

The McLean Hospital Corporation

**Report on Federal Awards in
Accordance with OMB Circular A-133
September 30, 2008
EIN 042697981**

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Part I
Financial Statements

Report of Independent Auditors

To the Board of Trustees of
The McLean Hospital Corporation

In our opinion, the accompanying balance sheets and the related statements of operations, changes in net assets and cash flows present fairly, in all material respects, the financial position of The McLean Hospital Corporation at September 30, 2008 and 2007, and the results of its operations, its changes in net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of The McLean Hospital Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 19, 2008 on our consideration of The McLean Hospital Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters for the year ended September 30, 2008. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards for the year ended September 30, 2008 is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects, in relation to the basic financial statements taken as a whole.



December 19, 2008

The McLean Hospital Corporation
Balance Sheets
September 30, 2008 and 2007

<i>(dollars in thousands)</i>	2008	2007
Assets		
Current assets		
Cash and equivalents	\$ 146	\$ 8,700
Investments	-	11,189
Current portion of investments limited as to use	8,378	16,158
Patient accounts receivable, net of allowance for bad debts: 2008 - \$2,081; 2007 - \$1,948	7,715	7,687
Research grants receivable	8,728	5,468
Other current assets	4,332	4,439
Total current assets	<u>29,299</u>	<u>53,641</u>
Investments limited as to use, less current portion	2,431	19,185
Long-term investments	1,209	8,539
Pledges receivable, net, less current portion	1,574	2,197
Interest in the net assets of The Massachusetts General Hospital	65,855	80,436
Property and equipment, net	60,303	55,589
Other assets	469	-
Total assets	<u>\$ 161,140</u>	<u>\$ 219,587</u>
Liabilities and Net Assets		
Current liabilities		
Current portion of long-term obligations	\$ 3,463	\$ 3,332
Accounts payable and accrued expenses	3,971	5,044
Accrued compensation and benefits	7,716	7,092
Accrual for settlements with third-party payers	507	1,440
Unexpended funds on research grants	7,069	7,145
Due to affiliates	893	1,502
Total current liabilities	<u>23,619</u>	<u>25,555</u>
Other liabilities		
Accrued professional liability	853	800
Accrued employee benefits	2,493	2,883
Accrued other	315	255
	<u>3,661</u>	<u>3,938</u>
Long-term obligations, less current portion	<u>19,372</u>	<u>22,835</u>
Total liabilities	<u>46,652</u>	<u>52,328</u>
Commitments and contingencies		
Net assets		
Unrestricted	54,970	86,964
Temporarily restricted	32,903	53,453
Permanently restricted	26,615	26,842
Total net assets	<u>114,488</u>	<u>167,259</u>
Total liabilities and net assets	<u>\$ 161,140</u>	<u>\$ 219,587</u>

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

The McLean Hospital Corporation
Statements of Operations
Years Ended September 30, 2008 and 2007

<i>(dollars in thousands)</i>	2008	2007
Operating revenue		
Net patient service revenue	\$ 97,206	\$ 91,562
Direct academic and research revenue	37,103	36,798
Indirect academic and research revenue	11,620	12,818
Other revenue	<u>10,745</u>	<u>10,404</u>
Total operating revenue	<u>156,674</u>	<u>151,582</u>
Operating expenses		
Employee compensation and benefits	73,905	70,002
Supplies and other expenses	31,825	31,423
Direct academic and research expenses	37,103	36,798
Depreciation and amortization	6,014	5,029
Provision for bad debts	1,772	1,903
Interest	<u>1,196</u>	<u>1,122</u>
Total operating expenses	<u>151,815</u>	<u>146,277</u>
Income from operations	<u>4,859</u>	<u>5,305</u>
Nonoperating gains (expenses)		
Income (loss) from investments	(1,904)	7,308
Gifts and other	(71)	(352)
Academic and research gifts, net of expenses	-	292
System development funding	<u>-</u>	<u>(2,740)</u>
Total nonoperating gains (expenses), net	<u>(1,975)</u>	<u>4,508</u>
Excess of revenues over expenses	2,884	9,813
Other changes in net assets		
Funds utilized for property and equipment	3,705	2,028
Transfers (to) from affiliates, net	(38,179)	1
Change in funded status of defined benefit plan	<u>(404)</u>	<u>150</u>
Increase (decrease) in unrestricted net assets	<u>\$ (31,994)</u>	<u>\$ 11,992</u>

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

The McLean Hospital Corporation
Statements of Changes in Net Assets
Years Ended September 30, 2008 and 2007

<i>(dollars in thousands)</i>	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Net assets at October 1, 2006	\$ 74,972	\$ 44,225	\$ 26,757	\$ 145,954
Increases (decreases)				
Income from operations	5,305	-	-	5,305
Income from investments	7,308	8,719	-	16,027
Gifts and other	(352)	509	85	242
Academic and research gifts, net of expenses	292	-	-	292
System development funding	(2,740)	-	-	(2,740)
Funds utilized for property and equipment	2,028	-	-	2,028
Transfers from affiliates, net	1	-	-	1
Change in funded status of defined benefit plan	150	-	-	150
Change in net assets	<u>11,992</u>	<u>9,228</u>	<u>85</u>	<u>21,305</u>
Net assets at September 30, 2007	<u>86,964</u>	<u>53,453</u>	<u>26,842</u>	<u>167,259</u>
Increases (decreases)				
Income from operations	4,859	-	-	4,859
Loss from investments	(1,904)	(11,844)	-	(13,748)
Gifts and other	(71)	(1,767)	(227)	(2,065)
Funds utilized for property and equipment	3,705	-	-	3,705
Transfers to affiliates, net	(38,179)	(6,939)	-	(45,118)
Change in funded status of defined benefit plan	(404)	-	-	(404)
Change in net assets	<u>(31,994)</u>	<u>(20,550)</u>	<u>(227)</u>	<u>(52,771)</u>
Net assets at September 30, 2008	<u>\$ 54,970</u>	<u>\$ 32,903</u>	<u>\$ 26,615</u>	<u>\$ 114,488</u>

