



**MT. WASHINGTON PEDIATRIC HOSPITAL, INC.  
AND SUBSIDIARY**

Consolidated Financial Statements and Schedules

June 30, 2012 and 2011

(With Independent Auditors' Report Thereon)

**MT. WASHINGTON PEDIATRIC HOSPITAL, INC.  
AND SUBSIDIARY**

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KPMG LLP  
1 East Pratt Street  
Baltimore, MD 21202-1128

## Independent Auditors' Report

The Board of Trustees  
Mt. Washington Pediatric Hospital, Inc. and Subsidiary:

We have audited the accompanying consolidated balance sheets of Mt. Washington Pediatric Hospital, Inc. and Subsidiary (the Corporation) as of June 30, 2012 and 2011, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mt. Washington Pediatric Hospital, Inc. and Subsidiary as of June 30, 2012 and 2011, and the results of their operations, the changes in net assets, and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information included in schedules 1 through 4 are 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 audits 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 taken as a whole.

**KPMG LLP**

October 26, 2012

**MT. WASHINGTON PEDIATRIC HOSPITAL, INC.  
AND SUBSIDIARY**

Consolidated Balance Sheets

June 30, 2012 and 2011

| <b>Assets</b>   | <b>2012</b>   | <b>2011</b> |
|---|---------------|-------------|
| Current assets:   |               |             |
| Cash and cash equivalents   | \$ 19,813,274 | 17,728,947  |
| Current portion of assets limited as to use   | 87,640        | 119,548     |
| Patient accounts receivable, less allowance for doubtful accounts<br>of \$2,069,747 and \$1,865,402, respectively | 5,722,579     | 5,682,019   |
| Other accounts receivable   | 94,749        | 56,201      |
| Inventories of supplies   | 138,991       | 122,165     |
| Prepaid expenses and other current assets   | 641,710       | 460,981     |
| Total current assets  | 26,498,943    | 24,169,861  |
| Investments   | 16,864,950    | 14,598,994  |
| Assets limited as to use, less current portion:   |               |             |
| Board-designated funds  | 4,009,991     | 4,017,500   |
| Eliasberg Second Floor Construction Fund  | 2,485,994     | 4,000,000   |
| Funds restricted by donor   | 6,069,613     | 6,191,372   |
| Self-insurance trust funds  | 1,813,759     | 1,323,147   |
|   | 14,379,357    | 15,532,019  |
| Property and equipment, net   | 20,540,200    | 17,850,797  |
| Other assets  | 1,049,576     | 254,171     |
| Total assets  | \$ 79,333,026 | 72,405,842  |
| <b>Liabilities and Net Assets</b>   |               |             |
| Current liabilities:  |               |             |
| Current portion of long-term debt   | \$ 280,000    | 260,000     |
| Trade accounts payable  | 2,317,352     | 2,294,411   |
| Accrued payroll benefits  | 3,610,619     | 3,098,217   |
| Advances from third-party payors  | 4,579,909     | 3,538,985   |
| Current portion of malpractice and other self-insurance liabilities   | 87,640        | 82,283      |
| Deferred revenue  | 1,996,105     | —           |
| Due to affiliates   | 247,947       | 363,762     |
| Total current liabilities   | 13,119,572    | 9,637,658   |
| Malpractice and other self-insurance liabilities  | 1,510,283     | 740,546     |
| Accrued pension obligations   | 1,406,432     | 795,735     |
| Other long-term liabilities   | 199,887       | —           |
| Long-term debt, less current portion  | 6,290,000     | 6,570,000   |
| Total liabilities   | 22,526,174    | 17,743,939  |
| Commitments and contingencies   |               |             |
| Net assets:   |               |             |
| Unrestricted  | 48,099,030    | 44,154,986  |
| Temporarily restricted  | 7,882,651     | 9,681,746   |
| Permanently restricted  | 825,171       | 825,171     |
| Total net assets  | 56,806,852    | 54,661,903  |
| Total liabilities and net assets  | \$ 79,333,026 | 72,405,842  |

See accompanying notes to consolidated financial statements.

**MT. WASHINGTON PEDIATRIC HOSPITAL, INC.  
AND SUBSIDIARY**

Consolidated Statements of Operations and Changes in Net Assets

Years ended June 30, 2012 and 2011

|   | <u>2012</u>          | <u>2011</u>       |
|---|----------------------|-------------------|
| Unrestricted revenue, gains and other support:  |                      |                   |
| Net patient service revenue   | \$ 48,091,824        | 50,087,871        |
| Other revenue   | 445,534              | 294,782           |
| Total unrestricted revenue, gains and other support   | <u>48,537,358</u>    | <u>50,382,653</u> |
| Operating expenses:   |                      |                   |
| Salaries, wages, and benefits   | 32,855,597           | 31,989,461        |
| Purchased services  | 11,499,405           | 12,124,000        |
| Interest expense  | 61,785               | 67,663            |
| Depreciation  | 1,777,490            | 1,790,107         |
| Provision for bad debts   | 495,836              | 482,381           |
| Total operating expenses  | <u>46,690,113</u>    | <u>46,453,612</u> |
| Operating income  | 1,847,245            | 3,929,041         |
| Nonoperating income and expenses, net:  |                      |                   |
| Contributions   | 193,775              | 138,188           |
| Investment income   | 768,093              | 1,666,994         |
| Change in fair value of investments   | (761,680)            | 3,959,332         |
| Excess of revenues over expenses  | 2,047,433            | 9,693,555         |
| Net unrealized losses on other-than-trading securities  | (265,749)            | (2,095,220)       |
| Net assets released from restrictions used for the purchase of<br>property and equipment upon donor request | 3,120,322            | 1,733,078         |
| Change in funded status of defined benefit plan   | (957,962)            | 576,710           |
| Increase in unrestricted net assets   | <u>3,944,044</u>     | <u>9,908,123</u>  |
| Changes in temporarily restricted net assets:   |                      |                   |
| Contributions   | 1,334,291            | 671,981           |
| Investment income, net  | 554,802              | 953,145           |
| Net unrealized (losses) gains on temporarily restricted investments   | (388,880)            | 723,764           |
| Net assets released from restrictions used for the purchase of<br>property and equipment                    | (3,120,322)          | (1,733,078)       |
| Net assets released from restrictions used for operations   | (178,986)            | (178,002)         |
| (Decrease) increase in temporarily restricted<br>net assets   | <u>(1,799,095)</u>   | <u>437,810</u>    |
| Total increase in net assets  | 2,144,949            | 10,345,933        |
| Net assets, beginning of year   | <u>54,661,903</u>    | <u>44,315,970</u> |
| Net assets, end of year   | <u>\$ 56,806,852</u> | <u>54,661,903</u> |

See accompanying notes to consolidated financial statements.

**MT. WASHINGTON PEDIATRIC HOSPITAL, INC.  
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Consolidated Statements of Cash Flows

Years ended June 30, 2012 and 2011

|  | <b>2012</b>   | <b>2011</b> |
|--|---------------|-------------|
| Cash flows from operating activities:  |               |             |
| Increase in net assets   | \$ 2,144,949  | 10,345,933  |
| Adjustments to reconcile increase in net assets<br>to net cash provided by operating activities: |               |             |
| Depreciation   | 1,777,490     | 1,790,107   |
| Amortization of debt issue costs   | 5,131         | 5,131       |
| Provision for bad debts  | 495,836       | 482,381     |
| Net realized gains on investments  | (970,748)     | (1,344,911) |
| Restricted contributions and investment income   | (1,889,093)   | (1,625,124) |
| Change in unrealized gains on other-than-trading securities                                      | 654,629       | (1,371,455) |
| Change in funded status of defined benefit plan  | 957,962       | (576,710)   |
| Changes in operating assets and liabilities:   |               |             |
| Net patient accounts receivable  | (536,398)     | (2,039,983) |
| Other accounts receivable  | (38,548)      | (3,433)     |
| Inventories of supplies  | (16,826)      | 1,362       |
| Prepaid expenses and other current assets  | (180,729)     | (68,347)    |
| Other long-term assets   | (800,536)     | 73,490      |
| Amounts due to affiliates  | (115,814)     | 314,055     |
| Trade accounts payable   | 22,944        | (587,871)   |
| Accrued payroll benefits   | 512,402       | 188,648     |
| Advances from third-party payors   | 1,040,924     | (5,266)     |
| Other liabilities  | 2,623,821     | (224,585)   |
| Net cash provided by operating activities  | 5,687,396     | 5,353,422   |
| Cash flows from investing activities:  |               |             |
| Purchases of property and equipment  | (4,466,894)   | (3,040,077) |
| Purchases and sales of investments, net  | (1,949,838)   | (5,859,848) |
| Decrease (increase) in assets limited as to use  | 1,184,570     | (828,882)   |
| Net cash used in investing activities  | (5,232,162)   | (9,728,807) |
| Cash flows from financing activities:  |               |             |
| Repayment of long-term debt  | (260,000)     | (250,000)   |
| Restricted contributions and investment income   | 1,889,093     | 1,625,124   |
| Net cash provided by financing activities  | 1,629,093     | 1,375,124   |
| Increase (decrease) in cash and cash equivalents   | 2,084,327     | (3,000,261) |
| Cash and cash equivalents at beginning of year   | 17,728,947    | 20,729,208  |
| Cash and cash equivalents at end of year   | \$ 19,813,274 | 17,728,947  |
| Supplemental disclosure of cash flow information:  |               |             |
| Cash paid during the year for interest   | \$ 56,654     | 63,032      |

See accompanying notes to consolidated financial statements.

