Consolidated Financial Statements and Supplementary Information

Frederick Regional Health System, Inc. and Subsidiaries
Years Ended June 30, 2015 and 2014
With Report of Independent Auditors

Ernst & Young LLP

Building a better
working world

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Consolidated Financial Statements
and Supplementary Information

Years Ended June 30, 2015 and 2014

Contents

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Report of Independent Auditors

The Board of Directors
Frederick Regional Health System, Inc. and Subsidiaries

We have audited the accompanying consolidated financial statements of Frederick Regional Health System, Inc. and Subsidiaries, which comprise the consolidated balance sheets as of June 30, 2015 and 2014, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of Monocacy Insurance, Ltd., a wholly-owned subsidiary, which statements reflect total assets of $13,231,952 and $12,400,961 as of June 30, 2015 and 2014, respectively, and net loss after elimination of intercompany revenues of $2,692,956 and $2,702,945, respectively, for the years then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Monocacy Insurance, Ltd., is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements.

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

Opinion

In our opinion, based on our audits and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Frederick Regional Health System, Inc. and subsidiaries as of June 30, 2015 and 2014, and the consolidated results of their operations, changes in their net assets, and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary consolidating information is presented for purposes of additional analysis and is not a required part of the 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 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. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Ernst & Young LLP

October 21, 2015

Frederick Regional Health System, Inc. and Subsidiaries

Consolidated Balance Sheets

(In Thousands)

	June 30	
	2015	**2014**
Assets		
Current assets:		
Cash and cash equivalents	**$ 31,432**	$ 33,668
Patient receivables, net	**48,100**	47,109
Other receivables	**1,860**	1,843
Inventory	**6,006**	4,405
Prepaid expenses	**2,430**	3,692
Loss on sale of property and equipment	**3,093**	4,033
Promises to give, net	**787**	711
Total current assets	**93,708**	95,461
Net property and equipment	**202,055**	199,089
Other assets:		
Assets limited as to use	**8,840**	19,546
Investments – donor restricted	**5,855**	3,705
Promises to give, net	**3,786**	3,447
Long-term investments	**134,931**	132,552
Other investments	**5,752**	3,489
Debt issuance costs, net	**1,379**	1,510
Other assets	**5,331**	5,739
Total other assets	**165,874**	169,988
Total assets	**$ 461,637**	$ 464,538

	June 30	
	2015	**2014**
Liabilities and net assets		
Current liabilities:		
Current maturities of long-term debt and capital lease obligations	**$ 5,103**	$ 5,697
Accounts payable	**22,052**	20,767
Accrued expenses	**18,402**	20,561
Advances from third-party payors	**9,813**	8,546
Loss on sale of property and equipment	**2,475**	4,693
Total current liabilities	**57,845**	60,264
Long-term liabilities, net of current portion:		
Long-term debt and capital lease obligations	**161,012**	166,275
Interest rate swap contract	**11,277**	11,238
Accrued pension expense	**18,868**	16,602
Other long-term liabilities	**19,487**	19,972
Total long-term liabilities, net of current portion	**210,644**	214,087
Total liabilities	**268,489**	274,351
Net assets:		
Unrestricted	**182,721**	182,314
Temporarily restricted	**9,451**	6,897
Permanently restricted	**976**	976
Total net assets	**193,148**	190,187
Total liabilities and net assets	**$ 461,637**	$ 464,538

See accompanying notes.

Frederick Regional Health System, Inc. and Subsidiaries

Consolidated Statements of Operations

(In Thousands)

	June 30 2015	June 30 2014
Unrestricted revenue and other support:		
Net patient service revenue	**$ 358,596**	$ 345,364
Provision for bad debts	**(3,099)**	(11,402)
Net patient service revenue less provision for bad debts	**355,497**	333,962
Other operating revenues	**9,068**	10,757
Gifts, bequests, and contributions	**2,968**	2,241
Loss on sale of property and equipment	**162**	132
Total unrestricted revenue and other support	**367,695**	347,092
Operating expenses:		
Salaries and wages	**130,059**	147,591
Employee benefits	**37,602**	38,027
Professional fees	**13,605**	12,978
Cost of goods sold	**58,211**	56,343
Supplies	**9,753**	9,357
Contract services	**71,287**	36,927
Other	**11,618**	11,985
Utilities	**4,265**	4,272
Insurance	**1,017**	3,821
Depreciation and amortization	**24,311**	25,852
Interest	**4,529**	4,874
Total operating expenses	**366,257**	352,027
Operating income (loss)	**1,438**	(4,935)
Other income gain (loss), net:		
Loss on sale of assets	**(97)**	(116)
Investment gain, net	**7,016**	6,161
Change in unrealized (losses) gains on trading securities, net	**(4,308)**	10,744
Realized and unrealized losses on interest rate swap contact, net	**(2,482)**	(2,156)
Other nonoperating income, net	**387**	944
Total other income, net	**516**	15,577
Excess of unrestricted revenue and other support over expenses	**1,954**	10,642
Other changes in unrestricted net assets:		
Pension adjustment	**(1,679)**	(3,738)
Released from restriction used to purchase capital	**132**	144
Increase in unrestricted net assets	**$ 407**	$ 7,048

See accompanying notes.

Frederick Regional Health System, Inc. and Subsidiaries

Consolidated Statements of Changes in Net Assets
(In Thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Net assets, June 30, 2013	$ 175,266	$ 5,367	$ 976	$ 181,609
Excess of unrestricted revenue and other support over expenses	10,642	–	–	10,642
Pension adjustment	(3,738)	–	–	(3,738)
Released from restriction used to purchase capital	144	(144)	–	–
Assets released from restrictions	–	(132)	–	(132)
Loss on sale of property and equipment	–	1,806	–	1,806
Changes in net assets	7,048	1,530	–	8,578
Net assets, June 30, 2014	182,314	6,897	976	190,187
Excess of unrestricted revenue and other support over expenses	**1,954**	**–**	**–**	**1,954**
Pension adjustment	**(1,679)**	**–**	**–**	**(1,679)**
Released from restriction used to purchase capital	**132**	**(132)**	**–**	**–**
Assets released from restrictions	**–**	**(162)**	**–**	**(162)**
Restricted gifts, bequests, and contributions	**–**	**2,848**	**–**	**2,848**
Changes in net assets	**407**	**2,554**	**–**	**2,961**
Net assets, June 30, 2015	**$ 182,721**	**$ 9,451**	**$ 976**	**$ 193,148**

See accompanying notes.

Frederick Regional Health System, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(In Thousands)

	Year Ended June 30	
	2015	**2014**
Operating activities		
Change in net assets	**$ 2,961**	$ 8,578
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation of property and equipment	**24,311**	25,852
Amortization of original issue discount, premium, and bond issue costs	**(29)**	(68)
Equity in earnings of joint ventures and Premier non-cash component	**(1,277)**	(232)
Loss on sale of property and equipment	**333**	116
Change in unrealized gains on trading securities, net	**4,311**	(10,744)
Proceeds from realized gains on investments – trading	**(6,554)**	(3,436)
Increase in investments – trading	**(1,828)**	(4,720)
Proceeds from restricted contributions	**(294)**	(276)
Change in pledges receivable	**(415)**	(1,062)
Realized and unrealized losses in interest rate swap, net	**2,482**	2,156
Change in operating assets and liabilities:		
Receivables, patient, and other	**(1,008)**	(470)
Other assets	**408**	(1,507)
Inventories and prepaids	**(339)**	(1,037)
Accounts payable	**1,285**	1,953
Accrued expenses	**(2,159)**	1,207
Accrued pension expense	**2,266**	4,441
Advances from third-party payors	**1,267**	(216)
Other short-term liabilities	**(2,218)**	1,420
Other long-term liabilities	**(485)**	3,134
Net cash provided by operating activities	**23,018**	25,089
Investing activities		
Decrease in assets limited as to use, nontrading, net	**11,646**	3,162
Realized losses on interest rate swap contract	**(2,442)**	(2,545)
Increase in other investments	**(1,444)**	–
Purchases of property and equipment	**(27,610)**	(21,132)
Net cash used in investing activities	**(19,850)**	(20,515)
Fundraising and financing activities		
Proceeds from restricted contributions	**294**	276
Repayments of long-term debt	**(5,698)**	(9,305)
Deferred financing costs paid	–	(70)
Proceeds from borrowings	–	5,000
Net cash used in fundraising and financing activities	**(5,404)**	(4,099)
Net (decrease) increase in cash and cash equivalents	**(2,236)**	475
Cash and cash equivalents at the beginning of the year	**33,668**	33,193
Cash and cash equivalents at the end of the year	**$ 31,432**	$ 33,668
Supplemental disclosures		
New capital lease obligation	**$ –**	$ –
Cash paid for interest	**$ 4,948**	$ 5,421

See accompanying notes.