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

The McLean Hospital Corporation
Statements of Cash Flows
Years Ended September 30, 2008 and 2007

<i>(dollars in thousands)</i>	2008	2007
Cash flows from operating activities		
Change in net assets	\$ (52,771)	\$ 21,305
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Change in funded status of defined benefit plan	404	(150)
Depreciation and amortization	6,014	5,029
Provision for bad debts	1,772	1,903
Net realized and change in unrealized appreciation on investments	11,876	(17,440)
Change in interest in the net assets of The Massachusetts General Hospital	2,705	1,936
Transfers to (from) affiliates, net	45,118	(1)
Restricted contributions	(3,850)	(3,634)
Increase (decrease) in cash resulting from a change in		
Patient accounts receivable	(1,800)	(2,413)
Research grants receivable	(3,260)	(2,903)
Other current assets	(425)	(435)
Pledges receivable	1,155	1,120
Increase in other assets	(568)	-
Accounts payable and accrued expenses	(1,073)	(1,731)
Accrued compensation and benefits	624	920
Accrual for settlements with third-party payers	(933)	983
Unexpended funds on research grants	(76)	(2,166)
Accrued employee benefits and other	(582)	263
Due to affiliates	(609)	635
Net cash provided by operating activities	<u>3,721</u>	<u>3,221</u>
Cash flows from investing activities		
Purchase of property and equipment	(10,728)	(11,180)
Purchase of investments	(7,229)	(27,575)
Proceeds from sales of investments	13,063	30,153
Net cash used for investing activities	<u>(4,894)</u>	<u>(8,602)</u>
Cash flows from financing activities		
Payments on long-term obligations	(3,332)	(2,529)
Proceeds from long-term obligations	-	5,277
Transfers from (to) affiliates	(7,899)	1
Restricted contributions	3,850	3,634
Net cash (used for) provided by financing activities	<u>(7,381)</u>	<u>6,383</u>
Net (decrease) increase in cash and equivalents	(8,554)	1,002
Cash and equivalents at beginning of year	8,700	7,698
Cash and equivalents at end of year	<u>\$ 146</u>	<u>\$ 8,700</u>

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

The McLean Hospital Corporation

Notes to Financial Statements

September 30, 2008 and 2007

(dollars in thousands)

1. Organization

The McLean Hospital Corporation (McLean) operates a psychiatric hospital established to provide healthcare services to patients primarily from the Greater Boston area as well as New England and beyond. In addition, McLean conducts research and provides education for physicians and other healthcare professionals. As such, operating revenue includes those generated from direct patient care and reimbursement of research and educational activities. McLean HealthCare, Inc. (MHC) is the sole member of McLean.

The Massachusetts General Hospital (MGH) is the sole member of MHC, The General Hospital Corporation, Inc. (General), Massachusetts General Physicians Organization, Inc., Nantucket Cottage Hospital, Martha's Vineyard Hospital, The MGH Institute of Health Professions, Inc. and The MGH Health Services Corporation.

Partners HealthCare System, Inc. (PHS) is the sole member of MGH, Brigham and Women's/Faulkner Hospitals, Inc., NSMC HealthCare Inc., Newton-Wellesley Health Care System, Inc., Partners Continuing Care, Inc., Partners Harvard Medical International, Inc. and Partners International Medical Services, LLC. PHS appoints the two physicians who are the members of Partners Community HealthCare, Inc. PHS, together with all of its affiliates, is referred to as "Partners HealthCare."

McLean and its parent are tax-exempt organizations under Section 501(c)(3) of the Internal Revenue Code.

2. Summary of Significant Accounting Policies

Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting. McLean follows the accounting policies and practices of PHS and these statements should be read in conjunction with the Partners HealthCare consolidated financial statements.

Use of Estimates

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

Fair Value of Financial Instruments

The fair value of financial instruments approximates the carrying amount reported in the balance sheets for cash and equivalents, investments, investments limited as to use, interest in the net assets of MGH, patient accounts receivable, research grants receivable, pledges receivable and accounts payable, except for long-term obligations which is disclosed in Note 7.

The McLean Hospital Corporation

Notes to Financial Statements

September 30, 2008 and 2007

(dollars in thousands)

Cash and Equivalents

Cash and equivalents represent money market and highly liquid debt instruments with a maturity at the date of purchase of three months or less.

Investments

McLean holds investments which represent units in a partnership (Note 4) and are recorded on the equity method of accounting, with the change in net unrealized appreciation included in excess of revenues over expenses as a component of income from investments. Separately invested investments (marketable investments) are measured at fair value, generally based on quoted market prices, with the change in net unrealized appreciation excluded from excess of revenues over expenses.

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

Investments with unrealized depreciation are reviewed each quarter to determine whether these investments are other-than-temporarily impaired. This review considers factors including the anticipated holding period for the investment and the extent and duration of below cost valuation.

A write-down in the cost basis of securities is recorded when the decline in fair value of certain investments below costs has been judged to be other-than-temporary. Depending on any donor-imposed restrictions on the underlying investments, the amount of the write-down is reported as a realized loss in either temporarily restricted net assets or in excess of revenues over expenses as a component of income from investments, with no adjustment in the cost basis for subsequent recoveries in fair value.

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

Investments Limited as to Use

Investments limited as to use primarily include assets whose use is contractually limited by external parties and assets set aside by the Board of Trustees (or management) for identified purposes, over which the Board (or management) retains control and may, at its discretion, subsequently use for other purposes. Certain investments corresponding to deferred compensation are accounted for such that all income and appreciation (depreciation) is recorded as a direct addition (reduction) to the asset balance and corresponding liability balance.