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Notes to Consolidated Financial Statements

June 30, 2012 and 2011

**(1) Organization**

The consolidated financial statements of Mt. Washington Pediatric Hospital, Inc. and Subsidiary (the Corporation) include the accounts of Mt. Washington Pediatric Hospital, Inc. (the Hospital) and its wholly owned subsidiary, Mt. Washington Pediatric Foundation, Inc. (the Foundation). The Corporation is structured as a joint venture with a 50% ownership interest by the University of Maryland Medical System Corporation (UMMS) and a 50% ownership interest by Johns Hopkins Health System Corporation (JHHS).

The Hospital is a not for profit, nonstock corporation formed under the laws of the State of Maryland. Its purpose is to operate a pediatric rehabilitation and specialty hospital while providing the highest quality services and programs to meet the individualized needs of infants, children, and adolescents in a nurturing environment. The Hospital has 102 licensed beds. The Foundation uses its funds and investment income to solely support the Hospital and its programs.

The Corporation incurred expenses of \$446,366 and \$467,993 for the years ended June 30, 2012 and 2011, respectively, for administrative services provided by UMMS. The Corporation is managed by UMMS, and accordingly, the results of the Corporation's operations and its financial condition could be different if it were autonomous.

**(2) Summary of Significant Accounting Policies**

**(a) Basis of Presentation**

The consolidated financial statements are prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles.

**(b) Cash and Cash Equivalents**

Cash and cash equivalents consist of cash and interest-bearing deposits with maturities of three months or less from date of purchase.

**(c) Inventories**

Inventories, consisting primarily of drugs and medical/surgical supplies, are carried at the lower of cost or market, on a first-in, first-out basis.

**(d) Investments and Assets Limited as to Use**

During the year ended June 30, 2011, the Hospital transferred its investment holdings to an investment pool of one of its owners, UMMS. The UMMS investment pool (investment pool) is classified as a trading portfolio. Accordingly, the Hospital has transferred the portion of unrealized holding gains or losses, which had previously been a component of net assets, into the excess of revenues over expenses. Each participating member of the investment pool has an undivided interest in the investment pool. The Hospital's percentage interest in the assets of the investment pool was approximately 4% and 3% at June 30, 2012 and 2011, respectively. Investment income and administrative expenses relating to the investment pool are allocated to the individual members based on this percentage.

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The Hospital's investment portfolio is classified as trading, and is reported in the consolidated balance sheets at its fair value, based on quoted market prices, at June 30, 2012 and 2011. Unrealized holding gains and losses on trading securities with readily determinable market value are included in the change in fair value of investments which is a component of nonoperating income in the accompanying consolidated statement of operations. Investment income, including realized gains and losses, is included in nonoperating income in the accompanying consolidated statements of operations.

The Foundation's investment portfolio is classified as other-than-trading and is reported in the consolidated balance sheets at its fair value, based on quoted market prices. Changes in fair value of securities with readily determinable market values below their recorded basis are recognized in the consolidated statements of operations and changes in net assets as realized losses as investment income, which is included in nonoperating income in the accompanying consolidated statements of operations. Unrealized gains on investments in securities with readily determinable market values are recognized as a component of net assets.

The Foundation does not have any alternative investments in its investment portfolio. However, the Hospital has alternative investments in assets limited as to use for self-insurance and the investment pool. Alternative investments are recorded under the equity method of accounting. Underlying securities of these alternative investments may include certain debt and equity securities that are not readily marketable. Because certain investments are not readily marketable, their fair value is subject to additional uncertainty, and therefore, values realized upon disposition may vary significantly from current reported values.

Assets limited as to use include investments set aside at the discretion of the board of trustees for the replacement or acquisition of property and equipment over which the board of trustees retains control and may at its discretion use for other purposes, self-insurance trust arrangements, and assets whose use is restricted by donors. Such investments are stated at fair value. Amounts required to meet current liabilities have been included in current assets in the consolidated balance sheets. Declines in fair value of these unrestricted investments below their cost basis are recognized in nonoperating income and expense. Changes in fair value of these unrestricted investments above their cost basis are recognized as unrealized gains on investments and are included in other changes in net assets. Changes in fair values of donor-restricted investments are recorded in unrestricted net assets unless otherwise required by the donor or state law to be included in the restricted fund balance.

Investments are exposed to certain risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, changes in the value of investment securities could occur in the near term, and these changes could materially differ from amounts reported in the accompanying consolidated financial statements.

**(e) Fair Value Measurements**

In January 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-06, *Improving Disclosures about Fair Value Measurements*. ASU No. 2010-06 amends Accounting Standards Codification (ASC Topic 820), *Fair Value*



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*Measurements and Disclosures*, to require a number of additional disclosures regarding fair value measurements and disclosure of the amounts of significant transfers between Level I and Level II investments and the reasons for such transfers, the reasons for any transfers in or out of Level III investments, and disclosure of the policy for determining when transfers among levels are recognized. ASU No. 2010-06 also clarified that disclosures should be provided for each class of assets and liabilities and clarified the requirement to disclose information about the valuation techniques and inputs used in estimating Level II and Level III measurements. Effective in fiscal year 2011, ASU No. 2010-06 also requires that information in the reconciliation of recurring Level III measurements about purchases, sales, issuances, and settlements be provided on a gross basis. The adoption of ASU No. 2010-06 only required additional disclosures and did not have an impact on the consolidated financial statements. As the Corporation did not have significant transfers between levels, or any Level III measurements, no additional disclosures were necessary.

The following methods and assumptions were used by the Corporation in estimating the fair value of its financial instruments:

*Cash and cash equivalents, accounts receivable, assets limited as to use, investments, accounts payable, accrued expenses, long-term debt, and advances from third-party payors* – The carrying amounts reported in the consolidated balance sheets approximate the related fair values.

**(f) Self-Insurance**

Under the Corporation's self-insurance programs (general and professional liability and employee health benefits), claims are reflected as a present value liability based upon actuarial estimates, including both reported and incurred but not reported claims taking into consideration the severity of incidents and the expected timing of claim payments.

**(g) Property and Equipment**

Property and equipment are stated at cost or estimated fair value at date of contribution, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. The estimated useful lives of the assets are as follows:

|                                     |                |
|-------------------------------------|----------------|
| Building and leasehold improvements | 25 to 40 years |
| Land improvements                   | 5 to 20 years  |
| Equipment                           | 3 to 15 years  |

Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

**(h) Deferred Financing Costs**

Costs incurred related to the issuance of long-term debt are deferred and are amortized over the life of the related debt using the straight-line method, which approximates the effective-interest method. Accumulated amortization of such costs amounted to \$23,944 and \$18,814 for the years ended June 30, 2012 and 2011, respectively.

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**(i) *Impairment of Long-Lived Assets***

Management regularly evaluates whether events or changes in circumstances have occurred that could indicate impairment in the value of long-lived assets. In accordance with the provisions of ASC Topic 360, *Property, Plant, and Equipment*, if there is an indication that the carrying amount of an asset is not recoverable, management estimates the projected undiscounted cash flows, excluding interest, to determine if an impairment loss should be recognized. The amount of impairment loss is determined by comparing the historical carrying value of the asset to its estimated fair value. Estimated fair value is determined through an evaluation of recent and projected financial performance using standard industry valuation techniques.

