Audited Consolidated Financial Statements and Other Financial Information

Doctors Community Hospital and Subsidiaries

June 30, 2014 and 2013

– Contents –

DIXON HUGHES GOODMAN LLP
Certified Public Accountants and Advisors

- Independent Auditors' Report -

The Board of Directors
Doctors Community Hospital and Subsidiaries
Lanham, Maryland

We have audited the accompanying consolidated financial statements of Doctors Community Hospital and Subsidiaries (the "Hospital"), which comprise the consolidated balance sheets as of June 30, 2014, and the related consolidated statements of operations and other changes in net assets, changes in net assets, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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 the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

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Opinion

In our opinion, the 2014 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Doctors Community Hospital and Subsidiaries as of June 30, 2014, and the results of its operations and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Prior Period Financial Statements

The consolidated financial statements as of June 30, 2013, were audited by Cohen, Rutherford, + Knight, P.C., certain of whose shareholders joined Dixon Hughes Goodman LLP as of June 1, 2014, and whose report dated October 15, 2013, expressed an unmodified opinion on those statements.

Supplemental Information

Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements as a whole. The consolidating information presented in the supplemental schedules is presented for purposes of additional analysis rather than to present the financial position and results of operations of the individual organizations, and is not a required part of the basic consolidated financial statements. Such information is the responsibility of management, 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 consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Tysons, Virginia
October 14, 2014

Dixon Hughes Goodman LLP

Consolidated Balance Sheets
Doctors Community Hospital and Subsidiaries

ASSETS	June 30 2014	2013
CURRENT ASSETS		
Cash and cash equivalents	$ 25,859,996	$ 25,123,464
Assets whose use is limited for debt service - *Note B*	6,975,671	6,925,305
Patient accounts receivable, less uncollectible accounts of $8,243,666 and $7,887,543	25,317,369	25,529,632
Other amounts receivable	4,394,636	4,239,635
Inventories	3,558,048	3,612,320
Prepaid expenses	2,476,124	2,094,249
TOTAL CURRENT ASSETS	68,581,844	67,524,605
INVESTMENTS		
Marketable securities -- *Note B*	14,325,294	13,513,806
Joint ventures and equity investments -- *Note C*	4,301,945	4,277,759
	18,627,239	17,791,565
ASSETS WHOSE USE IS LIMITED -- *Note B*		
Investments held by trustee or authority, less current portion	20,616,604	22,658,419
LAND, BUILDINGS, AND EQUIPMENT, NET -- *Note E*	116,477,584	121,823,767
DEFERRED FINANCING COSTS, NET	2,007,218	2,160,314
GOODWILL -- *Note L*	2,948,390	2,494,734
OTHER ASSETS -- *Note I*	22,992,957	21,825,131
TOTAL ASSETS	$ 252,251,836	$ 256,278,535

See the accompanying notes to the consolidated financial statements.

Consolidated Balance Sheets – Continued

Doctors Community Hospital and Subsidiaries

LIABILITIES	June 30 2014	June 30 2013
CURRENT LIABILITIES		
Accounts payable and accrued expenses	$ 14,943,813	$ 16,114,344
Salaries, wages, and related items	11,410,022	11,182,729
Advances from third party payers	7,834,889	6,690,340
Interest payable to bondholders	4,043,381	4,102,931
Current portion of long-term obligations - *Note F*	4,944,793	4,396,299
TOTAL CURRENT LIABILITIES	43,176,898	42,486,643
NONCURRENT LIABILITIES		
Other noncurrent liabilities - *Note I*	12,959,854	12,493,813
Pension obligation - *Note I*	5,564,662	5,969,173
Long-term obligations, net of current portion - *Note F*	143,952,393	148,638,270
TOTAL LIABILITIES	205,653,807	209,587,899
NET ASSETS		
Unrestricted	43,016,230	43,000,823
Noncontrolling interest	1,924,807	2,127,165
TOTAL UNRESTRICTED NET ASSETS	44,941,037	45,127,988
Temporarily restricted - *Note M*	1,656,992	1,562,648
TOTAL NET ASSETS	46,598,029	46,690,636
COMMITMENTS AND CONTINGENCIES - *Notes F, G, H, I and K*		
TOTAL LIABILITIES AND NET ASSETS	$ 252,251,836	$ 256,278,535

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

	Year Ended June 30	
	2014	**2013**
REVENUE		
Patient service revenue, net of contractual allowances and discounts -- *Note A*	$ 206,438,060	$ 191,725,858
Provision for bad debts	(6,833,168)	(4,317,821)
Net patient service revenue less provision for bad debts	199,604,892	187,408,037
Other operating revenue -- *Note A*	4,309,093	7,951,345
Pledges and contributions	222,477	408,247
Net assets released from restrictions used for operations	304,906	106,673
TOTAL OPERATING REVENUE	204,441,368	195,874,302
EXPENSES		
Salaries and wages	90,581,114	86,757,025
Employee benefits	15,406,330	15,171,707
Purchased services -- *Note D*	30,995,624	30,476,771
Supplies	34,591,586	34,705,354
Other expenses -- *Notes G and H*	14,160,455	13,127,190
Depreciation -- *Note E*	9,569,518	9,866,727
Amortization	153,096	156,899
Fundraising	182,953	189,133
Interest -- *Note F*	7,905,678	8,140,974
TOTAL EXPENSES	203,546,354	198,591,780
INCOME (LOSS) FROM OPERATIONS	895,014	(2,717,478)
NONOPERATING GAINS (LOSSES)		
Gain/(Loss) on sale of property	(80,162)	117,684
Unrealized gain/(loss) on trading securities -- *Note B*	2,572	(117,655)
Gain/(loss) in joint ventures -- *Note C*	(165,621)	1,302,371
EXCESS OF REVENUE OVER EXPENSES (EXPENSES OVER REVENUE)	651,803	(1,415,078)
Subsidiary distributions to noncontrolling interest-holders	(1,187,426)	(1,225,600)
Pension - related changes other than net periodic pension cost - *Note I*	160,998	1,615,830
DECREASE IN UNRESTRICTED NET ASSETS	$ (374,625)	$ (1,024,848)