1. Organization and Mission

Frederick Regional Health System, Inc. (the System) is a not-for-profit parent corporation formed on June 23, 2011, exempt from income tax under Section 501(a) of the Internal Revenue Code (the Code) as an organization described in Section 501(c)(3) whereby only unrelated business income as defined by Section 512(a)(1) of the Code is subject to federal income tax. The System has received a determination letter from the Internal Revenue Service (IRS) stating that it is exempt from federal income taxes under Section 501(c) of the Code.

Frederick Memorial Hospital, Inc. (FMH) is a not-for-profit hospital, exempt from federal income tax under Section 501(a) of the Code as an organization described in Section 501(c)(3) whereby only unrelated business income as defined by Section 512(a)(1) of the Code is subject to federal income tax. FMH is located in Frederick, Maryland, and provides health care services primarily to residents of Frederick County. FMH has received a determination letter from the IRS stating that it is exempt from federal income taxes under Section 501(c) of the Code.

Monocacy Insurance, LTD (MIL) is a Cayman Islands-domiciled single-parent captive incorporated on May 24, 2011, and holds an Unrestricted Class B insurance license issued under Section 7(2) of the Cayman Island Insurance Law. MIL directly provides primary medical professional liability and primary general liability coverage to the System.

Monocacy Health Partners, LLC (MHP) serves as a physician enterprise, providing governance, management, and support functions for employed physicians. MHP is a not-for-profit corporation, formed on June 23, 2011, and operational as of October 1, 2013, exempt from income tax under Section 501(a) of the Code as an organization described in Section 501(c)(3) only unrelated business income as defined by Section 512(a)(1) of the Code is subject to federal income tax. MHP has received a determination letter from the IRS stating that it is exempt from federal income taxes under Section 501(c) of the Code.

Frederick Health Services Corporation (FHSC) is a Maryland for-profit corporation, all of the stock of which is owned by the System. FHSC is subject to federal and state income taxes. No provision for income taxes has been recorded for 2015 or 2014 due to the availability of net operating loss carryforwards. As of June 30, 2015, FHSC recorded a net deferred tax asset of $807, which is presented in other assets on the balance sheet.

1. Organization and Mission (continued)

On March 25, 2014, Frederick Integrated Healthcare Network, LLC (FIHN) was formed and is operated exclusively as a charitable organization for charitable, scientific, and educational purposes within the meaning of Section 501(c)(3) of the Code and the Regulations thereunder as they now exist or as they may hereafter be amended. FIHN was formed to maintain and operate a program of clinical integration and an accountable care organization among health care providers. FIHN is a single-member LLC and a disregarded entity of FRHS for income tax purposes.

The Obligated Group for repayment of the Maryland Health and Higher Educational Facilities Authority (MHHEFA) Series 2012A and 2012B Bonds includes FMH, MHP, and FRHS.

On July 7, 2014, Frederick Memorial Hospital, Meritus Health, and Western Maryland Health System established Trivergent Health Alliance (THA), the parent company to Trivergent Health Alliance MSO (MSO). The MSO is a managed services organization that provides regional health care services. The purpose of the MSO is to increase operational efficiencies, reduce costs, and enhance the quality of care by focusing efforts in the following areas: human resources, information technology, laboratory services, materials management, pharmacy services, and revenue cycle. FMH contributed working capital of $100 to THA and $900 to the MSO for a 33% ownership interest, which is presented in Other Assets on the balance sheet. Upon establishment of the MSO all employees within the six service areas transferred employment from FMH to the MSO. The related cost to purchase the service from the MSO is recorded on the Consolidated Statement of Operations within Contract Services for the year ended June 30, 2015. The System paid a total of $33,494 to the MSO during the year ended June 30, 2015.

2. Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts and transactions of the System and its wholly owned subsidiaries: FMH, MIL, FHSC, MHP, and FIHN.

FMH has two wholly owned subsidiaries: Hospice of Frederick County, Inc. (HFC) and Emmitsburg Properties, LLC, both of which have been consolidated with FMH into the System in the accompanying consolidated financial statements. HFC, an independent 501(c)(3)

2. Significant Accounting Policies (continued)

organization controlled by FMH, operates as a fund raising organization for the benefit of hospice services and operates the Kline Hospice House. Emmitsburg Properties, LLC contains funds held as collateral on the outstanding Emmitsburg loans.

FHSC has four wholly owned subsidiaries: Rosehill of Frederick, LLC, Corporate Occupational Health Solutions, LLC, and Open MRI of Frederick, LLC, which are for-profit limited liability companies, and Frederick Surgical Services Corporation, all of which have been consolidated with FHSC into the System in the accompanying consolidated financial statements.

The accompanying consolidated financial statements include the accounts of the System and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Donor-Restricted Gifts

Unconditional promises to give cash and other assets 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. 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. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets if restricted for capital or reported in the statements of operations as net assets released from restrictions if restricted for operating purposes. Donations received with no restrictions and donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated statements of operations as other operating revenues.

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with an original maturity of three months or less. Those cash and money market funds that are classified as long-term investments are excluded from cash and cash equivalents.

2. Significant Accounting Policies (continued)

Patient Receivables and Allowances

The System's policy is to write off all patient accounts that have been identified as uncollectible. An allowance for doubtful accounts is recorded for accounts not yet written off that are anticipated to become uncollectible. Insurance coverage and credit information is obtained from patients when available. No collateral is obtained for accounts receivable.

When determining the allowance, the System considers the collectability of accounts based on past experience, taking into account contractually due amounts from third-party payors and current collection trends on third-party and self-pay receivables. Self-pay receivables include both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill. Credit risks are assessed based on historical write-offs, net of recoveries, as well as an analysis of the aged accounts receivable balances with allowances generally increasing as the receivable ages. The analysis of receivables is performed monthly, and the allowances are adjusted accordingly.

Inventory

Inventory is stated at the lower of cost or market. Cost is determined using the first-in, first-out method.

Cost of Goods Sold

Cost of goods sold consists primarily of drugs, medical supplies, and surgical implants used in the care and treatment of patients.

Investments and Assets Limited as to Use

The fair values of individual investments are based on quoted market prices of individual securities or investments or estimated amounts using quoted market prices of similar investments. Private equity investments are carried at cost, and hedge funds are accounted for using the equity method. Realized and unrealized investment return from all unrestricted investments and assets limited as to use are included in the consolidated statements of operations as part of nonoperating gains and losses. Investment income (loss) on investments of temporarily and permanently restricted assets is added to or deducted from the appropriate restricted fund

2. Significant Accounting Policies (continued)

balance if the income is restricted. The cost of securities sold is based on the specific-identification method. Investments are classified as either current or noncurrent based on maturity dates and availability for current operations.

Substantially all of the System's investment portfolio (excluding certain assets limited as to use) is classified as trading, with unrealized gains and losses included in excess of unrestricted revenue and other support over expenses. Certain trusteed assets that are included in assets limited as to use are classified as other than trading. These assets primarily consist of funds held under trust arrangements related to unreleased bond proceeds.

Investment Risk and Uncertainties

The System invests in professionally managed portfolios that contain corporate bonds, U.S. government obligations, municipal obligations, asset-backed securities, marketable equity securities, hedge funds, money market funds, private equity, and alternative investments. Such investments are exposed to various risks, such as interest rate, market, and credit. Due to the level of risk associated with such investments and the level of uncertainty related to changes in the value of such investments, it is at least reasonably possible that changes in risks in the near term would materially affect investment balances and the amounts reported in the financial statements.

Property and Equipment

Property and equipment are carried at historical cost. Items acquired by gift are recorded at fair value at the time of acquisition. Depreciation is recorded on the straight-line method over the estimated useful lives of the depreciable assets. Leasehold improvements are amortized using the straight-line method over the shorter of the lease term or the estimated useful lives of the assets.

Valuation of Long-Lived Assets

The System accounts for the valuation of long-lived assets under Accounting Standards Codification 360-10-45, *Accounting for the Impairment or Disposal of Long-Lived Assets.* This guidance requires that long-lived assets and certain identifiable intangible assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

2. Significant Accounting Policies (continued)

Recoverability of the long-lived asset is measured by a comparison of the carrying amount of the asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. Assets to be disposed of are reportable at the lower of the carrying amount or fair value, less costs to sell.

Debt Issuance Costs

Debt issuance costs related to the Series 2012 MHHEFA Bonds are being amortized over the life of the debt using the effective-interest method.

Patient Service Revenue and Allowances

The System has agreements with third-party payors that provide for payments to the System for patient services at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated adjustments under reimbursement agreements with third-party payors. Estimated adjustments are accrued in the period the related services are rendered and are adjusted in future periods as final settlements are determined.

The System's revenues may be subject to adjustment as a result of examination by government agencies or contractors and as a result of differing interpretation of government regulations, medical diagnosis, charge coding, medical necessity, or other contract terms. The resolution of these matters, if any, often is not finalized until subsequent to the period during which the services were rendered.