In addition to consideration of impairment upon the events or changes in circumstances described above, management regularly evaluates the remaining lives of its long-lived assets. If estimates are changed, the carrying value of affected assets is allocated over the remaining lives.

In estimating the future cash flows for determining whether an asset is impaired, the Corporation groups its assets at the lowest level for which there are identifiable cash flows independent of other groups of assets. If such costs are 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.

**(j) *Meaningful Use***

Under certain provisions of the American Recovery and Reinvestment Act of 2009 (ARRA), federal incentive payments are available to hospitals, physicians and certain other professionals (Providers) when they adopt, implement or upgrade (AIU) certified electronic health record (EHR) technology or become “meaningful users,” as defined under ARRA, of EHR technology in ways that demonstrate improved quality, safety and effectiveness of care. Providers can become eligible for annual Medicare incentive payments by demonstrating meaningful use of EHR technology in each period over four periods. Medicaid providers can receive their initial incentive payment by satisfying AIU criteria, but most demonstrate meaningful use of EHR technology in subsequent years in order to qualify for additional payments. Hospitals may be eligible for both Medicare and Medicaid EHR incentive payments; however, physicians and other professionals may be eligible for either Medicare or Medicaid incentive payments, but not both. The Hospital recognizes Medicaid EHR incentive payments when it is reasonably assured that the Hospital will successfully demonstrate compliance with the specified meaningful use criteria. During the year ended June 30, 2012, the Hospital received a Medicaid incentive payment in the amount of \$1,996,105, which is recorded as deferred revenue on the consolidated balance sheets. The Hospital intends to successfully demonstrate compliance with the specified meaningful use criteria during the next fiscal year.

**(k) *Net Assets***

The Corporation classifies net assets based on the existence or absence of donor-imposed restrictions. Unrestricted net assets represent contributions, gifts, and grants, which have no donor-imposed restrictions or which arise as a result of operations. Temporarily restricted net assets are subject to donor-imposed restrictions that must or will be met either by satisfying a specific purpose and/or passage of time. Permanently restricted net assets are subject to donor-imposed

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restrictions that must be maintained in perpetuity. Generally, the donors of these assets permit the use of all or part of the income earned on related investments for specific purposes. The restrictions associated with these net assets generally pertain to patient care, specific capital projects, and funding of specific hospital operations and community outreach programs.

**(l) Net Patient Service Revenue and Provision for Uncollectible Accounts**

Net patient service revenue reflects actual charges to patients based on rates established by the State of Maryland Health Services Cost Review Commission (HSCRC) in effect during the period in which the services are rendered, net of contractual adjustments. Contractual adjustments represent the difference between amounts billed as patient service revenue and amounts allowed by third-party payors. Such adjustments include discounts on charges as permitted by the HSCRC.

The Hospital records revenues and accounts receivable from patients and third-party payors at their estimated net realizable value. Revenue is reduced for anticipated discounts under contractual arrangements and for charity care. An estimated provision for bad debts is recorded in the period the related services are provided based upon anticipated uncompensated care, and is adjusted as additional information becomes available.

The provision for bad debts is based upon management's assessment of historical and expected net collections considering historical business and economic conditions, trends in healthcare coverage, and other collection indicators. Periodically throughout the year, management assesses the adequacy of the allowance for uncollectible accounts based upon historical collection and write-off experience by payor category. The results of this review are then used to make modifications to the provision for bad debts and to establish an allowance for uncollectible receivables. During the year ended June 30, 2011, the Hospital analyzed their bad debt collection rate and determined that based on current collection percentages, their current reserve rate was too high and reduced it accordingly. The Hospital maintained the reduced bad debt collection rate for the year ended June 30, 2012. After collection of amounts due from insurers, the Hospital follows internal guidelines for placing certain past-due balances with collection agencies.

**(m) Charity Care**

The Hospital provides charity care to patients who are unable to pay or who meet certain criteria under its charity care policy. Such patients are identified based on information obtained from the patient and subsequent analysis. Because the Hospital does not expect collection of amounts determined to qualify as charity care, such amounts are not reported as revenue. The Corporation maintains records to identify and monitor the level of charity care it provided. These records reflect the total direct and indirect costs to provide the charity care, which amounted to \$54,594 and \$78,721 in the years ended June 30, 2012 and 2011, respectively.

**(n) Nonoperating Income and Expenses, Net**

Other activities that are largely unrelated to the Corporation's primary mission are recorded as nonoperating income and expenses, and include investment income, change in fair value of investments and general donations and fund-raising activities.

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Notes to Consolidated Financial Statements

June 30, 2012 and 2011

**(o) Excess of Revenues over Expenses**

The consolidated statement of operations includes a performance indicator, the excess of revenues over expenses. Changes in unrestricted net assets that are excluded from the excess of revenues over expenses, consistent with industry practice, include the change in unrealized gains on investments (other-than-trading securities), contributions of long-lived assets (including assets acquired using contributions, which by donor restriction were to be used for the purposes of acquiring such assets), pension-related changes other than net periodic pension costs and other items which are required by generally accepted accounting principles to be reported separately.

**(p) Income Tax Status**

The Hospital is a not-for-profit corporation as described under Section 501(c)(3) of the Internal Revenue Code (the Code) and is exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. The Foundation is a not-for-profit corporation formed under the laws of the State of Maryland, organized for charitable purposes and recognized by the Internal Revenue Service as a tax-exempt organization under Section 501(c)(3) of the Code.

The Corporation follows a threshold of more likely than not for recognition and derecognition of tax positions taken or expected to be taken in a tax return. Management does not believe that there are any unrecognized tax benefits that should be recognized.

**(q) Donor-Restricted Gifts**

Unconditional promises to give cash and other assets to the Corporation 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 promise becomes unconditional. Contributions 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 is satisfied, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations as net assets released from restrictions. Such amounts are classified as other revenue or transfers and additions to property and equipment. Donor-restricted contributions for operations whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements. Revenue earned from contributed assets is considered unrestricted unless specifically restricted by the donor.

Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. An allowance for uncollectible contributions receivable is provided based upon management's judgment including such factors as prior collection history, type of contributions, and nature of fund-raising activity.

The Corporation follows accounting guidance for classifying the net assets associated with donor-restricted endowment funds held by organizations that are subject to an enacted version of the Uniform Prudent Management Institutional Funds Act of 2006 (UPMIFA).

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**(r) New Accounting Pronouncements**

In July 2011, the FASB issued ASU No. 2011-07, *Health Care Entities (Topic 954): Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debt, and the Allowance for Doubtful Accounts*. The ASU requires health care entities that recognize significant amounts of patient service revenue to present the provision for bad debts related to patient service revenue as a deduction from patient service revenue (net of contractual allowances and discounts) on their statement of operations. Additionally, enhanced disclosures about an entity's policies for recognizing, assessing bad debts, as well as qualitative and quantitative information about changes in the allowance for doubtful accounts are required. This ASU is effective for the Corporation on July 1, 2012, with early adoption permitted. The Corporation does not anticipate that the adoption of the aforementioned pronouncement, that will become effective in the next fiscal year, will have a material impact on its financial position or its results of operations.

In August 2010, the FASB issued ASU No. 2010-24, *Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries*. The amendments in the ASU clarify that a health care entity may not net insurance recoveries against related claim liabilities. In addition, the amount of the claim liability must be determined without consideration of insurance recoveries. This ASU was effective for the Corporation on July 1, 2011. The adoption of this guidance resulted in recording of additional accruals from medical malpractice claims liability and an insurance recoveries receivable of \$721,522 on the consolidated balance sheets. Such amounts are included in other assets and malpractice and other self-insurance liabilities. The Corporation did not retroactively adopt the provisions of this ASU. The adoption of this guidance did not have any impact on the results of operations or cash flows of the Corporation.

In August 2010, the FASB issued ASU No. 2010-23, *Health Care Entities (Topic 954): Measuring Charity Care for Disclosure*. ASU No. 2010-23 is intended to reduce the diversity in practice regarding the measurement basis used in the disclosure of charity care. ASU No. 2010-23 requires that cost be used as the measurement basis for charity care disclosure purposes and that cost be identified as the direct and indirect cost of providing the charity care, and requires disclosure of the method used to identify or determine such costs. This ASU was effective for the Corporation on July 1, 2011. The adoption of this pronouncement did not impact the financial position or results of operations of the Corporation. See note 2 (m) for related disclosure information.