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, 2014			Year Ended June 30, 2013		
	Total	Controlling Interests	Noncontrolling Interests	Total	Controlling Interests	Noncontrolling Interests
UNRESTRICTED NET ASSETS						
Excess of revenue over expenses (expenses over revenue)	$ 651,803	$ (333,265)	$ 985,068	$ (1,415,078)	$ (2,534,718)	$ 1,119,640
Dividends paid to noncontrolling interest-holders	(1,187,426)	0	(1,187,426)	(1,225,600)	0	(1,225,600)
Pension - related changes other than net periodic pension cost -- *Note I*	160,998	160,998	0	1,615,830	1,615,830	0
DECREASE IN UNRESTRICTED NET ASSETS AND NONCONTROLLING INTERESTS	(374,625)	(172,267)	(202,358)	(1,024,848)	(918,888)	(105,960)
TEMPORARILY RESTRICTED NET ASSETS						
Restricted contributions	586,922	586,922	0	616,423	616,423	0
Net assets released from restrictions for operations	(304,904)	(304,904)	0	(106,673)	(106,673)	0
INCREASE IN TEMPORARILY RESTRICTED NET ASSETS	282,018	282,018	0	509,750	509,750	0
INCREASE/(DECREASE) IN NET ASSETS	(92,607)	109,751	(202,358)	(515,098)	(409,138)	(105,960)
NET ASSETS, BEGINNING OF YEAR	46,690,636	44,563,471	2,127,165	47,205,734	44,972,609	2,233,125
NET ASSETS, END OF YEAR	$ 46,598,029	$ 44,673,222	$ 1,924,807	$ 46,690,636	$ 44,563,471	$ 2,127,165

See the accompanying notes to the consolidated financial statements.

Consolidated Statements of Cash Flows
Doctors Community Hospital and Subsidiaries

	Year Ended June 30	
OPERATING ACTIVITIES AND OTHER GAINS	**2014**	**2013**
Decrease in net assets	$ (92,607)	$ (515,098)
Adjustments to reconcile increase decrease in net assets to net cash and cash equivalents provided by operating activities		
Restricted contributions received	(586,922)	(616,423)
Depreciation	9,569,518	9,866,727
Provision for bad debts	6,833,168	4,317,821
Unrealized loss (gain) on investments	(2,572)	117,655
Gain on sale of property	80,162	(117,684)
Realized loss (gain) on sale of investments	122,027	(2,695)
Amortization on bond issue and premium and discount	17,327	(144,975)
Increase in joint ventures and equity investments	165,621	(1,389,681)
Increase (decrease) in:		
Accounts payable and accrued expenses, exclusive of accrual for equipment costs	(1,170,531)	310,387
Accrued salaries, wages, and related items	227,293	930,575
Advances from third party payers	1,144,549	(1,258,376)
Pension obligation	(404,511)	(1,606,483)
Interest payable	(59,550)	(49,701)
Other liabilities	466,041	469,846
Decrease (increase) in:		
Net patient accounts receivable	(6,620,905)	(849,571)
Other receivables	(155,001)	(468,247)
Inventories	54,272	85,954
Deferred financing costs	0	156,899
Prepaid expenses and other assets	(1,549,701)	(1,034,673)
NET CASH AND CASH EQUIVALENTS PROVIDED BY OPERATING ACTIVITIES AND OTHER GAINS	8,037,678	8,202,257
INVESTING ACTIVITIES		
Net sales of trading investments, including assets whose use is limited	1,060,506	1,765,739
Increase in Goodwill	(453,656)	0
Increase in joint ventures and equity investments	(189,807)	0
Proceeds from sale on property	0	238,740
Purchase of property, plant and equipment	(3,585,479)	(6,811,029)
NET CASH AND CASH EQUIVALENTS USED IN INVESTING ACTIVITIES	(3,168,436)	(4,806,550)

(Continued)

Consolidated Statements of Cash Flows - continued

Doctors Community Hospital and Subsidiaries

	Year Ended June 30	
FINANCING ACTIVITIES	**2014**	**2013**
Principal payments on debt	(4,719,632)	(3,809,406)
Restricted contributions received	586,922	616,423
NET CASH AND CASH EQUIVALENTS USED IN FINANCING ACTIVITIES	(4,132,710)	(3,192,982)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVILENTS	736,532	202,725
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	25,123,464	24,920,739
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 25,859,996	$ 25,123,464
SUPPLEMENTAL DISCLOSURE OF NON CASH INFORMATION:		
Acquisition of equipment under capital lease	$ 718,018	$ 498,260

See the accompanying notes to the consolidated financial statements.

Notes to the Consolidated Financial Statements
Doctors Community Hospital and Subsidiaries

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 198 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 several wholly owned/controlled subsidiaries: Doctors Community Health Ventures, Inc. (Health Ventures), Doctors Community Hospital Foundation, Inc. (the Foundation), and Doctors Community Healthcare Programs (CHP).

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.

CHP consists of four wholly owned/controlled entities: Spine Team Maryland, LLC (STM), Capital Orthopedics Specialists, LLC (COS), Doctors Community Hospital Clinics (CLINICS), LLC and DCH Integrated Healthcare Network, LLC (CIN). 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. COS is a limited liability company formed in Maryland for the purpose of providing surgical services for the residents of Prince Georges County and surrounding areas. CLINICS is a limited liability company formed in Maryland for the purpose of providing outpatient medical care for the residents of Prince Georges County and surrounding areas. The CIN is a limited liability company formed in Maryland for the purpose of providing a program of clinical integration and an accountable care organization among health care providers serving 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 CHP (collectively, the Company). All intercompany accounts and transactions have been eliminated in consolidation.

