COHEN RUTHERFORD + KNIGHT PC
Certified Public Accountants

Audited Consolidated Financial Statements and Other Financial Information

Doctors Community Hospital and Subsidiaries

June 30, 2011 and 2010

Audited Consolidated Financial Statements

Doctors Community Hospital and Subsidiaries

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– Contents –

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Report of Independent Auditors

Board of Directors
Doctors Community Hospital and Subsidiaries
Lanham, Maryland

We have audited the accompanying consolidated balance sheets of Doctors Community Hospital and Subsidiaries, (the Hospital) as of June 30, 2011 and 2010, and the related consolidated statements of operations and other changes in unrestricted net assets, changes in net assets, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform our audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. We were not engaged to perform an audit of the Hospital's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall consolidated financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Doctors Community Hospital and Subsidiaries as of June 30, 2011 and 2010, and the results of their operations, the changes in their net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Cohen, Rutherford + Knight, P.C.

September 29, 2011

6903 Rockledge Drive, Suite 500, Bethesda, MD 20817 **Tel:** 301.828.1000 **Fax:** 301.530.3625

Consolidated Balance Sheets

Doctors Community Hospital and Subsidiaries

ASSETS	June 30 2011		June 30 2010	
CURRENT ASSETS				
Cash and cash equivalents	$	27,349,012	$	14,521,680
Assets limited to use for debt service - *Note B*		6,522,989		4,682,633
Patient accounts receivable, less uncollectible accounts of $9,463,864 and $10,959,328		23,294,028		20,757,705
Accounts receivable - other		2,539,842		2,175,209
Inventories		3,498,391		2,772,283
Prepaid expenses		1,393,567		1,265,039
TOTAL CURRENT ASSETS		64,597,829		46,174,549
INVESTMENTS				
Marketable securities -- *Note B*		13,432,375		26,739,456
Joint ventures and equity investments -- *Note C*		2,359,764		2,182,857
		15,792,139		28,922,313
ASSETS WHOSE USE IS LIMITED -- *Note B*				
Investments held by trustee or authority, less current portion		28,101,884		32,790,163
LAND, BUILDINGS, AND EQUIPMENT -- *Note E*		126,965,136		138,555,389
DEFERRED FINANCING COSTS		2,477,547		3,542,287
GOODWILL		2,475,791		2,475,791
OTHER ASSETS		16,029,396		15,746,543
TOTAL ASSETS	$	256,439,722	$	268,207,035

See the accompanying notes to the consolidated financial statements.

Consolidated Balance Sheets – Continued

Doctors Community Hospital and Subsidiaries

LIABILITIES	June 30 2011	June 30 2010
CURRENT LIABILITIES		
Accounts payable and accrued expenses	$ 13,057,358	$ 18,239,568
Salaries, wages, and related items	10,936,073	10,211,101
Advances from third party payers	7,620,548	5,998,161
Interest rate swap -- *Note F*	0	24,135,956
Interest payable to bondholders	4,200,882	4,294,765
Current portion of long-term obligations - *Note F*	3,621,623	3,300,844
TOTAL CURRENT LIABILITIES	39,436,484	66,180,395
NONCURRENT LIABILITIES		
Other noncurrent liabilities - *Note I*	4,358,593	3,602,329
Pension obligation - *Note I*	5,013,496	7,166,902
Long-term obligations, net of current portion - *Note F*	156,583,346	157,276,508
TOTAL LIABILITIES	205,391,919	234,226,134
NET ASSETS		
Unrestricted	49,313,787	31,835,431
Noncontrolling interest	1,551,726	2,021,778
TOTAL UNRESTRICTED NET ASSETS	50,865,513	33,857,209
Temporarily restricted	182,290	123,692
TOTAL NET ASSETS	51,047,803	33,980,901
COMMITMENTS AND CONTINGENCIES - *NOTES F, G, H, I & K*		
TOTAL LIABILITIES AND NET ASSETS	$ 256,439,722	$ 268,207,035

See the accompanying notes to the consolidated financial statements.

Consolidated Statements of Operations and Other Changes in Unrestricted Net Assets

Doctors Community Hospital and Subsidiaries

	June 30 2011	June 30 2010
OPERATING REVENUE		
Patient revenue	$ 206,706,873	$ 191,744,078
Other operating revenue -- *Note B*	5,202,493	5,798,407
Pledges and contributions	616,392	207,351
Net assets released from restrictions used for operations	91,425	335,301
TOTAL OPERATING REVENUE	212,617,183	198,085,137
EXPENSES		
Salaries and wages	78,008,234	75,956,168
Employee benefits	16,154,539	15,012,104
Purchased services	30,304,704	29,144,131
Supplies	34,353,154	32,926,696
Other expenses	13,892,078	9,792,130
Provision for bad debts	14,467,766	16,070,689
Depreciation	9,691,089	9,260,387
Amortization	1,064,740	138,278
Fundraising	280,997	293,467
Interest	10,348,832	6,390,913
TOTAL EXPENSES	208,566,133	194,984,963
INCOME FROM OPERATIONS	4,051,050	3,100,174
NONOPERATING INCOME		
Gain from sale of professional office building -- *Note E*	8,390,497	0
Unrealized gain/(loss) on trading securities -- *Note B*	(575,127)	542,496
Equity in joint ventures -- *Note C*	(664,740)	357,865
Interest rate swap termination	(18,137,789)	0
Change in fair value of interest rate swap -- *Note F*	24,135,957	(5,638,447)
EXCESS OF REVENUE OVER EXPENSES (EXPENSES OVER REVENUE)	17,199,848	(1,637,912)
Subsidiary distributions to noncontrolling interest-holders	(1,909,796)	(2,172,170)
Net assets released from restrictions for capital acquisitions	(0)	255,883
Pension - related changes other than net periodic pension cost - *Note I*	1,718,275	(951,159)
INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS	$ 17,008,327	$ (4,505,358)

See the accompanying notes to the consolidated financial statements.

Consolidated Statements of Changes in Net Assets
Doctors Community Hospital and Subsidiaries

	Year Ended June 30, 2011			Year Ended June 30, 2010		
	Total	Controlling Interests	Noncontrolling Interests	Total	Controlling Interests	Noncontrolling Interests
UNRESTRICTED NET ASSETS						
Excess of revenue over expenses (expenses over revenue)	$ 17,199,848	$ 15,760,104	$ 1,439,744	$ (1,637,913)	$ (3,510,407)	$ 1,872,494
Net assets released from restrictions for capital expenditures	0	0	0	255,883	255,883	0
Dividends paid to noncontrolling interest-holders	(1,909,796)	0	(1,909,796)	0	0	0
Pension - related changes other than net periodic pension cost -- *Note I*	1,718,275	1,718,275	0	(3,123,329)	(951,159)	(2,172,170)
INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS AND NONCONTROLLING INTERESTS	17,008,327	17,478,379	(470,052)	(4,505,359)	(4,205,683)	(299,676)
TEMPORARILY RESTRICTED NET ASSETS						
Restricted contributions	150,000	150,000	0	687,458	687,458	0
Net assets released from restrictions for operations	(91,425)	(91,425)	0	(335,301)	(335,301)	0
Net assets released from restrictions for capital expenditures	0	0	0	(255,883)	(255,883)	0
INCREASE IN TEMPORARILY RESTRICTED NET ASSETS	58,575	58,575	0	96,274	96,274	0
INCREASE (DECREASE) IN NET ASSETS	17,066,902	17,536,954	(470,052)	(4,409,085)	(4,109,409)	(299,676)
NET ASSETS, BEGINNING OF YEAR	33,980,901	31,959,123	2,021,778	38,389,986	36,068,532	2,321,454
NET ASSETS, END OF YEAR	$ 51,047,803	$ 49,496,077	$ 1,551,726	$ 33,980,901	$ 31,959,123	$ 2,021,778

See the accompanying notes to the consolidated financial statements.