Other Operating Revenue

The American Recovery and Reinvestment Act of 2009 provides for Medicare and Medicaid incentive payments for eligible hospitals and professionals that implement and achieve meaningful use of certified electronic health record (EHR) technology. For Medicare and Medicaid EHR incentive payments, the System uses a grant accounting method to recognize the revenues. Under this accounting policy, EHR incentive payments are recognized as other operating revenue when attestation that the EHR meaningful use criteria for the required period

2. Significant Accounting Policies (continued)

of time were demonstrated. Accordingly, the System recognized $610 of EHR revenues for the year ended June 30, 2015, all from Medicare revenues. EHR revenues for the year ended June 30, 2014, were $1,541, of which $129 was Medicaid and $1,412 was Medicare.

These amounts are included in other operating revenues in the accompanying consolidated statements of operations. The System's attestation of compliance with the meaningful use criteria is subject to audit by the federal government or its designee. The recognition of revenues is based on management's best estimate of payments to be received. Any subsequent changes in the recognition of the revenue as result of any audits will impact the results of operations in the period in which they occur.

Performance Indicator

The performance indicator is the excess of unrestricted revenue and other support over expenses. Changes in unrestricted net assets, consistent with industry practice, includes pension adjustments and net assets released from restriction for capital purposes.

Fair Value of Financial Instruments

The carrying amounts reported on the accompanying consolidated balance sheets for cash and cash equivalents, other receivables, accounts payable, accrued expenses, and advances from third-party payors approximate their fair values. The fair value of the System's notes receivable, revenue bond notes, and other long-term debt approximate the carrying amounts, based on loans with similar terms and average maturities.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(Dollars in Thousands)

2. Significant Accounting Policies (continued)

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This guidance is intended to improve and converge with international standards the financial reporting requirements for revenue from contracts with customers. It will be effective for fiscal year 2020, and early adoption is permitted beginning in fiscal year 2018. We have not yet determined the impact from adoption of this new accounting pronouncement on our financial statements.

In April 2015, the FASB issued ASU No. 2015-03, Interest–Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. The amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This guidance is effective for fiscal year 2017. The guidance is not expected to materially impact the System's consolidated results of operations, net assets, or cash flows.

3. Patient Receivables and Patient Service Revenue

Patient receivables consist of the following at June 30:

	2015	2014
Gross patient receivables	**$ 65,450**	$ 68,811
Less estimated uncollectible accounts and contractual allowances	**(17,350)**	(21,702)
Net patient receivables	**$ 48,100**	$ 47,109

(Dollars in Thousands)

3. Patient Receivables and Patient Service Revenue (continued)

Patient service revenue consists of the following for the years ended June 30:

	2015	2014
Inpatient charges	**$ 176,322**	$ 183,608
Outpatient charges	**277,812**	264,405
Gross charges	**454,134**	448,013
Less contractual and other allowances	**(84,486)**	(88,127)
Less charity care	**(11,052)**	(14,522)
Net patient service revenue	**358,596**	345,364
Less provision for bad debts	**(3,099)**	(11,402)
Net patient service revenue less provision for bad debts	**$ 355,497**	$ 333,962

The System provides care to patients who meet certain criteria under its charity care policy. The System charges at its established rates but waives all or a portion of reimbursement. Because the System does not pursue collection of amounts determined to qualify as charity care, these revenues are not reported as net patient service revenue. Using the cost to charge ratio to approximate cost, charity care provided for the years ended June 30, 2015 and 2014, was $8,616 and $10,973, respectively. The state of Maryland rate system includes components within the rates to partially compensate hospitals for uncompensated care.

(Dollars in Thousands)

4. Assets Limited as to Use

A summary of assets that are limited as to use substantially for debt service and self-insurance at June 30 is as follows:

	2015	2014
Current:		
Principal, interest, and other – bonds	**$ 3,042**	$ 3,083
Loss escrow account	**51**	950
	$ 3,093	$ 4,033
Noncurrent:		
Construction funds	**$ 7,389**	$ 18,305
Deferred compensation trusts	**1,451**	1,241
	$ 8,840	$ 19,546

The assets that are limited as to use consist of the following at June 30:

	2015	2014
Current:		
Cash and money market accounts	**$ 3,042**	$ 3,083
Mutual funds	**51**	950
	$ 3,093	$ 4,033
Noncurrent:		
Cash and money market accounts	**$ 1**	$ 2,886
Agency securities	**7,388**	15,440
Equity securities	**–**	985
Corporate or other bonds	**183**	–
Mutual funds	**1,268**	235
	$ 8,840	$ 19,546

The noncurrent assets limited as to use mutual funds are primarily invested in cash and short-duration debt securities.

(Dollars in Thousands)

5. Promises to Give

Promises to give are discounted and are due as follows at June 30:

	2015	2014
Less than one year	**$ 926**	$ 837
One to five years	**2,968**	2,558
More than five years	**2,260**	2,217
	6,154	5,612
Less discounting and allowance for uncollectible promises	**1,581**	1,454
Total promises to give, net	**4,573**	4,158
Less current portion of promises to give, net	**787**	711
	$ 3,786	$ 3,447

Promises to give include $1,115 and $1,080 for the years ended June 30, 2015 and 2014 respectively, related to charitable remainder trusts. This net amount represents the excess of the fair value of the related trust accounts over the net present value of the annuities to be paid out of the trust to the named beneficiaries over their estimated life expectancy.

6. Investments

Long-term investments represent unrestricted investments and unrestricted income earned on unrestricted, temporarily restricted, and permanently restricted investments.

Donor-restricted investments are designated by the donors for expenses relating to capital projects, replacement or improvement of existing assets, or to cover the cost of services rendered as charity care and other programs.

(Dollars in Thousands)

6. Investments (continued)

Long-term and donor-restricted investments consist of the following at June 30:

	2015		2014	
	Cost	**Fair Value**	**Cost**	**Fair Value**
Cash and cash equivalents	**$ 6,136**	**$ 6,136**	$ 6,187	$ 6,187
U.S. government obligations	**4,356**	**4,354**	5,101	5,111
Corporate obligations	**4,036**	**4,072**	3,400	3,543
Mortgage-backed securities	**4,007**	**4,046**	3,237	3,284
Equity securities	**32,239**	**40,816**	31,582	42,932
Mutual funds	**61,616**	**62,548**	55,143	58,350
	$ 112,390	**$ 121,972**	$ 104,650	$ 119,407

Fair value of investments carried at cost at June 30 is as follows:

	2015		2014	
	Cost	**Fair Value**	**Cost**	**Fair Value**
Private equity and alternative investments	**$ 3,174**	**$ 4,593**	$ 1,837	$ 3,304
	$ 3,174	**$ 4,593**	$ 1,837	$ 3,304

The System is invested in a hedge fund that is accounted for under the equity method of accounting, which approximates fair value. The carrying value of the fund was $15,640 and $14,630 as of June 30, 2015 and 2014, respectively. Valuation of this equity investment is primarily based on financial data supplied by the underlying investee fund. The System has the ability to liquidate this investment on a quarterly basis. The System must provide notice of intent to redeem its shares 65 days prior to the redemption date. Within 45 days of the redemption date, 90% of the redemption value will be returned to the System, with the balance payable 30 days after the receipt of the fund’s annual audited financial statements. Value may be based on historical cost, appraisals, or other estimates that require varying degrees of judgment. The historic cost of these investments was $11,500 and $11,500 as of June 30, 2015 and 2014, respectively.

(Dollars in Thousands)

6. Investments (continued)

The private equity investments are shown at cost on the accompanying consolidated financial statements.

Investments are allocated as follows at June 30:

	2015	2014
Investment allocation:		
Unrestricted long-term investments	**$ 134,931**	$ 132,552
Donor-restricted investments	**5,855**	3,705
	$ 140,786	$ 136,257

Investment income, including income from short-term investments, for the years ended June 30, is as follows:

	2015	2014
Unrestricted:		
Net realized gains	**$ 4,099**	$ 3,442
Interest and dividends, net of investment expense	**2,891**	2,258
Income from joint ventures	**22**	461
	$ 7,012	$ 6,161

Investment expense was $375 and $416 for the fiscal years ended June 30, 2015 and 2014, respectively.