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

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.

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, consists of investments in equity and debt securities and 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 8% of Hospital charges are given to Medicare, Medicaid, and certain approved commercial health insurance providers 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

The Hospital signed a new agreement with HSCRC titled Global Budget Revenue (GBR) in December 2013, effective July 1, 2013. This agreement defines the patient revenue methodology for the hospitals in Maryland. The Commission defines the GBR in the Hospital's agreement as follows: "The Global Budget Revenue ("GBR") model is a revenue constraint and quality improvement system designed by the Maryland Health Services Cost Review Commission ("HSCRC") to provide hospitals with strong financial incentives to manage their resources efficiently and effectively in order to slow the rate of increase in health care costs and improve health care delivery processes and outcomes. The GBR model is consistent with the Hospital's mission to provide the highest value of care possible to its patients and the communities it serves." ("HSCRC – see Note J)

Patient Revenue and Accounts Receivable – Continued

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

	2014	2013
Medicare	42%	43%
Medicaid	16%	15%
Blue Cross Blue Shield	18%	18%
Other third-party payers	19%	19%
Self-pay patients	5%	5%
	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:

	2014	2013
Medicare	30%	32%
Medicaid	24%	16%
Blue Cross Blue Shield	10%	8%
Other third-party payers	20%	18%
Self-pay patients	16%	26%
	100%	100%

Patient service revenue, net of contractual allowances and discounts and after the provision for bad debts, is described in the table below for fiscal years 2014 and 2013. Amounts classified as self pay do not include coinsurance and deductibles related to third party payers.

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

Patient Revenue and Accounts Receivable – Continued

	2014	2013
Gross patient revenue:		
Third party payers	$ 240,113,397	$ 238,344,007
Self pay	12,726,263	11,410,812
Total gross patient revenue	$ 252,839,660	$ 249,754,819
Deductions:		
Discounts and allowances	(31,674,913)	(42,139,465)
Charity care	(14,726,686)	(15,889,496)
Net patient service revenue	206,438,061	191,725,858
Less: provisions for bad debt	(6,833,168)	(4,317,821)
Net patient service revenue	$ 199,604,893	$ 187,408,037

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.

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, 2014 and 2013, 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

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

policy is to treat restricted contributions recorded and released in the same fiscal year as unrestricted contributions.

Excess of Revenue over Expenses/(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 non-controlling 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.

Under current accounting standards, the Company is required to report the cost of providing charity care. The cost of charity care provided by the Hospital and DRCC totaled $14,730,363 and $15,889,496 for the years ended June 30, 2014 and 2013, respectively. Rates charged by the Hospital for regulated services are determined based on assessment of direct and indirect cost calculated pursuant to the methodology established by the Maryland Health Services Cost Review Commission ("HSCRC" – see *Note J*), and therefore the cost of charity services noted above for the Hospital are equivalent to its established rates for those services. For any charity services rendered by the Company other than from the Hospital, the cost of charity care is calculated by applying the estimated total cost-to-charge ratio for the non-Hospital services to the total amount of charges for services provided to patients benefitting from the charity care policies of the Company's non-Hospital affiliates. These charges are excluded from consolidated net patient service revenue.

The Hospital receives a payment from the HSCRC with respect to an Uncompensated Care Fund ("UCC") established for rate-regulated hospitals in Maryland. The UCC is intended to provide Maryland hospitals with funds to support the provision of uncompensated care at those hospitals. The Hospital received $1,866,843 for 2014 and $923,876 for 2013 in UCC payments. All hospitals contribute to the Health Care Coverage Fund (HCCF) that supports the expansion of Medicaid eligibility and support the Medicaid program. The Hospital contributed $2,252,528 for 2014 and $2,376,776 for 2013 to HCCF.

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 operations and 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 $356,883 and $333,062 at June 30, 2014 and 2014, respectively, and is included in other amounts receivable in the accompanying consolidated balance sheets.

Other Operating Revenues

The Hospital met compliance requirements to receive incentive payments for upgrading and implementing certified electronic health record systems and becoming a meaningful user under the provisions of the American Recovery and Reinvestment Act of 2009. The Hospital recognized $1,275,567 and $5,165,622 of meaningful use incentives during the years ended June 30, 2014 and 2013, respectively, and reported these amounts as other operating revenue in the accompanying statements of operations and other changes in unrestricted net assets. The portion of the meaningful use incentive earned during fiscal year 2014 and 2013 that was not yet received is $1,026,592 and $1,785,555 and is recorded as other amounts receivable in the accompanying consolidated balance sheets.

Advertising Costs

The Hospital expenses advertising costs as they are incurred. Advertising expense was $867,959 and $533,778 for the fiscal years June 30, 2014 and 2013, respectively, and is reported as other expense in the accompanying consolidated statements of operations and other changes in unrestricted net assets.

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

Functional Expenses

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

	Year Ended June 30	
	2014	**2013**
Health care services	$ 146,160,835	$ 142,518,752
Management and general	56,840,325	55,423,959
Fundraising	545,194	649,069
	$ 203,546,354	$ 198,591,780

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 noncurrent assets in the accompanying consolidated balance sheets, are as follows:

	2014	**2013**
Deferred financing costs	$ 3,008,043	$ 3,008,043
Accumulated amortization	(1,000,825)	(847,729)
	$ 2,007,218	$ 2,160,314

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

2015	$ 149,133
2016	144,974
2017	140,603
2018	136,015
2019	131,192
	$ 701,917

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

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 amounts receivable, 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 (see *Note B*)

- **Long-term debt***:* Fair values of the Hospital's fixed-rate debt are based on current traded values.

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 2014 and 2013.

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

Health Ventures is subject to corporate income tax, and incurred an income tax liability of $0 for each year ended June 30, 2014 and 2013.