Consolidated Statements of Cash Flows – Continued
Doctors Community Hospital and Subsidiaries

	Year Ended June 30	
OPERATING ACTIVITIES AND OTHER GAINS	**2011**	**2010**
Increase (decrease) in net assets	$ 17,066,902	$ (4,409,085)
Adjustments to reconcile increase (decrease) in net assets to net cash and cash equivalents provided by operating activities		
Restricted contributions received	(150,000)	(687,458)
Depreciation	9,691,089	9,260,387
Provision for bad debts	14,467,766	16,070,689
Unrealized loss (gain) on investments	575,127	(542,496)
(Gain) loss on disposal of building and other property	(8,390,497)	59,905
Decrease (increase) in joint ventures and equity investments	(176,907)	21,394
Realized loss (gain) on sale of investments	(687,498)	(8,188)
Amoritzation on bond issue	(158,433)	(138,278)
Change in fair value of interest swap rate	(24,135,957)	5,638,447
Increase (decrease) in:		
Accounts payable and accrued expenses, exclusive of accrual for equipment costs	(5,182,208)	(2,793,383)
Accrued salaries, wages, and related items	724,972	1,160,058
Advances from third party payers	1,622,387	1,063,993
Pension obligation	(2,153,406)	(152,237)
Interest payable	(93,883)	2,465,665
Other liabilities	756,264	679,977
Decrease (increase) in:		
Net patient accounts receivable	(17,004,089)	(20,063,617)
Other receivables	(364,633)	(2,418,722)
Inventories	(726,108)	(175,379)
Prepaid expenses and other assets	(411,381)	(954,035)
NET CASH AND CASH EQUIVALENTS PROVIDED BY (USED IN) OPERATING ACTIVITIES AND OTHER GAINS	(14,730,492)	4,077,637
INVESTING ACTIVITIES		
Net sales of trading investments, including assets whose use is limited	16,267,375	5,592,581
Proceeds from sale of property	21,999,194	0
Purchase of property, plant and equipment	(8,144,060)	(31,154,040)
NET CASH AND CASH EQUIVALENTS PROVIDED BY (USED IN) INVESTING ACTIVITIES	30,122,509	(25,561,459)

(Continued)

Consolidated Statements of Cash Flows – Continued

Doctors Community Hospital and Subsidiaries

	Year Ended June 30	
FINANCING ACTIVITIES	**2011**	**2010**
Principal payments on debt	(3,779,424)	(3,245,494)
Proceeds from issue of debt	0	80,798,114
Bond retirement	0	(59,160,000)
Deferred financing costs	1,064,740	(1,380,919)
Restricted contributions received	150,000	687,458
NET CASH AND CASH EQUIVALENTS PROVIDED BY (USED IN) FINANCING ACTIVITIES	(2,564,684)	17,699,159
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVILENTS	12,827,333	(3,784,663)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	14,521,680	18,306,343
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 27,349,013	$ 14,521,680
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Taxes paid for Health Ventures	$ 70,000	$ 350,000
SUPPLEMENTAL DISCLOSURE OF NON CASH INFORMATION:		
Acquisition of equipment under capital lease	$ 3,565,475	$ 0

See the accompanying notes to the consolidated financial statements.

Note A – Organization and Summary of Significant Accounting Principles

Organization

Doctors Community Hospital (the Hospital) is a not-for-profit, non-stock corporation that operates an acute care general hospital facility licensed for 195 beds. The Hospital serves the health care needs of the residents of Prince George's County, the District of Columbia, and the greater Washington, D.C. metropolitan area. The Hospital has three wholly owned/controlled subsidiaries: Doctors Community Health Ventures, Inc. (Health Ventures), Doctors Community Hospital Foundation, Inc. (the Foundation), and Spine Team Maryland, LLC (STM).

Health Ventures is a for-profit corporation that invests in corporations and other businesses consistent with the Hospital's mission and strategic plan.

The Foundation is a not-for-profit, non-stock corporation established to raise and invest funds to support or benefit the operations of the Hospital. The Foundation's bylaws provide that all funds raised, except those required for the operation of the Foundation, be distributed to or be held for the benefit of the Hospital. The Foundation's bylaws also provide the Hospital with the authority to direct its activities, management, and policies.

STM is a limited liability company formed in Maryland for the purpose of providing medical and surgical services for the residents of Prince Georges County and surrounding areas.

The Hospital owns a 60% interest in Doctors Regional Cancer Center, LLC (DRCC) and Doctors Community Hospital Sleep Center, LLC (the Sleep Center). DRCC is a limited liability company formed in Maryland for the purpose of providing outpatient cancer treatment services to the residents of central Maryland. The Sleep Center is a limited liability company formed in Maryland for the purpose of providing diagnostic sleep services for residents of Prince Georges County and surrounding areas.

Principles of Consolidation

The consolidated financial statements include the accounts of the Hospital, Health Ventures, the Foundation, DRCC, the Sleep Center, and STM (collectively, the Company). All intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Cash and Cash Equivalents

The Company has cash holdings in commercial banks routinely exceeding the Federal Deposit Insurance Corporation maximum insurance limit of $250,000. Cash and cash equivalents are reported at cost which approximates market value.

Investments

Marketable securities, including assets whose use is limited, are carried at fair value. All such investments are classified as trading. Assets whose use is limited that are required to meet current liabilities of the Hospital have been classified as current assets.

Unrestricted investment income, including realized gains and losses on the sale of trading securities, is reported as other operating revenue. The cost of securities sold is based on the specific-identification method. Unrealized gains and losses on trading securities are included in non-operating gains (losses) in the accompanying consolidated statements of operations and other changes in unrestricted net assets.

Patient Revenue and Accounts Receivable

Net patient service revenue and net patient accounts receivable are reported at estimated net realizable amounts from patients, third party payers, and others for services rendered. Discounts ranging from 2.25% to 6% of Hospital charges are given to Medicare, Medicaid, and certain approved commercial health insurance and health maintenance organizations. In addition, these payers routinely review patient billings and deny payments for certain charges that they deem medically unnecessary or performed without appropriate pre-authorization. Discounts and denials are recorded as reductions of net patient service revenue. Accounts receivable from these third-party payers have been adjusted to reflect the difference between charges and the estimated reimbursable amounts.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Patient Revenue and Accounts Receivable - Continued

Gross patient revenue was comprised of the following for the years ended June 30:

	2011	2010
Medicare	43%	40%
Medicaid	13%	12%
Blue Cross Blue Shield	20%	20%
Other third-party payers	19%	22%
Self-pay patients	5%	6%
	100%	100%

The Company bills third party payers directly for services provided. Insurance coverage and credit information are obtained from patients upon admission when available. No collateral is obtained for patient accounts receivable. Patient accounts receivable deemed to be uncollectible by management have been written off. An allowance for doubtful accounts is recorded based on historical trends for patient accounts receivable that are anticipated to become uncollectible in future periods.

Gross patient accounts receivable were comprised of the following for the years ended June 30:

	2011	2010
Medicare	29%	29%
Medicaid	22%	14%
Blue Cross Blue Shield	15%	18%
Other thrid-party payers	20%	20%
Self-pay patients	14%	19%
	100%	100%

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Company believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing that would have a material effect on the consolidated financial statements. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Inventories

Inventories consist of supplies and drugs and are carried at the lower of cost or market using the average-cost method.

Land, Buildings, and Equipment

Land, buildings, and equipment are recorded at cost. Depreciation is recorded over the estimated useful lives of the assets using the straight-line method. Maintenance and repairs are charged to expense as incurred. The straight-line method is used to amortize the cost of equipment under capital leases over the estimated useful lives of the equipment or the term of the lease, whichever is appropriate.

Restricted Net Assets

Temporarily restricted net assets are those whose use by the Hospital and the Foundation has been limited by donors to a specific time period or purpose. As of June 30, 2011 and 2010, the Company had no permanently restricted net assets. Temporarily restricted net assets are available to fund various health care services and other community benefits provided by the Hospital. The Company's policy is to treat restricted contributions recorded and released in the same fiscal year as unrestricted contributions.

Excess of Expenses over Revenue

The consolidated statements of operations and other changes in unrestricted net assets include the excess of revenue over expenses (expenses over revenue) (the "performance indicator"). Changes in unrestricted net assets, which are excluded from the excess of revenue over expenses (expenses over revenue), consistent with industry practice, include contributions received and used for additions of long-lived assets, distributions to noncontrolling interest-holders, and changes in the pension obligation other than net periodic pension cost.

