Stanford Health Care

Consolidated Financial Statements
August 31, 2015 and 2014

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Independent Auditor's Report

To the Board of Directors
Stanford Health Care

We have audited the accompanying consolidated financial statements of Stanford Health Care ("SHC"), which comprise the consolidated balance sheets as of August 31, 2015 and August 31, 2014, and the related consolidated statements of operations and changes in net assets and 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 SHC'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 SHC'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 Stanford Health Care at August 31, 2015 and August 31, 2014, and the results of their operations and 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 9, 2015

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Stanford Health Care
Consolidated Balance Sheets
August 31, 2015 and 2014
(in thousands of dollars)

	2015	2014
Assets		
Current assets:		
Cash and cash equivalents	$ 475,677	$ 467,655
Short term investments	101,677	100,970
Patient accounts receivable, net of allowance for doubtful accounts of $145,000 and $115,000 at August 31, 2015 and 2014, respectively	550,721	431,897
Other receivables	75,427	28,416
Inventories	42,935	25,374
Prepaid expenses and other	35,486	28,283
Total current assets	1,281,923	1,082,595
Investments	127,860	120,866
Investments in University managed pools	1,440,352	1,383,385
Assets limited as to use, held by trustee, net of current portion	580,701	491,594
Property and equipment, net	1,923,465	1,405,862
Other assets	163,578	263,766
Total assets	$ 5,517,879	$ 4,748,068
Liabilities and Net Assets		
Current liabilities:		
Accounts payable and accrued liabilities	$ 282,134	$ 173,160
Accrued salaries and related benefits	202,859	161,494
Due to related parties	43,324	62,106
Third-party payor settlements	9,018	22,334
Current portion of long-term debt	13,932	11,700
Debt subject to short-term remarketing arrangements	228,200	228,200
Self-insurance reserves and other	34,918	27,296
Total current liabilities	814,385	686,290
Self-insurance reserves and other, net of current portion	120,364	105,270
Other long-term liabilities	234,855	170,565
Pension liability	51,220	30,827
Long-term debt, net of current portion	1,237,347	1,067,799
Total liabilities	2,458,171	2,060,751
Net assets:		
Unrestricted:		
Stanford Health Care	2,467,393	2,137,389
Noncontrolling interests	22,979	23,304
Total unrestricted	2,490,372	2,160,693
Temporarily restricted	561,642	518,932
Permanently restricted	7,694	7,692
Total net assets	3,059,708	2,687,317
Total liabilities and net assets	$ 5,517,879	$ 4,748,068

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

Stanford Health Care
Consolidated Statements of Operations and Changes in Net Assets
Years Ended August 31, 2015 and 2014
(in thousands of dollars)

	2015	2014
Operating revenues:		
Net patient service revenue	$ 3,525,014	$ 2,980,067
Provision for doubtful accounts	(131,601)	(140,678)
Net patient service revenue less provision for doubtful accounts	3,393,413	2,839,389
Premium revenue	62,893	60,047
Other revenue	98,718	94,248
Net assets released from restrictions used for operations	15,663	4,639
Total operating revenues	3,570,687	2,998,323
Operating expenses:		
Salaries and benefits	1,428,100	1,232,251
Professional services	47,801	37,046
Supplies	484,036	421,899
Purchased services	912,886	741,565
Depreciation and amortization	109,735	100,625
Interest	40,485	43,636
Other	359,368	226,475
Expense recoveries from related parties	(93,640)	(83,422)
Total operating expenses	3,288,771	2,720,075
Income from operations	281,916	278,248
Interest and investment income	15,680	15,199
Increase in value of University managed pools	54,309	176,014
Interest rate swaps mark to market adjustments	(59,392)	(37,532)
Loss on extinguishment of debt and swaps	(35)	(71)
Contribution income from ValleyCare Health System affiliation	96,758	-
Excess of revenues over expenses	389,236	431,858
Other changes in unrestricted net assets:		
Transfer to Stanford University, net	(66,477)	(54,337)
Transfer from Lucile Salter Packard Children's Hospital	26,600	-
Change in net unrealized gains on investments	(2,445)	691
Net assets released from restrictions used for:		
Purchase of property and equipment	2,288	356
Change in pension and postretirement liability	(19,461)	6,650
Noncontrolling capital distribution, net	(62)	(1,482)
Increase in unrestricted net assets	329,679	383,736
Changes in temporarily restricted net assets:		
Transfer from Stanford University	4,062	2,480
Contributions and other	52,333	48,108
Contribution income from ValleyCare Health System affiliation	62	-
Investment income (loss)	1,667	(103)
Gains on University managed pools	2,537	2,875
Net assets released from restrictions for:		
Operations	(15,663)	(4,639)
Purchase of property and equipment	(2,288)	(356)
Increase in temporarily restricted net assets	42,710	48,365
Changes in permanently restricted net assets:		
Contributions	2	101
Increase in permanently restricted net assets	2	101
Increase in net assets	372,391	432,202
Net assets, beginning of year	2,687,317	2,255,115
Net assets, end of year	$ 3,059,708	$ 2,687,317

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

Stanford Health Care
Consolidated Statements of Cash Flows
Years Ended August 31, 2015 and 2014
(in thousands of dollars)

	2015	2014
Cash flows from operating activities:		
Increase in Stanford Health Care net assets	$ 372,716	$ 428,351
(Decrease) increase in noncontrolling interests	(325)	3,851
Total increase in net assets	372,391	432,202
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Contribution income from ValleyCare Health System affiliation	(96,820)	-
Loss on extinguishment of debt and swaps	35	71
Depreciation and amortization	107,809	98,634
Provision for doubtful accounts	131,601	140,678
Change in fair value of interest rate swaps	59,392	37,532
Increase in value of University managed pools	(54,309)	(176,014)
Unrealized losses (gains) on investments	1,460	(1,632)
Realized gains on investments	(9)	(10)
Contributions received for long lived assets or endowment and net equity transfers to/from related parties	(4,199)	23,156
Premiums received from bond issuance	5,627	-
Changes in operating assets and liabilities:		
Patient accounts receivable	(211,957)	(193,659)
Due to related parties	15,615	(6,059)
Other receivables, inventory, other assets, prepaid expenses and other	(56,749)	9,201
Accounts payable, accrued liabilities and pension liabilities	63,376	(38,073)
Accrued salaries and related benefits	19,211	25,653
Third-party payor settlements	(13,877)	8,819
Self-insurance reserves	12,769	6,030
Cash provided by operating activities	351,366	366,529
Cash flows from investing activities:		
Purchases of investments	(182,526)	(148,902)
Sales of investments	172,389	102,784
Purchases of investments in University managed pools	(25,781)	(1,473)
Sales of investments in University managed pools	24,108	1,676
(Increase) decrease in assets limited as to use and other	(74,101)	39,850
Cash acquired from ValleyCare, net of cash paid as consideration	(52,539)	-
Purchases of property and equipment	(447,635)	(352,747)
Cash used in investing activities	(586,085)	(358,812)
Cash flows from financing activities:		
Proceeds from issuance of debt	244,111	-
Costs of issuance of debt	(1,571)	-
Payment of long-term debt and capital lease obligations	(81,154)	(12,710)
Contributions received for long lived assets or endowment and net equity transfers to/from related parties	81,355	23,817
Cash provided by financing activities	242,741	11,107
Net increase in cash and cash equivalents	8,022	18,824
Cash and cash equivalents, beginning of year	467,655	448,831
Cash and cash equivalents, end of year	$ 475,677	$ 467,655
Supplemental disclosures of cash flow information:		
Interest paid	$ 42,481	$ 46,227
Supplemental disclosures of non cash information:		
Donated securities	$ -	$ 24,739
Payables for property and equipment	43,861	9,905
Equity transfers from (to) related parties, net	16,969	(19,021)

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

1. Organization

In October 2014, Stanford Hospital and Clinics was renamed as Stanford Health Care ("SHC") to reflect the range and focus of our organization and our commitment to healing humanity through science and compassion, one patient at a time. SHC operates a licensed acute care hospital ("Stanford Hospital") and a cancer center in Palo Alto, California, along with numerous outpatient physician clinics in the San Francisco Bay Area, in community settings, and in association with regional hospitals. Stanford Hospital is a principal teaching affiliate of the Stanford University School of Medicine ("SoM") and provides primary and specialty health services to adults, including cardiac care, cancer treatment, solid organ transplantation services, neurosciences, and orthopedics services designated by management as SHC's "Strategic Clinical Services". SHC, together with Lucile Salter Packard Children's Hospital at Stanford ("LPCH"), operates the clinical settings through which the SoM educates medical and graduate students, trains residents and clinical fellows, supports faculty and community clinicians and conducts medical and biological sciences research.

The Board of Trustees of Leland Stanford Junior University (the "University") is the sole corporate member of SHC and LPCH. As part of their ongoing operations, SHC and LPCH engage in certain related party transactions as described further in Note 15.

The consolidated financial statements include SHC's interest in University HealthCare Alliance ("UHA"), The Hospital Committee for the Livermore-Pleasanton Areas (dba ValleyCare Health System) ("VCHS"), Stanford Blood Center, LLC ("SBC LLC"), Stanford Emanuel Radiation Oncology Center, LLC ("SEROC"), CareCounsel, LLC ("CareCounsel"), SUMIT Holding International, LLC ("SHI"), Professional Exchange Assurance Company ("PEAC") and Stanford Health Care Advantage ("SHC Advantage") (collectively "SHC").

UHA, a physician medical foundation, supports Stanford University Medical Center's mission of delivering quality care to the community and conducting research and education. In addition, UHA leads the development of a high quality clinical delivery network, built on collaboration with and sponsorship of community hospitals, on behalf of the SoM, SHC, and UHA physicians. The SoM and SHC are the members of UHA, and appoint directors to the governing board. The UHA bylaws afford control to SHC. Effective January 1, 2011, SHC entered into a sponsorship agreement with UHA whereby SHC agreed to certain funding for the development and operation of UHA and continued additional funding for future or alternative clinical sites of UHA. Additional funding by SHC to UHA for operations and capital was $37,342 and $33,715 for the years ended August 31, 2015 and 2014, respectively.

VCHS, a leading community hospital system located in the East Bay's Tri-Valley region of Pleasanton, Livermore and Dublin, completed an affiliation agreement with SHC effective May 18, 2015. SHC is the sole corporate member of VCHS (see Note 3).

SBC LLC is a limited liability company organized effective July 31, 2015. SBC LLC will serve as a community blood center and provide blood products and testing services to hospitals, clinics, companies and other clients. SHC is the sole member of SBC LLC. On September 30, 2015, SBC LLC completed the acquisition of the Stanford Blood Center from the University for $36,000. SBC LLC paid consideration in excess of assets acquired in the amount of $31,101, which will be recorded in Transfer to Stanford University in the consolidated statements of operations and changes in net assets for the year ending August 31, 2016.