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 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 (IRC), 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.

The CHP entities are Maryland limited liability companies that have not elected to be taxed as corporations under current treasury regulations. CHP entities are wholly owned by the Hospital. As such, each CHP entity is a "disregarded entity" under current IRC 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, 2014 (see *Note L*).

Subsequent Events

Subsequent events have been evaluated by management through October 14, 2014, which is the date the consolidated financial statements were available to be issued.

Note B – Investments

The following is a summary of investment securities:

	As of June 30	
	2014	**2013**
Marketable securities:		
Cash and cash equivalents		
Cash	$ 79	$ 679
Money market funds	7,265,647	10,394,775
Equity		
Mutual funds	7,059,568	3,118,352
	$ 14,325,294	$ 13,513,806

	As of June 30	
	2014	**2013**
Assets whose use is limited:		
Cash and cash equivalents		
Money market funds	$ 13,995,368	$ 8,941,538
Fixed maturity		
U.S. government agency bonds/notes	13,596,906	20,642,186
	$ 27,592,275	$ 29,583,724

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

Note B - Assets Whose Use is Limited

	As of June 30	
	2013	**2013**
Funds held by Trustee or Authority:		
Debt service reserve fund	$ 27,592,275	$ 29,583,724
Less assets required for current obligations	(6,975,671)	(6,925,305)
	$ 20,616,604	$ 22,658,419

Note B – Investments – Continued

Investment return is summarized as follows:

	Other Operating Revenue	Non Operating Gains (Losses)	Total
2014			
Interest and dividend income	$ 295,859	$ 0	$ 295,859
Net realized gains	(122,027)	0	(122,027)
Net unrealized loss	0	2,572	2,572
Investment fees	(27,265)	0	(27,265)
	$ 146,566	$ 2,572	$ 149,138
2013			
Interest and dividend income	$ 195,125	$ 0	$ 195,125
Net realized gains	2,695	0	2,695
Net unrealized loss	0	(117,655)	(117,655)
Investment fees	(26,038)	0	(26,038)
	$ 171,783	$ (117,655)	$ 54,128

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. 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.

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, 2014.

	Level 1	Level 2	Level 3	Total Fair Value
Cash and Cash Equivalents				
Cash	$ 79	$ 0	$ 0	$ 79
Money Market Funds	0	21,261,016	0	21,261,016
Fixed Income				
U.S. Government Agency Bonds/Notes	0	13,596,906	0	13,596,906
Equity Securities				
Mutual Funds				
Short-Term Bond	545,535	0	0	545,535
Merger Arbitrage	6,058,037	0	0	6,058,037
World Bond	351,410	0	0	351,410
Floating Rate Bonds	212,872	0	0	212,872
High-Yield Bond	271,052	0	0	271,052
Intermediate-Term Bond	235,081	0	0	235,081
Equity Large Blend	301,401	0	0	301,401
Long/Short Equity	267,859	0	0	267,859
Moderate Allocation	307,287	0	0	307,287
Mid-Cap Growth	449,097	0	0	449,097
Real Estate	209,357	0	0	209,357
Foreign Large Blend	1,125,126	0	0	1,125,126
Large Blend	270,255	0	0	270,255
Diversified Emerging Markets	306,921	0	0	306,921
Large Growth	156,461	0	0	156,461
Small Growth	353,914	0	0	353,914
Total assets	$ 11,421,743	$ 34,857,922	$ 0	$ 46,279,665

The total Investments of $46,284,410 includes deposits in transit of $4,745 plus financial instruments of $46,279,665. The above table includes financial instruments of $4,366,839 included in other assets on the consolidated balance sheet for deferred compensation and other arrangements.

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, 2013:

	Level 1	Level 2	Level 3	Total Fair Value
Cash and Cash Equivalents				
Cash	$ 679	$ 0	$ 0	$ 679
Money Market Funds	0	19,336,313	0	19,336,313
Fixed Income				
U.S. Government Agency Bonds/Notes	0	20,642,187	0	20,642,187
Equity Securities				
Mutual Funds				
Short Government	1,146,782	0	0	1,146,782
Ultrashort Bond	798,149	0	0	798,149
Short-Term Bond	1,618,506	0	0	1,618,506
Intermediate Government	768,331	0	0	768,331
Market Neutral	10,101	0	0	10,101
World Bond	291,125	0	0	291,125
High-Yield Bond	221,094	0	0	221,094
Intermediate-Term Bond	216,217	0	0	216,217
Moderate Allocation	74,735	0	0	74,735
Mid-Cap Growth	368,443	0	0	368,443
Real Estate	181,215	0	0	181,215
Foreign Large Blend	917,340	0	0	917,340
Large Blend	216,532	0	0	216,532
Diversified Emerging Markets	231,627	0	0	231,627
Large Growth	117,348	0	0	117,348
Small Growth	263,029	0	0	263,029
Total assets	$ 7,441,252	$ 39,978,500	$ 0	$ 47,419,752

There were no significant transfers between fair value hierarchy levels for the years ended June 30, 2014 and 2013.

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 Health Ventures does not control the investee. The investment income of these joint ventures and equity investments is reported in non-operating gains/losses in the accompanying consolidated statements of operations and other changes in unrestricted net assets. These investments, which are reported as noncurrent assets in the accompanying consolidated statements, are summarized as follows as of June 30:

Name	Percent Ownership	Accounting Method	2014	2013
Magnolia Gardens LLC	51%	Equity	$ 3,477,137	$ 3,240,305
Metropolitan Ambulatory Urological Institute, LLC	30%	Equity	87,258	78,330
Diagnostic Imaging, LLC	50%	Equity	737,550	959,124
			$ 4,301,945	$ 4,277,759

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 (MMS). Since MMS is wholly owned by Health Ventures, the amounts loaned to MMS have been eliminated in consolidation.