Charity Care

A patient is classified as a charity patient by reference to certain established policies of the Hospital. These policies define charity services as those services for which no payment is anticipated. In assessing a patient's ability to pay, the Hospital utilizes the generally recognized poverty income levels in the local community, but also includes certain cases where incurred charges are significant when compared to income. Charity care provided in 2011 and 2010, measured at established rates, was $2,128,738 and $923,563 respectively. These charges are excluded from consolidated net patient service revenue. The cost of providing this care is included in consolidated operating expenses.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Contributions and Pledges

Unconditional promises to give cash and other assets to the Hospital and the Foundation are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received or when the conditions for receiving the donation have been satisfied. 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. Contributions restricted by donors for additions to the Hospital's operating property are transferred from temporarily restricted net assets to unrestricted net assets when the expenditure is made. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of changes in net assets as net assets released from restriction.

The Hospital and Foundation write off any grants and pledges receivable that are considered uncollectible; accordingly, there is no allowance for doubtful accounts recorded for these grants and pledges. Grants and pledges receivable have not been discounted because management considers the effect to be immaterial. The balance of pledges receivable was $274,805 and $162,459 at June 30, 2011 and 2010, respectively, and is included in other amounts receivable in the accompanying consolidated balance sheets.

Advertising Costs

The Hospital expenses advertising costs as they are incurred. Advertising expense was approximately $1,348,387 and $954,569 for the fiscal years June 30, 2011 and 2010, respectively, and is reported as other expense in the accompanying consolidated statements of operations and other changes in unrestricted net assets.

Functional Expenses

The Company's consolidated operating expenses by functional classification are as follows:

	Year Ended June 30	
	2011	**2010**
Health care services	$ 149,886,585	$ 139,933,762
Management and general	58,289,227	54,587,118
Fundraising	390,321	464,084
	$ 208,566,133	$ 194,984,964

Note A – Organization and Summary of Significant Accounting Principles – Continued

Deferred Financing Costs

Financing costs incurred in issuing the Maryland Health and Higher Educational Facilities Authority (the Authority or MHHEFA) Revenue Bonds have been capitalized by the Hospital. These costs are being amortized over the life of the related bond issue using the bonds-outstanding method, which approximates the interest method. Deferred financing costs and accumulated amortization, which are included in other assets in the accompanying consolidated balance sheets, are as follows:

	June 30	
	2011	**2010**
Deferred financing costs	$ 3,008,043	$ 3,984,004
Accumulated amortization	(530,496)	(441,717)
	$ 2,477,547	$ 3,542,287

The estimated aggregate amortization expense anticipated for the next five years is as follows:

2012	$ 160,334
2013	156,899
2014	153,096
2015	149,133
2016	144,974
	$ 764,436

Fair Value of Financial Instruments

The following methods and assumptions were used by the Company to estimate the fair value of financial instruments:

- **Cash and cash equivalents, patient accounts receivable, other receivables, notes receivable, accounts payable and accrued expenses, employee compensation and related payroll taxes, and advances from third-party payers**: The carrying amount reported in the balance sheets for each of these assets and liabilities approximates their fair value.

- **Marketable securities and assets limited as to use**: Fair values are based on quoted market prices of individual securities or investments if available, or are estimated using quoted market prices for similar securities.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Fair Value of Financial Instruments – Continued

- **Long-term debt***:* Fair values of the Hospital's fixed-rate debt are based on current traded values. The fair value of variable rate debt approximates carrying value (see *Note F*).

- **Interest rate swap:** The fair value of the Hospital's interest rate swap was based on the proprietary model of a third party valuation specialist (see *Note F*).

Income Taxes

The Hospital and the Foundation are exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code as public charities. Both entities are entitled to rely on this determination as long as there are no substantial changes in their character, purposes, or methods of operation. Management has concluded that there have been no such changes, and therefore the Hospital and Foundation's status as public charities exempt from federal income taxation remain in effect.

The state in which the Hospital and the Foundation operate also provides a general exemption from state income taxation for organizations that are exempt from federal income taxation. However, both entities are subject to federal and state income taxation at corporate tax rates on unrelated business income. Exemption from other state and local taxes, such as real and personal property taxes, is separately determined.

The Hospital and the Foundation had no unrecognized tax benefits or such amounts were immaterial during the periods presented. For tax periods with respect to which no unrelated business income was recognized, no tax return was required. Tax periods for which no return is filed remain open for examination indefinitely. Although informational returns were filed for the Hospital and the Foundation, no tax returns were filed during 2011 and 2010.

Health Ventures is subject to corporate income tax, and incurred an income tax liability of $70,000 and $350,000 for the years ended June 30, 2011 and 2010, respectively.

DRCC and Sleep Center are Maryland limited liability companies that have not elected to be taxed as a corporation under current Treasury regulations. DRCC and Sleep Center are owned by more than

Note A – Organization and Summary of Significant Accounting Principles – Continued

Income Taxes – Continued

one member. As such, DRCC and Sleep Center are subject to the partnership tax rules under Subchapter K of the Internal Revenue Code of 1986, as amended. Under these rules DRCC and Sleep Center are not subject to federal or state income tax, but must file annual information returns indicating their gross and taxable income to determine the tax results to their members.

STM is a Maryland limited liability company that has not elected to be taxed as a corporation under current treasury regulations. STM is wholly owned by the Hospital. As such, STM is a "disregarded entity" under current regulations.

Goodwill

Goodwill represents the excess of cost over the fair value of assets acquired. Management evaluates goodwill for impairment on an annual basis. Management reviewed the carrying value reported for goodwill in the accompanying consolidated balance sheets for impairment and believes there is none as of June 30, 2011.

Recent Changes in Accounting Standards

In August 2010, the Financial Accounting Standards Board (FASB) amended the Accounting Standards Codification (ASC) for Health Care Entities to require that cost be used as the measurement basis for charity care disclosures, and that cost be identified as the direct and indirect costs of providing the charity care. This amendment is effective for fiscal years beginning after December 15, 2010. Also, in August 2010, the FASB amended the ASC for Health Care Entities to clarify that a health care entity should not net insurance recoveries against a related claim liability. Additionally, the amount of the claim liability should be determined without consideration of insurance recoveries. This amendment is effective for fiscal years and interim periods within those years, beginning after December 15, 2010. In January 2010, the FASB issued Accounting Standards Update (ASU) No. 2010-06, *Improving Disclosures about Fair Value Measurements*. ASU 2010-06 amends FASB Topic 820, *Fair Value Measurements and Disclosures*, to require additional disclosures regarding fair value measurements. In addition to amendments already effective, entities will also be required to report purchases, sales, issuances, and settlement of Level 3 assets and liabilities on a gross basis, rather than net. This is effective for fiscal years beginning after December 15, 2010. In July 2011, FASB issued ASU No. 2011-7, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*. ASU 2011-7 affects entities within the scope of Topic 954, Health Care Entities that recognize significant amounts of patient service revenue at the time services are rendered even though the entities do not assess a patient's ability to pay. ASU 2011-7 requires certain health care entities to change the presentation of their statement of operations by reclassifying the provision for bad debts associated with patient service revenue from

Note A – Organization and Summary of Significant Accounting Principles – Continued

Recent Changes in Accounting Standards – Continued

an operating expense to a deduction from patient service revenue (net of contractual allowances and discounts). Additionally, those health care entities are required to provide enhanced disclosure about their policies for recognizing revenue and assessing bad debts. ASU 2011-7 also requires disclosure of patient service revenue (net of contractual allowances and discounts) as well as qualitative and quantitative information about changes in the allowances for doubtful accounts. This is effective for fiscal years beginning after December 15, 2011 for public entities and for the first annual period ending after December 15, 2012 for non-public entities (early adoption permitted). Application for periods presented in the statement of operations would be retrospective; however, the disclosures required by the amendments would be prospective. Management is currently evaluating the impact on the Company's future financial statements of adoption of these changes in accounting.

Reclassification

Certain prior year amounts have been reclassified to conform to the current year's presentation.