1. Organization (Continued)

SEROC was originally formed as a joint venture between SHC and Emanuel Medical Center ("EMC"). On July 31, 2014, EMC transferred its membership interest to Doctors Medical Center of Modesto, Inc. ("DMC"). SEROC operates an outpatient clinic that provides radiation oncology services to patients in Turlock, California and surrounding communities. SHC's interest in SEROC was 60% for the years ended August 31, 2015 and 2014. The remaining interest of 40% is recorded as a noncontrolling interest in unrestricted net assets on the consolidated balance sheets as of August 31, 2015 and 2014.

CareCounsel, a leading provider of employer-sponsored health advocacy and health care assistance services, was acquired by SHC effective July 18, 2012. The Bay Area company was founded in 1996 with a mission to help employees, retirees and their families navigate the complex health care environment through an employer-sponsored benefit that provides consumer education, advocacy and access to expert health care resources and information.

SHI is the sole owner of SUMIT Insurance Company Ltd. ("SUMIT") and Stanford University Medical Network Risk Authority, LLC ("SRA"). SHC and LPCH are the owners of SHI.

SHC's share of net assets in SUMIT, a captive insurance carrier, was 75.3% and 73.2% for the years ended August 31, 2015 and 2014, respectively. LPCH's share of net assets in SUMIT was 24.7% and 26.8% for the years ended August 31, 2015 and 2014, respectively, and is recorded as a noncontrolling interest in unrestricted net assets on the consolidated balance sheets.

SRA was formed on September 19, 2012 and began operations on December 1, 2012. SRA provides risk management services to SHI, the owners of SHI and other affiliated and unaffiliated parties and serves as attorney-in-fact to PEAC. SHC's share of net assets in SRA was 82% for the years ended August 31, 2015 and 2014. The remaining interest of 18% is recorded as a noncontrolling interest in unrestricted net assets on the consolidated balance sheets as of August 31, 2015 and 2014.

PEAC, a captive insurance carrier, provides insurance coverage to UHA, Packard Children's Health Alliance and other affiliated parties. SHC's share of net assets in PEAC was 70.2% and 74.7% for the years ended August 31, 2015 and 2014, respectively. The remaining interest of 29.8% and 25.3% for the years ended August 31, 2015 and 2014, respectively, is recorded as a noncontrolling interest in unrestricted net assets on the consolidated balance sheets.

SHC Advantage, a non-profit public benefit corporation, provides comprehensive healthcare coverage options to elderly and disabled eligible Medicare populations of Santa Clara County through their Medicare Advantage Plan and is solely controlled by SHC. This service is offered to Medicare-eligible residents of Santa Clara County effective January 1, 2015.

2. Summary of Significant Accounting Policies

Principles of Consolidation
The consolidated financial statements include the accounts of SHC and its subsidiaries, UHA, VCHS, SBC LLC, SEROC, CareCounsel, SHI, PEAC and SHC Advantage which are controlled and owned more than 50% by SHC. All significant inter-company accounts and transactions are eliminated in the consolidation.

2. Summary of Significant Accounting Policies (Continued)

Basis of Presentation
The accompanying consolidated financial statements are prepared on the accrual basis of accounting. Net assets of SHC and changes therein have been classified and are reported as follows:

- ***Unrestricted net assets*** — Unrestricted net assets represent those resources of SHC that are not subject to donor-imposed stipulations. The only limits on unrestricted net assets are broad limits resulting from the nature of SHC and the purposes specified in its articles of incorporation or bylaws and, limits resulting from contractual agreements, if any.

- ***Temporarily restricted net assets*** — Temporarily restricted net assets represent contributions, which are subject to donor-imposed restrictions that can be fulfilled by actions of SHC pursuant to those stipulations or by the passage of time.

- ***Permanently restricted net assets*** — Permanently restricted net assets represent contributions that are subject to donor-imposed restrictions that they be maintained permanently by SHC. Generally, the donors of these assets permit SHC to use all or part of the investment return on these assets.

Expenses are generally reported as decreases in unrestricted net assets. A restriction expires when the stipulated time period has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both. Temporarily restricted contributions are recorded as restricted revenue when received and when the restriction expires, the net assets are shown as released from restriction on the consolidated statements of operations and changes in net assets. Investment income on temporarily or permanently restricted assets that is restricted by donor or law is recorded within the respective net asset category, and when the restriction expires, the net assets are shown as released from restriction.

Cash and Cash Equivalents
Cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less. Cash equivalents consist primarily of demand deposits and money market mutual funds.

Assets Limited as to Use, Held by Trustee
Assets limited as to use include various accounts held by a trustee in accordance with indenture requirements. The indenture terms require that the trustee control the expenditure of bond proceeds for capital projects. Assets limited as to use consist of cash and cash equivalents and short-term investments, recorded at cost, which approximates fair value. There are no amounts required to fund current liabilities of SHC, therefore the entire amount has been classified as long-term in the consolidated balance sheets at August 31, 2015 and 2014.

Inventories
Inventories, which consist primarily of hospital operating supplies and pharmaceuticals, are stated at the lower of cost or market value determined using the first-in, first-out method.

Investments
Investments held directly by SHC consist of cash and cash equivalents and mutual funds and are stated at fair value. Fair value is determined in accordance with current accounting guidance as further described in Note 9. Investment earnings (including realized gains and losses on investments, interest, dividends and impairment loss on investment securities) are included in investment income unless the income or loss is restricted by donor or law. Income on investments of donor restricted funds is added to or deducted from the appropriate net asset category based on the donor's restriction. Unrestricted unrealized gains and losses on other than trading securities are separately reported below the excess of revenues over expenses.

2. Summary of Significant Accounting Policies (Continued)

Investments in University Managed Pools
Investments in University managed pools consist of funds invested in the University's Merged Pool ("MP") and Expendable Funds Pool ("EFP") (collectively the "Pools"). Under the terms of SHC's agreement with the University, the University has discretion to invest the funds in the Pools. SHC may deposit funds in the Pools at its discretion. Withdrawals from the MP and EFP require advance notice to the University. SHC accounts for its share of the Pools in accordance with current accounting guidance. The value of its share of the Pools is determined by the University and is based on the fair value of the underlying assets in the Pools.

The University allocates investment earnings to SHC from the University managed pools based on SHC's share of the Pools. Earnings include interest, dividends, distributions, investment gains and losses, and the increases or decreases in the value of SHC's share of the pools. In accordance with current accounting guidance, all investment gains and losses and increases and decreases in share value are treated as realized and included in the excess of revenues over expenses.

The increases or decreases in the value of SHC's share of the Pools are recorded as income and gains on University managed pools unless the income is restricted by donor or law. Income on investments of donor restricted funds invested in the University managed pools is added to or deducted from the appropriate net asset category based on the donor's restriction.

Property and Equipment
Property and equipment are stated at cost except for donated assets, which are recorded at fair market value at the date of donation. Depreciation and amortization of property and equipment is determined using the straight-line method over the estimated useful lives of the assets, which are as follows:

Land improvements	5 to 25 years
Buildings and improvements	5 to 40 years
Equipment	3 to 25 years

Significant replacements and improvements are capitalized, while maintenance and repairs, which do not improve or extend the life of the respective assets, are charged to expense as incurred. Upon sale or disposal of property and equipment, the cost and accumulated depreciation are removed from the respective accounts, and any gain or loss is included in the consolidated statements of operations and changes in net assets.

Equipment includes medical equipment, furniture and fixtures and computer software and hardware.

Equipment under capital leases is recorded at present value at the inception of the leases and is amortized on the straight-line method over the shorter of the lease term or the estimated useful life of the equipment. The amortization of the assets recorded under capital leases is included in depreciation and amortization expense in the accompanying consolidated statements of operations and changes in net assets.

Interest costs incurred on borrowed funds during the period of construction of capital assets is capitalized, net of any interest earned, as a component of the cost of acquiring those assets.

2. Summary of Significant Accounting Policies (Continued)

Asset Retirement Obligations
Asset retirement obligations ("ARO") are legal obligations associated with the retirement of long-lived assets. These liabilities are initially recorded at fair value as other long-term liabilities 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 accreted over the useful lives of the related assets. SHC recorded current period accretion expense of $358 and $367 in the consolidated statements of operations and changes in net assets for the years ended August 31, 2015 and 2014, respectively. ARO liability of $7,491 and $7,133 is included in other long-term liabilities on the consolidated balance sheets as of August 31, 2015 and 2014, respectively.

Other Assets
Other assets include deferred financing costs, long-term portion of contributions receivable, investments in Stanford PET-CT, LLC ("PET-CT"), intangible assets and other long-term assets.

Deferred financing costs represent costs incurred in conjunction with the issuance of SHC's long-term debt. These costs are amortized on a straight-line basis, which approximates the effective interest method, over the life of the debt.

PET-CT is a California limited liability company which provides radiological services to patients of the community, including patients served by SHC and physicians affiliated with the SoM. SHC and the University each appoint one-half of the members of the governing board of PET-CT and are its only members. SHC's interest in PET-CT was 50% for the years ended August 31, 2015 and 2014. As SHC has 50% ownership and does not have control, these investments are recorded using the equity method.

Contributions Receivable
Unconditional promises to give ("contributions") are recorded at fair value at the date the promise is received. Donations for specific purposes are reported as either temporarily or permanently restricted net assets. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved and applicable to the years in which the promises are received, and recorded in their respective net asset category. In accordance with current accounting guidance, the discount rates were determined using the risk free rate adjusted for the risk of donor default. Amortization of the discount is included in contributions and other in the consolidated statements of operations and changes in net assets. Conditional promises to give are recognized when the condition is substantially met.

Premiums and Discounts on Long-Term Debt
Premiums and discounts arising from the original issuance of long-term debt are amortized on either the effective interest method or the straight-line basis, which approximates the effective interest method, over the life of the debt. The unamortized portion of these premiums and discounts are included in long-term debt on the consolidated balance sheets.

Interest Rate Swap Agreements
SHC has entered into several interest rate swap agreements, also known as risk management or derivative instruments, to reduce the effect of interest rate fluctuation on its variable rate bonds. All swaps are recognized on the consolidated balance sheets at their fair value in accordance with current accounting guidance. Changes in the fair value of interest rate swaps are included in excess of revenues over expenses. The net cash payments or receipts under the interest rate swap agreements have been recorded as an increase (decrease) to interest expense.

2. Summary of Significant Accounting Policies (Continued)

Excess of Revenues over Expenses
The consolidated statements of operations include excess of revenues over expenses. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, include transfers of assets to and from affiliates for other than goods and services, change in unrealized gains and losses on marketable investments, contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets), changes in pension and postretirement liability and other changes related to noncontrolling interests.

Net Patient Service Revenue
Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers including Medicare and Medi-Cal, and others for services rendered, including estimated retroactive audit adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined. Contracts, laws and regulations governing the Medicare and Medi-Cal programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates may change by a material amount in the near term.