A member of the board of directors maintains a business that had transactions with the Hospital that amounted to $494,640 and $465,317 for the years ended June 30, 2014 and 2013, respectively. The Medical Director of Radiology for the Hospital is an investor in Diagnostic Imaging, LLC, which is an unconsolidated subsidiary of Health Ventures.

Note E – Land, Buildings, and Equipment

Land, buildings, and equipment are summarized as follows:

		June 30	
Name	**Useful Life**	**2014**	**2013**
Land improvements	10-40 Years	$ 3,809,176	$ 3,809,176
Buildings	4-40 Years	125,455,198	124,956,992
Leasehold improvements	4-40 Years	2,434,001	2,506,001
Furniture and equipment	2-20 Years	82,156,651	80,940,538
Equipment under capital lease obligations	2-20 Years	10,399,214	10,209,215
		224,254,240	222,421,922
Less accumulated depreciation		116,908,275	107,654,905
		107,345,965	114,767,017
Construction in progress		2,993,117	918,248
Land		6,138,502	6,138,502
		$ 116,477,584	$ 121,823,767

Accumulated depreciation includes accumulated amortization of capital leased equipment in the amount of $4,161,728 and $3,625,467 as of June 30, 2014 and 2013, respectively. Depreciation expense related to capital leased equipment was $1,193,793 and $1,139,367 for fiscal year 2014 and 2013, respectively.

Note F – Long-Term Debt

Long-term indebtedness consisted of the following:

	June 30 2014	June 30 2013
Maryland Health and Higher Education Facilities Authority Revenue Bonds, Series 2007A:		
4.00% term bonds due July 1, 2013	$ 0	$ 2,580,000
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	5,030,000	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 Orthopedics Practice Purchase	350,428	0
Capital leases	2,819,628	4,291,670
	149,140,056	153,141,670
Current portion of long-term debt	(4,944,793)	(4,396,299)
Original issue premium, net of accumulated amortization	1,484,325	1,658,412
Original issue discount, net of accumulated amortization	(1,727,195)	(1,765,513)
	$ 143,952,393	$ 148,638,270

The fair value of the Company's long-term debt, based on quoted market prices, was $150,048,105 and $149,981,460 at June 30, 2014 and 2013, 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:

2015	$ 4,944,793
2016	4,207,445
2017	3,414,849
2018	3,537,970
2019	3,650,000
2020 and after	129,385,000
	$ 149,140,056

Total interest paid for the years ended June 30, 2014 and 2013 was $7,805,067 and $8,055,098, 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 Series 2010 Bonds and the Series 2007 Bonds are secured by the revenue and accounts receivable of the Hospital. 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 2014 and 2013.

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 $1,766,359 and $2,523,453 on June 30, 2014 and 2013, 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, 2014 are as follows:

2015	$	784,871
2016		813,688
2017		104,849
2018		62,970
	$	1,766,378

In July 2012, DRCC refinanced the capital lease. The refinanced balance was $2,711,191 at an interest rate of 3.6%. Other debt includes the Hospital's obligations under various other capital leases (see *Note H*).

In September 2013, the Hospital acquired an orthopedic practice. The payment for the practice included a down payment and 23 monthly payments. The amount paid in FY 2014 was $394,572 and the remaining liability totals $350,428 as of June 30, 2014.

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 partial interest in the captive that is accounted for using the cost method. The cost of $15,000 is recorded in other noncurrent assets in the accompanying consolidated balance sheets as of June 30, 2014 and 2013. 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 insureds 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, 2014. If the financial condition of Freestate were to materially deteriorate in the future, and Freestate

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

was unable to pay its claim obligations, the responsibility to pay those claims would return to the member hospitals.

The captive is responsible for claims up to $1,000,000 for each and every loss event. Additional 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 estimated unpaid loss liability reserved by the captive for the Hospital was $7,760,584 and $7,332,914 at June 30, 2014 and 2013, respectively. These amounts are included in long term assets and long term liabilities in the accompanying consolidated balance sheets. The liability for all claims incurred but not reported for the Hospital was $1,242,792 and $1,314,231 at June 30, 2014 and 2013, respectively. In accordance with current accounting standards, the June 30, 2014 and 2013 unpaid loss liabilities are recorded in noncurrent liabilities and the related anticipated insurance recoveries were reported in noncurrent assets, in the accompanying consolidated balance sheets. The Hospital engages a consulting actuary to assist in the determination of all professional liability claims incurred but not reported.

The Hospital is self-insured against workers' compensation claims up to a per-claim limit of $500,000 with an annual limitation of approximately $1,000,000. A liability has been recorded for all known claims and an estimate for claims incurred but not reported in the amount of $312,102 and $713,992 at June 30, 2014 and 2013, 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, COS, 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 deprecation expense in the consolidated statements of operations and other changes in unrestricted net assets.

Note H – Leases - Continued

Future minimum lease payments as of June 30, 2014 are as follows:

	Capital Leases	Operating Leases
2015	$ 1,621,322	$ 1,916,842
2016	1,030,487	1,876,380
2017	104,849	1,446,584
2018	62,970	1,239,495
2019 and thereafter	-	3,473,191
Total minimum lease payments	2,819,628	9,952,493
Current portion of capital leases	(1,621,322)	
Capital lease obligations, less current portion	$ 1,198,306	

Total rental expense reported in the accompanying consolidated statements of operations and other changes in unrestricted net assets for the years ended June 30, 2014 and 2013 was $4,389,620 and $4,039,310, respectively.