Subsequent Events

Subsequent events have been evaluated by management through September 29, 2011, which is the date the financial statements were available to be issued.

Note B – Investments

The following is a summary of investment securities:

	For the Year Ended 2011	For the Year Ended 2010
Marketable securities:		
Corporate debt securities	$ 0	$ 3,061,161
Mutual funds	13,432,375	23,678,295
	$ 13,432,375	$ 26,739,456
Assets whose use is limited:		
Mutual funds	$ 6,148,427	$ 1,200,476
Government obligations	28,476,447	36,272,320
	$ 34,624,874	$ 37,472,796

Assets whose use is limited are held in the following funds:

	2011	2010
Funds held by Trustee or Authority:		
Debt service reserve fund	$ 34,624,874	$ 37,472,796
Less assets required for current obligations	(6,522,990)	(4,682,633)
	$ 28,101,885	$ 32,790,163

Note B – Investments – Continued

Investment return is summarized as follows:

	Other Operating Revenue	Non Operating Gains (Losses)	Total
2011			
Interest and dividend income	$ 582,467	$ 0	$ 582,467
Net realized gains	687,498	0	687,498
Net unrealized loss	0	(575,127)	(575,127)
Investment fees	(48,363)	0	(48,363)
	$ 1,221,602	$ (575,127)	$ 646,475
2010			
Interest and dividend income	$ 775,525	$ 0	$ 775,525
Net realized gains	8,188	0	8,188
Net unrealized gains	0	542,496	542,496
Investment fees	(81,282)	0	(81,282)
	$ 702,431	$ 542,496	$ 1,244,927

Current accounting standards define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, and establish a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels of inputs that may be used to measure fair value are as follows:

Level 1: Quoted prices in active markets for identical assets or liabilities.

Level 2: Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

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

Note B – Investments – Continued

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

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

Fair values of the Company's investments in mutual funds classified at Level 1 are based on quoted market prices. The fair values of mutual funds classified at Level 2 are based on the Company's pro-rata share of the each fund's net asset value.

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

The fair value of the Company's interest rate swap (level 3) is based on the proprietary model of a third party valuation specialist. The fair value takes into consideration the prevailing interest rate environment and the specific terms and conditions of the swap, and considers the credit risk of the Company and the counterparty. The method used to determine the fair value calculates the estimated future payments required by the swap and discounts these payments using an appropriate discount rate. The value represents the estimated exit price that the Company would pay to terminate the agreement.

Note B – Investments – Continued

The following table presents the Company's fair value hierarchy for financial instruments measured at fair value on a recurring basis as of June 30, 2011.

	Level 1	Level 2	Level 3	Total Fair Value
Cash	$ 1,542	$ 0	$ 0	$ 1,542
Fixed maturity				
U.S. government agency bonds/notes	0	28,476,446	0	28,476,446
Money markets	0	6,406,219	0	6,406,219
Equity securities				
Mutual funds				
Short government	3,288,099	0	0	3,288,100
Ultrashort bond	3,300,001	0	0	3,300,001
Short-term bond	3,292,694	0	0	3,292,694
Intermediate government	3,292,247	0	0	3,292,247
World bond	281,775	0	0	281,775
High-yield bond	205,362	0	0	205,362
Short-term bond	1,778,142	0	0	1,778,142
Intermediate-term bond	208,389	0	0	208,389
Moderate allocation	99,381	0	0	99,381
Mid-cap growth	334,754	0	0	334,754
Real estate	145,370	0	0	145,370
Foreign large blend	954,239	0	0	954,239
Large blend	193,154	0	0	193,154
Diversified emerging markets	235,754	0	0	235,754
Large growth	107,519	0	0	107,519
Small blend	338,742	0	0	338,742
Total assets	$ 18,057,164	$ 34,882,666	$ 0	$ 52,939,830

Note B – Investments – Continued

The following table presents the Company's fair value hierarchy for financial instruments measured at fair value on a recurring basis as of June 30, 2010:

	Level 1	Level 2	Level 3	Total Fair Value
Mutual funds	$ 1,785,848	$ 29,559,079	$ 0	$ 31,344,927
Fixed maturity	0	37,013,091	0	37,013,091
Total	$ 1,785,848	$ 66,572,170	$ 0	$ 68,358,018
Interest rate swap	0	0	24,135,957	24,135,957
Total	$ 0	$ 0	$ 24,135,957	$ 24,135,957

The following table summarizes the activity for fair value measurements using significant unobservable inputs (Level 3):

	Level 3	
	2011	2010
Fair value, beginning	$ 24,135,957	$ 18,497,509
Changes in interest rate swap	(24,135,957)	5,638,448
Fair value, ending	$ 0	$ 24,135,957

There were no significant transfers between fair value hierarchy levels for the year ended June 30, 2011.

Note C – Joint Ventures and Equity Investments

Health Ventures invests in corporations and other forms of business consistent with the mission and strategic plan of the Company. Health Ventures' unconsolidated investments are carried at cost or at equity depending on the percentage of ownership and control. Health Venture's investment in Magnolia Gardens L.L.C. is not consolidated with the financial statements of the Company because the Health Ventures does not control the investee. The investment income of these joint ventures and equity investments is reported in non operating revenue in the accompanying consolidated statements of operations and other changes in unrestricted net assets. These investments are summarized as follows:

			June 30	
Name	**Percent Ownership**	**Accounting Method**	**2011**	**2010**
Magnolia Gardens LLC	51.0%	Equity	$ 2,325,301	$ 1,834,835
Neighborcare Home Medical Equipment of Maryland LLC	5.0%	Cost	250,000	250,000
Metropolitan Ambulatory Urological Institute, LLC	31.7%	Equity	90,457	114,260
Diagnostic Imaging, LLC	50.0%	Equity	(305,995)	(16,238)
			$ 2,359,764	$ 2,182,857

Note D – Related Party Transactions

The Hospital has income guarantee agreements with certain physicians. These advances are held as promissory notes and are often forgiven based on the established terms of these notes, such as maintaining an active practice in the Hospital's community.

The Hospital advanced funds to Health Ventures in its establishment of Metropolitan Medical Group, LLC and Diagnostic Imaging, LLC (DI). The Medical Director of Radiology for the Hospital is an investor in DI. Since MMS is wholly owned by Health Ventures, the amounts loaned to MMS have been eliminated in consolidation; however, amounts due from DI have not been eliminated since DI are included in the accompanying consolidated financial statements and amount to $812,072 ($1,812,072 net of a reserve of $1,000,000) and $1,534,139 as of June 30, 2011 and 2010, respectively (*See Note C).*

A member of the board of directors maintains a business that had transactions with the Hospital that amounted to $606,915 and $650,363 for the years ended June 30, 2011 and 2010, respectively.

The Foundation transferred $106,746 and $4,537 for the years ended June 30, 2011 and 2010, respectively, of restricted net assets to the Hospital, which were then released from restriction by the Hospital for use in operations.

Note E – Land, Buildings, and Equipment

Land, buildings, and equipment are summarized as follows:

Name	Useful Life	June 30 2011	June 30 2010
Land improvements	10-40 Years	$ 7,135,958	$ 6,450,639
Buildings	4-40 Years	123,641,789	135,014,745
Furniture and equipment	2-20 Years	70,956,441	66,364,811
Equipment under capital lease obligations	2-20 Years	9,987,859	6,042,072
		211,722,047	213,872,267
Less accumulated depreciation		91,636,409	83,448,166
		120,085,638	130,424,101
Construction in progress		740,996	1,992,786
Land		6,138,502	6,138,502
		$ 126,965,136	$ 138,555,389

The Company capitalized interest of $0 in 2011 and $3,991,443 in 2010 related to construction activities, and total capitalized interest reported as a component of land, buildings and equipment, net of accumulated depreciation, was $3,240,315 and $6,506,594 as of June 30, 2011 and June 30, 2010. Capitalized interest related to construction activities includes the relevant portions of applicable interest payments to creditors on bonds and other debt obligations, net payments/receipts to counterparties on interest rate swap arrangements, letter of credit fees, and income received on trustee-held funds.