Other investments consist of the following at June 30:

	Carrying Value		Income	
	2015	2014	2015	2014
Premier Class B	**$ 1,876**	$ 662	**$ –**	$ –
Joint ventures	**3,876**	2,827	**22**	461
	$ 5,752	$ 3,489	**$ 22**	$ 461

(Dollars in Thousands)

6. Investments (continued)

Investments in joint ventures are accounted for using the equity method, unless otherwise noted, at June 30, and are as follows:

	Entity	Interest %	2015	2014
Colonial Regional Alliance	FMH	14.3%	**$ 30**	$ 30
Carroll Occupational Health, LLC	FHSC	25.0	**105**	66
Comp Claim Management, LLC	FHSC	50.0	**33**	32
Open MRI of Frederick, LLC	FHSC	–	**–**	117
Premier Purchasing Partners (cost method)	FMH	–	**392**	392
Mt. Airy Health Services, LLC	FMH	50.0	**(33)**	47
Mt. Airy Med-Services, LLC	FHSC	50.0	**375**	200
Mt. Airy Plaza, LLC	FHSC	50.0	**(67)**	(103)
Trivergent Health Alliance	FMH	33.3	**1,000**	–
Advanced Health Collaborative	FRHS	–	**42**	–
Frederick Surgical Center, LLC	FHSC	34.7	**1,999**	2,046
			$ 3,876	$ 2,827

Group Purchasing Organization Initial Public Offering

The System has participated and owned equity in the Premier Limited Partnership (Premier), which has served as a group purchasing organization for many years. This participation provides purchasing contract rates and rebates the System would not be able to obtain on its own. The System accounts for its investment in Premier on the cost method of accounting.

During the year ended June 30, 2014, Premier restructured from a privately held company to a public company and completed an initial public offering (IPO) of its equity securities. Several financial transactions occurred with those holding equity in Premier before the IPO, including the System. As a result, the System received a cash payment of approximately $1.1 million in exchange for 16% of its previous ownership in Premier. In addition, in exchange for the extension of the group purchasing contract, the System received partial ownership of the new public company (the Class B units).

6. Investments (continued)

During the year ended June 30, 2014, the System recognized a gain of approximately $1.0 million on the sale of its 16% interest, which is presented in other operating revenues in the accompanying consolidated financial statements. The System received 233,669 Class B units that are earned in seven separate tranches over an 85-month period ending October 31, 2020. The opportunity will exist in the future for these Class B units to be converted to the Premier public company stock. Prior to vesting, the Class B units may be transferred or sold with the approval of Premier. The System recognized $1.2 million and $0.7 million related to vesting of 32,525 and 22,254 Class B units for the years ended June 30, 2015 and 2014, respectively. These amounts are recorded as an investment on the accompanying consolidated balance sheets and were recognized as a reduction of supplies expense in the accompanying consolidated statements of operations, as the value of the Class B shares is tied to the group purchasing contract and is considered a vendor incentive.

7. Fair Value Measurements

Assets and liabilities recorded at fair value in the accompanying consolidated balance sheets are categorized based upon the level of judgment associated with the inputs used to measure their fair value.

FASB guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the measurement date, emphasizing that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, the FASB establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

7. Fair Value Measurements (continued)

The Level inputs, as defined by FASB guidance for fair value measurements and disclosures, are as follows:

- Level 1 **–** Inputs utilize unadjusted quoted prices in active markets for identical assets or liabilities that the System has the ability to access at the measurement date.

- Level 2 **–** Inputs are inputs other than quoted prices included in Level 1 that are observable for the assets or liabilities, either directly or indirectly. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the assets or liabilities (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals.

- Level 3 **–** Inputs are unobservable inputs for the assets or liabilities, which are typically based on an entity's own assumptions, as there is little, if any, related market activity.

(Dollars in Thousands)

7. Fair Value Measurements (continued)

The determination of the fair value level within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The System's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the assets or liabilities. The following tables present the System's assets and liabilities measured at fair value on a recurring basis, aggregated by the level in the fair value hierarchy within which those measurements fall, as of June 30:

		Fair Value Measurements at Reporting Date Using		
	Fair Value at June 30, 2015	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Assets				
Cash and cash equivalents	$ 41,318	$ 41,318	$ –	$ –
Equity securities	40,109	40,109	–	–
U.S. government obligations	4,354	–	4,354	–
Agency securities	7,493	–	7,493	–
Corporate and other bonds	4,150	–	4,150	–
Mutual funds	63,867	63,867	–	–
Mortgage-backed securities	4,045	–	4,045	–
Private equity and alternative investments	4,593	–	–	4,593
Contributions receivable	4,573	–	–	4,573
Total assets	$ 174,502	$ 145,294	$ 20,042	$ 9,166
Liabilities				
Interest rate swap liability	$ (11,277)	$ –	$ (11,277)	$ –
Total liabilities	$ (11,277)	$ –	$ (11,277)	$ –

(Dollars in Thousands)

7. Fair Value Measurements (continued)

		Fair Value Measurements at Reporting Date Using		
	Fair Value at June 30, 2014	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Assets				
Cash and cash equivalents	$ 45,857	$ 45,857	$ –	$ –
Equity securities	43,928	43,928	–	–
U.S. government obligations	5,112	–	5,112	–
Agency securities	15,439	–	15,439	–
Corporate and other bonds	3,543	–	3,543	–
Mutual funds	59,526	59,526	–	–
Mortgage-backed securities	3,284	–	3,284	–
Private equity and alternative investments	3,304	–	–	3,304
Contributions receivable	4,158	–	–	4,158
Total assets	$ 184,151	$ 149,311	$ 27,378	$ 7,462
Liabilities				
Interest rate swap liability	$ (11,238)	$ –	$ (11,238)	$ –
Total liabilities	$ (11,238)	$ –	$ (11,238)	$ –

The fair value of the System's trading securities is determined by third-party service providers utilizing various methods dependent upon the specific type of investment. Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Where significant inputs, including benchmark yields, broker-dealer quotes, issuer spreads, bids, offers, the London Interbank Offered Rate (LIBOR) curve, and measures of volatility, are used by these third-party dealers or independent pricing services to determine fair values, the securities are classified within Level 2. Private equity and alternative investments are carried at cost. Hedge fund investments are carried under the equity method of accounting.

7. Fair Value Measurements (continued)

Assets utilizing Level 1 inputs include exchange-traded equity securities and equity and fixed-income mutual funds. Assets and liabilities utilizing Level 2 inputs include U.S. government securities, corporate bonds, mortgage-backed securities, and interest rate swaps. Assets utilizing Level 3 inputs are contributions receivable and private equity and alternative investments.

Interest Rate Swap

The System entered into an interest rate swap agreement in conjunction with the issuance of variable rate bonds. The swap contract is valued using models based on readily observable market parameters for all substantial terms of the contract. The fair market value of the swap agreement is included as interest rate swap contract in the accompanying consolidated balance sheets. The fair market value calculation includes a credit valuation adjustment as required of $684 and $700, reducing the interest rate swap agreement liability position on June 30, 2015 and 2014, respectively. The change in the fair market value of the swap agreement is included in excess of unrestricted revenue and other support over expenses, as the swap is not designated as an effective hedge.

Credit exposure associated with nonperformance by the counterparty to the derivative instrument is generally limited to the uncollateralized fair value of the asset related to instruments recognized in the balance sheets.

Other

Assets utilizing Level 3 inputs are contributions receivable and private equity investments. Contributions receivable are recorded net of allowance for uncollectible pledges and discounted to net present value. The present value of estimated future cash flows using a discount rate commensurate with the risks involved is an appropriate measure of fair value for unconditional promises to give cash and is considered Level 3. The private equity and alternative investments are carried at cost of $3,174 and $1,837 on the accompanying consolidated financial statements on June 30, 2015 and 2014, respectively.

(Dollars in Thousands)

7. Fair Value Measurements (continued)

The following table provides a reconciliation of the beginning and ending balances of items measured at fair value on a recurring basis in the previous table that used significant unobservable inputs (Level 3):

	Contributions Receivable	Private Equity and Alternative Investments	Total
Balance at June 30, 2013	$ 3,096	$ 3,073	$ 6,169
Purchases, issuances, and settlements	1,062	231	1,293
Balance at June 30, 2014	4,158	3,304	7,462
Purchases, issuances, and settlements	**415**	**1,289**	**1,704**
Balance at June 30, 2015	**$ 4,573**	**$ 4,593**	**$ 9,166**

8. Property and Equipment

Property and equipment consist of the following at June 30:

	Estimated Useful Lives	2015	2014
Land	–	**$ 3,734**	$ 3,734
Land improvements	08–20 years	**2,012**	1,225
Buildings	20–40 years	**208,423**	210,514
Fixed equipment	10–20 years	**16,679**	16,594
Movable equipment	03–20 years	**198,478**	193,486
Leasehold improvements	05–20 years	**25,452**	24,806
		454,778	450,359
Less accumulated depreciation	–	**266,610**	254,370
		188,168	195,989
Construction in process, renovations, and deposits	–	**13,887**	3,100
		$ 202,055	$ 199,089

(Dollars in Thousands)

8. Property and Equipment (continued)

Construction in progress consists of the System's building renovations. As these projects are completed, the related assets are transferred out of construction in progress and into the appropriate asset category and are depreciated over the applicable useful lives.