The provision for doubtful accounts is based upon management's assessment of expected net collections considering historical experience and other collection indicators. Throughout the year, management assesses the adequacy of the allowance for uncollectible accounts based upon historical write-off experience. The results of this review are then used to make any modifications to the provision for doubtful accounts to establish an appropriate allowance for uncollectible accounts.

Charity Care
SHC provides either full or partial charity care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Amounts determined to qualify as charity care are not reported as net patient service revenue. SHC also provides services to other indigent patients under Medi-Cal and other publicly sponsored programs, which reimburse at amounts less than the cost of the services provided to the recipients. The difference between the cost of services provided to these indigent persons and the expected reimbursement is included in the estimated cost of charity care.

Premium Revenue
UHA has capitated agreements with various health maintenance organizations ("HMOs") to provide medical services to enrollees. Under these agreements, monthly payments are received based on the number of health plan enrollees. These receipts are recorded as premium revenue in the consolidated statements of operations and changes in net assets. Costs are accrued when services are rendered under these contracts, including cost estimates of incurred but not reported ("IBNR") claims. The IBNR accrual (which is included in accounts payable and accrued liabilities in the consolidated balance sheets) includes an estimate of the costs of services for which UHA is responsible, including referrals to outside healthcare providers.

Income Taxes
SHC, UHA and VCHS are not-for-profit corporations and tax-exempt pursuant to Section 501(c)(3) of the Internal Revenue Code. SBC LLC, SEROC, CareCounsel and SHI are limited liability companies and taxable income flows through to the individual members. SUMIT is currently exempt from all taxes until March 31, 2035. SRA is a limited liability company, but has elected to be taxed as a corporation. PEAC is a taxable corporation. SHC and its subsidiaries have no uncertain tax positions pertaining to unrelated business income.

2. Summary of Significant Accounting Policies (Continued)

Self-Insurance Plans
SHC and VCHS self-insure for professional liability risks, postretirement medical benefits, workers' compensation and health and dental benefits. These liabilities are reflected as self-insurance reserves in the consolidated balance sheets.

- ***Professional Liability*** — SHC and VCHS are self-insured through SUMIT for medical malpractice and general liability losses under claims-made coverage. SHC also maintains professional liability reserves for claims not covered by SUMIT which totals $5,410. VCHS maintains professional liability reserves for claims not covered by SUMIT which totals $4,629. Since September 1, 2005, SUMIT has retained 100% of the risk related to the first $15,000 per occurrence. The next $165,000 is transferred to various reinsurance companies. Prior to September 1, 2005, SHC maintained various coverage limits.

- ***Postretirement Medical Benefits*** — Liabilities for post-retirement medical claims for current and retired employees are actuarially determined.

- ***Workers' Compensation*** — SHC purchases insurance for workers' compensation claims with a $750 deductible per occurrence. VCHS purchases insurance for workers' compensation claims with a $250 deductible per occurrence. Workers' compensation insurance provides statutory limits for the State of California. An actuarial estimate of retained losses (or losses retained within the deductible) has been used to record a liability.

- ***Health and Dental*** — Liabilities for health and dental claims for current employees are based on estimated costs.

Fair Value of Financial Instruments
Due to the short-term nature of cash and cash equivalents, accounts payable and accrued liabilities, and accrued salaries and related benefits, their carrying value approximates their fair value. The fair value of the amounts payable under third-party reimbursement contracts is not readily determinable. The fair value of long-term debt is estimated based on quoted market prices for the bonds or similar financial instruments.

Concentration of Credit Risk
Financial instruments, which potentially subject SHC to concentrations of credit risk, consist principally of cash and cash equivalents, patient accounts receivable, and investments in University managed pools.

SHC's concentration of credit risk relating to patient accounts receivable is limited by the diversity and number of patients and payers. Patient accounts receivable consist of amounts due from commercial insurance companies, governmental programs, private pay patients and other third-party payers.

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. The most significant estimates relate to patient accounts receivable allowances, amounts due to third party payers, retirement plan obligations, and self-insurance reserves. Actual results could differ from those estimates.

Reclassification
Certain reclassifications have been made to the 2014 consolidated financial statements to conform to the 2015 presentation. Such reclassifications had no effect on excess of revenues over expenses as previously reported.

2. Summary of Significant Accounting Policies (Continued)

Recent Pronouncements

The Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") is the sole source of authoritative non-governmental U.S. generally accepted accounting principles.

In May 2014, the FASB issued an update to the ASC to improve the consistency of revenue recognition practices across industries for economically similar transactions. The core principle is that an entity recognizes revenue for goods or services to customers in an amount that reflects the consideration it expects to receive in return. In August 2015, the FASB voted to defer the implementation of the new guidance. The new effective date is for annual periods beginning after December 15, 2017. SHC is currently evaluating the impact that this guidance will have on its consolidated financial statements.

In February 2015, the FASB issued an update to the ASC which focuses on the consolidation evaluation for reporting organizations that are required to evaluate whether they should consolidate certain legal entities. The number of consolidation models has been reduced from four to two, and the new guidance places more emphasis on risk of loss when determining a controlling financial interest. This guidance is effective for annual and interim periods beginning after December 15, 2015. SHC is currently evaluating the impact that this guidance will have on its consolidated financial statements.

In April 2015, the FASB issued an update to the ASC which requires debt issuance costs to be presented in the balance sheet as a direct deduction from the carrying value of the associated debt liability, and amortization of those costs reported as interest expense. This guidance is effective for annual and interim periods beginning after December 15, 2015, and early adoption is permitted. The new guidance should be applied on a retrospective basis for each period presented in the balance sheet. SHC is currently evaluating the impact that this guidance will have on its consolidated financial statements.

In April 2015, FASB issued an update to the ASC which allows employers with a fiscal year end that does not coincide with a calendar month end to make an accounting policy election to measure defined benefit plan assets and obligations as of the end of the month closest to their fiscal year end. This guidance is effective for annual and interim periods beginning after December 15, 2015. Prospective application is required, and early adoption is permitted. SHC does not believe adoption of this guidance will have a material impact on its consolidated financial statements.

In May 2015, the FASB issued an update to the ASC which removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient as well as limiting disclosure requirement to investments for which the entity has elected to measure the fair value using that practical expedient. The guidance is effective for fiscal years beginning after December 15, 2015. SHC is currently evaluating the impact that this guidance will have on its consolidated financial statements.

In July 2015, FASB issued an update to the ASC which require entities to compare inventory cost to its net realizable value. In situations where there is evidence that the net realizable value of inventory is less than its cost, an entity would recognize the difference as a loss in earnings in the period in which it occurred. This guidance is effective for annual and interim periods beginning after December 15, 2016. SHC is currently evaluating the impact that this guidance will have on its consolidated financial statements.

(in thousands of dollars)

2. Summary of Significant Accounting Policies (Continued)

Recent Pronouncements (continued)
In September 2015, the FASB issued an update to the ASC which requires that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. This update requires the acquirer record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. The guidance is effective for fiscal years beginning after December 15, 2015. SHC is currently evaluating the impact that this guidance will have on its consolidated financial statements.

3. Business Acquisitions

On September 23, 2014, SHC entered into an affiliation agreement with VCHS, which will advance leading edge and highly coordinated care in the Bay Area. Under this agreement, SHC was substituted as the sole corporate member of VCHS with the associated control of VCHS, including Valley Memorial Hospital ("VMH"), ValleyCare Medical Center ("VCMC"), ValleyCare Medical Foundation ("VCMF"), and ValleyCare Senior Housing, Inc. ("VCSH"). On May 18, 2015, with all conditions of the affiliation agreement satisfied and all regulatory approvals obtained, the affiliation between VCHS and SHC was consummated and became effective. VCHS, which owns VMH and VCMC, and which is the member of VCMF and VCSH, became a subsidiary of SHC.

On May 18, 2015, as part of the affiliation with VCHS, SHC acquired assets and assumed liabilities with estimated fair values as follows:

Cash and cash equivalents	$	29,550
Patient accounts receivable, net		38,468
Property and equipment, net		135,618
Other assets		29,573
Total fair value of acquired assets	$	233,209

Accounts payable and accrued liabilities	$	17,064
Accrued salaries and related benefits		18,691
Other liabilities		28,523
Total fair value of assumed liabilities	$	64,278

SHC also paid $3,000 to the ValleyCare Charitable Foundation. In addition, VCHS's outstanding 2007 Series A and 2009 Series Revenue Bonds were defeased to their respective redemption dates, June 15, 2017 and August 3, 2015, at a price equal to the principal of the defeased bonds and interest accrued to such date and the outstanding taxable 2007 Series B Revenue Bonds were redeemed at a price equal to 102% of the principal amount plus interest accrued to the redemption date for a total of $69,111.

The affiliation was accounted for as a business combination in accordance with the authoritative accounting guidance. The excess of net assets over consideration paid in the VCHS affiliation was $96,820 and is recorded in the consolidated statements of operations and changes in net assets. The operating results of VCHS for the period from May 18, 2015 to August 31, 2015 included operating revenue of $81,024 and excess of revenues over expenses of $4,291 recorded in the consolidated financial statements of SHC.

On June 1, 2015, UHA entered into a Professional Services Agreement with ValleyCare Physicians Associates, and VCMF ceased operations.

4. Net Patient Service Revenue

SHC has agreements with third-party payers that provide for payments at amounts different from SHC's established rates. A summary of payment arrangements with major third-party payers follows:

- ***Medicare*** — Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Medicare reimburses hospitals for covered outpatient services rendered to its beneficiaries by way of an outpatient prospective payment system based on ambulatory payment classifications. SHC's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review.

  Inpatient non-acute services, certain outpatient services and medical education costs related to Medicare beneficiaries are paid based, in part, on a cost reimbursement methodology. SHC is reimbursed for cost reimbursable items at a tentative rate with final settlement of such items determined after submission of annual cost reports and audits thereof by the Medicare fiscal intermediary. The estimated amounts due to or from the program are reviewed and adjusted annually based on the status of such audits and any subsequent appeals. Differences between final settlements and amounts accrued in previous years are reported as adjustments to net patient service revenue in the year examination is substantially completed. SHC's Medicare cost reports have been audited by the Medicare fiscal intermediary through August 31, 2006. Professional services are reimbursed based on a fee schedule.

- ***Medi-Cal*** — Inpatient services rendered to Medi-Cal program beneficiaries are reimbursed under a contract at a prospectively determined negotiated per diem rate. Outpatient services are reimbursed based upon prospectively determined fee schedules. Professional services are reimbursed based on a fee schedule.

- ***Managed Care Organizations*** — SHC has entered into agreements with numerous non-government third-party payers to provide patient care to beneficiaries under a variety of payment arrangements. These include arrangements with:

  - Commercial insurance companies, including workers' compensation plans, which reimburse SHC at negotiated charges.