Patient Accounts Receivable

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

The McLean Hospital Corporation

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(dollars in thousands)

Research Grants Receivable

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

Interest in the Net Assets of The Massachusetts General Hospital

MGH holds investment assets for the benefit of McLean. Due to the corporate relationship between MGH, MHC and McLean, these organizations are all financially interrelated. Accordingly, McLean recognizes its interest in the net assets of MGH and adjusts that interest for its share of the change in the net assets of MGH. Changes due to gifts, investment income (including realized gains and losses) and unrealized appreciation are recognized in nonoperating activity.

Property and Equipment

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

Asset Retirement Obligations

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

Other Assets

Other assets consist of benefit assets for overfunded defined benefit plans.

Compensated Absences

In accordance with formal policies concerning vacation and other compensated absences, accruals of approximately \$3,560 and \$3,398 were recorded as of September 30, 2008 and 2007, respectively.

Unexpended Funds on Research Grants

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

The McLean Hospital Corporation

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September 30, 2008 and 2007

(dollars in thousands)

Self-Insurance Reserves

McLean is self-insured for employee healthcare, workers' compensation and certain other employee benefits. These costs are accounted for on an accrual basis to include estimates of future payments for claims incurred.

Net Assets

Permanently restricted net assets include only the historical dollar amounts of gifts which are required by donors to be permanently retained. Temporarily restricted net assets include gifts, and income and gains on permanently restricted net assets which can be expended but for which restrictions have not yet been met. Such restrictions include purpose restrictions where donors have specified the purpose for which the net assets are to be spent, or time restrictions imposed by donors or implied by the nature of the gift (capital projects, pledges to be paid in the future, life income funds) or by interpretations of law (gains available for appropriation but not appropriated in the current period). Unrestricted net assets include all the remaining net assets of McLean. See Note 13 for further information on the composition of restricted net assets.

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

Gifts and Grants

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

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

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

Statements of Operations

All activities of McLean deemed by management to be ongoing, major and central to the provision of healthcare services, training and research activities are reported as operating revenue and expenses. Other activities are deemed to be nonoperating and include unrestricted gifts (net of fund-raising expenses), net change in unexpended academic and research gifts, substantially all income from investments and system development funding. System development funding represents payments made to PHS for corporate expenses and to support clinical and other initiatives provided by PHS for the benefit of Partners HealthCare. Academic and research gifts

The McLean Hospital Corporation

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September 30, 2008 and 2007

(dollars in thousands)

largely consist of donor contributions (and the related investment income including realized gains and losses) designated to support the clinical, teaching or research efforts of a physician or department as directed by the donor. These gifts are reported as unrestricted support as any donor restrictions are of a general nature that are inherent in the normal activities of the organization and do not require classification of these gifts as temporarily or permanently restricted.

McLean recognizes changes in third-party payer settlements and other estimates in the year of the change in estimate. For the years ended September 30, 2008 and 2007, adjustments to prior year estimates resulted in an increase to income from operations of \$888 and \$1,733, respectively.

The statements of operations include excess of revenues over expenses. Changes in unrestricted net assets which are excluded from excess of revenues over expenses include change in unrealized appreciation on marketable investments, transfers of assets to and from affiliates, contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for acquisition of such assets) and change in funded status of the defined benefit plan.

Net Patient Service Revenue

McLean maintains agreements with the Centers for Medicare and Medicaid Services (CMS) of the United States Department of Health and Human Services (DHHS) under the Medicare Program, The Commonwealth of Massachusetts under the Medical Assistance Program (Medicaid) and various managed care payers that govern payment to McLean for services rendered to patients covered by these agreements. The agreements generally provide for payments based on allowable costs, subject to certain limitations, or per diem rates for inpatient care and fee schedules for outpatient care.

Net patient service revenue is reported at estimated net realizable amounts from patients, third-party payers, and others for services rendered and includes estimated retroactive revenue adjustments due to future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations. Contracts, laws and regulations governing the Medicare and Medicaid programs and managed care payer arrangements are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

Charity Care

McLean provides either full or partial charity care to patients who cannot afford to pay for their medical services based on income and family size. Charity care is reported at gross charges with an offsetting allowance, as there is no expectation of collection. Accordingly, there is no net patient service revenue related to charity care.

Other Revenue

Other revenue primarily consists of institutional revenue (for example, billing for services provided to other healthcare providers) and tuition revenue.

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

Reclassifications

Certain amounts in the 2007 financial statements have been classified to conform with the 2008 presentation. Direct academic and research revenue and direct academic research expenses have been reduced by \$408 for the year ended September 30, 2007 to reflect the elimination of intercompany research activity.

3. Investment Transfer

Effective October 1, 2007, the Board of Trustees of McLean approved the permanent transfer of substantially all unrestricted investments to its parent, MHC. In addition, in conjunction with this board resolution, all system development funding (Note 2) has become the responsibility of MHC. As a result, substantially all unrestricted investments, related investment income, gifts and expenses, and all system development funding have been eliminated on McLean's financial statements as of and for the year ended September 30, 2008. McLean has accounted for this transaction as a net asset transfer in fiscal 2008. The impact of this transfer was to reduce investments and unrestricted net assets by \$37,219. Had these changes been made as of October 1, 2006, investments and unrestricted net assets would have been reduced by \$31,556. In the statement of operations, the excess of revenues over expenses and the increase in unrestricted net assets would have been reduced by \$3,107 for the year ended September 30, 2007. The individual financial statement line items that would have been impacted in 2007 are the following:

	As Reported	Pro Forma
Income from operations	\$ 5,305	\$ 5,305
Nonoperating gains (expenses)		
Income from investments	7,308	1,669
Gifts and other	(352)	(268)
Academic and research gifts, net of expenses	292	-
System development funding	<u>(2,740)</u>	<u>-</u>
Excess of revenues over expenses	<u>\$ 9,813</u>	<u>\$ 6,706</u>

Temporarily and permanently restricted investments, as well as externally limited investments, will continue to be included in the financial statements of McLean.