Capitalized computer software, net of accumulated amortization, as of June 30, 2015 and 2014, was $8,504 and $10,444, respectively. Amortization of computer software was $3,731 for fiscal year 2015. There was no amortization of computer software in fiscal year 2014.

The net book value of assets under capital lease arrangements totaled $2,353 and $3,854 as of June 30, 2015 and 2014, respectively. Depreciation expense related to assets under capital lease arrangements was $1,605 and $1,807 for the fiscal years ended June 30, 2015 and 2014, respectively.

9. Long-Term Debt

Long-term debt consists of the following as of June 30:

	2015	2014
MHHEFA Series 2012A Bonds	**$ 98,090**	$ 99,099
MHHEFA Series 2012B Bonds	**66,140**	68,930
Note payable – Emmitsburg	**–**	62
Capital lease obligations	**1,885**	3,881
	166,115	171,972
Less current maturities	**5,103**	5,697
	$ 161,012	$ 166,275

Series 2012A MHHEFA Revenue Bonds

In December 2012, the System obtained a loan of $96,240 in MHHEFA Revenue Bonds, Frederick Memorial Hospital Issue, Series 2012A. The MHHEFA Series 2012A Bonds were issued to refund all of the MHHEFA Series 2002 Bonds and to finance a portion of certain construction and equipment costs of the System. The Series 2012A Bonds were issued with a premium of $3,990, which is being amortized over the life of the bonds. The accumulated

9. Long-Term Debt (continued)

amortization was $410 at June 30, 2015. The annual interest rate on the bond loan ranges between 3% and 5% over the term of the bond. Interest is payable semiannually on each January 1 and July 1, through July 1, 2038.

Series 2012A Bonds maturing on or after July 1, 2023, are subject to redemption prior to maturity beginning on July 1, 2022, at the option of the authority at the principal amount of the Series 2012A Bonds to be redeemed plus accrued interest thereon to the date set for redemption.

Under the provisions of the bond agreement, the System has granted to the authority a security interest in all receipts now owned and hereafter acquired. The Series 2012A Bonds are secured ratably with the Series 2012B Bonds. The fair value of the Series 2012A MHHEFA Revenue Bonds is estimated based on the quoted market prices for the same or similar issues. The fair value of the 2012A Bonds as of June 30, 2015, is estimated at $94,618.

There is no debt service reserve requirement associated with the Series 2012A Bonds.

The bond agreement contains certain financial covenants.

Series 2012B MHHEFA Revenue Bonds

In December 2012, the System obtained a loan of $70,020 in MHHEFA Revenue Bonds, Frederick Memorial Hospital Issue, Series 2012B. The MHHEFA Series 2012B Bonds were issued to refund all of the MHHEFA Series 2008 Bonds. Upon settlement of the bonds, MHHEFA and the obligated group entered into a financing agreement with Branch Banking and Trust (BB&T) whereby BB&T became the initial purchaser of the 2012B Bonds. The interest rate on the bonds is based on an index floating rate determined by BB&T equal to the applicable percentage multiplied by LIBOR plus the applicable spread plus the TEFRA adjustment, if any. Interest on the bonds is paid monthly and averaged 1.33% and 1.33% for the 12 months ended June 30, 2015 and 2014, respectively.

Series 2012B Bonds are subject to redemption at the option of the authority at the principal amount of the Series 2012B Bonds to be redeemed plus accrued interest to the date set for redemption. The Series 2012B Bonds, which mature on July 1, 2035, are secured ratably with the Series 2012A Bonds. The System is required to make annual payments to BB&T sufficient to

(Dollars in Thousands)

9. Long-Term Debt (continued)

meet the annual debt service requirements of the refunding bond issue for the succeeding year. Annual sinking fund installments for the 2012B bonds range from $1,090 on July 1, 2013, to $4,855 on July 1, 2028.

There is no debt service reserve requirement associated with the Series 2012B Bonds.

The bond agreement contains certain financial covenants.

Note Payable – Emmitsburg

In December 1994, the System acquired a 100% interest in Emmitsburg Properties. In accordance with the terms of the purchase agreement, the System executed two notes payable to the former owners aggregating $1,219. There is no outstanding balance on either loan as of June 30, 2015.

Capital Lease Obligations

As of June 30, 2015, the System has entered into certain capital lease obligations to secure major medical diagnostic equipment. Future payments under these obligations are as follows:

Years ending June 30:	
2016	$ 1,371
2017	530
2018	23
2019	–
2020	–
Total payments	1,924
Less interest payments	40
Total lease obligations, principal	1,884
Less current portion	1,338
Long-term obligations under capital leases	$ 546

(Dollars in Thousands)

9. Long-Term Debt (continued)

Debt service requirements on long-term debt and capital lease obligations, excluding original issue premium on bonds at June 30, 2015, of $3,580 is as follows:

	Principal
Years ending June 30:	
2016	$ 5,103
2017	4,429
2018	4,087
2019	4,220
2020	4,405
Thereafter	140,291
	$ 162,535

On September 9, 2013, the System entered into a $20,000 revolving line of credit with a lending institution for the purpose of funding short-term working capital needs. The line of credit bears a variable interest rate of One Month LIBOR plus 1.5% per annum, adjusted monthly. All outstanding principal and interest must be repaid within two years of closing. There must not be any outstanding principal balance for at least 30 consecutive days during each year the line of credit is available. A $5,000 draw was taken upon closing. There is no outstanding balance on this line of credit as of June 30, 2015 or June 30, 2014. The line of credit terminates on December 1, 2015.

10. Interest Rate Swap Contract

The System records its derivatives as assets or liabilities at fair value. A derivative is typically defined as an instrument, whose value is derived from an underlying instrument, index or rate, has a notional amount, requires little or no initial investment, and can be net settled. The System participates in an interest rate swap contract that is considered a derivative financial instrument.

In conjunction with the issuance of the Series 2008 Bonds, the System modified its interest rate swap contract with a third-party to a notional amount of $72,160, which reduces annually by an amount equal to the sinking fund installment due on the 2008 Bonds until maturity of July 1, 2035. The notional amount is $66,140 on June 30, 2015. The swap agreement remains in effect after the issuance of the 2012 Series Bonds. The System is exposed to credit loss in the

10. Interest Rate Swap Contract (continued)

event of nonperformance by the counterparty to the interest rate swap contract. However, the System does not anticipate nonperformance by the counterparty. Under the swap contract, the System pays interest at a fixed rate of 3.0804% per annum and receives interest at a variable rate equal to 67% of the one-month LIBOR (0.1859% as of June 30, 2015). The swap contract requires payments to be made or received monthly. The fair value of the swap contract was a liability of $11,277 and $11,238 at June 30, 2015 and 2014, respectively.

The System accrued net payments under its interest rate swap program of $2,442 and $2,545 during fiscal years 2015 and 2014, respectively. These amounts are included within realized and unrealized losses on interest rate swap contract, net in the accompanying consolidated statements of operations and investing activities in the accompanying consolidated statements of cash flows.

The interest rate swap contract is not designated as an effective cash flow hedge. The System's objectives of entering into the interest rate swap contract include limiting or hedging variable interest rate payments to achieve lower overall borrowing costs than a comparable unhedged fixed rate borrowing, to alter the pattern of debt service payments, and to improve asset/liability matching. Changes in the fair value of the derivative financial instrument are recognized in the consolidated statements of operations as a component of other loss. The carrying value of the System's derivative financial instrument approximates fair value. The interest rate swap contract is valued using models based on readily observable market parameters for all substantial terms of the contract.

Credit exposure associated with nonperformance by the counterparties to derivative instruments is generally limited to the uncollateralized fair value of the asset related to instruments recognized in the consolidated balance sheets. The System attempts to mitigate the risk of nonperformance by selecting counterparties with high credit ratings and monitoring their creditworthiness.

(Dollars in Thousands)

10. Interest Rate Swap Contract (continued)

The System's derivative agreements do not contain any credit support provisions that require it to post collateral if there are declines in the derivative value or its credit rating.