Accumulated depreciation includes accumulated amortization of capital leased equipment in the amount of $1,509,807and $1,118,566 as of June 30, 2011 and 2010, respectively. Depreciation expense of capital leased equipment was $560,291 and $268,405 for fiscal year 2011 and 2010, respectively.

Note F – Long-Term Debt

Long-term indebtedness consisted of the following:

	June 30 2011	June 30 2010
Maryland Health and Higher Education Facilities Authority Revenue Bonds, Series 2007A:		
4.00% term bonds due July 1, 2013	$ 7,450,000	$ 9,750,000
5.00% term bonds due July 1, 2020	21,890,000	21,890,000
5.00% term bonds due July 1, 2027	30,795,000	30,795,000
5.00% term bonds due July 1, 2029	10,915,000	10,915,000
Maryland Health and Higher Education Facilities Authority Revenue Bonds, Series 2010:		
5.30% term bonds due July 1, 2025	5,330,000	5,330,000
5.625% term bonds due July 1, 2030	9,095,000	9,095,000
5.75% term bonds due July 1, 2038	68,245,000	68,245,000
Capital leases	6,273,608	3,777,401
Notes payable	19,688	429,845
	160,013,296	160,227,246
Current portion of long-term debt	(3,621,623)	(3,300,844)
Original issue premium, net of accumulated amortization	2,027,513	2,221,992
Original issue discount, net of accumulated amortization	(1,835,840)	(1,871,886)
	$ 156,583,346	$ 157,276,508

The fair value of the Company's long-term debt, based on quoted market prices, was$ 140,854,447 and $144,210,999 at June 30, 2011 and 2010, respectively.

Note F – Long-Term Debt – Continued

The aggregate maturities of long-term debt, including sinking fund principal requirements during the next five fiscal years, are as follows:

2012	$	3,621,623
2013		4,078,970
2014		4,264,593
2015		4,480,300
2016		4,092,810
2017 and after		139,475,000
	$	160,013,296

Total interest paid for the years ended June 30, 2011 and 2010 net of capitalized interest, was $10,348,832 and $4,084,370, respectively.

Revenue Bonds

On May 15, 2010, the Hospital issued $82,670,000 principal amount of Revenue Bonds, Series 2010 (Series 2010 Bonds). The proceeds of this issue were used to retire the Revenue Bonds, Series 2008 and to finance the costs of renovation and equipment purchases.

On January 4, 2007, the Hospital issued $77,685,000 principal amount of Revenue Bonds, Series 2007A (Series 2007 Bonds). The proceeds of this issue were used to retire certain existing bonds, pooled loans, and to finance the costs of renovation and equipment purchases.

The Hospital is required to maintain certain debt ratios as defined by the Agreement. In the opinion of the management, the Hospital has complied with the required covenants for 2011 and 2010.

Note F – Long-Term Debt – Continued

Other Debt

During 2008, DRCC obtained a $4,000,000 revolving line of credit from a commercial lender to finance the acquisition of certain medical equipment. The line of credit was converted to a capital lease during 2009. The outstanding principal balance was $3,184,329 and $3,702,031 on June 30, 2011 and 2010, respectively. Beginning in October 2009, monthly payments of principal and interest at 6.8% per annum become due. Aggregate future principal payments as of June 30, 2011 are as follows:

2012	$ 553,879
2013	592,585
2014	633,995
2015	678,298
2016	725,572
	$ 3,184,329

Other debt includes the Hospital's obligations under various other capital leases (see *Note H*).

Derivative Instrument

Generally accepted accounting principles require that all derivative instruments be recognized in the financial statements at their fair value. The Hospital entered into an interest rate swap agreement that was considered to be a derivative financial instrument. The interest rate swap contract was not designated as an effective cash flow hedge under current accounting principles. Consequently, changes in the fair value of the interest rate swap agreement were recognized in the consolidated statement of operations as a component of excess of revenue over expenses (expenses over revenue).

Note F – Long-Term Debt – Continued

Derivative Instruments – Continued

The Hospital's interest rate swap had an initial notional amount of $75,000,000 subject to scheduled amortization, an effective date of January 1, 2009, and a termination date of July 1, 2040. It provided for the Hospital to pay a fixed rate of approximately 4.6% and receive a variable rate based on 79% of one month London Interbank Offered Rate. Subject to the terms of the agreement, either party had the option to terminate the agreement prior to the termination date provided that no event of default or termination had occurred. Specifically, the interest rate swap provider had the optional right to terminate this transaction (provided that no event of default or termination event had occurred) on May 1, 2011 and annually thereafter until scheduled termination. Upon election to optionally terminate this transaction, a termination amount in respect of such termination would be due from one counterparty to this transaction to the other counterparty.

The Hospital entered into an agreement with the counterparty to terminate the interest rate swap agreement on April 14, 2011. The Hospital made payments to the counterparty that totaled $18,137,789 to terminate the interest rate swap, and such payments are reported as a nonoperating loss in the associated consolidated statements of operations and changes in unrestricted net assets.

Note G – Medical Malpractice and Workers' Compensation Insurance

From October 18, 2001 to October 31, 2004, the Hospital maintained occurrence-based professional liability insurance with a per-claim limit of $8,000,000 and aggregate annual limit of $10,000,000 with a commercial carrier. The Hospital was liable for a deductible up to $250,000 for each occurrence up to a maximum of $750,000. Prior to October 18, 2001, the Hospital's policy had no deductible. Effective November 1, 2004, due to the commercial carrier discontinuing services in Maryland and rising insurance costs, the Hospital purchased coverage on a claims-made basis from Freestate Healthcare Insurance Company, Ltd., a group captive formed by several Maryland hospitals. The Hospital owns a ⅛ interest in the captive that is accounted for using the cost method. The cost of $15,000 is recorded in other assets in the accompanying consolidated balance sheets as of June 30, 2011 and 2010. Premiums are expensed as incurred and are established based on the Hospital's historical experience supplemented as necessary with industry experience. The total premium is allocated to each of the shareholders based on their experience. Retrospective premium assessments and credits are calculated based on the aggregate experience of all named insured under the policy. Each named insured's assessment of credit is based on the percentage of their actual exposure to the actual exposure of all named insureds. In management's opinion, the assets of Freestate are sufficient to meet its obligations as of June 30, 2011. If the financial condition of Freestate were to materially deteriorate in the future, and Freestate was unable to pay its claim obligations, the responsibility to pay those claims would return to the member hospitals.

Note G – Medical Malpractice and Workers' Compensation Insurance – Continued

The captive is responsible for claims up to $1,000,000 for each and every loss event. Excess coverage has been purchased for all claims in excess of $1,000,000 to a limit of $6,000,000 effective March 1, 2006. The liability for all known claims and an estimate for claims incurred but not reported were for the Hospital were $1,176,824 and $1,145,208 at June 30, 2011 and 2010, respectively. These amounts are included in accounts payable and accrued expenses in the accompanying consolidated balance sheets.

The Hospital is self-insured against workers' compensation claims up to a per-accident limit of $400,000 with an annual limitation of approximately $1,200,000. A liability has been recorded for all known claims and an estimate for claims incurred but not reported in the amount of $888,587 and $679,114 at June 30, 2011 and 2010, respectively. These amounts are included in accounts payable and accrued expenses in the accompanying consolidated balance sheets.

Note H – Leases

The Company has operating leases covering various medical and other equipment and facilities. Generally, the leases carry renewal provisions and require the Hospital to pay maintenance costs.

The Hospital and DRCC have entered into capital leases for certain equipment. The cost of assets under capital leases is included in land, building, and equipment (see *Note E*), and related capital lease obligations are included in long-term debt (see *Note F*) in the accompanying consolidated balance sheets. Depreciation expense on these assets is included with depreciation and amortization in the consolidated statements of operations and other changes in unrestricted net assets.

Future minimum lease payments as of June 30, 2011 are as follows:

	Capital Leases	Operating Leases
2012	$ 1,216,935	$ 1,851,425
2013	1,293,970	1,763,136
2014	1,374,593	1,318,700
2015	1,460,300	1,060,203
2016 and thereafter	927,810	1,002,631
Total minimum lease payments	6,273,608	6,996,096
Current portion of long-term debt	(1,216,935)	
Capital lease obligations, less current portion	$ 5,056,673	

Total rental expense reported in the accompanying consolidated statements of operations and other changes in unrestricted net assets for the years ended June 30, 2011 and 2010 was $3,076,681 and $2,120,190, respectively.