4. Investments and Investments Limited as to Use

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

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(dollars in thousands)

The Partnership participates in a securities lending program with its custodian bank whereby securities are loaned to qualified financial institutions in exchange for collateral. Investments that have been loaned to another institution are reported as pledged assets in the consolidated balance sheets of Partners HealthCare. Cash or investments received as collateral on the securities lending transaction are also reported as assets in such consolidated balance sheets. Because the collateral must be returned in the future, a corresponding liability is reported in such consolidated balance sheets.

The composition of investments and investments limited as to use is as follows:

	September 30, 2008			
	Cost	Gross Unrealized Appreciation	Gross Unrealized Depreciation	Fair Value
Pooled investments				
Invested cash equivalents	\$ 333	\$ -	\$ -	\$ 333
Equities	2,924	22	(267)	2,679
U.S. Government, domestic and foreign fixed income securities	1,691	20	(114)	1,597
Private partnerships and other	4,988	154	(176)	4,966
Accruals, net	12	-	-	12
	<u>9,948</u>	<u>196</u>	<u>(557)</u>	<u>9,587</u>
Separately invested				
Invested cash equivalents	557	-	-	557
Equities	982	-	-	982
U.S. Government and domestic fixed income securities	892	-	-	892
	<u>2,431</u>	<u>-</u>	<u>-</u>	<u>2,431</u>
	<u>\$ 12,379</u>	<u>\$ 196</u>	<u>\$ (557)</u>	<u>\$ 12,018</u>

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

		September 30, 2007		
	Cost	Gross Unrealized Appreciation	Gross Unrealized Depreciation	Fair Value
Pooled investments				
Invested cash equivalents	\$ 2,845	\$ -	\$ -	\$ 2,845
Equities	11,550	2,850	-	14,400
U.S. Government, domestic and foreign fixed income securities	16,084	319	(61)	16,342
Private partnerships and other	13,309	4,726	(33)	18,002
Accruals, net	187	-	-	187
	<u>43,975</u>	<u>7,895</u>	<u>(94)</u>	<u>51,776</u>
Separately invested				
Invested cash equivalents	661	-	-	661
Equities	1,731	-	-	1,731
U.S. Government and domestic fixed income securities	903	-	-	903
	<u>3,295</u>	<u>-</u>	<u>-</u>	<u>3,295</u>
	<u>\$ 47,270</u>	<u>\$ 7,895</u>	<u>\$ (94)</u>	<u>\$ 55,071</u>

Subsequent to September 30, 2008, the U.S. and global financial markets have experienced significant volatility and illiquidity, due in part, to current economic conditions and declines in the financial sector. McLean's investment portfolio has experienced similar negative volatility. However, McLean has been able to maintain its liquidity and its operations have not been significantly impacted.

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

	September 30,	
	2008	2007
Current assets		
Investments	\$ -	\$ 11,189
Current portion of investments limited as to use	<u>8,378</u>	<u>16,158</u>
	8,378	27,347
Investments limited as to use, less current portion	2,431	19,185
Long-term investments	<u>1,209</u>	<u>8,539</u>
	<u>\$ 12,018</u>	<u>\$ 55,071</u>

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

Investments limited as to use consist of the following:

	September 30, 2008		September 30, 2007	
	Current Portion	Long-Term Portion	Current Portion	Long-Term Portion
Internally designated funds				
Reserve for capital expenditures	\$ -	\$ -	\$ 4,466	\$ -
Unexpended academic and research gifts	-	-	-	13,048
Deferred compensation	-	2,321	-	3,016
Other	-	-	4,045	2,844
	<u>-</u>	<u>2,321</u>	<u>8,511</u>	<u>18,908</u>
Externally limited funds				
Unexpended funds on research	7,069	-	7,145	-
Contributions held for others	1,309	-	502	-
Held by trustees under debt and other agreements	-	110	-	277
	<u>\$ 8,378</u>	<u>\$ 2,431</u>	<u>\$ 16,158</u>	<u>\$ 19,185</u>

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

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

	Years Ended September 30,	
	2008	2007
Unrestricted		
Dividends and interest income	\$ 278	\$ 1,178
Endowment income distributions, net of reinvested gains	281	2,322
Net realized gains (losses) on investments		
Trading gains	196	2,373
Other-than-temporary impairment	(15)	(289)
Change in net unrealized appreciation on equity method investments	(1,907)	5,172
Losses on endowment funds	(29)	-
Total unrestricted investment activity	<u>(1,196)</u>	<u>10,756</u>
Temporarily restricted		
Dividends and interest income	790	857
Endowment income distributions	(2,513)	(2,322)
Net realized gains (losses) on investments		
Trading gains	1,072	2,750
Other-than-temporary impairment	(5)	(121)
	<u>(656)</u>	<u>1,164</u>
Change in net unrealized appreciation on equity method investments	(11,217)	7,555
Losses on endowment funds	29	-
Total temporarily restricted investment activity	<u>(11,844)</u>	<u>8,719</u>
	<u>\$ (13,040)</u>	<u>\$ 19,475</u>

Investment income (loss) included in operating results and excess of revenues over expenses are comprised of the following:

	Years Ended September 30,	
	2008	2007
Investment income (loss) included in operations and reported in		
Other revenue	\$ 708	\$ 649
Investment income (loss) included in nonoperating gains (expenses) and reported in		
Income (loss) from investments	(1,904)	7,308
Academic and research gifts, net of expenses	-	2,799
Total investment activity included in excess of revenues over expenses	<u>(1,196)</u>	<u>10,756</u>