Balance Sheet Location	Fair Value 2015	Fair Value 2014
Asset derivatives		
Derivatives not designated as hedging instruments:		
Interest rate contracts	**$ –**	$ –
Liability derivatives		
Long-term liabilities	**$ 11,277**	$ 11,238
Total derivatives not designated as hedging instruments	**$ 11,277**	$ 11,238

A summary of the effect of the nonhedging derivatives on the System's income statement for the year ended June 30, 2015, is as follows:

Type of Nonhedging Derivatives	Income Statement Location of (Loss) Gain Recognized	Derivative (Loss) Gain Recognized
Interest rate swap contract – realized losses	Other loss	**$ (2,442)**
Interest rate swap contract – unrealized losses	Other loss	**(40)**
Total		**$ (2,482)**

(Dollars in Thousands)

10. Interest Rate Swap Contract (continued)

A summary of the effect of the nonhedging derivatives on the System's income statement for the year ended June 30, 2014, is as follows:

Type of Nonhedging Derivatives	Income Statement Location of Loss Recognized	Derivative Loss Recognized
Interest rate swap contract – realized losses	Other loss	$ (2,545)
Interest rate swap contract – unrealized gains	Other gain	389
Total		$ (2,156)

11. Employee Benefit Plans

The System has a defined benefit pension plan that was curtailed on June 30, 2007. The System uses a measurement date of June 30 to determine plan assets and benefit obligations. The curtailment is such that participants will no longer accrue benefits under the plan and no new participants will be accepted. Current participant accounts will not receive any service credits or increases in benefits for post-curtailment compensation increases beyond June 30, 2007; however, the System will make annual contributions to the plan in accordance with actuarially determined amounts to meet future accumulated benefit obligations under the frozen plan. Effective July 1, 2007, a modified defined contribution plan (403b) was implemented as described below.

11. Employee Benefit Plans (continued)

The following provides a reconciliation of the changes in fair value of the plan's assets and projected benefit obligations and the plan's funded status based on a June 30, 2015 and 2014, measurement date:

	2015	2014
	(In Thousands)	
Accumulated benefit obligation	**$ 88,930**	$ 84,128
Change in projected benefit obligation:		
Projected benefit obligation at beginning of year	**$ 84,128**	$ 74,887
Service cost	**569**	495
Interest cost	**3,706**	3,763
Actuarial loss (gain)	**2,431**	7,485
Benefits paid	**(2,654)**	(2,502)
Projected benefit obligation at end of year	**88,180**	84,128
Change in plan assets:		
Fair value of plan assets at beginning of year	**67,526**	62,726
Actual return on plan assets	**1,940**	6,133
Employer contribution	**2,500**	1,169
Benefits paid	**(2,654)**	(2,502)
Fair value of plan assets at end of year	**69,312**	67,526
Funded status	**(18,868)**	(16,602)
Net amount recognized	**$ (18,868)**	$ (16,602)

The discount rate actuarial assumption was changed from 4.47% to 4.42%, resulting in a $700 decrease in the projected benefit obligation as of June 30, 2015.

(Dollars in Thousands)

11. Employee Benefit Plans (continued)

Net amounts recognized in unrestricted net assets that have not been recognized in net periodic benefit cost are as follows:

	June 30	
	2015	**2014**
Net actuarial loss	**$ 21,834**	$ 20,104
Prior service cost	**237**	288
Total recognized in unrestricted net assets	**$ 22,071**	$ 20,392

The following table sets forth the weighted-average assumptions used to determine benefit obligations:

	June 30	
	2015	**2014**
Discount rate	**4.42%**	4.47%
Rate of compensation increase	**N/A**	N/A

The following table sets forth the weighted-average assumptions used to determine net periodic benefit cost:

	Year Ended June 30	
	2015	**2014**
Discount rate	**4.47%**	5.10%
Expected return on plan assets	**4.50%**	5.75%
Rate of compensation increase	**N/A**	N/A

(Dollars in Thousands)

11. Employee Benefit Plans (continued)

Net periodic pension cost included the following components:

	2015	2014
Service cost	**$ 569**	$ 495
Interest cost	**3,706**	3,763
Expected return on plan assets	**(3,087)**	(3,603)
Amortization of prior service cost	**52**	52
Unrecognized net actuarial loss	**1,847**	1,166
Net periodic pension cost	**$ 3,087**	$ 1,873

The estimated net loss that is expected to be amortized from other changes in unrestricted net assets into net periodic benefit cost for the year ending June 30, 2016, is $2,191.

The System determines the expected long-term rate of return on plan assets by taking into consideration the historical returns of various asset classes and the types of investments the plan is expected to hold.

The defined benefit pension plan asset allocation as of the measurement date presented as a percentage of total plan assets was as follows:

	2015	2014
Equity securities	**24%**	30%
Debt securities	**60**	–
Cash	**3**	54
Hedge funds	**13**	16
Total	**100%**	100%

The plan assets are recorded at fair value and are categorized based upon the level of judgment associated with the inputs used to measure their fair value.

11. Employee Benefit Plans (continued)

FASB guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the measurement date, emphasizing that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, the FASB establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy). The Level inputs, as defined by FASB guidance for fair value measurements and disclosures, are as follows:

- Level 1 – Inputs utilize unadjusted quoted prices in active markets for identical assets or liabilities that the System has the ability to access at the measurement date.

- Level 2 – Inputs are inputs other than quoted prices included in Level 1 that are observable for the assets or liabilities, either directly or indirectly. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the assets or liabilities (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals.

- Level 3 – Inputs are unobservable inputs for the assets or liabilities, which are typically based on an entity's own assumptions, as there is little, if any, related market activity.

The determination of the fair value level within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

(Dollars in Thousands)

11. Employee Benefit Plans (continued)

The System's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the assets or liabilities. The following tables present the plan's assets and liabilities measured at fair value on a recurring basis, aggregated by the level in the fair value hierarchy within which those measurements fall, as of June 30:

		Fair Value Measurements at Reporting Date Using		
	Fair Value at June 30, 2015	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Other Unobservable Inputs (Level 3)**
Assets				
Cash and cash equivalents	**$ 2,710**	**$ 2,710**	**$ –**	**$ –**
Equity securities	**16,308**	**16,308**	**–**	**–**
Fixed income mutual funds	**41,436**	**41,436**	**–**	**–**
Hedge funds and other alternative	**8,858**	**–**	**–**	**8,858**
Total assets	**$ 69,312**	**$ 60,454**	**$ –**	**$ 8,858**

		Fair Value Measurements at Reporting Date Using		
	Fair Value at June 30, 2014	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Other Unobservable Inputs (Level 3)**
Assets				
Cash and cash equivalents	$ 36,676	$ 36,676	$ –	$ –
Equity securities	20,197	20,197	–	–
Fixed income mutual funds	–	–	–	–
Hedge funds and other alternative	10,653	–	–	10,653
Total assets	$ 67,526	$ 56,873	$ –	$ 10,653

(Dollars in Thousands)

11. Employee Benefit Plans (continued)

The following table provides a reconciliation of the beginning and ending balances of items measured at fair value on a recurring basis in the previous table that used significant unobservable inputs (Level 3):

	Hedge Funds	Total
Balance at June 30, 2013	$ 9,934	$ 9,934
Purchases, issuances, and settlements	719	719
Balance at June 30, 2014	10,653	10,653
Purchases, issuances, and settlements	**(1,795)**	**(1,795)**
Balance at June 30, 2015	**$ 8,858**	**$ 8,858**

The fair value of the plan's trading securities is determined by third-party service providers utilizing various methods dependent upon the specific type of investment. Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Assets utilizing Level 1 inputs include exchange-traded equity securities and equity and fixed income mutual funds. Assets utilizing Level 3 inputs are hedge funds.

The hedge fund is accounted for at fair value, which has been estimated using the net asset value per share of the fund as of June 30, 2015. The plan has the ability to liquidate this investment on a quarterly basis. The plan must provide notice of intent to redeem its shares 65 days prior to the redemption date. Within 45 days of the redemption date, 90% of the redemption value will be returned to the plan, with the balance payable 30 days after the receipt of the fund's annual audited financial statements.

Assets of the plan are invested in a manner consistent with fiduciary standards of the Employee Retirement Income Security Act of 1974, namely, (a) the safeguards and diversity to which a prudent investor would adhere must be present and (b) all transactions undertaken on behalf of the plan must be for the sole interest of plan participants and beneficiaries to provide benefits in a prudent manner. Investment objectives of the plan also include the following:

- Achieve an annualized total return that equals or exceeds the actuarial target
- Preserve the value of the plan's assets

(Dollars in Thousands)

11. Employee Benefit Plans (continued)

- Diversify assets sufficiently, and, in accordance with modern portfolio theory, avoid large specific risks (losses) and minimize the volatility of the portfolio

- Provide sufficient liquidity to plan benefit payment outflows and meet the plan's requirements

The strategic target asset allocation for the plan is 23% in equities, 62% in fixed income securities, 10% in hedge funds, and 5% real estate.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

2016	$	2,691
2017		2,789
2018		3,014
2019		3,274
2020		3,560
2021–2025		21,430

The System also has a tax-deferred annuity savings (403b) plan available to substantially all employees. In conjunction with the curtailment of the defined benefit pension plan, the System modified the (403b) plan effective July 1, 2007. Under the terms of the modified plan, every eligible employee receives a base contribution of 2.5% of earnings. The System will match 50.0% to 70.0% on employee contributions up to 5.0% of employee earnings depending on years of service. In addition, certain employees are eligible for transition credits based on age and years of service to the System. The System's contribution for base matching and transition credits totaled $5,454 and $5,499 for fiscal years 2015 and 2014, respectively.