Note I – Retirement Plans

The Hospital froze the defined benefit pension plan (the Plan) covering substantially all employees, as a result a Plan curtailment was recognized during fiscal year 2011. The decision to terminate in the Plan has not been made by the board of directors. The benefits are based on years of service and the employee's compensation during years of employment. The Hospital's funding policy is to make sufficient contributions to the Plan to comply with the minimum funding provisions of the Employee Retirement Income Security Act of 1974 (ERISA). The Hospital expects to contribute $1,000,000 to the Plan during 2012 to keep the funding levels at the IRS requirements. The measurement date of the Plan is June 30.

Note I – Retirement Plans – Continued

The following table provides a reconciliation of the benefit obligation, Plan assets, and funded status of the Plan in the Company's consolidated financial statements based on actuarial valuations:

	2011	2010
Accumulated Benefit Obligation	$ 18,093,874	$ 16,816,115
Change in Benefit Obligation		
Benefit obligation at beginning of year	$ 17,122,151	$ 14,761,171
Service cost	879,214	1,197,246
Interest cost	905,352	876,049
Curtailment gain	(262,388)	0
Actuarial loss	989	592,967
Benefits paid	(551,444)	(305,282)
Benefit Obligation at End of Year	18,093,874	17,122,151
Change in Plan Assets		
Fair value of plan assets at beginning of year	$ 9,955,249	$ 7,442,032
Actual return on plan assets	1,545,345	(257,242)
Employer contributions	2,131,228	3,075,741
Benefits paid	(551,444)	(305,282)
Fair Value of Plan Assets at End of Year	13,080,378	9,955,249
Funded Status (Pension Obligation)	$ (5,013,496)	$ (7,166,902)
Components of Net Periodic Benefit Cost		
Service cost	$ 879,214	$ 1,197,246
Interest cost	905,352	876,049
Expected return on plan assets	(724,028)	(598,055)
Amortization of prior service cost	8,033	12,049
Curtailment loss	92,333	0
Amortization of net loss	534,262	485,036
Net Periodic Pension Cost	$ 1,695,166	$ 1,972,325

Note I – Retirement Plans – Continued

The total amount recognized in unrestricted net assets for 2011 and 2010 is as follows:

	2011	2010
Net loss	$ 6,041,350	$ 7,658,328
Prior service cost	0	100,366
	$ 6,041,350	$ 7,758,694

The total amount of prior service cost and net gain (loss) expected to be recognized in net periodic benefit cost during 2012 is $453,101.

The Plan's assets are invested primarily in cash and cash equivalents and mutual funds as follows as of June 30:

	2011	2010
Equity sercurities	52%	24%
Debt securities	36%	20%
Other	12%	56%
	100%	100%

Plan assets are invested to ensure that the Plan has the ability to pay all benefit and expense obligations when due, to maximize return within prudent levels of risk for pension assets, and to maintain a funding cushion for unexpected developments. The target weighted-average asset allocation of pension investments was 50% equities and 50% debt securities and cash as of June 30, 2011.

The Plan's estimated future benefit payments are as follows:

2012	$ 1,770,267
2013	789,010
2014	837,135
2015	658,420
2016	792,558
2017 - 2021	6,029,121
Total	$ 10,876,511

Note I – Retirement Plans – Continued

The weighted-average assumptions used to determine net periodic benefit cost and the projected benefit obligation for the years ended June 30 were as follows:

	2011	2010
Discount rate	5.25%	6.00%
Expected return on Plan assets	6.50%	7.50%
Rate of compenstion increase	2.00%	2.00%

The following table presents the Company's fair value hierarchy for financial instruments measured at fair value on a recurring basis as of June 30, 2011:

	Level 1	Level 2	Level 3	Total Fair Value
Cash and cash equivalents				
Money market funds	$ 226,769	$ 0	$ 0	$ 226,769
Equity securities				
Mutual funds				
Diversified emerging markets	671,943	0	0	671,943
Foreign large growth	682,662	0	0	682,662
Foreign small/mid growth	1,370,670	0	0	1,370,670
Inflation-protected bond	603,099	0	0	603,099
Intermediate government	524,033	0	0	524,033
Intermediate-term bond	2,950,422	0	0	2,950,422
Large growth	669,312	0	0	669,312
Large value	1,322,320	0	0	1,322,320
Mid-cap blend	666,513	0	0	666,513
Multisector bond	609,237	0	0	609,237
Small growth	792,324	0	0	792,324
Small value	690,635	0	0	690,635
World allocation	1,300,439	0	0	1,300,439
Total assets	$ 13,080,378	$ 0	$ 0	$ 13,080,378

The Company's management considers the balance of Plan assets of $9,955,249 as of June 30, 2010, to be based entirely on level 1 fair value measures.

There were no significant transfers between fair value hierarchy levels for the year ended June 30, 2011.

DCH established a Tax Deferred Savings Plan (the TSA) available to all eligible employees who may make elective tax deferred contributions up to the IRS threshold of pretax annual compensation, as defined in the TSA. DCH contributes a discretionary match after the TSA year end equal to the lesser of 50% of the participant's contribution or 50% of 40% of the participants' eligible wages. The participant is eligible to receive a match if they were employed at the end of the TSA year, have

Note I – Retirement Plans – Continued

completed two years of eligible service and have an eligible job status as defined by the TSA. Matching employer contributions totaled $738,521 and $665,751 for the years ended June 30, 2011 and 2010, respectively.

The Hospital has a deferred compensation plan that permits certain executives to defer receiving a portion of their compensation. The deferred amounts are included in other assets in the accompanying consolidated balance sheets. The associated liability of an equal amount is included in other liabilities in the accompanying consolidated balance sheets. The liability recorded regarding the deferred compensation was $4,358,593 and $3,602,329 as of June 30, 2011 and 2010, respectively. During 2011 and 2010, distributions of $136,142 and $77,677 were made to participants in the deferred compensation plan, respectively.

The Hospital is the beneficiary of life insurance policies in place for certain executives. Approximately $9,400,000 and $9,200,000 is included in other assets at June 30, 2011 and 2010, which is the amount that could be realized by the Hospital under the insurance contracts.

Note J – Maryland Health Services Cost Review Commission

Certain of the Hospital's charges are subject to review and approval by the Maryland Health Services Cost Review Commission (the Commission). Hospital management has filed the required forms with the Commission and believes the Hospital is in compliance with Commission requirements.

The current rate of reimbursement for principally all inpatient services and certain other services to patients under the Medicare and Medicaid programs is based on an agreement between the Centers for Medicare and Medicaid Services and the Commission. This agreement is based upon a waiver from Medicare reimbursement principles under Section 1814(b) of the Social Security Act and will continue as long as all third-party payers elect to be reimbursed under this program and the rate of increase for costs per hospital inpatient admission is below the national average. Management believes that this program will remain in effect at least through June 2012.

The Commission and the Hospital entered into an agreement that is based on a rate methodology for those Hospital service centers that provide only inpatient services. Under this methodology, a target average charge per case is established for the Hospital, based on past actual charges and case mix indices. The actual average charge per case is compared with the target average charge-per-case and to the extent that the actual average exceeds the target, the overcharge plus applicable penalties will reduce the approved target for future years. At June 30, 2011, the Hospital was in compliance with its average charge per case target.

Note J – Maryland Health Services Cost Review Commission – Continued

The Commission's rate-setting methodology for Hospital service centers that provide both inpatient and outpatient services or only outpatient services consists of establishing an acceptable unit rate for defined inpatient and outpatient service centers within the Hospital. The actual average unit charge for each service center is compared to the approved rate monthly. Overcharges and undercharges due to either patient volume or price variances, plus penalties where applicable, are applied to decrease (in the case of overcharges) or increase (in the case of undercharges) future approved rates on an annual basis.