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

5. Pledges Receivable

Pledges receivable represent unconditional promises to give and are net of allowances for uncollectible amounts. Pledges are recorded at the present value of their estimated future cash flows. Pledges collectible within one year are classified as other current assets and total \$976 and \$1,508 as of September 30, 2008 and 2007, respectively. Estimated cash flows due after one year are discounted using published treasury bond and note yields that are commensurate with estimated collection risks. The blended discount rate was 2.1% and 4.1% for 2008 and 2007, respectively. Pledges are expected to be collected as follows:

	September 30,	
	2008	2007
Amounts due		
Within one year	\$ 1,268	\$ 1,808
In one to five years	1,681	2,482
In more than five years	<u>10</u>	<u>20</u>
Total pledges receivable	2,959	4,310
Less: Unamortized discount	<u>87</u>	<u>259</u>
	2,872	4,051
Less: Allowance for uncollectibles	<u>322</u>	<u>346</u>
Net pledges receivables	<u>\$ 2,550</u>	<u>\$ 3,705</u>

6. Property and Equipment

Property and equipment consists of the following:

	September 30,	
	2008	2007
Land and land improvements	\$ 5,122	\$ 1,550
Buildings and building improvements	92,148	87,443
Equipment	17,484	11,977
Construction in progress	<u>6,402</u>	<u>10,131</u>
	121,156	111,101
Accumulated depreciation	<u>(60,853)</u>	<u>(55,512)</u>
Property and equipment, net	<u>\$ 60,303</u>	<u>\$ 55,589</u>

For the years ended September 30, 2008 and 2007, fully depreciated assets with an original cost of \$673 and \$6,808, respectively, were written off.

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

In 2005, McLean sold 26.2 acres of land to Northland Development Company for \$14,376 and recorded a net gain of \$10,567. McLean has also executed purchase and sale agreements to sell 24.7 acres of land for development of a senior housing community and a research and development facility. The sale is subject to a number of conditions.

7. Long-Term Obligations

Long-term obligations consist of the following:

	September 30,	
	2008	2007
Note payable to PHS		
Partners HealthCare Capital Framework Loan, variable interest rate of 4.88% and 5.10% at September 30, 2008 and 2007, respectively, final maturity in 2015	\$ 22,835	\$ 26,167
Less current portion	<u>3,463</u>	<u>3,332</u>
	<u>\$ 19,372</u>	<u>\$ 22,835</u>

The Partners HealthCare Capital Framework Loan bears interest at a variable rate based upon the weighted average cost of Partners HealthCare's debt, reset annually, effective October 1.

Aggregate maturities and payments of long-term obligations during the next five years are as follows: 2009 - \$3,463; 2010 - \$3,636; 2011 - \$3,160; 2012 - \$3,325 and 2013 - \$3,499.

Long-term obligations have variable interest rates that reflect currently available terms and conditions for similar debt. The carrying amounts for this debt is a reasonable estimate of its fair value.

Interest expense approximates interest paid during the years ended September 30, 2008 and 2007.

8. Leases

McLean has noncancelable operating leases for certain equipment and a building. Rental expense under these and other contracts approximated \$772 and \$999 in 2008 and 2007, respectively. Minimum future lease commitments under noncancelable leases are as follows:

	Operating Leases
2009	\$ 189
2010	70
2011	<u>6</u>
	<u>\$ 265</u>

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

9. Pension and Postretirement Healthcare Plans

Pension Plan

Substantially all employees of MGH and its affiliates are covered under The Massachusetts General Hospital Cash Balance Retirement Plan (MGH Plan), a noncontributory defined benefit plan. Benefits under the MGH Plan consist of annual allocations to participants' accounts based on the participants' employer, age, years of service and salary. Interest is credited to participants' accounts annually at market rates.

Pension expense under the MGH Plan for all affiliates amounted to \$62,106 in 2008 and \$67,026 in 2007. The amount of pension expense allocated to McLean was \$4,099 in 2008 and \$3,952 in 2007.

Postretirement Healthcare Benefit Plan

McLean also provides subsidized healthcare benefits for qualified retired employees on a self-insured basis. These benefits are administered through an insurance company and are accounted for on the accrual basis, which includes an estimate of future payments for claims incurred. McLean uses a measurement date of June 30 for the postretirement healthcare benefit plan.

Benefit Obligation

Change in Benefit Obligation	2008	2007
Benefit obligation at beginning of year	\$ 4,214	\$ 4,165
Service cost	1	2
Interest cost	247	245
Actuarial (gain) loss	(260)	302
Benefits paid	<u>(511)</u>	<u>(500)</u>
Benefit obligation at end of year	<u>\$ 3,691</u>	<u>\$ 4,214</u>

Weighted-Average Assumptions Used to Determine End of Year Benefit Obligation

	2008	2007
Discount rate	5.75%	6.25%
Healthcare cost trend rate for next year	9.00%	9.00%
Rate to which the cost trend rate is to decline	5.00%	5.00%
Year that rate reaches the ultimate trend rate	2017	2012

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

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on postretirement benefit obligation	\$ 148	\$ (136)

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

Plan Assets

Change in Plan Assets	2008	2007
Fair value of plan assets at beginning of year	\$ 4,883	\$ 4,689
Actual return on plan assets	(367)	738
Net employer contributions (disbursements)	25	(44)
Benefits paid	<u>(511)</u>	<u>(500)</u>
Fair value of plan assets at end of year	<u>\$ 4,030</u>	<u>\$ 4,883</u>

Subsequent to June 30, 2008 (measurement date), there has been significant volatility and illiquidity in the U.S. and global financial markets which has had a significant negative effect on the valuation of plan assets. However, McLean is able to meet the obligations of the plans with existing plan assets or any additional contributions as may be required under federal pension regulations.