**(s) Use of Estimates**

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

**(t) Reclassifications**

Certain amounts for 2011 have been reclassified to conform to the presentation for 2012.

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**(3) Investments and Assets Limited as to Use**

The carrying value of assets limited or restricted as to use is summarized as follows at June 30:

|   | <u>2012</u>          | <u>2011</u>       |
|---|----------------------|-------------------|
| Cash and cash equivalents                                 | \$ 97,131            | 150,852           |
| U.S. government and agency securities                     | 364,144              | 369,089           |
| Corporate obligations                                     | 1,763,135            | 1,963,773         |
| Foreign bonds   | —                    | 369,698           |
| Common stocks   | 6,341,188            | 7,392,725         |
| Assets held by other organizations – UMMS Investment Pool | 4,000,000            | 4,000,000         |
| Assets held by other organizations – MMCIP                | 1,901,399            | 1,405,430         |
| Total assets limited or restricted as to use              | <u>14,466,997</u>    | <u>15,651,567</u> |
| Less amounts available for current liabilities            | <u>(87,640)</u>      | <u>(119,548)</u>  |
| Total assets limited as to use, less current portion      | <u>\$ 14,379,357</u> | <u>15,532,019</u> |

Board-designated assets represent assets designated by the Hospital's board of trustees for future capital improvements and expansion. The board retains control of these assets and may, at its discretion, subsequently use them for other purposes. The assets consist primarily of cash and cash equivalents, fixed income securities, and equity instruments.

Self-insurance trust funds include amounts held by the Maryland Medicine Comprehensive Insurance Program (MMCIP) for payment of malpractice claims. These assets consist primarily of stocks, fixed income corporate obligations, and alternative investments. MMCIP is a funding mechanism for the Corporation's malpractice insurance. As MMCIP is not an insurance provider, transactions with MMCIP are recorded under the deposit method of accounting. Accordingly, the Corporation accounts for its participation in MMCIP by carrying limited-use assets representing the amount of funds contributed to MMCIP and recording a liability for claims, which is included in malpractice and other self-insurance liabilities in the accompanying consolidated balance sheets.

The composition and carrying value of investments were as follows at June 30:

|   | <u>2012</u>          | <u>2011</u>       |
|---|----------------------|-------------------|
| U.S. government and agency securities                     | \$ 135,381           | 130,911           |
| Corporate obligations                                     | 655,497              | 696,522           |
| Foreign bonds   | —                    | 131,127           |
| Common stocks   | 2,357,523            | 2,622,095         |
| Assets held by other organizations – UMMS Investment Pool | 13,716,549           | 11,018,339        |
|   | <u>\$ 16,864,950</u> | <u>14,598,994</u> |

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The composition and carrying value of total cash and investments held in the investment pool as of June 30 are as follows:

|  | <u>2012</u>           | <u>2011</u>        |
|--|-----------------------|--------------------|
| Cash and cash equivalents                        | \$ 15,346,744         | 42,721,303         |
| Corporate bonds                                  | 33,642,444            | 36,232,293         |
| Collateralized corporate obligations             | 75,999,613            | 68,482,673         |
| U.S. government and agency securities            | 30,973,480            | 36,096,893         |
| Common stocks                                    | 187,225,614           | 170,815,328        |
| Alternative investments                          | 142,679,310           | 121,945,204        |
|  | <u>\$ 485,867,205</u> | <u>476,293,694</u> |
| Hospital's allocation (investments)              | \$ 13,716,549         | 11,018,339         |
| Hospital's allocation (assets limited as to use) | \$ 4,000,000          | 4,000,000          |

Investment income and realized and unrealized gains (losses) for investments limited or restricted as to use and other long-term investments are summarized as follows for the years ended June 30:

|   | <u>2012</u>        | <u>2011</u>      |
|---|--------------------|------------------|
| Interest and dividend income, net of fees                           | \$ 352,147         | 322,084          |
| Net realized gains  | 970,748            | 2,298,055        |
| Change in fair value of trading securities                          | (761,680)          | 3,959,332        |
| Net unrealized (losses) gains on temporarily restricted investments | (388,880)          | 723,764          |
| Net unrealized losses on other-than-trading securities              | (265,749)          | (2,095,220)      |
|   | <u>\$ (93,414)</u> | <u>5,208,015</u> |

Total investment return is classified in the consolidated statements of operations and changes in net assets, for the years ended June 30, as follows:

|  | <u>2012</u>        | <u>2011</u>      |
|--|--------------------|------------------|
| Nonoperating investment income                         | \$ 768,093         | 1,666,994        |
| Investment gains on restricted net assets              | 165,922            | 1,676,909        |
| Change in fair value of trading securities             | (761,680)          | 3,959,332        |
| Net unrealized losses on other-than-trading securities | (265,749)          | (2,095,220)      |
|  | <u>\$ (93,414)</u> | <u>5,208,015</u> |

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**(4) Fair Value Measurements**

As discussed in note 1(e), the Corporation has implemented the provisions of ASC Topic 820 in relation to fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the consolidated financial statements on a recurring basis. This guidance established a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted market prices in active markets for identical assets or liabilities (Level I measurement) and the lowest priority to measurements involving significant unobservable inputs (Level III measurements). The three levels of the fair value hierarchy are as follows:

- Level I inputs are quoted market prices (unadjusted) in active markets for identical assets or liabilities that the Corporation has the ability to access at the measurement date.
- Level II inputs are inputs other than quoted market prices including within Level I that are observable for the asset or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term, a Level II input must be observable for substantially the full term of the asset or liability.
- Level III inputs are unobservable inputs for the asset or liability.

Assets and liabilities classified as Level I are valued using unadjusted quoted market prices for identical assets or liabilities in active markets. The Corporation uses techniques consistent with the market approach and the income approach for measuring fair value of its Level II and Level III assets and liabilities. The market approach is a valuation technique that uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. The income approach generally converts future amounts (cash flows or earnings) to a single present value amount (discounted).

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

As of June 30, 2012 and 2011, the Level II assets and liabilities listed in the fair value hierarchy tables below utilize the following valuation techniques and inputs:

***Corporate and Foreign Bonds***

The fair value of investments in U.S. and international corporate bonds, including commingled funds that invest primarily in such bonds, and foreign government bonds is primarily determined using techniques that are consistent with the market approach. Significant observable inputs include benchmark yields, reported trades, observable broker/dealer quotes, issuer spreads, and security specific characteristics, such as early redemption options.



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The following table presents assets and liabilities that are measured at fair value on a recurring basis, excluding alternative investments in the amount of \$5,632,014 for investments and \$1,642,400 for assets limited as to use which are accounted for under the equity method, as of June 30, 2012:

|   | <u>Level I</u>       | <u>Level II</u>  | <u>Level III</u> | <u>Total</u>      |
|---|----------------------|------------------|------------------|-------------------|
| Investments:                            |                      |                  |                  |                   |
| U.S. government and agency securities   | \$ 135,381           | —                | —                | 135,381           |
| Corporate obligations                   | 655,497              | —                | —                | 655,497           |
| Common stocks                           | 2,357,523            | —                | —                | 2,357,523         |
| Investments held by other organizations | 6,469,728            | 1,614,807        | —                | 8,084,535         |
| Subtotal                                | <u>9,618,129</u>     | <u>1,614,807</u> | <u>—</u>         | <u>11,232,936</u> |
| Assets limited as to use:               |                      |                  |                  |                   |
| Cash and cash equivalents               | 97,131               | —                | —                | 97,131            |
| U.S. government and agency securities   | 364,144              | —                | —                | 364,144           |
| Corporate obligations                   | 1,763,135            | —                | —                | 1,763,135         |
| Common stocks                           | 6,341,188            | —                | —                | 6,341,188         |
| Investments held by other organizations | 1,886,692            | 2,372,307        | —                | 4,258,999         |
| Subtotal                                | <u>10,452,290</u>    | <u>2,372,307</u> | <u>—</u>         | <u>12,824,597</u> |
|   | <u>\$ 20,070,419</u> | <u>3,987,114</u> | <u>—</u>         | <u>24,057,533</u> |