Note I – Retirement Plans

The Hospital froze the defined benefit pension plan that it sponsors (the Plan) in 2011, which covered substantially all employees. The Plan curtailment was recognized in 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 employee 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 $1,011,842 to the Plan during 2015 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:

	For the Year Ended	
	2014	2013
Accumulated Benefit Obligation	$ 22,243,504	$ 21,113,509
Change in Benefit Obligation		
Benefit Obligation at beginning of year	$ 21,113,509	$ 22,021,920
Interest cost	842,064	770,733
Actuarial loss/(gain)	978,837	(1,240,851)
Benefits paid	(690,906)	(438,293)
Benefit Obligation at End of Year	$ 22,243,504	$ 21,113,509
Change in Plan Assets		
Fair value of plan assets at beginning of year	$ 15,144,336	$ 14,446,264
Actual return on plan assets	1,644,471	789,666
Employer contributions	580,941	346,699
Benefits paid	(690,906)	(438,293)
Fair Value of Plan Assets at End of Year	$ 16,678,842	$ 15,144,336
Funded Status (Pension Obligation)	$ (5,564,662)	$ (5,969,173)
Components of Net Periodic Benefit Costs		
Interest cost	842,064	770,733
Expected return on plan assets	(906,673)	(889,123)
Recognition of loss from change in measurement date	402,037	474,436
Net Period Pension Costs	$ 337,428	$ 356,046

Note I – Retirement Plans – Continued

The total amount recognized in unrestricted net assets in the accompanying consolidated financial statements for 2014 and 2013 is as follows:

	2014	2013
Net loss	$ 8,258,310	$ 8,419,308
Prior service costs	0	0
	$ 8,258,310	$ 8,419,308

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

	2014	2013
Equity securities	39%	40%
Fixed maturity	61%	60%
	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% fixed maturity securities and cash as of June 30, 2014.

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

2015	$ 2,022,201
2016	792,762
2017	1,017,056
2018	1,276,859
2019	1,199,765
2020 - 2024	6,901,764
Total	$ 13,210,407

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:

	2014	2013
Discount rate	3.85%	4.30%
Expected return on Plan assets	6.50%	6.50%
Rate of compensation increase	N/A	N/A

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, 2014:

	Level 1	Level 2	Level 3	Total Fair Value
Equity Securities				
Mutual Funds				
Diversified Emerging Mkts	$ 463,577	$ 0	$ 0	$ 463,577
Foreign Large Blend	369,470	0	0	369,470
Foreign Small/Mid Growth	93,747	0	0	93,747
High Yield Bond	1,744,697	0	0	1,744,697
Inflation-Protected Bond	1,652,923	0	0	1,652,923
Intermediate Government	1,634,118	0	0	1,634,118
Intermediate-Term Bond	2,621,475	0	0	2,621,475
Large Growth	1,479,316	0	0	1,479,316
Large Value	1,283,333	0	0	1,283,333
Mid-Cap Growth	909,283	0	0	909,283
Mid-Cap Value	931,320	0	0	931,320
Multisector Bond	2,558,017	0	0	2,558,017
Small Growth	375,837	0	0	375,837
Small Value	561,729	0	0	561,729
Total assets	$ 16,678,842	$ 0	$ 0	$ 16,678,842

Note I – Retirement Plans – 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, 2013:

	Level 1	Level 2	Level 3	Total Fair Value
Equity Securities				
Mutual Funds				
Diversified emerging markets	$ 302,772	$ 0	$ 0	$ 302,772
Foreign large blend	317,085	0	0	317,085
Foreign small/mid growth	168,542	0	0	168,542
Inflation-protected bond	1,438,426	0	0	1,438,426
Intermediate government	2,072,049	0	0	2,072,049
Intermediate-term bond	3,281,486	0	0	3,281,486
Large growth	1,371,019	0	0	1,371,019
Large value	1,239,208	0	0	1,239,208
Mid-cap growth	839,180	0	0	839,180
Mid-cap value	857,523	0	0	857,523
Multisector bond	2,358,510	0	0	2,358,510
Small growth	375,371	0	0	375,371
Small value	523,165	0	0	523,165
Total assets	$ 15,144,336	$ 0	$ 0	$ 15,144,336

There were no significant transfers between fair value hierarchy levels for the years ended June 30, 2014 and 2013.

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 $3,956,478 and $3,846,668 as of June 30, 2014 and 2013, respectively. During 2014 and 2013, distributions of $360,855 and $1,075,072 were made to participants in the deferred compensation plan, respectively.

The Hospital is the beneficiary of split dollar life insurance policies in place for certain executives. Approximately $9,300,000 is included in other assets at June 30, 2014 and 2013, 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.

In January 2014, the State of Maryland signed a new CMS waiver focused on population health. The current rate of reimbursement for principally all hospital inpatient and outpatient 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, the rate of increase for costs per hospital services is below the national average, and other specific quality indicators are met. In anticipation of this new waiver, the Commission developed a new methodology on the rate orders provided to the hospitals which is called Global Budgeted Rate (GBR).

The Commission defines the GBR in the Hospital's agreement as follows: "The Global Budget Revenue ("GBR") model is a revenue constraint and quality improvement system designed by the Maryland Health Services Cost Review Commission ("HSCRC") to provide hospitals with strong financial incentives to manage their resources efficiently and effectively in order to slow the rate of increase in health care costs and improve health care delivery processes and outcomes. The GBR model is consistent with the Hospital's mission to provide the highest value of care possible to its patients and the communities it serves."

The Hospital signed its GBR in December 2013, effective July 1, 2013. Management believes that a waiver program will remain in effect at least through June 2015. At June 30, 2014, the Hospital was in compliance with the GBR agreement.

The timing of the Commission's rate adjustments to the annual GBR for the Hospital could result in an increase or reduction in rates due to the variances and penalties 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.

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,

Note K – Commitments and Contingencies – Continued

Risk Factor - Continued

operating results and cash flows of the Hospital. In June 2013 the Hospital was surveyed by Joint Commission and received a full three-year Joint Commission accreditation through July 2016.

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.

Construction Commitments

The Hospital has entered into a contract related to a construction project. The total contract committed to by the Company was approximately $8,400,000. As of June 30, 2014, the remaining commitment under the contract was approximately $7,200,000.