McLean's benefit plan weighted-average target asset allocation ranges as well as actual allocations by asset category for 2008 and 2007 are as follows:

Asset Category	Target Allocation	Percentage of Plan Assets	
		2008	2007
Domestic equity securities	40% - 60%	47.3%	50.4%
Foreign equity securities	10% - 30%	24.3%	24.9%
Fixed income securities	30% - 50%	28.4%	24.7%
	<u>100%</u>	<u>100%</u>	<u>100%</u>

The investment objective is to achieve the highest reasonable total return after considering (i) plan liabilities, (ii) funding status and projected cash flows, (iii) projected market returns, valuations and correlations for various asset classes, and (iv) Partners' ability and willingness to incur market risk.

Funded Status

In September 2006, the Financial Accounting Standards Board issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* (SFAS 158). SFAS 158 focuses primarily on balance sheet reporting for the funded status of benefit plans and requires recognition of benefit liabilities for under-funded plans and benefit assets for over-funded plans, with offsetting impacts to unrestricted net assets.

SFAS 158 also requires companies to measure benefit plan assets and liabilities and determine the discount rate for subsequent year expense recognition as of the balance sheet date for financial reporting purposes, thus eliminating the opportunity to use a measurement date up to 90 days prior to the balance sheet date. The effective date for this change is 2009. McLean currently uses a June 30 measurement date and will adopt a September 30 measurement date in 2009 as required. Converting to the new measurement date will require a one-time adjustment to unrestricted net assets per the transition guidance in SFAS 158.

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

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

End of Year	2008	2007
Fair value of plan assets at measurement date	\$ 4,030	\$ 4,883
Net contributions (disbursements) recorded after measurement date	130	(364)
Benefit obligation at measurement date	<u>(3,691)</u>	<u>(4,214)</u>
Funded status	<u>\$ 469</u>	<u>\$ 305</u>
Amounts recognized in the balance sheet consist of:		
Noncurrent assets	\$ 469	\$ 305
Amounts recognized in unrestricted net assets consist of:		
Actuarial net loss	\$ 1,347	\$ 943

Expected Cash Flows

Information about the expected cash flows for the postretirement healthcare benefit plan are as follows:

Expected employer contributions 2008	\$ 436	
	Gross Benefit Payments	Medicare Subsidy
Expected benefit payments (receipts)		
2009	\$ 479	\$ (43)
2010	480	(42)
2011	470	(41)
2012	452	(40)
2013	428	(38)
2014 and thereafter	1,750	(151)

Net Periodic Benefit Cost	2008	2007
Service cost	\$ 1	\$ 2
Interest cost	247	245
Expected return on plan assets	(347)	(352)
Amortization of actuarial net loss	50	66
Net periodic benefit cost (benefit)	<u>\$ (49)</u>	<u>\$ (39)</u>

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

The actuarial net loss of McLean for the retirement healthcare benefit plan that will be amortized from unrestricted net assets into net periodic benefit cost in 2009 is \$106.

Weighted-Average Assumptions Used to Determine Net Periodic Cost	2008	2007
Discount rate	6.25%	6.25%
Expected return on plan assets	7.50%	7.50%
Healthcare cost trend rate for this year	9.00%	9.00%
Rate to which the cost trend rate is to decline	5.00%	5.00%
Year that rate reaches the ultimate trend rate	2012	2011

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

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on service and interest cost	\$ 11	\$ (10)

10. Professional Liability Insurance

McLean insures substantially all of its professional and general liability risk on a claims-made basis in cooperation with PHS affiliates and other organizations in the Greater Boston area through a captive insurance company, Controlled Risk Insurance Company Ltd. (CRICO). The policy covers claims made during its term, but not those occurrences for which claims may be made after expiration of the policy, except for certain tail liabilities which CRICO has assumed on an occurrence basis through December 31, 2008. Management intends to renew its coverage on a claims-made basis and has no reason to believe that it will be prevented from such renewal.

McLean follows the accounting policy of establishing reserves to cover all professional liability claims incurred but not reported to the insurance company as of the end of the year (tail liability), excluding the tail liability assumed by CRICO. These reserves have been estimated by consulting actuaries on a discounted basis using an interest rate of 5.75% at September 30, 2008 and 2007.

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

11. Transactions with Affiliated Corporations

McLean received fund-raising, investment management, legal, financial and administrative services from PHS and affiliates. These services are reimbursed on an estimated cost basis and amounted to \$11,406 in 2008 and \$13,940 in 2007. McLean received salary and other expense reimbursements from PHS of \$374 in 2008 and \$346 in 2007.

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

During 2008 and 2007, McLean received net funds from PHS. These equity transfers are reported separately as changes in net assets and are excluded from excess of revenues over expenses. Amounts transferred were as follows:

	Years Ended September 30,	
	2008	2007
Transfers from (to)		
MHC	\$ (7,899)	\$ -
PHS	-	1
	<u>(7,899)</u>	<u>1</u>
Investment transfer to MHC (Note 3)	<u>(37,219)</u>	<u>-</u>
	<u>\$ (45,118)</u>	<u>\$ 1</u>

12. Concentration of Credit Risk

Financial instruments that potentially subject McLean to concentration of credit risk consist of patient accounts receivable, research grants receivable, pledges receivable and certain investments. McLean receives a significant portion of its payments for services rendered from a limited number of government and commercial third-party payers, including Medicare, Medicaid, Blue Cross and Blue Shield of Massachusetts, Harvard Pilgrim Health Care and Tufts Associated Health Plan. Research funding is provided through many government and private sponsors. Pledges receivable are due from multiple donors. McLean considers the credit risk for pledges to be minimal based on history and the financial wherewithal of donors, most of which are individuals or organizations well known to the hospital. Investments, which include government and agency securities, stocks and corporate bonds, and private partnerships and other investments are not concentrated in any corporation or industry or with any single counterparty.