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The following table presents assets and liabilities that are measured at fair value on a recurring basis, excluding alternative investments in the amount of \$3,923,316 for investments and \$1,424,286 for assets limited as to use, which are accounted for under the equity method, as of June 30, 2011:

|   | <u>Level I</u>       | <u>Level II</u>  | <u>Level III</u> | <u>Total</u>      |
|---|----------------------|------------------|------------------|-------------------|
| Investments:                            |                      |                  |                  |                   |
| U.S. government and agency securities   | \$ 130,911           | —                | —                | 130,911           |
| Corporate obligations                   | 696,522              | —                | —                | 696,522           |
| Foreign bonds                           | —                    | 131,127          | —                | 131,127           |
| Common stocks                           | 2,622,095            | —                | —                | 2,622,095         |
| Investments held by other organizations | 5,547,539            | 1,547,484        | —                | 7,095,023         |
| Subtotal                                | <u>8,997,067</u>     | <u>1,678,611</u> | <u>—</u>         | <u>10,675,678</u> |
| Assets limited as to use:               |                      |                  |                  |                   |
| Cash and cash equivalents               | 150,852              | —                | —                | 150,852           |
| U.S. government and agency securities   | 369,089              | —                | —                | 369,089           |
| Corporate obligations                   | 1,963,773            | —                | —                | 1,963,773         |
| Foreign bonds                           | —                    | 369,698          | —                | 369,698           |
| Common stocks                           | 7,392,725            | —                | —                | 7,392,725         |
| Investments held by other organizations | 2,013,929            | 1,967,215        | —                | 3,981,144         |
| Subtotal                                | <u>11,890,368</u>    | <u>2,336,913</u> | <u>—</u>         | <u>14,227,281</u> |
|   | <u>\$ 20,887,435</u> | <u>4,015,524</u> | <u>—</u>         | <u>24,902,959</u> |

**(5) Property and Equipment**

A summary of property and equipment and related accumulated depreciation is as follows at June 30:

|                               | <u>2012</u>          | <u>2011</u>         |
|-------------------------------|----------------------|---------------------|
| Land and land improvements    | \$ 499,870           | 499,870             |
| Buildings and fixed equipment | 27,843,279           | 27,595,040          |
| Leasehold improvements        | 625,037              | 587,779             |
| Major moveable equipment      | 10,321,733           | 9,786,549           |
| Minor equipment               | 3,321,818            | 3,076,122           |
| Construction in progress      | 5,584,422            | 2,183,906           |
|                               | 48,196,159           | 43,729,266          |
| Less accumulated depreciation | <u>(27,655,959)</u>  | <u>(25,878,469)</u> |
| Property and equipment, net   | <u>\$ 20,540,200</u> | <u>17,850,797</u>   |

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Construction in progress includes building and renovation costs for assets that have not yet been placed into service. These costs relate to major construction projects as well as routine renovations under way at the Hospital's facilities.

Depreciation expense for the years ended June 30, 2012 and 2011 amounted to \$1,777,490 and \$1,790,107, respectively.

The Hospital entered into a construction contract for the expansion and renovation of its hospital building. The Hospital had unspent commitments under the construction contract of approximately \$1,250,000 as of June 30, 2012.

**(6) Retirement Plans**

Employees of the Corporation became eligible to participate in the Baltimore Washington Medical System, Inc.'s (BWMS) noncontributory defined benefit pension plan (the Plan) effective July 1, 1997. In connection with BWMS' sale of 50% interest in the Hospital, this Plan was amended effective July 1, 2006 to become a multiple employer plan whereby the assets and liabilities of this Plan related to the Corporation's participants have been transferred to the Corporation. The Plan covers employees who have completed one year of eligibility service and have reached 21 years of age.

Under the Plan, upon normal retirement, participants shall be eligible to receive benefits based on the value of their vested accrued benefit. Vested accrued benefits are calculated as the sum of: (a) the present value of a participant's accrued benefit under the previous plan as of June 30, 1989, plus (b) a percentage (3.0% for less than 15 years, 4.0% for years 15 to 19, 5.6% for years 20 to 24, and 7.2% for 25 years and higher) of the participant's annual compensation and compensation in excess of the Social Security Wage Base, as defined, plus (c) annual interest credited at a rate equal to the average yield of six-month United States Treasury Bills at the beginning of the plan year.

Vesting begins after three years of participation in the Plan. The funding policy is to make annual contributions to the Plan in amounts sufficient to satisfy the funding standards of the Employee Retirement Income Security Act of 1974. Pension expense for the defined benefit pension plan was approximately \$372,000 and \$498,000 for the years ended June 30, 2012 and 2011, respectively.

The Corporation also has a 403(b) retirement plan (Retirement Plan) covering substantially all employees. Employees are immediately eligible for elective deferrals of compensation as contributions to the Retirement Plan. The Retirement Plan currently has a discretionary provision for employer matching contributions.

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The following table sets forth the change in the benefit obligation and plan assets as of and for the years ended June 30, the measurement date:

|  | <u>2012</u>         | <u>2011</u>      |
|--|---------------------|------------------|
| Change in projected benefit obligations:       |                     |                  |
| Benefit obligations at beginning of year       | \$ 4,932,297        | 4,473,217        |
| Service cost                                   | 444,982             | 459,864          |
| Interest cost                                  | 253,365             | 220,219          |
| Actuarial loss                                 | 589,083             | (186,547)        |
| Benefits paid                                  | <u>(95,898)</u>     | <u>(34,456)</u>  |
| Projected benefit obligations at end of year   | <u>\$ 6,123,829</u> | <u>4,932,297</u> |
| Change in plan assets:                         |                     |                  |
| Fair value of plan assets at beginning of year | \$ 4,136,562        | 3,168,929        |
| Actual return on plan assets                   | (42,042)            | 572,492          |
| Employer contributions                         | 718,775             | 429,597          |
| Benefits paid                                  | <u>(95,898)</u>     | <u>(34,456)</u>  |
| Fair value of plan assets at end of year       | <u>\$ 4,717,397</u> | <u>4,136,562</u> |
| Accumulated benefit obligation at end of year  | \$ 5,552,980        | 4,372,640        |

The funded status of the Plan and amounts recognized as other long-term liabilities in the consolidated balance sheets at June 30 are as follows:

|  | <u>2012</u>           | <u>2011</u>        |
|--|-----------------------|--------------------|
| Funded status, end of period:                                |                       |                    |
| Fair value of plan assets                                    | \$ 4,717,397          | 4,136,562          |
| Projected benefit obligations                                | <u>6,123,829</u>      | <u>4,932,297</u>   |
| Funded status  | <u>\$ (1,406,432)</u> | <u>(795,735)</u>   |
| Amounts recognized in unrestricted net assets as of June 30: |                       |                    |
| Net actuarial loss   | \$ (1,932,340)        | (971,738)          |
| Unamortized prior service cost                               | <u>(29,742)</u>       | <u>(32,382)</u>    |
|  | <u>\$ (1,962,082)</u> | <u>(1,004,120)</u> |

The estimated amounts that will be amortized from unrestricted net assets into net periodic pension cost in fiscal 2013 are as follows:

|                    |                   |
|--------------------|-------------------|
| Net actuarial gain | \$ 8,463          |
| Prior service cost | <u>140,872</u>    |
|                    | <u>\$ 149,335</u> |

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The components of net periodic pension cost for the years ended June 30 is as follows:

|                                    | <b>2012</b> | <b>2011</b> |
|------------------------------------|-------------|-------------|
| Service cost                       | \$ 444,982  | 459,864     |
| Interest cost                      | 253,365     | 220,219     |
| Expected return on plan assets     | (357,198)   | (253,090)   |
| Amortization of prior service cost | 2,641       | 2,641       |
| Amortization of actuarial loss     | 27,720      | 68,120      |
| Net periodic pension cost          | \$ 371,510  | 497,754     |

The information below related to the assumptions relates to the entire Plan. Certain information related to the Corporation is not separately identifiable.

The following table presents the weighted average assumptions used to determine benefit obligations for the Plan at June 30:

|                               | <b>2012</b> | <b>2011</b> |
|-------------------------------|-------------|-------------|
| Discount rate                 | 4.32%       | 5.25%       |
| Rate of compensation increase | 4.50        | 5.00        |

The following table presents the weighted average assumptions used to determine net periodic benefit cost for the Plan for the years ended June 30:

|  | <b>2012</b> | <b>2011</b> |
|--|-------------|-------------|
| Discount rate                            | 5.25%       | 5.00%       |
| Expected long-term return on plan assets | 7.75        | 7.75        |
| Rate of compensation increase            | 4.50        | 5.00        |

All of the Plan's assets are held in the UMMS Master Pension Trust (the Master Trust), which was established during the year ended June 30, 2011 for the investment assets of multiple-sponsored retirement plans. Each participating plan has an undivided interest in the Master Trust. The Plan's percentage interest in the net assets of the Master Trust was approximately 4% at June 30, 2012 and 2011. Investment income and administrative expenses relating to the Master Trust are allocated to the individual plans based on this percentage.