  - Managed care contracts such as those with HMOs and PPOs, which reimburse SHC at contracted or per diem rates, which are usually less than full charges.

  - Counties in the State of California, which reimburse SHC for certain indigent patients covered under county contracts.

- ***Uninsured*** — For uninsured patients that do not qualify for charity care, SHC recognizes revenue on the basis of its standard rates for services less an uninsured discount applied to the patient's account that approximates the average discount for managed care payers.

(in thousands of dollars)

4. Net Patient Service Revenue (Continued)

Patient service revenue, net of contractual allowances (but before provision for doubtful accounts), by major payor for the years ended August 31 is as follows:

	2015	2014
Medicare	$ 732,377	$ 564,361
Medi-Cal	77,950	48,453
Managed Care - Discounted Fee for Services	2,421,560	2,077,301
Self pay and other	246,040	246,277
Related party	47,087	43,675
Patient service revenue, net of contractual allowances	$ 3,525,014	$ 2,980,067
Provision for doubtful accounts	(131,601)	(140,678)
Net patient service revenue	$ 3,393,413	$ 2,839,389

SHC recognized net patient service revenue adjustments of $29,495 and $1,341 as a result of prior years favorable developments related to reimbursement for the years ended August 31, 2015 and 2014, respectively. SHC also recognized revenues of $4,703 and $21 as a result of prior years appeals settled during the years ended August 31, 2015 and 2014, respectively.

Amounts due from Blue Cross, Medicare, and Blue Shield as a percentage of net patient accounts receivable at August 31 are as follows:

	2015	2014
Blue Cross	16%	18%
Blue Shield	15%	14%
Medicare	13%	13%

SHC does not believe significant credit risks exist with these payers.

California Hospital Quality Assurance Fee Program

The State of California enacted legislation in 2009 which established a Hospital Quality Assurance Fee ("HQAF") Program and a Hospital Fee Program. These programs imposed a provider fee on certain California general acute care hospitals that, combined with federal matching funds, would be used to provide supplemental payments to certain hospitals and support the State's effort to maintain health care coverage for children. The effective period of this Hospital Fee Program was April 1, 2009 through December 31, 2010. The State received final approval from the Centers for Medicare & Medicaid Services ("CMS") in December of 2010 on the rates. Subsequent legislation extended the HQAF and Hospital Fee programs from January 1, 2011 through June 30, 2011, which was approved by CMS in December 2011. Additional legislation extended the HQAF and Hospital Fee programs for thirty months from July 1, 2011 through December 31, 2013. CMS approved the thirty month of the fee-for-service (FFS) Medi-Cal supplement in June 2012. CMS approved twenty four months and six months of the managed care supplemental payments in June 2013 and November 2014. HQAF and Hospital Fee programs were further extended by State legislation Senate Bill No. 239 for a new three-year period from January 1, 2014 to December 31, 2016. CMS approved FFS Medi-Cal supplemental payment portion of this three-year extension in December 2014 and approved six months of the managed care supplemental payments in June 2015.

SHC recognized $103,667 and $9,543 in net patient service revenue under these programs and $73,585 and $7,581 in other expense for HQAF to the California Department of Health Care Services ("DHCS") for the years ended August 31, 2015 and 2014, respectively.

(in thousands of dollars)

5. Charity Care and Uncompensated Costs

SHC engages in numerous community benefit programs and services. These services include health research, education and training and other benefits for the larger communities that are excluded from the information below.

Uncompensated charity care is provided to vulnerable populations. Additionally, Medi-Cal and Medicare program reimbursements do not cover the estimated costs of services provided.

Information related to SHC's charity care for the years ended August 31 is as follows:

	2015	2014
Charity care at established rates	$ 42,036	$ 63,789
Estimated cost of charity care, net	$ 9,701	$ 14,792

The estimated cost of providing charity care is based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on SHC's total expenses divided by gross patient service charges. SHC received $526 and $684 during the years ended August 31, 2015 and 2014, respectively, from contributions that were restricted for the care of indigent patients.

Estimated cost of services in excess of reimbursement for the years ended August 31 is as follows:

	2015	2014
Charity care	$ 9,701	$ 14,792
Medi-Cal	196,659	148,896
Medicare	413,324	327,355
Total	$ 619,684	$ 491,043

6. The American Recovery and Reinvestment Act of 2009

The American Recovery and Reinvestment Act of 2009 ("ARRA") increased domestic spending on education, infrastructure and health care, including up to $31 billion in new spending on health information technology, most of which is for incentive payments to physicians and hospitals through the Medicare and Medicaid ("Medi-Cal") programs. On July 13, 2010, CMS issued two final rules related to the adoption and dissemination of electronic health records ("EHRs"). One of the rules defines the "meaningful use" requirements that hospitals and other providers must meet to qualify for federal incentive payments for adopting certified EHRs under ARRA, and the other final rule describes the technical capabilities required for certified EHR technology.

The Medi-Cal Electronic Health Record Incentive Program provides incentive payments to eligible hospitals, physicians and certain other professionals ("Providers") as they adopt, implement, or upgrade certified EHR technology in their first year of participation and demonstrate meaningful use for up to five remaining participation years. Medi-Cal EHR incentive payments to Providers are paid through DHCS, but are 100% federally funded.

(in thousands of dollars)

6. The American Recovery and Reinvestment Act of 2009 (Continued)

The Medicare incentive payments to individual hospitals are made over a four-year, front-weighted period. Hospitals that fail to become meaningful users of EHRs (and fail to submit quality data) by 2015 will be subject to penalties in the form of a reduction in Medicare payments. The Medi-Cal incentives are also received in four front-weighted annual payments, but are subject to more flexible payment and compliance standards than Medicare incentive payments. There are no Medi-Cal payment adjustments related to the failure to comply with meaningful use requirements. SHC recognized $4,121 and $5,458 of EHR incentives in other revenue for the years ended August 31, 2015 and 2014, respectively, related to the Medi-Cal EHR incentive program.

7. Contributions Receivable

Current and long-term portions of contributions receivable are included in other receivables and other assets in the consolidated balance sheets, respectively, and contribution revenue is included in the financial statements in the appropriate net asset category. Contributions are recorded at the discounted net present value of the future cash flows, adjusted for the risk of donor default, using a discount rate of 2.20% for new receivables recorded in 2015 and 2.01% for receivables recorded in 2014.

Contributions receivable at August 31 are expected to be realized in the following periods:

	2015	2014
In one year or less	$ 19,371	$ 16,220
Between one year and five years	106,733	224,669
More than five years	18,504	25,348
	144,608	266,237
Less: discount/allowance	(14,151)	(26,338)
Total contributions receivable, net	130,457	239,899
Less: current portion	(18,224)	(15,183)
Contributions receivable, net of current portion	$ 112,233	$ 224,716

Contributions receivable at August 31 are to be utilized for the following purposes:

	2015	2014
Plant replacement and expansion	$ 138,329	$ 262,156
Other patient and clinical services	6,279	4,081
Total	$ 144,608	$ 266,237

There were no conditional pledges at August 31, 2015 and 2014.

(in thousands of dollars)

8. Investments and Investments in University Managed Pools

The composition of investments held directly by SHC at August 31 is as follows:

	2015		2014	
	Cost	Fair Value	Cost	Fair Value
Short Term Investments:				
Mutual funds	$ 103,872	$ 101,677	$ 100,840	$ 100,970
Investments:				
Cash and cash equivalents	$ 54,094	$ 54,094	$ 56,826	$ 56,826
Mutual funds	57,486	58,411	57,167	58,214
Other	15,355	15,355	5,826	5,826
Total	$ 126,935	$ 127,860	$ 119,819	$ 120,866

The composition of investments in University managed pools at August 31 is as follows:

	Fair Value	
	2015	2014
Investments in University managed pools:		
Merged Pool	$1,434,885	$1,354,539
Securities	-	23,891
Expendable Funds Pool	5,467	4,955
Total	$1,440,352	$1,383,385

The Merged Pool (“MP”) is the primary investment pool in which funds are invested. The MP is invested with the objective of maximizing long-term total return. It is a unitized pool in which the fund holders purchase investments and withdraw funds based on a monthly share value. The MP's investments at August 31, 2015 and 2014 consist of approximately 5% and 7% cash and cash equivalents, 5% and 5% fixed income, 26% and 26% public equity securities, 9% and 9% real estate, 8% and 8% natural resources, 21% and 21% absolute returns, and 26% and 24% private equity securities, respectively.

Securities were donated in August 2014 and recorded at fair market value as of August 31, 2014. The University sold the securities and invested the funds in the MP during fiscal year 2015.

9. Fair Value Measurements

Current accounting guidance defines fair value as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability.

The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity. In addition, the fair value of liabilities should include consideration of non-performance risk.

In addition to defining fair value, this guidance expands the disclosure requirements around fair value and establishes a fair value hierarchy for valuation inputs. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels which are determined by the lowest level input that is significant to the fair value measurement in its entirety.

These levels are:

Level 1: Quoted prices are available in active markets for identical assets or liabilities as of the measurement date. Financial assets and liabilities in Level 1 include U.S. Treasury securities and listed equities.

Level 2: Pricing inputs are based on quoted market prices for similar instruments in active markets, quoted prices for identical or similar instruments in inactive markets, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Financial assets and liabilities in this category generally include asset-backed securities, corporate bonds and loans, municipal bonds and interest rate swap instruments.

Level 3: Pricing inputs are generally unobservable for the assets or liabilities and include situations where there is little, if any, market activity for the investment. The inputs into the determination of the fair value require management's judgment or estimation of assumptions that market participants would use in pricing the assets or liabilities. The fair values are therefore determined using factors that involve considerable judgment and interpretations, including but not limited to private and public comparables, third party appraisals, discounted cash flow models, and fund manager estimates.

(in thousands of dollars)

9. Fair Value Measurements (Continued)

The following table summarizes SHC's assets and liabilities measured at fair value on a recurring basis as of August 31, based on the inputs used to value them:

	2015			
	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	$ 475,677	$ -	$ -	$ 475,677
Short term investments	-	101,677	-	101,677
Assets limited as to use, held by trustee	580,701	-	-	580,701
Investments	54,094	58,411	15,355	127,860
Investments in University managed pools	-	1,440,352	-	1,440,352
Total assets	$1,110,472	$1,600,440	$ 15,355	$2,726,267
Liabilities				
Interest rate swap instruments	$ -	$ 215,376	$ -	$ 215,376

	2014			
	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	$ 467,655	$ -	$ -	$ 467,655
Short term investments	-	100,970	-	100,970
Assets limited as to use, held by trustee	491,594	-	-	491,594
Investments	56,826	58,214	5,826	120,866
Investments in University managed pools	23,891	1,359,494	-	1,383,385
Total assets	$1,039,966	$1,518,678	$ 5,826	$2,564,470
Liabilities				
Interest rate swap instruments	$ -	$ 155,984	$ -	$ 155,984

The table below sets forth a summary of the changes in the fair value of the level 3 investments for the year ended August 31:

	2015	2014
Balance, beginning of year	$ 5,826	$ -
Purchases	9,529	5,826
Balance, end of year	$ 15,355	$ 5,826

(in thousands of dollars)

10. Property and Equipment

Property and equipment consist of the following as of August 31:

	2015	2014
Land and improvements	$ 67,541	$ 28,177
Buildings and improvements	1,237,008	1,020,692
Equipment	867,053	766,221
	2,171,602	1,815,090
Less: Accumulated depreciation	(1,185,187)	(1,082,021)
Construction-in-progress	937,050	672,793
Property and equipment, net	$ 1,923,465	$ 1,405,862

Depreciation and amortization expense totaled $109,735 and $100,625 for the years ending August 31, 2015 and 2014, respectively, and is included in the consolidated statements of operations and changes in net assets.