13. Restricted Net Assets

Restricted net assets are available for the following purposes:

	September 30,	
	2008	2007
Temporarily restricted		
Charity care	\$ 4,916	\$ 6,051
Buildings and equipment	1,430	7,037
Clinical care, research and academic	<u>26,557</u>	<u>40,365</u>
	<u>\$ 32,903</u>	<u>\$ 53,453</u>
Permanently restricted		
Charity care	\$ 456	\$ 454
Clinical care, research and academic	<u>26,159</u>	<u>26,388</u>
	<u>\$ 26,615</u>	<u>\$ 26,842</u>

The McLean Hospital Corporation
Notes to Financial Statements
September 30, 2008 and 2007

(dollars in thousands)

14. Functional Expenses

Total operating expenses by function are as follows:

	Years Ended September 30,	
	2008	2007
Healthcare services	\$ 89,925	\$ 82,726
Research and academic	48,723	49,616
General and administrative	13,167	13,935
	<u>\$ 151,815</u>	<u>\$ 146,277</u>

15. Contingencies

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

The McLean Hospital Corporation

Schedule of Expenditures of Federal Awards

Year Ended September 30, 2008

	Federal CFDA Number	Pass-Through Number	Total Federal Expenditures
RESEARCH AND DEVELOPMENT AND RESEARCH TRAINING CLUSTER			
Research and Development Direct Programs			
Department of Health and Human Services			
National Institutes of Health			
National Institute on Deafness & Other Communication Disorders	93.173		\$ 149,011
National Center for Complementary & Alternative Medicine	93.213		1,131,563
Mental Health Research Grant	93.242		8,716,377
Alcohol Research Programs	93.273		276,535
Drug Abuse Research Programs	93.279		10,077,910
Drug Abuse Research Programs	93		972,909
National Center for Research Resources	93.389		(104)
Neurological Disorders Research	93.853		3,304,091
Child Health and Human Development	93.865		436,905
Aging Research	93.866		129,009
Subtotal - Department of Health and Human Services			<u>25,194,206</u>
Department of Defense			
Military Medical Research and Development	12.420		<u>1,098,767</u>
Subtotal - Department of Defense			<u>1,098,767</u>
National Science Foundation			
Education and Human Resources	47.076		<u>283,794</u>
Subtotal - National Science Foundation			<u>283,794</u>
Total Research and Development Direct Programs			<u>26,576,767</u>
Research and Development Passed Through Other Organizations			
Department of Health and Human Services			
National Institutes of Health			
Albany Medical College	93.213	5R21 AT003371-02	71,656
Bedford VA Research Corporation, Inc.	93.866	5R01 AG020654-05	242,091
Beth Israel Deaconess Medical Center	93.156	1D01 HP05057-01	(28,215)
Beth Israel Deaconess Medical Center	93.242	1P50 MH080272-01	121,974
Brigham and Women's Hospital, Inc.	93.273	1 R01 AA016318-01	108,568
Eagle Vision Pharmaceutical Corporation	93.848	5R43 DK076429	55,884
Harvard Medical School	93.156	6 D01 HP000002-01-03	(35,641)
Harvard Medical School	93.242	5P50 MH60450-02	(119)
Harvard Medical School	93.242	R01 MH040799	186,494
Harvard University Center for AIDS Research	93.855	P30 AI060354	13,440
Joslin Diabetes Center	93.847	5 R01 DK60754	37,038
Joslin Diabetes Center	93.847	1 R01 DK073843-01A2	138,247
Massachusetts General Hospital	93.279	1 R01 DA022276-01	79,902
Massachusetts General Hospital	93.279	5 U01 DA019378-02	71,547
McGill University	93.242	N01MH90002	(1)
MyNeuroLab.com	93.853	1 R43 NS055600-01	10,650
Natural Pharmacia International	93.273	2 R44 AA01522-03A2	38,850
Molecular NeuroImaging, LLC.	93.242	1 R43 MH71022	(923)
Research Foundation for Mental Hygiene	93.242	N01MH60012	(23,983)
Research Foundation for Mental Hygiene	93.866	2R01AG016381-06	57,375
Research Foundation for Mental Hygiene	93.866	P01 AG017617-05	101,108
University of Chicago	93.279	R01 DA017323-02	79,024

The McLean Hospital Corporation
Schedule of Expenditures of Federal Awards
Year Ended September 30, 2008

	Federal CFDA Number	Pass-Through Number	
University of Chicago	93.279	R01 DA014644-06	\$ 31,930
University of Cincinnati	93.846	1R01 AR053207-01A2	24,726
University of Maryland	93.213	5 P01 AT0026050-02	42,318
University of Texas Southwestern Medical	93.242	5 P50 MH066172-06	155,307
University of Texas Southwestern Medical	93.279	5 P01 DA008227-16	57,675
University of Utah	93.242	1 R01 MH080826-01	27,606
Subtotal - Department of Health and Human Services			<u>1,664,528</u>
Department of Defense			
Military Medical Research and Development			
The Michael Stern Parkinson's Research Foundation	12.420	W81XWH-05-1-0555	2,370,799
Massachusetts General Hospital	12.420	W81XWH-07-2-0011	20,316
Massachusetts General Hospital	12.420	W81XWH-08-2-0126	32
Subtotal - Department of Defense			<u>2,391,147</u>
Department of Education			
Southwest Educational Development Laboratory	84.133	ED-03-CO-0048	45,517
Subtotal - Department of Education			<u>45,517</u>
National Science Foundation			
The Exploratorium	47.076	ESI-0639656	3,838
Subtotal - National Science Foundation			<u>3,838</u>
Total Research and Development Pass-Through Programs			<u>4,105,030</u>
Total Research and Development			<u>30,681,797</u>
Research Training Direct Programs			
Department of Health and Human Services			
National Institutes of Health			
Alcohol Research Career Development Awards	93.271		111,985
Drug Abuse Research Programs	93.278		9,315
Drug Abuse Research Service Awards	93.277		470,897
Mental Health Research Career/Scientist Development Awards	93.281		419,131
Mental Health Research Grants	93.242		188,432
Extramural Research Programs in the Neurosciences and Neurological Disorders	93.853		20,471
Drug Abuse and Addiction Research Programs	93.279		1,333,242
Subtotal - Department of Health and Human Services			<u>2,553,473</u>
Total Research Training Direct Programs			<u>2,553,473</u>
Research Training Passed Through Other Organizations			
Department of Health and Human Services			
National Institute of Health			
Harvard Medical School	93.121	5K12 DE014528	(107)
Harvard Medical School	93.242	5T32 MH016259-28	159,009
Harvard Medical School	93.282	2T32 MH016259-29	13,667
Harvard Medical School	93.866	5T32 AG000222	47,470
Subtotal - Department of Health and Human Services			<u>220,039</u>
Total Research Training Pass-Through Programs			<u>220,039</u>
Total Research Training			<u>2,773,512</u>
Total Research and Development and Research Training Cluster			<u>33,455,309</u>
Total Federal Expenditures			<u>\$ 33,455,309</u>