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The fair values of total cash and investments held in the Master Trust are as follows as of June 30:

|                                 | <u>2012</u>           | <u>2011</u>        |
|---------------------------------|-----------------------|--------------------|
| Cash and cash equivalents       | \$ 4,867,252          | 6,692,505          |
| Common and preferred stocks     | 7,639,825             | 6,676,862          |
| Equity mutual funds             | 27,485,563            | 27,617,424         |
| Fixed income mutual funds       | 27,045,860            | 23,449,037         |
| Other mutual funds              | 10,583,740            | 10,273,370         |
| Alternative investments         | 30,379,100            | 27,602,484         |
|                                 | <u>\$ 108,001,340</u> | <u>102,311,682</u> |
| Plan's interest in Master Trust | \$ 4,717,397          | 4,136,562          |

The investment policies of the Master Trust incorporate asset allocation and investment strategies designed to earn superior returns on plan assets consistent with reasonable and prudent levels of risk. Investments are diversified across classes, sectors, and manager style to minimize the risk of loss. The Master Trust uses investment managers specializing in each asset category, and regularly monitors performance and compliance with investment guidelines. In developing the expected long-term rate of return on assets assumption, the Master Trust considered the current level of expected returns on risk-free investments, the historical level of the risk premium associated with the other asset classes in which the portfolio is invested, and the expectations for future returns of each asset class. The expected return for each asset class was then weighted based on the target allocation to develop the expected long-term rate of return on assets assumption for the portfolio.

The Plan's target allocation and weighted average asset allocations at the measurement date of June 30, by asset category, are as follows:

| <u>Asset category</u>     | <u>Target<br/>allocation</u> | <u>Percentage of plan assets<br/>as of June 30</u> |             |
|---------------------------|------------------------------|--|-------------|
|                           |                              | <u>2012</u>  | <u>2011</u> |
| Cash and cash equivalents | 0 – 10%                      | 4%   | 7%          |
| Equity securities         | 30 – 50%                     | 40   | 27          |
| Fixed income securities   | 25 – 45%                     | 30   | 39          |
| Global asset allocation   | 10 – 20%                     | 16   | 17          |
| Hedge funds               | 5 – 15%                      | 10   | 10          |
|                           |                              | <u>100%</u>  | <u>100%</u> |

Equity and fixed income securities include investments in hedge fund of funds that are categorized in accordance with the fund's respective investment holdings. At both June 30, 2012 and 2011, the Corporation was in the process of implementing changes to its investment classification, which required the liquidation of certain assets, resulting in more cash on hand than targeted. This cash was used to

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purchase additional securities in subsequent periods in order to restore compliance with the target allocation.

The table below presents the Master Trust's and the Plan's allocated share of investments as of June 30, 2012 aggregated by the three level valuation hierarchies as described in note 4:

|                             | <u>Level I</u>       | <u>Level II</u>   | <u>Level III</u>  | <u>Total</u>       |
|-----------------------------|----------------------|-------------------|-------------------|--------------------|
| Cash and cash equivalents   | \$ —                 | 4,867,252         | —                 | 4,867,252          |
| Common and preferred stocks | 7,639,825            | —                 | —                 | 7,639,825          |
| Equity mutual funds         | 27,485,563           | —                 | —                 | 27,485,563         |
| Fixed income mutual funds   | 27,045,860           | —                 | —                 | 27,045,860         |
| Other mutual funds          | 10,583,740           | —                 | —                 | 10,583,740         |
| Alternative investments     | —                    | 19,763,903        | 10,615,197        | 30,379,100         |
|                             | <u>\$ 72,754,988</u> | <u>24,631,155</u> | <u>10,615,197</u> | <u>108,001,340</u> |
| The Plan's allocation       | \$ 3,177,872         | 1,075,864         | 463,661           | 4,717,397          |

The table below presents the Master Trust's and the Plan's allocated share of investments as of June 30, 2011 aggregated by the three level valuation hierarchies as described in note 4:

|                             | <u>Level I</u>       | <u>Level II</u>   | <u>Level III</u>  | <u>Total</u>       |
|-----------------------------|----------------------|-------------------|-------------------|--------------------|
| Cash and cash equivalents   | \$ 6,692,505         | —                 | —                 | 6,692,505          |
| Common and preferred stocks | 6,676,862            | —                 | —                 | 6,676,862          |
| Equity mutual funds         | 27,617,424           | —                 | —                 | 27,617,424         |
| Fixed income mutual funds   | 23,449,037           | —                 | —                 | 23,449,037         |
| Other mutual funds          | 10,273,370           | —                 | —                 | 10,273,370         |
| Alternative investments     | —                    | 17,293,411        | 10,309,073        | 27,602,484         |
|                             | <u>\$ 74,709,198</u> | <u>17,293,411</u> | <u>10,309,073</u> | <u>102,311,682</u> |
| The Plan's allocation       | \$ 3,020,567         | 699,190           | 416,805           | 4,136,562          |

Changes to Level I and Level II inputs between June 30, 2011 and June 30, 2012 were the result of strategic investments and reinvestments, interest income earnings, and changes in the fair value of investments.

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Changes to the fair values based on the Level 3 inputs in the Master Trust are summarized as follows:

|                             | <b>Equity<br/>mutual funds</b> | <b>Hedge<br/>funds</b> | <b>Total</b> |
|-----------------------------|--------------------------------|------------------------|--------------|
| Balance as of June 30, 2011 | \$ —                           | 10,309,073             | 10,309,073   |
| Additions/purchases         | —                              | 2,011,506              | 2,011,506    |
| Withdrawals/sales           | —                              | (779,289)              | (779,289)    |
| Net change in value         | —                              | (926,093)              | (926,093)    |
| Balance as of June 30, 2012 | \$ —                           | 10,615,197             | 10,615,197   |

The following summarizes the redemption terms for the hedge fund-of-funds vehicles held as of June 30, 2012:

|  | <b>Fund 1</b> | <b>Fund 2</b> |
|--|---------------|---------------|
| Redemption timing:                     |               |               |
| Redemption frequency                   | Monthly       | Quarterly     |
| Required notice                        | 20 days       | 70 days       |
| Audit reserve:                         |               |               |
| Percentage held back for audit reserve | —             | —             |
| Gates:                                 |               |               |
| Potential gate holdback                | None          | None          |
| Potential gate release timeframe       | N/A           | N/A           |

The Corporation expects to contribute approximately \$600,000 to its defined benefit pension plans for the fiscal year ending June 30, 2013.

The following benefit payments, which reflect expected future employee service, as appropriate, are expected to be paid from plan assets in the following years ending June 30:

|             |            |
|-------------|------------|
| 2013        | \$ 187,949 |
| 2014        | 205,408    |
| 2015        | 262,099    |
| 2016        | 234,684    |
| 2017        | 355,992    |
| 2018 – 2022 | 1,660,862  |



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The expected benefits to be paid are based on the same assumptions used to measure the Corporation's benefit obligation at June 30, 2012 and 2011.

**(7) Leases**

The Corporation rents office and clinical space from Prince George's County Hospital. Total rent expense for the years ended June 30, 2012 and 2011 was \$70,792 and \$82,198, respectively. The lease is month to month, and therefore, there are no future obligations on the lease.

**(8) Functional Expenses**

The Corporation considers healthcare services and management and general to be its primary functional categories for purposes of expense classification. Depreciation and interest costs are allocated ratably to each classification. The Hospital's operating expenses by functional classification for the years ended June 30 is as follows:

|                        | <b>2012</b>   | <b>2011</b> |
|------------------------|---------------|-------------|
| Healthcare services    | \$ 39,686,596 | 39,485,570  |
| Management and general | 7,003,517     | 6,968,042   |
|                        | \$ 46,690,113 | 46,453,612  |

**(9) Maryland Health Services Cost Review Commission (HSCRC)**

Most of the Corporation's revenues are subject to review and approval by the Maryland Health Services Cost Review Commission (HSCRC). Hospital management has filed the required forms with the HSCRC and believes the Hospital to be in compliance with the HSCRC's requirements.