As of August 31, 2015, medical equipment acquired under capital leases totaled $6,472 and building improvements acquired under capital leases totaled $1,970 and are included in property and equipment in the consolidated balance sheets. Amortization expense under capital leases is included in depreciation expense in the consolidated statements of operations and changes in net assets. Accumulated amortization was $6,975 and $6,472 as of August 31, 2015 and 2014, respectively.

Interest expense on debt issued for construction projects and income earned on the funds held pending use are capitalized until the projects are placed in service and depreciated over the estimated useful life of the asset. Capitalized interest expense net of capitalized investment income was $20,232 and $19,084 for the years ended August 31, 2015 and 2014, respectively.

Certain land and building, with a carrying value of $11,340 at August 31, 2015, are used as collateral on notes payable (see Note 11).

(in thousands of dollars)

11. Long-Term Debt

SHC's outstanding debt at August 31 is summarized below:

	Year of Maturity	Interest Rates 2015/2014	Outstanding Principal 2015	Outstanding Principal 2014
Fixed Rate Obligations				
2008 Series A-1 Refunding Revenue Bonds	2040	2.25% to 5.15%	$ 68,510	$ 68,785
2008 Series A-2 Refunding Revenue Bonds	2040	1.00% to 5.25%	101,350	101,750
2008 Series A-3 Refunding Revenue Bonds	2040	1.00% to 5.50%	81,940	82,240
2010 Series A Refunding Revenue Bonds	2031	4.00% to 5.75%	130,220	135,305
2010 Series B Refunding Revenue Bonds	2036	4.50% to 5.75%	146,710	146,710
2012 Series A Revenue Bonds	2051	5.00%	340,000	340,000
2012 Series B Refunding Revenue Bonds	2023	2.00% to 5.00%	52,880	58,520
2015 Series A Revenue Bonds	2054	4.25% to 5.00%	100,000	-
Note payable, collateralized by certain land and building	2024	5.95%	5,348	-
Note payable, collateralized by certain equipment	2016	7.83%	219	-
Variable Rate Obligations				
2008 Series B Refunding Revenue Bonds	2045	0.07%/0.08%	168,200	168,200
2012 Series C Revenue Bonds	2051	0.15%/0.13%	60,000	60,000
2012 Series D Revenue Bonds	2051	0.53%/0.71%	100,000	100,000
2015 Series B Revenue Bonds	2054	0.68%	75,000	-
Total principal amounts			1,430,377	1,261,510
Unamortized original issue premiums/discounts, net			49,102	46,189
Current portion of long-term debt			(13,932)	(11,700)
Debt subject to short-term remarketing arrangements			(228,200)	(228,200)
Long-term portion, net of current portion			$ 1,237,347	$ 1,067,799

In June 2008, the California Health Facilities Financing Authority ("CHFFA"), on behalf of SHC, issued Variable Rate Demand Bonds ("VRDB's") in the aggregate principal amount of $428,500 (the "2008 Bonds") to refund its previously issued 2006 Bonds. The 2008 Bonds were comprised of $260,300 of 2008 Series A VRDB's that were issued as Series A-1, Series A-2, and Series A-3; and $168,200 of 2008 Series B VRDB's that were issued as Series B-1 and Series B-2.

In June 2009, SHC remarketed the 2008 Series A-1 bonds in the aggregate principal amount of $70,500. In June 2010, SHC converted the 2008 Series A-1 bonds from an annual put mode to a long-term fixed interest rate mode. The remarketing of the 2008 Series A-1 bonds generated an original issue premium of approximately $140; that, pursuant to the requirements of the underlying documents, was used to reduce the principal amount of the bonds from $70,500 to $70,360.

In June 2010, CHFFA, on behalf of SHC, issued fixed rate revenue bonds in the aggregate principal amount of $296,055 (the "2010 Bonds"). The 2010 Bonds were comprised of $149,345 of 2010 Series A bonds, proceeds of which were used to refund the 1998B bonds, and $146,710 of 2010 Series B bonds, proceeds of which were used to refund the 2003 Series B, C and D bonds. The issuance of the 2010 Series A and Series B bonds generated original issue premiums of $10,944 and $3,292, respectively.

11. Long-Term Debt (Continued)

In June 2011, SHC remarketed the 2008 Series A-2, A-3 and B-2 bonds in the aggregate principal amount of $272,365. SHC converted the 2008 Series A-2 bonds from a weekly interest rate mode and the 2008 Series A-3 bonds from a multi-annual put mode to a long-term fixed interest rate mode. The remarketing of the 2008 Series A-3 bonds generated an original issue premium of approximately $1,535; that, pursuant to the requirements of the underlying documents, was used to reduce the principal amount of the bonds from $85,700 to $84,165. SHC converted the 2008 Series B-2 bonds from a weekly interest rate mode to a commercial paper mode. As a part of the conversion, the 2008 Series B-2 bonds were split into two sub-series in the amount of $42,050 each. Bonds in a commercial paper mode are remarketed for various periods that can be no longer than 270 days and are established at the beginning of each commercial paper rate period. Bondholders in a commercial paper mode have the option to tender their bonds only at the end of the commercial paper rate period.

In May 2012, CHFFA, on behalf of SHC, issued four series of revenue bonds in the aggregate principal amount of $568,320 (the "2012 Bonds"). The 2012 Bonds were comprised of $340,000 of 2012 Series A bonds, $68,320 of Series B bonds, $60,000 of Series C bonds and $100,000 of Series D bonds. The issuance of the 2012 Series A and Series B bonds generated original issue premiums of $29,097 and $10,877, respectively. Proceeds of the 2012 Series A, C and D bonds will be used to finance a portion of the New Stanford Hospital. Proceeds of the 2012 Series B bonds were used to advance refund the 2003 Series A bonds.

In June 2015, CHFFA, on behalf of SHC, issued two series of revenue bonds in the aggregate principal amount of $175,000 (the "2015 Bonds"). The 2015 Bonds were comprised of $100,000 of 2015 Series A bonds, and $75,000 of Series B bonds. The 2015 Series A bonds generated an original issue premium of $5,627. Proceeds of the 2015 Series A and B bonds will be used to finance a portion of the New Stanford Hospital.

The 2008 Series B-1 bonds are in a weekly interest rate mode and are remarketed every 7 days at the then prevailing interest rate. Bondholders in a weekly interest rate mode have the option of tendering their bonds on a weekly basis. The 2012 Series C bonds are in a Windows weekly floating index mode and cannot be tendered for 180 days after a 30 day notice and remarketing period. The 2008 Series B bonds and the 2012 Series C bonds are supported by SHC's self-liquidity and are classified as current liabilities. The 2012 Series D and 2015 Series B bonds are also in a floating index mode with monthly interest rate resets and were directly placed with U.S. Bank. The 2012 Series D and 2015 Series B bonds are not subject to remarketing or tender until May 13, 2020 and June 28, 2024, respectively. Both series of bonds are classified as long-term liabilities.

The 2015 Bonds, together with the 2012, 2010, and 2008 Bonds are collectively referred to as the "Revenue Bonds". The Revenue Bonds are limited obligations of CHFFA and are payable solely from payments made by SHC. Payments of principal and interest on the Revenue Bonds are collateralized by a pledge against the revenues of SHC secured under a master trust indenture between SHC and the master trustee. The master trust indenture includes, among other things, limitations on additional indebtedness, liens on property, restrictions on the disposition or transfer of assets, and maintenance of certain financial ratios. SHC may redeem the Revenue Bonds, in whole or in part, prior to the stated maturities. Total debt outstanding under the master trust indenture is in the aggregate principal amounts of $1,424,810 and $1,261,510 as of August 31, 2015 and 2014, respectively.

(in thousands of dollars)

11. Long-Term Debt (Continued)

Scheduled principal payments on long-term debt including unsecured promissory notes are summarized below:

	Scheduled Maturities	Bonds Supported by SHC Liquidity	Total
2016	$ 13,932	$ 228,200	$ 242,132
2017	13,726	-	13,726
2018	13,850	-	13,850
2019	15,052	-	15,052
2020	14,815	-	14,815
Thereafter	1,130,802	-	1,130,802
	$ 1,202,177	$ 228,200	$ 1,430,377

The scheduled principal payments above represent the annual payments required under debt repayment schedules. The current portion of long-term obligations, including debt subject to short term remarketing arrangements, includes payments scheduled to be made in 2016 and the VRDB's supported by SHC's liquidity. The VRDB's supported by self-liquidity provide the bondholder with an option to tender the bonds to SHC. Generally accepted accounting principles require that bonds supported by SHC's liquidity be classified as current liabilities.

The estimated fair value of the Revenue Bonds as of August 31, 2015 and 2014 was $1,546,143 and $1,371,231, respectively, and is considered level 2 based on the inputs used to value the Revenue Bonds as defined in Note 9.

In 1998, SHC advance refunded its 1993 bonds in the amount of $89,520 by issuing the 1998 Series B bonds. As of August 31, 2015 and 2014, $22,550 and $27,295, respectively, of advance refunded bonds, which are considered extinguished, remain outstanding.

Interest Rate Swap Agreements

SHC has entered into various interest rate swap agreements ("swap agreements") with varying maturities through November 2051. SHC uses swap agreements, also known as risk management or derivative instruments, principally to manage interest rate risk and has entered into derivatives to lock in fixed rates for anticipated issuance and refunding of debt. By using swap agreements to manage the risk of changes in interest rates, SHC exposes itself to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the swap agreements. When the fair value of a swap agreement is positive, the counterparty owes SHC, which creates credit risk. When the fair value of a swap agreement is negative, SHC owes the counterparty and, therefore, it does not possess credit risk.

SHC minimizes its credit risk by entering into swap agreements with at least two counterparties and requiring the counterparty to post collateral for the benefit of SHC based on the credit rating of the counterparty and the fair value of the swap agreement. 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.