The McLean Hospital Corporation
Notes to Schedule of Expenditures of Federal Awards
September 30, 2008

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant transactions of The McLean Hospital Corporation (the "Hospital") recorded on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in or used in the preparation of the basic financial statements. Negative amounts represent adjustments to amounts reported as expenditures in prior years. Pass-through numbers are provided where available.

2. Facilities and Administrative Costs

The predetermined facilities and administrative cost rates were based on financial information submitted utilizing the method prescribed in OASC-3. The Hospital negotiated and was awarded a predetermined facilities and administrative cost rate of 61% for the period October 1, 2007 through September 30, 2008 for research and development. The Hospital also was awarded a fixed fringe benefit rate of 29% for the period October 1, 2007 through September 30, 2008.

3. Subrecipients

During fiscal 2008, the Hospital provided to subrecipients in the Research and Development and Research Training Cluster \$2,979,073, as follows. These amounts are included in the accompanying Schedule of Expenditures of Federal Awards:

Adcare Hospital	\$ 19,438
Autism Speaks	224,210
Beth Israel Deaconess Hospital	73,767
Boston University	262,421
Brandeis University	294,479
Brown University	3,439
Cab Health and Recovery Services	20,239
Exploratorium	15,098
Massachusetts General Hospital	684,951
Mercy Hospital	5,731
Northeastern University	17,193
Research Foundation Mental Hygiene	161,753
Research Foundation of the State University of New York	31,134
Reginald Clark and Associates	32,625
Stanley Street Treatment Resources	346,254
Temple University	171,357
Tufts University	3,845
University of California	42,858
University of North Carolina	116,569
University of Rochester	119,669
University of Stellenbosch	65,060
University of Texas	149,983
Wellesley College	117,000
	<u>\$ 2,979,073</u>

Part II

Reports on Compliance and Internal Controls

**Report of Independent Auditors on Internal Control over Financial Reporting and on
Compliance and Other Matters Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards***

To the Board of Trustees of
The McLean Hospital Corporation

We have audited the financial statements of The McLean Hospital Corporation as of and for the year ended September 30, 2008 and have issued our report thereon dated December 19, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered The McLean Hospital Corporation's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of The McLean Hospital Corporation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of The McLean Hospital Corporation's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control

that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether The McLean Hospital Corporation's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of The McLean Hospital Corporation in a separate letter dated December 17, 2008.

This report is intended solely for the information and use of The McLean Hospital Corporation's Board of Trustees, management, federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "PricewaterhouseCoopers LLP".

December 19, 2008

**Report of Independent Auditors on Compliance with Requirements
Applicable to Each Major Program and on Internal Control over Compliance
in Accordance with OMB Circular A-133**

To the Board of Trustees of
The McLean Hospital Corporation

Compliance

We have audited the compliance of The McLean Hospital Corporation with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2008. The McLean Hospital Corporation's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of The McLean Hospital Corporation's management. Our responsibility is to express an opinion on The McLean Hospital Corporation's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about The McLean Hospital Corporation's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of The McLean Hospital Corporation's compliance with those requirements.

In our opinion, The McLean Hospital Corporation complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2008.

Internal Control over Compliance

The management of The McLean Hospital Corporation is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered The McLean Hospital Corporation's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly we do not express an opinion on the effectiveness of The McLean Hospital Corporation's internal control over compliance.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of The McLean Hospital Corporation's Board of Trustees, management, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

The logo for PricewaterhouseCoopers LLP, written in a cursive script.

December 19, 2008

Part III
Findings

The McLean Hospital Corporation
Schedule of Findings and Questioned Costs
Year Ended September 30, 2008

I. Summary of Auditor's Results

Financial Statements

Type of auditor's report issued	Unqualified
Internal control over financial reporting	
Material weakness(es) identified?	___ yes <u>X</u> no
Significant deficiency(ies) identified that are not considered to be material weaknesses?	___ yes <u>X</u> none reported
Noncompliance material to financial statements noted?	___ yes <u>X</u> no

Federal Awards

Internal control over major programs	
Material weakness(es) identified?	___ yes <u>X</u> no
Significant deficiency(ies) identified that are not considered to be material weaknesses?	___ yes <u>X</u> none reported
Type of auditor's report issued on compliance for major programs	Unqualified
Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133?	___ yes <u>X</u> no

Identification of Major Programs

Name of Federal Program or Cluster

Various CFDA numbers	Research and Development and Research Training Cluster
Dollar threshold used to distinguish between Type A and Type B programs	\$1,003,659
Auditee qualified as low-risk auditee?	<u>X</u> yes ___ no

II. Financial Statement Findings

There were no findings noted in the current year.

III. Federal Award Findings and Questioned Costs

There were no findings or questioned costs noted in the current year.

The McLean Hospital Corporation
Summary Schedule of the Status of Prior Audit Findings
Year Ended September 30, 2008

There were no findings from prior years to update.