The current rate of reimbursement for services to patients under the Medicare and Medicaid programs is based on an agreement between the Center for Medicare and Medicaid Services (CMS) and the HSCRC. 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 third-party payors elect to be reimbursed under this program and the rate of increase for costs per hospital inpatient admission is below the national average. Management believes that this program will remain in effect at least through June 30, 2013.

Patient service revenue is recorded at established rates regulated by the HSCRC. Such rates are adjusted prospectively giving effect to, among other things, the projected impact of inflation, and variances between actual unit rates and previously approved unit rates (price variances) during the previous year.

The timing of the HSCRC's adjustment for the Hospital could result in an increase or reduction in rates (revenue) due to the variances described above in a year subsequent to the year in which the variances occur. The Corporation's policy is to accrue revenue based on actual charges for services to patients in the year in which the services are performed.

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**(10) Long-Term Debt**

Long-term debt, including current maturities of Maryland Health and Higher Education Facilities Authority Series D Revenue Bonds, totaled \$6,570,000 and \$6,830,000 at June 30, 2012 and 2011, respectively. The bonds were issued on November 1, 2007, interest payable monthly at a variable rate payable in fiscal years 2010 through 2029. Interest rates during fiscal year 2012 ranged from 0.05% to 0.40%.

The annual future maturities of long-term debt according to the original terms of the Loan Agreement in each of the next five fiscal years are as follows:

|            |    |           |
|------------|----|-----------|
| 2013       | \$ | 280,000   |
| 2014       |    | 285,000   |
| 2015       |    | 305,000   |
| 2016       |    | 315,000   |
| 2017       |    | 325,000   |
| Thereafter |    | 5,060,000 |
|            | \$ | 6,570,000 |

The Corporation's Series D Revenue Bonds are variable rate demand bonds requiring remarketing agents to purchase and remarket any bonds tendered before the stated maturity date. To provide liquidity support for the timely payment of any bonds that are not successfully remarketed, the Corporation has entered into a Security Agreement and obtained an irrevocable letter of credit for \$7,668,740. If the bonds are not successfully remarketed, the Corporation is required to pay an interest rate specified in the letter of credit agreement, and the principal repayment of bonds may be accelerated, at the sole discretion of the bank, to require full repayment of the outstanding balance on the mandatory prepayment date, which is on or after November 1, 2015, as defined in the Amendment to Loan Agreement. The Corporation has reflected the current portion of its long-term debt that is subject to these remarketing arrangements as a component of current liabilities. As of June 30, 2012, the Corporation did not have any amounts outstanding on the letter of credit.

The following table for the years ended June 30 reflects the approximate required repayment terms of the Corporation's debt obligations in the event that the put options associated with variable rate demand bonds subject to the remarketing agreement were exercised, but the related bonds were not successfully remarketed:

|      |    |           |
|------|----|-----------|
| 2013 | \$ | 280,000   |
| 2014 |    | 285,000   |
| 2015 |    | 305,000   |
| 2016 |    | 5,700,000 |
|      | \$ | 6,570,000 |

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The Loan Agreement contains certain restrictive covenants, including requirements that rates and charges be set at certain levels, that incurrence of additional debt be limited, and that compliance with certain operating ratios be maintained. As further security under the Loan Agreement, the Foundation has guaranteed the Corporation's repayment of principal and interest due on the bonds.

**(11) Insurance**

**(a) Professional Liability Insurance**

In connection with the affiliation agreement with UMMS and effective July 1, 2006, the Corporation became self-insured with respect to professional and general liability through its participation in the Maryland Medicine Comprehensive Insurance Program Self Insurance Trust (the Trust). The Corporation is self-insured for claims up to the limits of \$1,000,000 on individual claims and \$3,000,000 in the aggregate on an annual basis. For amounts in excess of these limits, the risk of loss has been transferred to the Terrapin Insurance Company (Terrapin), an unconsolidated joint venture of UMMS. For the year ended June 30, 2012, Terrapin provided insurance for claims related to UMMS and the Corporation for claims in excess of \$1,000,000 on individual claims and \$3,000,000 in the aggregate up to \$80,000,000 individually and \$80,000,000 in the aggregate under modified claims made policies between the aforementioned entities and Terrapin. For claims in excess of Terrapin's coverage limits, if any, the Corporation retains the risk of loss.

Based upon estimates made by independent actuaries, the Corporation provides for and funds the present value of the costs for professional and general liability claims and insurance coverage related to the projected liability from asserted and unasserted incidents that the Corporation believes may ultimately result in a loss, risk management expenses, and the projected costs to adjudicate claims. These accrued malpractice losses are discounted using a discount rate of 2.5% and, in management's opinion, provide an adequate and appropriate loss reserve.

The Corporation may become involved in claims and litigation on malpractice matters that arise in the normal course of business, none of which, in the opinion of management, is expected to result in losses in excess of insurance limits or have a materially adverse effect on the Corporation's financial position.

Total malpractice insurance expense for the Corporation in 2012 and 2011 was \$259,340 and \$148,610, respectively.

**(b) Workers' Compensation**

The Corporation is insured against workers' compensation claims through membership in the Maryland Hospital Association Workers' Compensation Self-Insurance Group. Premiums are paid quarterly and adjusted yearly based on the group's actual experience.

**(c) Health Insurance**

The Corporation maintains a self-insurance plan for employee health insurance. The Corporation has accrued \$508,821 and \$421,842 as of June 30, 2012 and 2011, respectively, for estimated claims incurred but not reported.

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**(12) Business and Credit Concentrations**

The Corporation provides services to patients in the Baltimore Metropolitan area, the majority of whom are under the age of 18 and are covered by third-party health insurance or state Medicaid programs. Insurance coverage and credit information is obtained from patients upon admission when available. The Corporation bills the insurer directly for services provided. No collateral is obtained for accounts receivable.

Gross receivables from patients and third-party payors consisted of the following at June 30:

|                              | <u>2012</u> | <u>2011</u> |
|------------------------------|-------------|-------------|
| Medicaid                     | 59%         | 45%         |
| Blue Cross                   | 19          | 25          |
| Commercial insurance and HMO | 20          | 29          |
| Self-pay and others          | 2           | 1           |
|                              | <u>100%</u> | <u>100%</u> |

Gross patient service revenue, by payor class, consisted of the following at June 30:

|                              | <u>2012</u> | <u>2011</u> |
|------------------------------|-------------|-------------|
| Medicaid                     | 70%         | 71%         |
| Blue Cross                   | 12          | 12          |
| Commercial insurance and HMO | 17          | 16          |
| Self-pay and others          | 1           | 1           |
|                              | <u>100%</u> | <u>100%</u> |

**(13) Endowment**

The Corporation's endowment consists of four individual funds established based on donor-imposed restrictions. Net assets associated with endowment funds are classified and reported based on the existence of donor-imposed restrictions.

**(a) Interpretation of Relevant Law**

The board of trustees has interpreted UPMIFA as requiring that donor-restricted endowment funds be managed with the long-term objective of at least maintaining the real value (after inflation) of the funds. The Corporation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the directions of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the board of trustees in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Corporation considers the

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following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

Endowment net assets consist of the following as of June 30, 2012:

|                                  |    | <u>Unrestricted</u> | <u>Temporarily<br/>restricted</u> | <u>Permanently<br/>restricted</u> | <u>Total</u> |
|----------------------------------|----|---------------------|-----------------------------------|-----------------------------------|--------------|
| Donor-restricted endowment funds | \$ | —                   | 5,130,918                         | 825,171                           | 5,956,089    |
| Board-designated endowment funds |    | —                   | 2,485,995                         | —                                 | 2,485,995    |
| Total endowed net assets         | \$ | —                   | 7,616,913                         | 825,171                           | 8,442,084    |

Endowment net assets consist of the following as of June 30, 2011:

|                                  |    | <u>Unrestricted</u> | <u>Temporarily<br/>restricted</u> | <u>Permanently<br/>restricted</u> | <u>Total</u> |
|----------------------------------|----|---------------------|-----------------------------------|-----------------------------------|--------------|
| Donor-restricted endowment funds | \$ | —                   | 5,042,329                         | 825,171                           | 5,867,500    |
| Board-designated endowment funds |    | —                   | 4,435,483                         | —                                 | 4,435,483    |
| Total endowed net assets         | \$ | —                   | 9,477,812                         | 825,171                           | 10,302,983   |

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Changes in endowment net assets for the year ended June 30, 2012 are as follows:

|  | <u>Unrestricted</u> | <u>Temporarily<br/>restricted</u> | <u>Permanently<br/>restricted</u> | <u>Total</u>     |
|--|---------------------|-----------------------------------|-----------------------------------|------------------|
| Endowment net assets,<br>June 30, 2011                           | \$ —                | 9,477,812                         | 825,171                           | 10,302,983       |
| Released for purchases of<br>equipment and<br>construction costs | —                   | (2,026,820)                       | —                                 | (2,026,820)      |
| Investment return  | —                   | 165,921                           | —                                 | 165,921          |
| Endowment net assets,<br>June 30, 2012                           | <u>\$ —</u>         | <u>7,616,913</u>                  | <u>825,171</u>                    | <u>8,442,084</u> |

**(b) Funds with Deficiencies**

From time to time, the fair value of assets associated with an individual donor-restricted endowment fund may fall below the original value of the fund. As of June 30, 2012, there have been no deficiencies of this nature. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as an increase in unrestricted net assets, as appropriate.