(in thousands of dollars)

11. Long-Term Debt (Continued)

Interest Rate Swap Agreements (continued)

SHC maintains interest rate swap programs on certain of its variable rate revenue bonds. These bonds expose SHC 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, SHC entered into various interest rate swap agreements to manage fluctuations in cash flows resulting from interest rate risk. Certain of these agreements involve the exchange of fixed rate payments for variable rate payments based on a percentage of the One Month London Interbank Offered Rate ("LIBOR"). In February 2014, SHC terminated the 2008 B-1 and B-2 swap agreements. As a result of the termination, a loss of $71 was included in loss on extinguishment of swaps for the year ended August 31, 2014.

The following is a summary of the outstanding positions under these interest rate swap agreements at August 31, 2015:

Description	Current Notional	Maturity Date	Rate Paid	Rate Received
2003 Series B	$ 48,800	11/15/2036	3.365%	70% 1-month LIBOR
2003 Series C	48,700	11/15/2036	3.365%	70% 1-month LIBOR
2003 Series D	52,500	11/15/2036	3.365%	70% 1-month LIBOR
Subtotal LIBOR Swaps	150,000			
2008 Series A-1	68,650	11/01/2040	3.693%	70% 1-month LIBOR
2008 Series A-2	102,775	11/15/2051	3.999%	67% 1-month LIBOR
2008 Series A-3	84,600	11/15/2051	3.902%	67% 1-month LIBOR
Subtotal LIBOR Swaps	256,025			
2012 Series A	68,350	11/15/2045	4.081%	67% 1-month LIBOR
2012 Series B	68,375	11/15/2045	4.077%	67% 1-month LIBOR
2012 Series C	34,175	11/15/2045	4.008%	67% 1-month LIBOR
Subtotal Forward Swaps	170,900			
Total	$ 576,925			

SHC designates its interest rate swaps that are used to minimize the variability in cash flows of interest-bearing liabilities or forecasted transactions caused by changes in interest rates as hedging instruments at the inception of each contract, with the intention of maintaining hedge accounting treatment over the term of the agreement. However, circumstances may arise whereby the representations made at the inception of the agreement became invalid, or the structure of the bonds is changed, resulting in de-designation of the hedge. In June 2008, the underlying bonds that were being hedged were refinanced and as a result, none of the swap agreements are treated as a hedge for accounting purposes.

(in thousands of dollars)

11. Long-Term Debt (Continued)

Interest Rate Swap Agreements (continued)
The fair value of interest rate swaps (all of which are designated as non-hedging instruments) is shown on the balance sheets as of August 31 as follows:

	Fair Value		
Description	**2015**	**2014**	**Balance Sheet Location**
Fixed Payment Swaps	$ 215,376	$ 155,984	Other long-term liabilities

The change in fair value of the interest rate swaps (all of which are designated as non-hedging instruments) is shown on the consolidated statements of operations and changes in net assets for the years ended August 31 as follows:

	Unrealized Losses		
Description	**2015**	**2014**	**Statement of Operations Location**
Fixed Payment Swaps	$ 59,392	$ 37,532	Interest rate swap mark to market adjustments

Certain swap agreements require posting of collateral by SHC or the counterparties should the fair market value of the swap agreements exceed a predetermined threshold dollar amount. The collateral thresholds reflect the current credit ratings issued by major credit rating agencies on SHC's and the counterparty's debt. Declines in SHC's or the counterparties' credit ratings would result in decreases in the collateral thresholds and consequently, the potential for additional collateral postings by SHC or the counterparty. There was $1,660 and $0 of cash collateral required to be posted with one counterparty at August 31, 2015 and 2014, respectively.

Upon the occurrence of certain events of default or termination events identified in the derivative contracts, either SHC 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 derivatives contract, SHC will make a payment to the counterparty. Conversely, if interest rates at such time are higher, the counterparty will make a payment to SHC.

Bond Interest Expense
The components of bond interest expense for the years ended August 31 are as follows:

	2015	**2014**
Interest and fees	$ 25,962	$ 26,186
Swap settlements	14,087	16,982
Bond interest expense	$ 40,049	$ 43,168
Interest capitalized as a cost of construction	$ 20,232	$ 19,084

12. Retirement Plans

SHC provides retirement benefits through defined benefit and defined contribution retirement plans covering substantially all benefit eligible employees.

Defined Contribution Retirement Plan
Employer contributions to the defined contribution retirement plan are based on a percentage of participant annual compensation. Employer contributions to this plan for SHC employees excluding LPCH employees (see Note 15) totaling $61,244 and $55,066 for the years ended August 31, 2015 and 2014, respectively, and UHA employer contributions totaling $2,487 and $1,958 for the years ended August 31, 2015 and 2014, respectively, are included in salaries and benefits expense in the consolidated statements of operations and changes in net assets. There were no employer contributions made by VCHS for the stub period ending August 31, 2015.

Defined Benefit Pension Plan
Certain employees of the Hospitals are covered by a noncontributory defined benefit pension plan (the "Staff Pension Plan"). Benefits are based on years of service and the employee's compensation. Contributions to the plans are based on actuarially determined amounts sufficient to meet the benefits to be paid to plan participants.

As of August 31, 2004, SHC assumed the pension liability of the LPCH employees. SHC received $286 and $434 in cash for the years ending August 31, 2015 and 2014, respectively, which represented the current year pension expense related to LPCH employees.

Postretirement Medical Benefit Plan
SHC currently provides health insurance coverage for SHC employees upon retirement as early as age 55, with years of service as defined by specific criteria. The health insurance coverage for retirees who are under age 65 is the same as that provided to active employees. A Medicare supplement option is provided for retirees over age 65.

The following tables present information on plan assets and obligations, costs, and actuarial assumptions for the Staff Pension Plan and the Postretirement Medical Benefit Plan for the years ended August 31, 2015 and 2014, respectively.

In 2014, the Society of Actuaries issued a new mortality table ("RP-2014") and a new mortality improvement (projection) scale that recognize increases in life expectancy. In selecting its assumptions for determining the benefit obligations as of August 31, 2015, SHC adopted a modified version of the RP-2014 mortality table and a projection scale based on the 2014 Trustees Report of the Social Security Administration. The use of the new mortality table and projection scale resulted in an increase of approximately $18,400 and $6,400 to the Staff Pension Plan and Postretirement Medical Benefit Plan benefit obligations as of August 31, 2015, respectively.

The tables for the Postretirement Medical Benefit Plan include SHC and LPCH employees. The total postretirement medical benefit liability was $84,751 and $84,616 as of August 31, 2015 and 2014, respectively. SHC recorded a liability within self-insurance reserves in the consolidated balance sheets of $66,547 and $66,959 as of August 31, 2015 and 2014, respectively, which represents the liability for SHC employees excluding LPCH employees.

(in thousands of dollars)

12. Retirement Plans (Continued)

The change in pension and other post-retirement plan assets and the related change in benefit obligations, using a measurement date of August 31, as of and for the years ended August 31 are as follows:

	Staff Pension Plan Obligations		Postretirement Medical Benefits Net of Medicare Part D Subsidy	
	2015	2014	2015	2014
Change in plan assets:				
Fair value of plan assets at beginning of year	$ 214,575	$ 182,510	$ -	$ -
Actual return on plan assets	(4,727)	36,886	-	-
Employer contributions	-	5,820	4,914	4,703
Participants contributions	-	-	1,038	1,237
Benefits paid	(11,045)	(10,175)	(6,082)	(5,940)
Medicare subsidies received	-	-	130	-
Expenses paid	(914)	(466)	-	-
Fair value of plan assets at end of year	$ 197,889	$ 214,575	$ -	$ -
Change in benefit obligation:				
Benefit obligation at beginning of year	$ 245,402	$ 224,361	$ 84,616	$ 82,846
Service cost	2,006	2,324	2,068	1,839
Interest cost	9,182	10,036	2,995	3,507
Participants contributions	-	-	1,038	1,237
Benefits paid	(11,045)	(10,175)	(6,082)	(5,940)
Medicare subsidies received	-	-	130	-
Expenses paid	(914)	(466)	-	-
Actuarial loss (gain)	4,478	19,322	(14)	1,127
Benefit obligation at end of year	$ 249,109	$ 245,402	$ 84,751	$ 84,616
Amounts recognized in consolidated balance sheets:				
Plan assets minus benefit obligation	$ (51,220)	$ (30,827)	$ (84,751)	$ (84,616)
Net benefit liability recognized	$ (51,220)	$ (30,827)	$ (84,751)	$ (84,616)
Amounts recognized in consolidated balance sheets:				
Current liabilities	$ -	$ -	$ (5,121)	$ (5,149)
Noncurrent liabilities	(51,220)	(30,827)	(79,630)	(79,467)
Net benefit liability recognized	$ (51,220)	$ (30,827)	$ (84,751)	$ (84,616)
Amounts recognized in unrestricted net assets:				
Prior service cost	$ -	$ -	$ (2,586)	$ (3,401)
Net (loss) gain	(84,990)	(65,146)	4,730	5,054
Unrestricted net assets	$ (84,990)	$ (65,146)	$ 2,144	$ 1,653

The estimated net loss for the staff pension plan that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year is $2,327.

The estimated net gain and prior service cost for the postretirement medical plan that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year are $313 and $773, respectively.

(in thousands of dollars)

12. Retirement Plans (Continued)

Total benefit obligation at the end of the year for Postretirement Medical Benefits excluding Medicare Part D subsidy decreased to $87,895.

The accumulated benefit obligation for the defined benefit pension plan was $246,998 and $242,963 as of August 31, 2015 and 2014, respectively.

Net benefit expense related to the plans for the years ended August 31 includes the following components:

	Staff Pension Plan Obligations	
	2015	2014
Service cost	$ 2,006	$ 2,324
Interest cost	9,182	10,036
Expected return on plan assets	(13,195)	(13,163)
Amortization of net actuarial loss	2,556	2,175
Total net periodic benefit cost	$ 549	$ 1,372

	Postretirement Medical Benefits			
	Net of Medicare Part D Subsidy		Excluding Medicare Part D Subsidy	
	2015	2014	2015	2014
Service cost	$ 2,068	$ 1,839	$ 2,068	$ 1,841
Interest cost	2,995	3,507	3,122	3,636
Amortization of prior service cost	815	815	815	815
Amortization of net actuarial gain	(338)	(463)	(567)	(727)
Total net periodic benefit cost	$ 5,540	$ 5,698	$ 5,438	$ 5,565

Changes recognized in unrestricted net assets for the years ended August 31 include the following components:

	Staff Pension Plan Obligations		Postretirement Medical Benefits Net of Medicare Part D Subsidy	
	2015	2014	2015	2014
Net loss (gain) arising during period	$ 22,400	$ (4,401)	$ (14)	$ 1,127
Amortizations				
Prior service cost	-	-	(815)	(815)
(Loss) gain	(2,556)	(2,175)	338	463
Total recognized in unrestricted net assets	$ 19,844	$ (6,576)	$ (491)	$ 775
Total recognized in net periodic benefit cost and unrestricted net assets	$ 20,393	$ (5,204)	$ 5,049	$ 6,473

(in thousands of dollars)

12. Retirement Plans (Continued)

Actuarial Assumptions
The weighted-average assumptions used to determine benefit obligations are as follows for the years ended August 31:

	Staff Pension Plan Obligations		Postretirement Medical Benefits	
	2015	2014	2015	2014
Weighted-average assumptions				
Discount rate	4.20%	3.84%	4.01%	3.65%
Rate of compensation increase	3.00%	3.00%	N/A	N/A

The discount rate, expected rate of return on plan assets, and the projected covered payroll growth rates used in determining the above net benefit expense are as follows for the years ended August 31:

	Staff Pension Plan Obligations		Postretirement Medical Benefits	
	2015	2014	2015	2014
Weighted-average assumptions				
Discount rate	3.84%	4.59%	3.65%	4.37%
Expected return on plan assets	7.00%	7.50%	N/A	N/A
Rate of compensation increase	3.00%	3.00%	N/A	N/A

To develop the assumption for the expected rate of return on plan assets, SHC considered the historical and future expected returns. An independent investment consulting firm provided SHC with an estimate of the future expected returns for each asset class based on SHC's asset allocation targets. The evaluation of the historical returns and the future expected returns resulted in the use of 7.00% as the assumption for the expected return on plan assets.