Note L – Goodwill

The Company uses the acquisition method of accounting to record goodwill when purchasing physician practices and other similar entities. The table below presents goodwill that has been recorded as of June 30 for the following acquisitions:

	June 30	
	2014	**2013**
Cancer center	$ 1,062,531	$ 1,062,531
Orthopedic practice	376,316	0
Nursing home	766,285	766,285
Cancer center	646,975	646,975
Surgical practice	77,340	0
ENT practice	18,943	18,943
	$ 2,948,390	$ 2,494,734

Note M – Temporarily Restricted Net Assets

Temporarily restricted net assets are available as of June 30 for the following programs and projects:

	2014	2013
Nancy Heilman Scholarship Fund	$ 1,479	$ 1,479
Brian Erfan Memorial Fund	5,850	5,850
Jane Schafer Scholarship Fund	10,785	10,784
Rehabilitation Services	12,937	12,937
Cardiac Rehab Services	1,622	3,962
Borden Breast Center	20,000	20,000
Surgical Services	930,812	591,032
Diabetes Center	0	1,424
Lymphedema Center	12,976	20,000
Smoking Grant	9,684	0
Community Outreach	213	0
Komen Grant	618,439	892,984
UASI 2008 grant	2,177	2,177
MHA HPP Disaster Grant	19	19
Health fair Screening	30,000	0
	$ 1,656,992	$ 1,562,648

Supplemental Information

Doctors Community Hospital and Subsidiaries

Consolidating Balance Sheet Information
Doctors Community Hospital and Subsidiaries
June 30, 2014

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	DOCTORS COMMUNITY HEALTHCARE PROGRAMS	ELIMINATIONS	CONSOLIDATED
CURRENT ASSETS								
Cash and cash equivalents	$ 23,387,055	$ 447,316	$ 200,126	$ 814,017	$ 314,191	$ 697,291	$ 0	$ 25,859,996
Assets whose use is limited for debt service	6,975,671	0	0	0	0	0	0	6,975,671
Patient accounts receivable, net	20,982,049	0	2,251,137	952,418	28,720	1,103,045	0	25,317,369
Other amounts receivable	3,630,522	482,760	9,529	118,888	0	152,937	0	4,394,636
Inventories	3,478,600	0	3,951	0	75,497	0	0	3,558,048
Prepaid expenses	2,306,675	10,779	13,866	118,900	0	25,904	0	2,476,124
TOTAL CURRENT ASSETS	60,760,572	940,855	2,478,609	2,004,223	418,408	1,979,177	0	68,581,844
INVESTMENTS								
Marketable securities	14,162,333	162,961	0	0	0	0	0	14,325,294
Investment in Doctors Regional Cancer Center	2,508,569	0	0	0	0	0	(2,508,569)	0
Investment in Sleep Services of America, Inc.	378,663	0	0	0	0	0	(378,663)	0
Joint ventures and equity investments	0	0	4,301,945	0	0	0	0	4,301,945
Due to DCH	23,479,651	0	0	0	300,564	0	(23,780,215)	0
	40,529,216	162,961	4,301,945	0	300,564	0	(26,667,447)	18,627,239
ASSETS WHOSE USE IS LIMITED								
Investments held by trustee or authority, less current portic	20,616,604	0	0	0	0	0	0	20,616,604
Land and land improvements	9,947,647	0	0	0	0	0	0	9,947,647
Building and fixed equipment	117,393,104	0	0	0	0	476,040	0	117,869,144
Medical office building	8,062,095	0	0	0	0	0	0	8,062,095
Major movable equipment	82,656,553	0	800,370	9,344,376	1,308,385	404,143	0	94,513,827
Construction in progress	2,993,147	0	0	0	0	0	0	2,993,147
Accumulated depreciation	(109,576,355)	0	(489,764)	(5,353,493)	(1,243,705)	(244,958)	0	(116,908,275)
LAND, BUILDINGS, AND EQUIPMENT, NET	111,476,190	0	310,606	3,990,883	64,680	635,225	0	116,477,584
DEFERRED FINANCING COSTS, NET	2,007,218	0	0	0	0	0	0	2,007,218
GOODWILL	1,438,847	0	766,285	646,975	0	96,283	0	2,948,390
OTHER ASSETS	23,082,957	0	10,000	0	0	0	(100,000)	22,992,957
TOTAL ASSETS	$ 259,911,604	$ 1,103,816	$ 7,867,445	$ 6,642,081	$ 783,652	$ 2,710,685	$ (26,767,447)	$ 252,251,836

See Independent Auditors' Report.

