealthCare.

(dollars in thousands)

Investments, which include government and agency securities, stocks and corporate bonds, and private partnerships and other investments are not concentrated in any corporation or industry or with any single counterparty. Alternative investments are less liquid than Partners HealthCare's other investments. The reported values of the alternative investments may differ significantly from the values that would have been used had a ready market for those securities existed. These instruments may contain elements of both credit and market risk. Such risks include, but are not limited to, limited liquidity, absence of oversight, dependence upon key individuals, emphasis on speculative investments and nondisclosure of portfolio composition.

Partners HealthCare minimizes the credit risk it is exposed to under interest rate swap agreements by utilizing several counterparties and requiring the counterparties to post collateral for the benefit of Partners HealthCare when the fair value of the swap is positive. Partners HealthCare minimizes its counterparty risk by contracting with six counterparties, none of which accounts for more than 30% of the aggregate notional amount of the swap contracts.

16. Net Assets

Restricted net assets are available for the following purposes:

	September 30, 2014	2013
Temporarily restricted		
Charity care	$ 98,170	$ 99,808
Buildings and equipment	102,109	97,826
Clinical care, research and academic	655,675	595,135
	$ 855,954	$ 792,769
Permanently restricted		
Charity care	$ 19,763	$ 19,664
Buildings and equipment	2,433	2,433
Clinical care, research and academic	441,578	390,112
	$ 463,774	$ 412,209

Endowment

Partners HealthCare's endowment consists of over 1,000 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the boards to function as endowment.

Partners HealthCare has interpreted UPMIFA as requiring the preservation of the value of the original gift of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Partners HealthCare classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts donated to the permanent endowment, and (c) 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 that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Partners HealthCare

(dollars in thousands)

in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, Partners HealthCare considers several factors in making a determination to appropriate or accumulate donor-restricted endowment funds. These factors include: the duration and preservation of the fund; the purposes of the organization and the donor-restricted endowment fund; general economic conditions; the possible effect of inflation and deflation; the expected total return from income and the appreciation of investments; other resources of the organization; and the investment policies of the organization.

Endowment Funds With Deficits

From time to time, the value of assets associated with individual donor-restricted endowment funds may fall below the value of the initial and subsequent donor gift amounts. When such endowment deficits exist, they are classified as a reduction to unrestricted net assets. Deficits of this nature reported in unrestricted net assets were $247 and $338 as of September 30, 2014 and 2013, respectively. These deficits resulted from unfavorable market fluctuations that occurred after the investment of new permanently restricted contributions or subsequent endowment additions.

The following presents the endowment net asset composition by type of fund as of September 30, 2014 and 2013 and the changes in endowment assets for the years ended September 30, 2014 and 2013:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net asset composition by type of fund as of September 30, 2014				
Donor-restricted endowment funds	$ (247)	$ 498,238	$ 447,607	$ 945,598
Board-designated endowment funds	942,366	-	-	942,366
Total funds	$ 942,119	$ 498,238	$ 447,607	$ 1,887,964

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Changes in endowment net assets				
Endowment net assets at September 30, 2013	$ 903,255	$ 468,273	$ 397,472	$ 1,769,000
Investment return				
Investment income	4,894	14,570	13	19,477
Net realized and unrealized appreciation (depreciation)	76,199	51,383	291	127,873
Total investment return	81,093	65,953	304	147,350
Contributions	8,509	5,566	49,877	63,952
Appropriation of endowment assets for expenditure	(39,258)	(41,234)	-	(80,492)
Other changes	(11,480)	(320)	(46)	(11,846)
Total changes	38,864	29,965	50,135	118,964
Endowment net assets at September 30, 2014	$ 942,119	$ 498,238	$ 447,607	$ 1,887,964

(dollars in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net asset composition by type of fund as of September 30, 2013				
Donor-restricted endowment funds	$ (338)	$ 468,273	$ 397,472	$ 865,407
Board-designated endowment funds	903,593	-	-	903,593
Total funds	$ 903,255	$ 468,273	$ 397,472	$ 1,769,000

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Changes in endowment net assets				
Endowment net assets at October 1, 2012	$ 853,737	$ 433,316	$ 359,985	$ 1,647,038
Investment return				
Investment income	4,067	4,799	2	8,868
Net realized and unrealized appreciation (depreciation)	83,141	66,920	280	150,341
Total investment return	87,208	71,719	282	159,209
Contributions	3,963	(202)	35,008	38,769
Appropriation of endowment assets for expenditure	(37,535)	(38,291)	-	(75,826)
Other changes	(4,118)	1,731	2,197	(190)
Total changes	49,518	34,957	37,487	121,962
Endowment net assets at September 30, 2013	$ 903,255	$ 468,273	$ 397,472	$ 1,769,000

Conditional Pledge

During 2009, the General signed an agreement (Ragon Agreement) with The Massachusetts Institute of Technology (MIT), The President and Fellows of Harvard College (Harvard) and The Phillip T. and Susan M. Ragon Foundation (Ragon Foundation) to establish the Phillip T. and Susan M. Ragon Institute (Ragon Institute) as a joint research center of the General, MIT and Harvard with the purpose of harnessing the potential of the immune response to combat and conquer human diseases, integrating biomedical research with emerging engineering technologies (with the main initial focus being the development of an AIDS vaccine) and educating and training scientists. The Ragon Foundation committed to provide funding for the Ragon Institute of $100,000 over ten years through the General (as the administrative home for the Ragon Institute), beginning retroactively on January 1, 2008. The Ragon Foundation has the ability to slow, suspend or eliminate funding based on restrictions described in the Ragon Agreement. Additionally, any funding not paid by December 31, 2017 would no longer be due by the Ragon Foundation. In February 2014, an amendment was signed that noted that the current agreement would be completed by December 2018 and that an additional $50,000 of funding would be committed by the Ragon Foundation over five years beginning in 2019. Due to the conditions within the Ragon Agreement, funding is recognized when received, with no pledge receivable recorded for the balance of the amended commitment.

(dollars in thousands)

Through September 30, 2014, total funding of $74,000 was received, with $10,000 received for the year ended September 30, 2014, and total net expenses of $60,496 were incurred, including $11,834 for the year ended September 30, 2014. As of September 30, 2014, unspent funding of $13,504 has been recorded as temporarily restricted net assets, to be released to unrestricted net assets after qualifying expenses have been incurred.

17. Functional Expenses

Total operating expenses by function are as follows:

	Years Ended September 30,	
	2014	**2013**
Healthcare services	$ 6,852,795	$ 6,577,800
Research and academic	1,578,693	1,594,449
Medical claims and related expenses	1,463,972	1,061,630
General and administrative	1,032,197	954,521
	$ 10,927,657	$ 10,188,400

18. Contingencies

Partners HealthCare is subject to complaints, claims and litigation which have risen in the normal course of business. In addition, Partners HealthCare is subject to reviews and investigations by various federal and state government agencies to assure compliance with applicable laws, some of which are subject to different interpretations. Governmental review of compliance by healthcare institutions, including Partners HealthCare, has increased.

19. Subsequent Events

Partners HealthCare has assessed the impact of subsequent events through December 12, 2014, the date the audited financial statements were issued. During this period, there were no subsequent events that require adjustment to the audited financial statements.