The System is partially self-insured against employee medical claims. Plan expenses include claims paid and a provision for claims incurred but not reported. As of June 30, 2015 and 2014, the System has recorded a liability for claims incurred but not reported of $1,855 and $1,854, respectively. The program has an annual aggregate stop-loss provision of $500 per employee.

(Dollars in Thousands)

11. Employee Benefit Plans (continued)

In December 2005, the System adopted two nonqualified deferred compensation plans with an effective date of December 15, 2004, for certain members of executive management. Under the plans, participating employees may contribute amounts from their compensation to the plan and may receive a discretionary employer contribution. Employees are fully vested in all employee contributions to the plans. Vesting in employer contributions occurs in accordance with the underlying plan documents. All assets of the plans are held in separate trusts. Total contributions by the System to the plans were $334 and $313 for the years ended June 30, 2015 and 2014, respectively.

12. Concentration of Credit Risk

The System has funds on deposit with financial institutions in excess of amounts insured by the Federal Deposit Insurance Corporation. The System grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors (in percentages) at June 30 was as follows:

	2015	**2014**
Medicare	**25%**	24%
Medicaid	**19**	20
Blue Cross	**17**	16
HMOs and PPOs	**18**	20
Commercial insurance and other third-party payors	**7**	7
Patients	**14**	13
	100%	100%

(Dollars in Thousands)

13. Functional Expenses

The System and its subsidiaries provide general health care services to residents within its geographic location. Expenses related to providing these services are as follows:

	2015	2014
Health care services	**$ 319,664**	$ 305,764
General and administrative	**46,593**	46,263
	$ 366,257	$ 352,027

14. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available for the following purposes or periods at June 30:

	2015	2014
Health care services:		
Buildings and equipment	**$ 7,738**	$ 2,440
Restricted by time only	**815**	3,627
Education programs	**403**	407
Indigent care and research	**495**	423
	$ 9,451	$ 6,897

Permanently restricted net assets consist of investments to be held in perpetuity, the income from which is expendable for:

	2015	2014
General health care services (reported as operating income)	**$ 971**	$ 971
Specific health care services (reported as temporarily restricted income)	**5**	5
	$ 976	$ 976

During 2015 and 2014, net assets were released from donor restrictions by incurring expenses or capital expenditures satisfying the restricted purposes in the amounts of $294 and $276, respectively.

15. Contingencies

The System has been named as a defendant in various legal proceedings arising from the performance of its normal activities. In the opinion of management, after consultation with legal counsel and after consideration of applicable insurance, the amount of the System's ultimate liability under all current legal proceedings will not have a material adverse effect on its consolidated financial position or results of operations.

FMH was insured for professional liability under an occurrence-based policy through June 30, 2005. Effective July 1, 2005, FMH established an irrevocable self-insurance trust to set aside funds to cover future professional liability claims. The initial funding to the trust was $1,500. Total disbursements from the fund for a covered loss by one or more persons as a result of any one occurrence were not to exceed $1,000 and $3,000 in the aggregate in any one fiscal year. The funded balance of the trust was $6,984 at June 30, 2011. Concurrently, FMH purchased excess umbrella coverage through a commercial carrier with a per-occurrence and aggregate limit of $10,000 per policy period.

As of July 1, 2011, MIL, a single-parent captive, was created to provide a flexible risk financing structure to meet the needs of the System's organization. MIL coverage limits are $1,000 per incident and $5,000 in the aggregate in any one fiscal year on a mature claims-made basis retroactive to July 1, 2005. Commercial general liability is covered under the captive program for $1,000 per incident on a claims-made basis retroactive to July 1, 2005, as well.

As of June 30, 2012, MIL assumed the FMH Professional Liability and Comprehensive General Liability coverage previously included under the self-insurance trust for incidents occurring between July 1, 2005 and June 30, 2011, that were reported to FMH prior to June 30, 2011. The policy for this period provides limits of $1,000 per medical incident, with a $3,000 annual aggregate limit. The FMH self-insurance trust was fully liquidated as of June 30, 2012.

There are known claims and incidents that could result in the assertion of additional claims, as well as claims from unknown incidents that could be asserted arising from services provided to patients. Effective July 1, 2011, the System adopted ASU 2010-23, *Measuring Charity for Disclosure*, which clarified that a health care entity should not net insurance recoveries against a related claim liability. The System maintains reserves, including excess coverage, in the amount of $13,224, at June 30, 2015, and $13,652 at June 30, 2014, and a related reinsurance receivable of $4,467 at June 30, 2015, and $4,698 at June 30, 2014. The System employs an independent actuary to estimate the ultimate settlement of such claims.

(Dollars in Thousands)

15. Contingencies (continued)

These reserves are recorded on an undiscounted basis at June 30, 2015 and 2014. In management's opinion, the amounts recorded provide an adequate reserve for loss contingencies. However, changes in circumstances affecting professional liability claims could cause these estimates to change by material amounts in the short term.

16. Commitments

Operating Leases

The System and its subsidiaries lease facilities under various operating leases, the last of which expires in 2030. The System has various options to renew the leases. The System also leases equipment under various operating leases. Rent expense under all operating leases was $4,346 and $4,355 for 2015 and 2014, respectively. Future minimum payments under noncancelable operating leases are as follows:

Years ending June 30:	
2016	$ 3,876
2017	3,380
2018	3,248
2019	3,029
2020	2,616
Thereafter	20,561
	$ 36,710

Workers' Compensation

The System is self-insured against workers' compensation claims, up to $500 per occurrence, and has excess insurance coverage of $1,000 per occurrence. Expenses include claims paid and a provision for claims incurred but not reported.

Supply Chain Management Agreement

The System has a master service agreement with a vendor to provide supply chain management functions. This agreement contains certain purchase volume commitments.

16. Commitments (continued)

Letter of Credit

The System has a letter of credit issued by a lending institution in the amount of $1,372. This letter of credit is renewed on an annual basis and is required by the state of Maryland as collateral for unemployment benefits.

17. Regulatory Environment

Medicare and Medicaid

The Medicare and Medicaid reimbursement programs represent a substantial portion of the System's revenues. The System's operations are subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse.

Over the past several years, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs, together with the imposition of fines and penalties, as well as repayments for patient services previously billed. Compliance with fraud and abuse standards and other government regulations can be subject to future government review and interpretation.

Also, future changes in federal and state reimbursement funding mechanisms and related government budgeting constraints could have an adverse effect on the System.

In 1983, Congress approved a Medicare prospective payment plan for most inpatient services as part of the Social Security Amendment Act of 1983. Hospitals in Maryland are currently exempt from these federal reimbursement regulations under a special waiver. The waiver currently in effect is subject to renewal based upon criteria defined in the federal law. Under these payment arrangements with Medicare, a retroactive adjustment could occur if certain performance standards are not attained by all hospitals on a statewide basis. The impact, if any, of any retroactive adjustment of the Medicare prospective payment system, should hospitals in Maryland become subject to such system, on future operations of the System, has not been determined.

17. Regulatory Environment (continued)

State of Maryland Health Services Cost Review Commission

Certain hospital charges are subject to review and approval by the Maryland Health Services Cost Review Commission (HSCRC or the Commission). Hospital management has filed the required forms with the Commission and believes the hospital to be in compliance with Commission requirements.

Through June 2015, 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 prospective payment system reimbursement principles granted to the state of Maryland under Section 1814(b) of the Social Security Act and will continue as long as the rate of increase for costs per hospital inpatient admission in Maryland is below the national average.

Beginning in fiscal year 2014, the System entered into an agreement with the HSCRC to participate in the Global Budgeted Revenue (GBR) program. GBR methodology encourages hospitals to focus on population health strategies by establishing a fixed annual revenue cap for each GBR hospital. The agreement is evergreen in nature and covers both regulated inpatient and outpatient revenues.

Under GBR, hospital revenue is known at the beginning of each fiscal year. Annual revenue is calculated from a base year and is adjusted annually for inflation, infrastructure requirements, population changes, performance in quality-based programs, and changes in levels of uncompensated care. Revenue may also be adjusted annually for market levels and shifts of services to unregulated services.

As of January 2014, the Centers for Medicare and Medicaid Services approved a modernized waiver that will be in place as long as Maryland hospitals commit to achieving significant quality improvements, limits on all-payor per capita hospital growth, and limits on annual Medicare per capita hospital cost growth to a rate lower than the national annual per capita growth rate.

17. Regulatory Environment (continued)

The Commission's rate-setting methodology for hospital service centers 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 month and annually. Overcharges and undercharges due to either patient volume or price variances, adjusted for 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 System exceeded the allowable target by $932 as of June 30, 2015, which is within the allowable corridor as specified in the GBR Agreement. For the year ended June 30, 2014, the System exceeded the allowable target by $1,575.