Consolidating Balance Sheet Information

Doctors Community Hospital and Subsidiaries

June 30, 2014

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	DOCTORS COMMUNITY HEALTHCARE PROGRAMS	ELIMINATIONS	CONSOLIDATED
CURRENT LIABILITIES								
Accounts payable and accrued expenses	$ 14,310,596	$ 9,081	$ 83,228	$ 617,391	$ 119,883	$ 104,199	$ (300,565)	$ 14,943,813
Due to DCH	0	58,378	0	77,377	32,664	9,051,754	(9,220,173)	-
Salaries, wages, and related items	10,762,794	0	737,500	0	0	(90,272)	0	11,410,022
Advances from third party payers	7,834,889	0	0	0	0	0	0	7,834,889
Interest payable to bondholders	4,043,381	0	0	0	0	0	0	4,043,381
Current portion of long-term obligation	4,125,140	0	0	784,872	0	34,781	0	4,944,793
TOTAL CURRENT LIABILITIES	41,076,800	67,459	820,728	1,479,640	152,547	9,100,462	(9,520,738)	43,176,898
NONCURRENT LIABILITIES								
Other noncurrent liabilities	12,959,854	0	0	0	0	0	0	12,959,854
Pension obligation, net of current portion	5,564,662	0	0	0	0	0	0	5,564,662
Long-term obligations, net of current portion	142,961,411	0	14,259,479	981,507	0	9,475	(14,259,479)	143,952,393
TOTAL LIABILITIES	202,562,727	67,459	15,080,207	2,461,147	152,547	9,109,937	(23,780,217)	205,653,807
NET ASSETS AND MEMBERS' EQUITY								
Unrestricted	56,728,242	0	0	0	0	(1,842,484)	(11,869,528)	43,016,230
Members' equity	0	0	(7,212,762)	4,180,934	631,105	(4,556,768)	6,957,491	0
Noncontrolling interest	0	0	0	0	0	0	1,924,807	1,924,807
Total unrestricted net assets	56,728,242	0	(7,212,762)	4,180,934	631,105	(6,399,252)	(2,987,230)	44,941,037
Temporarily restricted	620,635	1,036,357	0	0	0	0	0	1,656,992
TOTAL NET ASSETS	57,348,877	1,036,357	(7,212,762)	4,180,934	631,105	(6,399,252)	(2,987,230)	46,598,029
TOTAL NET ASSETS AND LIABILITIES	$ 259,911,604	$ 1,103,816	$ 7,867,445	$ 6,642,081	$ 783,652	$ 2,710,685	$ (26,767,447)	$ 252,251,836

See Independent Auditors' Report.

Consolidating Balance Sheet Information

Doctors Community Hospital and Subsidiaries

For the Year Ended June 30, 2014

	DOCTORS COMMUNITY HOSPITAL	DOCTORS COMMUNITY HOSPITAL FOUNDATION, INC	DOCTORS COMMUNITY HEALTH VENTURES, INC	DOCTORS REGIONAL CANCER CENTER, LLC	DOCTORS COMMUNITY HOSPITAL SLEEP CENTER, LLC	DOCTORS COMMUNITY HEALTHCARE PROGRAMS	ELIMINATIONS	CONSOLIDATED
UNRESTRICTED NET ASSETS								
OPERATING REVENUE								
Inpatient revenue	$ 129,691,646	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0	$ 129,691,646
Outpatient revenue	89,447,130	0	9,436,970	7,250,796	3,282,789	13,730,328	0	123,148,013
Contractuals	(36,402,914)	0	(2,317,977)	0	0	(7,680,708)	0	(46,401,599)
Net patient service revenue, net of contractual allowances and discounts	$ 182,735,862	$ 0	$ 7,118,993	$ 7,250,796	$ 3,282,789	$ 6,049,620	$ 0	$ 206,438,060
Less provision for bad debts	(6,838,297)	0	0	(20,029)	0	25,158	0	(6,833,168)
Net patient service revenue less provision for bad debt	175,897,565	0	7,118,993	7,230,767	3,282,789	6,074,778	0	199,604,892
Other operating revenue	4,687,403	6,343	-	36,690	120,370	96,646	(638,357)	4,309,095
Pledges and contributions	6,120	216,357	0	0	0	0	0	222,477
Net assets released from restrictions used for operations	304,904	0	0	0	0	0	0	304,904
TOTAL OPERATING REVENUE	180,895,992	222,700	7,118,993	7,267,457	3,403,159	6,171,424	(638,357)	204,441,368
EXPENSES								
Salaries and wages	77,218,444	259,850	7,141,301	0	758,819	5,202,700	0	90,581,114
Employee benefits	13,511,218	65,087	661,235	0	156,741	1,012,049	0	15,406,330
Purchased services	24,031,951	11,083	492,099	4,995,572	241,065	1,223,854	0	30,995,624
Supplies	33,985,253	17,157	252,133	54,459	47,019	235,564	0	34,591,586
Other expenses	11,515,900	9,065	814,841	902,064	209,220	1,347,724	(638,359)	14,160,455
Depreciation	8,553,474	0	98,290	656,654	107,523	153,577	0	9,569,518
Amortization	153,096	0	0	0	0	0	0	153,096
Fundraising	0	182,953	0	0	0	0	0	182,953
Interest	7,826,868	0	0	78,810	0	0	0	7,905,678
TOTAL EXPENSES	176,796,204	545,195	9,459,899	6,687,559	1,520,387	9,175,468	(638,359)	203,546,354
INCOME (LOSS) FROM OPERATIONS	4,099,788	(322,495)	(2,340,906)	579,898	1,882,772	(3,004,044)	2	895,014
NONOPERATING INCOME								
Loss from sale of property	(80,162)	0	0	0	0	0	0	(80,162)
Unrealized loss on trading securities	2,572	0	0	0	0	0	0	2,572
Equity (loss) in joint ventures	1,477,601	0	(165,621)	0	0	0	(1,477,601)	(165,621)
EXCESS OF REVENUE OVER EXPENSES (EXPENSES OVER REVENUE)	5,499,799	(322,495)	(2,506,527)	579,898	1,882,772	(3,004,044)	(1,477,599)	651,803
Net asset transfer	(134,820)	134,820	0	0	0	0	0	0
Dividends paid	0	0	0	(784,564)	(2,184,000)	0	1,781,138	(1,187,426)
Contributions	0	586,922	0	0	0	0	0	586,922
Net assets released from restrictions for use in operations	(274,544)	(30,360)	0	0	0	0	0	(304,904)
Pension - related changes other than net periodic pension cost	160,998	0	0	0	0	0	0	160,998
Increase (decrease) in net assets	5,251,433	368,887	(2,506,527)	(204,666)	(301,228)	(3,004,044)	303,539	(92,607)
Net assets, beginning of year	52,097,444	667,471	(4,706,235)	4,385,600	932,333	(3,395,208)	(3,290,769)	46,690,636
Net assets, end of year	$ 57,348,877	$ 1,036,358	$ (7,212,762)	$ 4,180,934	$ 631,105	$ (6,399,252)	$ (2,987,230)	$ 46,598,029

See Independent Auditors' Report.