The Commission changed the charge-per-case reimbursement methodology for all Maryland hospitals effective July 1, 2005. The Commission chose a severity-adjusted method of grouping hospital discharges to measure differences in patient acuity and to align payments appropriately to that acuity. This policy decision reflects the Commission's desire to continuously improve the rate-setting system and to remain a leader in the development of policies that ensure cost containment, access to care, equity in payment, and financial stability of the hospital industry.

The timing of the Commission's rate adjustments for the Hospital could result in an increase or reduction in rates due to the variances and penalties described above in a year subsequent to the year in which such items occur. The Hospital's policy is to accrue revenue based on actual charges for services to patients in the year in which the services to patients are performed and billed.

Note K – Commitments and Contingencies

Litigation

There are several lawsuits pending in which the Hospital has been named as defendant. In the opinion of Hospital management, after consultation with legal counsel, the potential liability, in the event of adverse settlement, will not have a material impact on the Hospital's consolidated financial position.

Note K – Commitments and Contingencies – Continued

Risk Factors

The Company's ability to maintain and/or increase future revenues could be adversely affected by:

- the growth of managed care organizations promoting alternative methods for health care delivery and payment of services such as discounted fee for service networks and capitated fee arrangements (the rate setting process in the State of Maryland prohibits hospitals from entering into discounted fee arrangements; however, managed care contracts may provide for exclusive service arrangements);

- proposed and/or future changes in the laws, rules, regulations, and policies relating to the definition, activities, and/or taxation of not-for-profit tax-exempt entities;

- the enactment into law of all or any part of the current budget resolutions under consideration by Congress related to Medicare and Medicaid reimbursement methodology and/or further reductions in payments to hospitals and other health care providers;

- the future of Maryland's certificate of need program, where future deregulation could result in the entrance of new competitors, or future additional regulation may eliminate the Company's ability to expand new services; and

- the ultimate impact of the federal Patient Protection and Affordable Care Act and the Health Care Education Affordability Reconciliation Act of 2010.

The Joint Commission, a non-governmental privately owned entity, provides accreditation status to hospitals and other health care organizations in the United States. Such accreditation is based upon a number of requirements such as undergoing periodic surveys conducted by Joint Commission personnel. Certain managed care payers require hospitals to have appropriate Joint Commission accreditation in order to participate in those programs. In addition, the Center for Medicare and Medicaid Services (CMS), the agency with oversight of the Medicare and Medicaid programs, provides "deemed status" for facilities having Joint Commission accreditation. By being Joint Commission accredited, facilities are "deemed" to be in compliance with the Medicare and Medicaid conditions of participation. Termination as a Medicare provider or exclusion from any or all of these programs/payers would have a materially negative impact on the future financial position, operating results and cash flows of the Hospital. In April 2010 the Hospital was surveyed by Joint Commission and received a full three-year Joint Commission accreditation through July 2013.

Note K – Commitments and Contingencies – Continued

During September 2008, certain large U.S. financial institutions failed, primarily as a result of holdings in troubled subprime loans or assets collateralized with such distressed loans. These institutional failures, and the negative economic conditions that contributed to these failures, generated substantial volatility in global financial markets and substantial uncertainty regarding access to capital and the continued viability of many other financial institutions. Despite the federal legislative initiatives to ameliorate these conditions, global credit markets remain volatile and the health of the global economy continues to be uncertain. These conditions create uncertainty regarding the future valuation of the Company's invested funds and the resulting impact on the future financial position, results of operations and cash flows of the Company could be material.

The Company invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in values of investment securities will occur in the near term, and such changes could materially affect the amounts reported as investments on the consolidated balance sheets.

Note L – Goodwill

During June 2007, the Hospital purchased a 60% interest in DRCC. Goodwill in the amount of $1,062,531 resulted from the transaction and has been included in the accompanying consolidated balance sheets as of June 30, 2011 and 2010.

Upon inception of DRCC in 2007, and as part of its initial capital contribution, Maryland Regional Cancer Care, LLC, the founding member of DRCC, transferred a portion of its goodwill to DRCC. The amount of goodwill transferred to DRCC was $646,975 and has been included in the accompanying consolidated balance sheets at June 30, 2011 and 2010.

Health Ventures has a 51% ownership interest in Magnolia Gardens, LLC. Goodwill in the amount of $766,285 resulted from the purchase of ownership and has been included in the accompanying consolidated balance sheets as of June 30, 2011 and 2010.

Note M – Temporarily Restricted Net Assets

Temporarily restricted net assets are available for the years ended June 30 for the following programs and projects:

	2011	2010
Nancy Heilman Scholarship Fund	$ 1,479	$ 1,479
Brian Erfan Memorial Fund	5,850	5,850
Jane Schafer Scholarship Fund	10,785	10,785
Cardiac Rehab Scholarship	11,980	12,648
Borden Breast Center	150,000	0
UASI 2008 grant	2,177	92,930
MHA HPP Disaster Grant	19	0
	$ 182,290	$ 123,692

COHEN
RUTHERFORD
+ KNIGHT PC
Certified Public Accountants

Report of Independent Auditors on Other Financial Information

Board of Directors
Doctors Community Hospital and Subsidiaries
Lanham, Maryland

The 2011 and 2010 audited consolidated financial statements of Doctors Community Hospital and Subsidiaries and our report thereon are presented in the preceding section of this report. Those audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The supplementary information presented hereinafter as of and for the year ended June 30, 2011 is presented for purposes of additional analysis of the basic consolidated financial statements, and is not a required part of the basic consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Cohen, Rutherford + Knight, P.C.

September 29, 2011

6903 Rockledge Drive, Suite 500, Bethesda, MD 20817 **Tel:** 301.828.1000 **Fax:** 301.530.3625

Consolidating Balance Sheet Information

Doctors Community Hospital and Subsidiaries

June 30, 2011

ASSETS	DOCTORS COMMUNITY HOSPITAL	DOCTORS COMMUNITY HOSPITAL FOUNDATION, INC	DOCTORS COMMUNITY HEALTH VENTURES, INC	DOCTORS REGIONAL CANCER CENTER, LLC	DOCTORS COMMUNITY HOSPITAL SLEEP CENTER, LLC	SPINE TEAM MARYLAND, LLC	ELIMINATIONS	CONSOLIDATED
CURRENT ASSETS								
Cash and cash equivalents	$ 24,950,706	$ 338,879	$ 726,238	$ 801,981	$ 383,982	$ 147,226	$ 0	$ 27,349,012
Assets limited to use for debt service	6,522,989	0	0	0	0	0	0	6,522,989
Patient accounts receivable, net	21,973,438	0	414,336	600,389	(1,548,776)	261,876	1,592,765	23,294,028
Other amounts receivable	2,131,503	371,814	43,360	194,799	67,080	2,533	(271,247)	2,539,842
Inventories	3,351,016	0	5,265	1,495	140,615	0	0	3,498,391
Prepaid expenses	1,224,155	1,477	3,649	191,555	0	0	(27,269)	1,393,567
TOTAL CURRENT ASSETS	60,153,807	712,170	1,192,848	1,790,219	(957,099)	411,635	1,294,249	64,597,829
INVESTMENTS								
Marketable securities	13,269,293	163,082	0	0	0	0	0	13,432,375
Investment in Doctors Regional Cancer Center	2,521,489	0	0	0	0	0	(2,521,489)	0
Investment in Sleep Services of America, Inc.	(193,894)	0	0	0	0	0	193,894	0
Joint ventures and equity investments	0	0	2,359,764	0	0	0	0	2,359,764
Due to DCH	7,761,349	0	0	0	528,873	0	(8,290,222)	0
	23,358,237	163,082	2,359,764	0	528,873	0	(10,617,817)	15,792,139
ASSETS WHOSE USE IS LIMITED								
Investments held by trustee or authority, less current portion	28,101,884	0	0	0	0	0	0	28,101,884
Land and land improvements	9,589,025	0	0	0	0	0	0	9,589,025
Building and fixed equipment	116,300,300	0	0	0	0	0	0	116,300,300
Medical office building	7,341,489	0	0	0	0	0	0	7,341,489
Major movable equipment	69,986,569	0	724,620	8,575,684	1,246,547	158,645	0	80,692,065
Construction in progress	4,671,283	0	0	0	0	0	0	4,671,283
Accumulated depreciation	(87,512,801)	0	(220,948)	(2,983,387)	(891,227)	(20,662)	0	(91,629,025)
LAND, BUILDINGS, AND EQUIPMENT	120,375,864	0	503,672	5,592,297	355,320	137,983	0	126,965,136
DEFERRED FINANCING COSTS	2,477,547	0	0	0	0	0	0	2,477,547
GOODWILL	1,062,531	0	766,285	646,975	0	0	0	2,475,791
OTHER ASSETS	15,212,363	0	1,917,033	0	0	0	(1,100,000)	16,029,396
TOTAL ASSETS	$ 250,742,233	$ 875,252	$ 6,739,602	$ 8,029,491	$ (72,906)	$ 549,618	$ (10,423,568)	$ 256,439,722

See the accompanying report of independent auditors on other financial information.