The timing of the HSCRC's rate adjustments for the System 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, and there is at least a possibility that the amounts may be material. The System's policy is to record revenue based on actual charges for services to patients in the year in which the services are performed. The hospital recognizes unbilled revenue for in-house patients.

The HSCRC established an uncompensated care fund whereby certain hospitals are required to contribute to the fund to help cover the costs associated with uncompensated care for all Maryland hospitals equitably. The System's contribution to the fund was $2,456 and $4,193 for the years ended June 30, 2015 and 2014, respectively.

18. Subsequent Events

The System has evaluated subsequent events for the year ended June 30, 2015 through October 21, 2015, the date these financial statements were issued. No significant subsequent events were noted that would require recognition or disclosure at this time.

Supplementary Information

Frederick Regional Health System, Inc. and Subsidiaries

Supplementary Consolidating Balance Sheet

(Dollars in Thousands)

June 30, 2015

	Frederick Regional Health System, Inc.	Frederick Memorial Hospital, Inc. Consolidated	Monocacy Insurance LTD	Monocacy Health Partners LLC	Frederick Health Services Corporation	Frederick Integrated Health Network	Elimination	Frederick Regional Health System, Inc. Consolidated
Assets								
Current assets:								
Loss on sale of property and equipment	$ 38	$ 25,206	$ 74	$ 1,937	$ 4,174	$ 3	$ –	$ 31,432
Patient receivables, net	–	45,271	–	2,232	597	–	–	48,100
Other receivables	–	1,860	–	–	–	–	–	1,860
Inventory	–	6,006	–	–	–	–	–	6,006
Prepaid expenses	–	2,291	17	–	122	–	–	2,430
Assets limited as to use	–	3,042	51	–	–	–	–	3,093
Promises to give, net	–	787	–	–	–	–	–	787
Total current assets	38	84,463	142	4,169	4,893	3	–	93,708
Net property and equipment	–	197,118	–	1,840	3,097	–	–	202,055
Other assets:								
Assets limited as to use	–	8,840	–	–	–	–	–	8,840
Investments – donor restricted	–	5,855	–	–	–	–	–	5,855
Promises to give, net	–	3,786	–	–	–	–	–	3,786
Long-term investments	–	125,741	9,190	–	–	–	–	134,931
Other investments	209,086	19,596	–	–	2,444	–	(225,374)	5,752
Debt issuance costs, net	–	1,379	–	–	–	–	–	1,379
Other assets	–	6,629	3,900	–	807	–	(6,005)	5,331
Intercompany receivables	–	19,661	–	–	–	–	(19,661)	–
Total other assets	209,086	191,487	13,090	–	3,251	–	(251,040)	165,874
Total assets	$ 209,124	$ 473,068	$ 13,232	$ 6,009	$ 11,241	$ 3	$ (251,040)	$ 461,637

Frederick Regional Health System, Inc. and Subsidiaries

Supplementary Consolidating Balance Sheet (continued)

(Dollars in Thousands)

	Frederick Regional Health System, Inc.	Frederick Memorial Hospital, Inc. Consolidated	Monocacy Insurance LTD	Monocacy Health Partners LLC	Frederick Health Services Corporation	Frederick Integrated Health Network	Elimination	Frederick Regional Health System, Inc. Consolidated
Liabilities and net assets								
Current liabilities:								
Current maturities of long-term debt and capital lease obligations	$ –	$ 5,103	$ –	$ –	$ –	$ –	$ –	$ 5,103
Accounts payable	–	22,232	–	(137)	206	3	(252)	22,052
Accrued expenses	–	15,434	85	2,198	685	–	–	18,402
Advances from third-party payors	–	9,813	–	–	–	–	–	9,813
Loans payable, affiliates	–	–	–	–	3,185	–	(3,185)	–
Other current liabilities	–	1,940	2,583	535	–	–	(2,583)	2,475
Total current liabilities	–	54,522	2,668	2,596	4,076	3	(6,020)	57,845
Long-term liabilities, net of current portion:								
Long-term debt and capital lease obligations	–	161,012	–	–	–	–	–	161,012
Interest rate swap contract	–	11,277	–	–	–	–	–	11,277
Accrued pension expense	–	18,868	–	–	–	–	–	18,868
Other long-term liabilities	–	9,043	10,444	–	–	–	–	19,487
Intercompany liabilities	411	–	–	18,880	–	370	(19,661)	–
Total long-term liabilities, net of current portion	411	200,200	10,444	18,880	–	370	(19,661)	210,644
Total liabilities	411	254,722	13,112	21,476	4,076	373	(25,681)	268,489
Net assets:								
Unrestricted	208,713	207,919	120	(15,467)	7,165	(370)	(225,359)	182,721
Temporarily restricted	–	9,451	–	–	–	–	–	9,451
Permanently restricted	–	976	–	–	–	–	–	976
Total net assets	208,713	218,346	120	(15,467)	7,165	(370)	(225,359)	193,148
Total liabilities and net assets	$ 209,124	$ 473,068	$ 13,232	$ 6,009	$ 11,241	$ 3	$ (251,040)	$ 461,637

Frederick Regional Health System, Inc. and Subsidiaries

Supplementary Consolidating Statement of Operations

(Dollars in Thousands)

Year Ended June 30, 2015

	Frederick Regional Health System, Inc.	Frederick Memorial Hospital, Inc.	Monocacy Insurance LTD	Monocacy Health Partners LLC	Frederick Health Services Corporation	Frederick Integrated Health Network	Elimination	Frederick Regional Health System, Inc. Consolidated
Net patient service revenue	$ –	$ 329,661	$ –	$ 23,842	$ 5,218	$ –	$ (125)	$ 358,596
Provision for bad debts	–	(2,410)	–	(689)	–	–	–	(3,099)
Net patient service revenue less provision for bad debts	–	327,251	–	23,153	5,218	–	(125)	355,497
Other operating revenue	–	5,256	2,109	1,857	2,990	–	(3,144)	9,068
Gifts, bequests and contributions	–	2,968	–	–	–	–	–	2,968
Net assets released from restrictions	–	162	–	–	–	–	–	162
Total unrestricted revenue and other support	–	335,637	2,109	25,010	8,208	–	(3,269)	367,695
Operating expenses:								
Salaries and contract labor	–	104,888	–	21,239	3,973	10	(51)	130,059
Employee benefits	–	31,958	–	4,699	980	1	(36)	37,602
Professional fees	13	13,038	138	187	81	156	(8)	13,605
Cost of goods sold	–	56,038	–	1,357	816	–	–	58,211
Supplies	–	9,671	–	148	–	4	(70)	9,753
Contract services	2	67,660	–	3,240	686	197	(498)	71,287
Other	–	9,237	53	2,137	673	2	(484)	11,618
Utilities	–	3,969	–	193	116	–	(13)	4,265
Insurance	–	266	2,073	687	100	–	(2,109)	1,017
Depreciation and amortization	–	23,279	–	418	614	–	–	24,311
Interest	–	4,528	–	–	108	–	(107)	4,529
Total operating expenses	15	324,532	2,264	34,305	8,147	370	(3,376)	366,257
Operating income	(15)	11,105	(155)	(9,295)	61	(370)	107	1,438

Frederick Regional Health System, Inc. and Subsidiaries

Supplementary Consolidating Statement of Operations (continued)

(Dollars in Thousands)

	Frederick Regional Health System, Inc.	Frederick Memorial Hospital, Inc.	Monocacy Insurance LTD	Monocacy Health Partners LLC	Frederick Health Services Corporation	Frederick Integrated Health Network	Elimination	Frederick Regional Health System, Inc. Consolidated
Other income (loss):								
Gain (loss) on sale of assets	$ –	$ 138	$ –	$ –	$ (235)	$ –	$ –	$ (97)
Loss on extinguishment of debt	–	–	–	–	–	–	–	–
Investment income (loss)	–	6,946	76	–	101	–	(107)	7,016
Change in unrealized gains (losses) on								–
trading securities, net	–	(4,387)	79	–	–	–	–	(4,308)
Realized and unrealized gains (losses)								–
on interest rate swap contract, net	–	(2,482)	–	–	–	–	–	(2,482)
Other nonoperating	–	364	–	–	23	–	–	387
Total other income (loss)	–	579	155	–	(111)	–	(107)	516
Excess of unrestricted revenue and other support over expenses	(15)	11,684	–	(9,295)	(50)	(370)	–	1,954
Other changes in unrestricted net assets:								
Additional minimum pension adjustment	–	(1,679)	–	–	–	–	–	(1,679)
Released from restriction used to purchase capital	–	132	–	–	–	–	–	132
Other changes in unrestricted net assets	–	–	–	–	–	–	–	–
Total other changes in unrestricted net assets	–	(1,547)	–	–	–	–	–	(1,547)
(Decrease) increase in unrestricted net assets	$ (15)	$ 10,137	$ –	$ (9,295)	$ (50)	$ (370)	$ –	$ 407

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