To determine the accumulated post-retirement benefit obligation as of August 31, 2015, a 7.00% annual rate of increase in the per capita cost of covered health care was assumed for calendar year 2015, declining gradually to 4.75% by 2024, and remaining at this rate thereafter.

Assumed healthcare cost trend rates have a significant effect on the amounts reported for the post-retirement medical benefit plan. Increasing the health care cost trend rate by 1% in each future year would increase the accumulated post-retirement benefit obligation by $2,144 and the aggregate service and interest cost by $133. Decreasing the health care cost trend rate by 1% in each future year would decrease the accumulated post-retirement benefit obligation by $2,004 and the aggregate service and interest cost by $123.

Plan Assets
SHC's staff pension plan weighted-average asset allocations as of the measurement date August 31, 2015 and 2014, respectively, by asset category are as follows:

Asset Category	August 31, 2015	August 31, 2014
Debt securities	51%	50%
Equity securities	48%	50%
Other	1%	0%
Total	100%	100%

(in thousands of dollars)

12. Retirement Plans (Continued)

Plan Assets (continued)
The following table summarizes SHC's staff pension plan assets measured at fair value on a recurring basis as of August 31, based on the inputs used to value them as defined in Note 9:

	2015			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$ 1,288	$ -	$ -	$ 1,288
Mutual funds	196,601	-	-	196,601
Total assets	$ 197,889	$ -	$ -	$ 197,889

	2014			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$ 938	$ -	$ -	$ 938
Mutual funds	213,637	-	-	213,637
Total assets	$ 214,575	$ -	$ -	$ 214,575

Plan Investments
The investment objective of the staff pension plan funds is to maximize the total rate of return (income and appreciation) within the limits of prudent risk taking and Section 404 of the Employee Retirement Income Security Act. The funds are diversified across asset classes to achieve an optimal balance between risk and return and between income and capital appreciation. Many of the pension liabilities are long-term. The investment horizon is also long-term; however, the investment plan also ensures adequate near-term liquidity to meet benefit payments.

The allowable asset mix range and target asset allocations are:

Asset Category	Acceptable Range	Target Allocation
Equity securities	36% to 60%	50%
Debt securities	20% to 80%	50%

Appropriate investments include common, preferred and convertible equities of domestic and foreign companies, mutual and commingled trust funds, top tier commercial paper, certificates of deposit, and fixed income securities whose assets are rated investment grade or better.

Financial futures and options on futures traded on exchanges are also permitted for hedging purposes. Prohibited investments include commodities, unregistered securities and short sales. Derivative products may not be used to leverage a portfolio or to speculate. All assets must have readily ascertainable market value and be easily marketable.

Portfolios are expected to be well diversified with respect to industry and economic sectors. Equity investments in any one company shall be limited to the greater of 5% of the market value of the portfolio at time of purchase or twice the applicable benchmark weighting of the security. The investment manager shall not hold more than 15% of any company's outstanding equity.

Fixed income investments may consist of U.S. government, U.S. government guaranteed, and U.S. government agency securities. Corporate bond holdings must have an investment grade credit rating at the time of purchase and during the holding period. No single issuer of fixed income or cash equivalent securities (with the exception of the U.S. Government and its Agencies) will account for more than 10% of the market value of the fixed income securities in a manager's portfolio.

(in thousands of dollars)

12. Retirement Plans (Continued)

Concentration of Risk

SHC manages a variety of risks, including market, credit, and liquidity risks, across plan assets through investment managers. Concentration of risk is defined as an undiversified exposure to one of the above–mentioned risks that increases the exposure of the loss of plan assets unnecessarily. Risk is minimized by diversifying our exposure to such risks across a variety of instruments, markets, and counterparties. As of August 31, 2015, SHC did not have concentrations of risk in any single entity, manager, counterparty, sector, industry or country.

Expected Contributions

SHC expects to make no contributions to its Staff Pension Plan for both SHC and LPCH employees during the fiscal year ending August 31, 2016. SHC expects to contribute $4,371 to its Postretirement Medical Plan for only SHC employees during the fiscal year ending August 31, 2016.

Expected Benefit Payments

The following benefit payments, which reflect expected future service, are expected to be paid for the fiscal years ending August 31:

		Postretirement Medical Benefits	
	Pension Benefits	Net of Medicare Part D Subsidy	Excluding Medicare Part D Subsidy
2016	$ 13,178	$ 5,121	$ 5,408
2017	13,726	5,361	5,640
2018	14,238	5,675	5,950
2019	14,707	6,019	6,289
2020	15,175	6,358	6,621
2021 - 2025	79,860	34,476	35,641

13. Unrestricted Net Assets

The changes in consolidated unrestricted net assets attributable to the controlling financial interest of SHC and the noncontrolling interests, for the years ended August 31, are as follows:

	Total	Controlling Interest	Noncontrolling Interests
Balance September 1, 2013	$ 1,776,957	$ 1,757,504	$ 19,453
Excess of revenues over expenses	431,858	426,527	5,331
Noncontrolling capital distribution, net	(1,482)	-	(1,482)
Other changes in unrestricted net assets	(46,640)	(46,642)	2
Balance August 31, 2014	2,160,693	2,137,389	23,304
Excess of revenues over expenses	389,236	389,469	(233)
Noncontrolling capital distribution, net	(62)	-	(62)
Other changes in unrestricted net assets	(59,495)	(59,465)	(30)
Balance August 31, 2015	$ 2,490,372	$ 2,467,393	$ 22,979

(in thousands of dollars)

14. Temporarily and Permanently Restricted Net Assets

Temporarily Restricted Net Assets

Temporarily restricted net assets consist of the following at August 31:

	2015	2014
Plant replacement and expansion	$ 499,269	$ 454,334
Other patient services	38,188	39,587
Clinical services	13,543	14,767
Indigent care	6,630	6,366
Education	4,012	3,878
Total	$ 561,642	$ 518,932

Permanently Restricted Net Assets

In 2009, California adopted a version of the Uniform Prudent Management of Institutional Funds Act ("UPMIFA"). SHC has interpreted UPMIFA as requiring the preservation of the original gift as of the gift date of donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, SHC classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts 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 portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure in a manner consistent with the standard of prudence prescribed by UPMIFA.

In accordance with UPMIFA, SHC considers the following factors in making a determination to appropriate or accumulate endowment funds:

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

Endowment funds by net asset classification as of August 31, 2015 and 2014 are as follows:

	2015			2014		
	Temporarily Restricted	Permanently Restricted	Total	Temporarily Restricted	Permanently Restricted	Total
Donor restricted endowment	$ 10,666	$ 7,694	$ 18,360	$ 10,293	$ 7,692	$ 17,985
Total endowment	$ 10,666	$ 7,694	$ 18,360	$ 10,293	$ 7,692	$ 17,985

(in thousands of dollars)

14. Temporarily and Permanently Restricted Net Assets (Continued)

Permanently Restricted Net Assets (continued)

Changes in SHC's endowment for the years ended August 31, 2015 and 2014 are as follows:

	2015			2014		
	Temporarily Restricted	Permanently Restricted	Total	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ 10,293	$ 7,692	$ 17,985	$ 8,542	$ 7,591	$ 16,133
Investment return:						
Investment income	478	-	478	467	-	467
Mark to market adjustments	314	-	314	1,896	-	1,896
Total investment return	792	-	792	2,363	-	2,363
Contributions	-	2	2	-	101	101
Expenditures	(419)	-	(419)	(612)	-	(612)
Endowment net assets, end of year	$ 10,666	$ 7,694	$ 18,360	$ 10,293	$ 7,692	$ 17,985

The following provides descriptions of amounts classified as permanently restricted net assets and temporarily restricted net assets (endowment only). The portion of endowment funds that is required to be retained permanently or temporarily, either by explicit donor stipulation or by California UPMIFA, as of August 31, 2015 and 2014 is as follows:

	2015			2014		
	Temporarily Restricted	Permanently Restricted	Total	Temporarily Restricted	Permanently Restricted	Total
Clinical services	$ 1,117	$ 4,000	$ 5,117	$ 1,125	$ 4,000	$ 5,125
Education	4,017	1,235	5,252	3,831	1,235	5,066
Indigent care and other	5,532	2,459	7,991	5,337	2,457	7,794
Total endowment classified as net assets	$ 10,666	$ 7,694	$ 18,360	$ 10,293	$ 7,692	$ 17,985

All of SHC's endowment, totaling $18,360 and $17,985 at August 31, 2015 and 2014, respectively, are invested in the MP. The funds are held in perpetuity and invested to generate income to support operating and strategic initiatives.

Return Objectives and Risk Parameters

The return objective for the endowment assets is to generate optimal total return while maintaining an appropriate level of risk established by the University.

Strategies Employed for Achieving Investment Objectives

SHC relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized gain) and current yield (interest and dividend) managed by the MP.

15. Related-Party Transactions

Transactions with the University and SoM

SHC has various transactions with the University and the SoM. SHC records expense transactions where direct and incremental economic benefits are received by SHC.

Expenses paid to the University and the SoM are reported as operating expenses in the consolidated statements of operations and changes in net assets and are management's best estimates of SHC's arms-length payments of such amounts for its market specific circumstances. To the extent that payments to the University and the SoM exceed an arms-length estimated amount relative to the benefits received by SHC, they are recorded as transfers to the University and the SoM in other changes in net assets.

15. Related-Party Transactions (Continued)

Transactions with the University and SoM (continued)
SHC purchases certain services from the University and the SoM. Payment for these services is based on management's best estimate of its market specific circumstances.