Consolidating Balance Sheet Information

Doctors Community Hospital and Subsidiaries

June 30, 2011

LIABILITIES AND NET ASSETS	DOCTORS COMMUNITY HOSPITAL	DOCTORS COMMUNITY HOSPITAL FOUNDATION, INC	DOCTORS COMMUNITY HEALTH VENTURES, INC	DOCTORS REGIONAL CANCER CENTER, LLC	DOCTORS COMMUNITY HOSPITAL SLEEP CENTER, LLC	SPINE TEAM MARYLAND, LLC	ELIMINATIONS	CONSOLIDATED
CURRENT LIABILITIES								
Accounts payable and accrued expenses	$ 13,088,579	$ 0	$ 50,630	$ 295,786	$ 207,119	$ 224,612	$ (809,368)	$ 13,057,358
Due to DCH	0	695,158	0	109,070	43,131	1,159,985	(2,007,344)	0
Salaries, wages, and related items	10,790,125	0	145,948	0	0	0	0	10,936,073
Advances from third party payers	7,620,548	0	0	0	0	0	0	7,620,548
Interest rate swap	0	0	0	0	0	0	0	0
Interest payable to bondholders	4,200,882	0	0	0	0	0	0	4,200,882
Current portion of long-term obligation	3,048,056	0	0	573,567	0	0	0	3,621,623
TOTAL CURRENT LIABILITIES	38,748,190	695,158	196,578	978,423	250,250	1,384,597	(2,816,712)	39,436,484
NONCURRENT LIABILITIES								
Other noncurrent liabilities	4,358,594	0	0	218,141	0	0	(218,142)	4,358,593
Interest rate swap	-	0	0	0	0	0	0	0
Pension obligation, net of current portion	5,013,496	0	0	0	0	0	0	5,013,496
Long-term obligations, net of current portion	153,952,896	0	5,597,016	2,630,450	0	0	(5,597,016)	156,583,346
TOTAL LIABILITIES	202,073,176	695,158	5,793,594	3,827,014	250,250	1,384,597	(8,631,870)	205,391,919
NET ASSETS AND MEMBERS' EQUITY								
Unrestricted	48,666,861	0	0	0	0	0	646,926	49,313,787
Members' equity	0	0	946,008	4,202,477	(323,156)	(834,979)	(3,990,350)	0
Noncontrolling interest	0	0	0	0	0	0	1,551,726	1,551,726
Total unrestricted net assets	48,666,861	0	946,008	4,202,477	(323,156)	(834,979)	(1,791,698)	50,865,513
Temporarily restricted	2,196	180,094	0	0	0	0	0	182,290
TOTAL NET ASSETS	48,669,057	180,094	946,008	4,202,477	(323,156)	(834,979)	(1,791,698)	51,047,803
TOTAL NET ASSETS AND LIABILITIES	$ 250,742,233	$ 875,252	$ 6,739,602	$ 8,029,491	$ (72,906)	$ 549,618	$ (10,423,568)	$ 256,439,722

See the accompanying report of independent auditors on other financial information.

Consolidating Statement of Operations Information

Doctors Community Hospital and Subsidiaries

For the Year Ended June 30, 2011

	DOCTORS COMMUNITY HOSPITAL	DOCTORS COMMUNITY HOSPITAL FOUNDATION, INC	DOCTORS COMMUNITY HEALTH VENTURES, INC	DOCTORS REGIONAL CANCER CENTER, LLC	DOCTORS COMMUNITY HOSPITAL SLEEP CENTER, LLC	SPINE TEAM MARYLAND, LLC	ELIMINATIONS	CONSOLIDATED
UNRESTRICTED NET ASSETS								
OPERATING REVENUE								
Inpatient revenue	$ 136,451,728	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0	$ 136,451,728
Outpatient revenue	68,758,306	0	2,977,920	7,633,400	5,339,321	642,358	1,635,896	86,987,201
Contractuals	(16,732,056)	0	0	0	0	0	0	(16,732,056)
Other operating revenue	6,460,712	738	0	0	0	0	(1,258,957)	5,202,493
Pledges and contributions	120,735	495,657	0	0	0	0	0	616,392
Net assets released from restrictions used for operations	90,753	672	0	0	0	0	0	91,425
TOTAL OPERATING REVENUE	195,150,178	497,067	2,977,920	7,633,400	5,339,321	642,358	376,939	212,617,183
EXPENSES								
Salaries and wages	76,457,236	65,646	0	0	916,470	568,882	0	78,008,234
Employee benefits	15,931,765	0	0	0	222,774	0	0	16,154,539
Purchased services	24,231,255	32,234	211,455	5,071,895	450,424	307,441	0	30,304,704
Supplies	33,891,543	894	0	106,060	309,575	45,082	0	34,353,154
Other expenses	9,990,452	10,550	3,903,543	546,997	342,835	356,658	(1,258,957)	13,892,078
Provision for bad debts	14,467,766	0	0	0	0	0	0	14,467,766
Depreciation	8,379,132	0	125,519	1,021,638	145,506	19,294	0	9,691,089
Amortization	1,064,740	0	0	0	0	0	0	1,064,740
Fundraising	0	280,997	0	0	0	0	0	280,997
Interest	10,109,669	0	0	239,163	0	0	0	10,348,832
TOTAL EXPENSES	194,523,558	390,321	4,240,517	6,985,753	2,387,584	1,297,357	(1,258,957)	208,566,133
INCOME (LOSS) FROM OPERATIONS	626,620	106,746	(1,262,597)	647,647	2,951,737	(654,999)	1,635,896	4,051,050
NONOPERATING INCOME								
Gain from sale of professional office building -- *Note E*	8,390,497	0	0	0	0	0	0	8,390,497
Unrealized (loss) on trading securities -- *Note B*	(575,127)	0	0	0	0	0	0	(575,127)
Investment income from subsidiary	2,159,630	0	335,260	0	0	0	(3,159,630)	(664,740)
Interest rate swap termination	(18,137,789)	0	0	0	0	0	0	(18,137,789)
Change in fair value of interest rate swap -- *Note F*	24,135,957	0	0	0	0	0	0	24,135,957
EXCESS OF REVENUE OVER EXPENSES (EXPENSES OVER REVENUE)	16,599,788	106,746	(927,337)	647,647	2,951,737	(654,999)	(1,523,734)	17,199,848
Net asset transfer	106,746	(106,746)	0	0	0	0	0	0
Dividends paid	0	0	0	0	(4,774,500)	0	2,864,704	(1,909,796)
Contributions	0	150,000	0	0	0	0	0	150,000
Net assets released from restrictions for use in operations	(90,753)	(672)	0	0	0	0	0	(91,425)
Pension - related changes other than net periodic pension cost	1,718,275	0	0	0	0	0	0	1,718,275
Increase (decrease) in net assets	18,334,056	149,328	(927,337)	647,647	(1,822,763)	(654,999)	1,340,970	17,066,902
Net assets, beginning of year	30,334,999	30,765	1,873,346	3,554,830	1,499,606	(179,979)	(3,132,666)	33,980,901
Net assets, end of year	$ 48,669,055	$ 180,093	$ 946,009	$ 4,202,477	$ (323,157)	$ (834,978)	$ (1,791,696)	$ 51,047,803

See the accompanying report of independent auditors on other financial information.