Services provided by the SoM include physician services that benefit SHC, such as emergency room coverage, physicians providing medical direction to SHC, and physicians providing service to the clinical practice, which are covered by the Professional Services Agreement ("PSA"). Such expenses are reflected as purchased services in the consolidated statements of operations and changes in net assets, and total $506,349 and $406,982 for the years ended August 31, 2015 and 2014, respectively.

Services provided by the University and other SoM non-physician services include telecommunications, transportation, utilities, blood products, and certain administrative services, which consist of legal and internal audit. Total costs incurred by SHC were $132,545 and $114,366 for the years ended August 31, 2015 and 2014, respectively, and are reflected in various categories in the consolidated statements of operations and changes in net assets.

SHC paid service fees to the University in the amount of $2,211 for the years ended August 31, 2015 and 2014. The service fees represent costs for the utilization of infrastructure owned by the University such as road improvements, parking garages and generators and are reflected in the consolidated statements of operations and changes in net assets as other expense. Expected payments over the next 18 years total $23,363. Annual service fees range from approximately $2,378 for the year ending August 31, 2016 to $575 for the year ending August 31, 2033.

SHC also received payment for services provided to the University including primarily building maintenance, housekeeping, and security. Costs incurred by SHC in providing these services are reflected in the respective categories in the consolidated statements of operations and changes in net assets. Reimbursement from the University totaled $31,452 and $30,161 for the years ended August 31, 2015 and 2014, respectively, and is reflected in the consolidated statements of operations and changes in net assets as expense recoveries.

In addition, SHC received certain grant monies for clinical trials from the University. Grant revenue totaled $4,747 and $4,682 for the years ended August 31, 2015 and 2014, respectively, and is reflected in the consolidated statements of operations and changes in net assets as net patient service revenue and recoveries.

During the year ended August 31, 2004, SHC paid $5,500 to the University. The amount represented a prepayment of a 51 year lease for property owned by the University. The short term portion of $108 is included in prepaid expenses and other in the consolidated balance sheets as of August 31, 2015 and 2014. The remaining amount included in other assets in the consolidated balance sheets is $3,918 and $4,026 as of August 31, 2015 and 2014, respectively.

For the years ended August 31, 2015 and 2014, SHC transferred $66,477 and $54,337, respectively, to the University. These funds are used by the University to support the academic mission of the SoM and its initiatives as well as the general support of the academic community and physical plant and are included in other changes in unrestricted net assets in the consolidated statements of operations and changes in net assets.

SHC also received equity transfers of $4,062 and $2,480 during the years ended August 31, 2015 and 2014, respectively, which represented restricted gifts originally donated to the University. These gifts were subsequently re-designated mostly for SHC patient care services and are included in changes in temporarily restricted net assets in the consolidated statements of operations and changes in net assets.

(in thousands of dollars)

15. Related-Party Transactions (Continued)

Transactions with LPCH

Shared Services - SHC and LPCH share certain departments, including facilities design and construction, materials management, managed care contracting, compliance and general services. Shared service costs are included in the respective categories on the consolidated statements of operations and changes in net assets, and are allocated between SHC and LPCH based on negotiated rates. Reimbursement received from LPCH totaled $28,556 and $25,449 for the years ended August 31, 2015 and 2014, respectively, and is reflected in the consolidated statements of operations and changes in net assets as expense recoveries.

Purchased Services - SHC provides various services to LPCH. These services include operating room, cardiac catheterization, interventional radiology, radiation oncology and laboratory. The cost of these services is charged back to LPCH based on a percentage of charges intended to approximate cost or a cost per procedure. Costs of these purchased services are reflected in the appropriate category in the consolidated statements of operations and changes in net assets. Reimbursement of purchased services from LPCH totaled $47,087 and $43,675 for the years ended August 31, 2015 and 2014, respectively, and is reflected in the consolidated statements of operations and changes in net assets as net patient service revenue.

Other Services - Other services provided by SHC include services provided by interns and residents, building maintenance, IT and utilities. Reimbursement of these services totaled $30,064 and $25,022 for the years ended August 31, 2015 and 2014, respectively, and is reflected in the consolidated statements of operations and changes in net assets as expense recoveries.

Equity Transfers - SHC received equity transfers of $26,600 during the year ended August 31, 2015, which represented reimbursement for capital projects.

16. Operating and Capital Leases

SHC leases various equipment and facilities under non-cancelable lease agreements expiring at various dates. Total rental expense (included in other expense in the consolidated statements of operations and changes in net assets) under these leases for the years ended August 31, 2015 and 2014 was $65,351 and $56,045, respectively.

Net minimum future lease payments under all non-cancelable operating leases and capital lease obligations for periods subsequent to August 31, 2015 are as follows:

Year Ending August 31,	Operating	Capital
2016	$ 65,616	$ 342
2017	63,571	49
2018	61,201	-
2019	56,692	-
2020	46,828	-
Thereafter	146,337	-
	$ 440,245	391
Less amount representing interest		(11)
Subtotal		380
Current portion		(332)
Long-term portion, net of current portion		$ 48

(in thousands of dollars)

16. Operating and Capital Leases (Continued)

Capital lease obligations totaled $380 of which $332 is included in accounts payable and accrued liabilities on the consolidated balance sheets. The remaining capital lease obligation of $48 is included in other long term liabilities on the consolidated balance sheets.

SHC leases space in its medical office buildings to others under non-cancelable operating lease arrangements. Future minimum base rentals to be received under these leases in place as of August 31, 2015 are as follows:

Year Ending August 31,	
2016	$ 3,032
2017	1,976
2018	1,626
2019	1,211
2020	1,225
Thereafter	11,565
	$ 20,635

17. Commitments and Contingencies

SHC is aware of certain asserted and unasserted legal claims. While the outcome cannot be determined at this time, management is of the opinion that the liability, if any, from these actions will not have a material effect on SHC's financial position.

SHC has irrevocable standby letters of credit in the amount of $17,353, which are required as security for the workers' compensation self-insurance arrangements and $10,093 to serve as a security deposit for certain construction projects being undertaken by SHC. No amounts have been drawn on these letters of credit as of August 31, 2015.

At August 31, 2015, SHC had contractual obligations of approximately $607,850 primarily related to the construction of the new hospital and other capital projects and approximately $253,482 to support SHC's operations, such as maintenance, food services, valet services and other purchased services.

Effective December 23, 2014, SHC entered into a five year agreement with a global technology services and outsourcing company, pursuant to which SHC will receive certain information technology services. Under the terms of the agreement, SHC will be charged fixed fees for one-time transition services (through August 31, 2015), ongoing recurring and event-based fees for information technology services, and additional fees plus expenses for project work agreed upon pursuant to work orders. SHC has the right to extend the agreement for up to two consecutive one-year periods. SHC anticipates that it will spend approximately $36,000 over the initial term of the agreement. SHC has certain rights to reduce the scope of services to be purchased and to terminate the agreement early for a termination fee. The amount of the termination fee depends on when the right to terminate is exercised, what services are terminated, and changes monthly from $1,602 to terminate all services in the month ending September 30, 2015 and decreasing gradually to $459 for the month ending December 31, 2019.

17. Commitments and Contingencies (Continued)

The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. Compliance with these laws and regulations can be subject to future government review and interpretation, as well as to regulatory actions unknown or unasserted at this time. Recently, government activity has increased with respect to investigations and allegations concerning possible violations by healthcare providers of regulations that could result in the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. SHC is subject to similar regulatory reviews, and while such reviews may result in repayments and/or civil remedies that could have a material effect on SHC's financial results of operations in a given period, management believes that such repayments and/or civil remedies would not have a material effect on SHC's financial position.

As with many medical centers across the country, information security and privacy is a growing risk area based on developments in the law and expanding mobile technology practices. SHC has policies, procedures, and training in place to safeguard protected information, but select incidents have occurred in the past and may occur in the future involving potential or actual disclosure of such information (including, for example, certain identifiable information relating to patients or research participants). In most cases, there has been no evidence of unauthorized access to, or use/disclosure of, such information, yet laws may require reporting to potentially affected individuals and federal and state governmental agencies. Governmental agencies have the authority to investigate and request further information about an incident or safeguards, to cite SHC for a deficiency or regulatory violation, and/or require payment of fines, corrective action, or both. California law also allows a private right to sue for a breach of medical information. The cost of such possible consequences has not been material to date to SHC, and management does not believe that any future consequences of these incidents will be material to the consolidated financial statements.

The percentage of SHC employees that are covered by collective bargaining arrangements is approximately 32%. There are currently no expired agreements.

California's Hospital Seismic Safety Act requires licensed acute care functions to be conducted only in facilities that meet specified seismic safety standards. Facilities classified by the State of California as non-compliant in the event of an earthquake must be retrofitted, replaced or removed from acute-care service by applicable deadlines in 2013, 2020 or 2030.

The California Office of Statewide Health Planning and Development ("OSHPD") has classified a substantial portion of Stanford Hospital as compliant with seismic safety structural standards until 2030 and beyond. Certain patient care activities are located in existing buildings that are structurally compliant until 2030. However, these facilities have utility system configurations that must be modified no later than January 1, 2020 in order to remain in use for acute patient care. SHC is constructing a new hospital facility to address seismic safety requirements, which will also enable retrofit work of the existing hospital facility utility infrastructure.

Amendments of the Hospital Seismic Safety Act, through Senate Bill 90, allow extensions to compliance timelines for hospitals that meet certain eligibility requirements. SHC has received approval from the State to extend the compliance deadline to mid-2019 for all buildings subject to the requirement. These extensions will allow sufficient time to construct the new hospital and mitigate the deficiencies of the existing facility.

(in thousands of dollars)

17. Commitments and Contingencies (Continued)

In June 2011, the Palo Alto City Council certified the Final Environmental Impact Report, land use changes, permits and a Development Agreement with SHC, LPCH and the University as part of the Renewal Project. In July 2011, the Palo Alto City Council provided final approval for the Renewal Project at the second reading of the Development Agreement. The Renewal Project will rebuild Stanford Hospital and expand LPCH to assure adequate capacity, meet State-mandated earthquake safety standards, and provide modern, technologically-advanced hospital facilities. The Renewal Project also includes replacement of outdated laboratory facilities at the SoM and remodeling of Hoover Pavilion. SHC's share of the estimated cost is approximately $2 billion. As of August 31, 2015, SHC has capitalized $838 million, inclusive of $74 million in capitalized interest, related to this project.

Based on current estimated schedules, management currently projects that the Renewal Project construction will be complete in 2017.

18. Functional Expenses

Expenses are categorized on a functional basis for the years ended August 31:

	2015	2014
Patient services	$ 2,973,295	$ 2,488,922
Management and general	305,910	222,110
Fundraising	9,566	9,043
Total functional expenses	$ 3,288,771	$ 2,720,075

19. Subsequent Events

SHC has evaluated subsequent events occurring between the end of the most recent fiscal year and December 9, 2015, the date the financial statements were issued.