**(c) Return Objectives and Risk Parameters**

The Foundation has adopted investment and funding policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Under the investment policy, as approved by the board of trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of a benchmark that includes the S&P 500, Barclays Government/Credit, and T-Bill Index while assuming a moderate level of investment risk. The Foundation expects its endowment funds, over three to five years, to provide an average annual real rate of return of at least 5%. Actual returns in any given year may vary from this amount.

**(d) Strategies Employed for Achieving Objectives**

To satisfy its long-term rate-of-return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Foundation targets a diversified asset allocation that places emphasis on investments in equities, bonds, cash, and cash equivalents in a ratio to achieve its long-term return objectives within prudent risk constraints.

**(e) Funding Policy and How the Investment Objectives Relates to Funding Policy**

The Foundation has historically distributed to the Hospital an amount equal to approximately 5% after investment expenses of the average assets of the Foundation. The terms and provisions of the original endowment subfunds must be honored in considering the Hospital's requests. Funding

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requests are submitted to the Foundation for approval by the Hospital annually. In determining distributions, the Foundation considered the expected and actual return on the endowment.

**(14) Temporarily and Permanently Restricted Net Assets**

The Corporation classifies net assets based on the existence or absence of donor-imposed restrictions.

Temporarily and permanently restricted net assets consisted of the following at June 30:

|   | <b>2012</b>  | <b>2011</b> |
|---|--------------|-------------|
| Temporarily restricted net assets:                  |              |             |
| Funds to be used for programs and outdoor area      | \$ 239,355   | 177,551     |
| Callaway Fund                                       | 26,383       | 26,383      |
| Endowment funds to be used for 2nd floor renovation | 2,485,995    | 4,000,000   |
| Endowment funds, other                              | 5,130,918    | 5,477,812   |
| Total   | \$ 7,882,651 | 9,681,746   |
| Permanently restricted net assets:                  |              |             |
| Eliasberg Fund                                      | \$ 5,000     | 5,000       |
| White Fund  | 150,576      | 150,576     |
| Williams Fund                                       | 86,829       | 86,829      |
| Redman Fund   | 582,766      | 582,766     |
| Total   | \$ 825,171   | 825,171     |

**(15) Certain Significant Risks and Uncertainties**

The Corporation provides pediatric rehabilitation and specialty services in the state of Maryland. The Corporation and other healthcare providers in Maryland are subject to certain inherent risks, including the following:

- Dependence on revenues derived from reimbursement by the state Medicaid programs;
- Regulation of hospital rates by the State of Maryland Health Services Cost Review Commission;
- Government regulation, government budgetary constraints, and proposed legislative and regulatory changes; and
- Lawsuits alleging malpractice and related claims.

Such inherent risks require the use of certain management estimates in the preparation of the Corporation's consolidated financial statements, and it is reasonably possible that a change in such estimates may occur.

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The state Medicaid reimbursement programs represent a substantial portion of the Corporation's revenues and the Corporation's operations are subject to a variety of other federal, state, and local regulatory requirements. Failure to maintain required regulatory approvals and licenses and/or changes in such regulatory requirements could have a significant adverse effect on the Corporation.

Changes in federal and state reimbursement funding mechanisms and related government budgetary constraints could have a significant adverse effect on the Corporation.

The healthcare industry is subject to numerous laws and regulations from federal, state, and local governments. The Corporation's compliance with these laws and regulations can be subject to periodic governmental review and interpretation, which can result in regulatory action unknown or unasserted at this time. Management is aware of certain asserted and unasserted legal claims and regulatory matters arising in the ordinary course of business, none of which, in the opinion of management, is expected to result in losses in excess of insurance limits or have a materially adverse effect on the Corporation's financial position.

The federal government and many states have aggressively increased enforcement under Medicaid anti-fraud and abuse laws and physician self-referral laws (STARK law and regulation). Recent federal initiatives have prompted a national review of federally funded healthcare programs. In addition, the federal government and many states have implemented programs to audit and recover potential overpayments to providers from the Medicaid program. The Corporation has implemented a compliance program to monitor conformance with applicable laws and regulations, but the possibility of future government review and enforcement action exists.

As a result of recently enacted and pending federal healthcare reform legislation, substantial changes are anticipated in the U.S. healthcare system. Such legislation includes numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement to healthcare providers, and the legal obligations of health insurers, providers, and employers. These provisions are currently slated to take effect at specified times over the next decade. This federal healthcare reform legislation does not affect the consolidated financial statements for the year ended June 30, 2012.

**(16) Subsequent Events**

The Corporation evaluated all events and transaction that occurred after June 30, 2012 and through October 26, 2012. The Corporation did not have any material recognizable subsequent events during the period.



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Consolidating Balance Sheet Information

June 30, 2012

| <b>Assets</b>   | <b>Mt. Washington<br/>Pediatric<br/>Hospital, Inc.</b> | <b>Mt. Washington<br/>Pediatric<br/>Foundation, Inc.</b> | <b>Elimination<br/>entries</b> | <b>Consolidated<br/>total</b> |
|---|--|--|--------------------------------|-------------------------------|
| Current assets:   |  |  |                                |                               |
| Cash and cash equivalents   | \$ 17,653,537  | 2,159,737  | —                              | 19,813,274                    |
| Current portion of assets limited as to use   | 87,640   | —  | —                              | 87,640                        |
| Patient accounts receivable, less allowance for<br>doubtful accounts of \$2,069,747 | 5,722,579  | —  | —                              | 5,722,579                     |
| Other accounts receivable   | 94,749   | —  | —                              | 94,749                        |
| Inventories of supplies   | 138,991  | —  | —                              | 138,991                       |
| Prepaid expenses and other current assets   | 620,338  | 21,372   | —                              | 641,710                       |
| Total current assets  | 24,317,834   | 2,181,109  | —                              | 26,498,943                    |
| Investments   | 13,716,549   | 3,148,401  | —                              | 16,864,950                    |
| Assets limited as to use, less current portion:                                     |  |  |                                |                               |
| Board-designated funds  | 4,009,991  | —  | —                              | 4,009,991                     |
| Eliasberg Second Floor Construction Fund  | —  | 2,485,994  | —                              | 2,485,994                     |
| Funds restricted by donor   | 87,140   | 5,982,473  | —                              | 6,069,613                     |
| Self-insurance trust funds  | 1,813,759  | —  | —                              | 1,813,759                     |
|   | 5,910,890  | 8,468,467  | —                              | 14,379,357                    |
| Property and equipment, net   | 20,540,200   | —  | —                              | 20,540,200                    |
| Economic interest in net assets of the Foundation                                   | 13,797,977   | —  | (13,797,977)                   | —                             |
| Other assets  | 1,049,576  | —  | —                              | 1,049,576                     |
| Total assets  | \$ 79,333,026  | 13,797,977   | (13,797,977)                   | 79,333,026                    |
| <b>Liabilities and Net Assets</b>   |  |  |                                |                               |
| Current liabilities:  |  |  |                                |                               |
| Current portion of long-term debt   | \$ 280,000   | —  | —                              | 280,000                       |
| Trade accounts payable  | 2,317,352  | —  | —                              | 2,317,352                     |
| Accrued payroll benefits  | 3,610,619  | —  | —                              | 3,610,619                     |
| Advances from third-party payors  | 4,579,909  | —  | —                              | 4,579,909                     |
| Current portion of malpractice and other<br>self-insurance liabilities              | 87,640   | —  | —                              | 87,640                        |
| Deferred revenue  | 1,996,105  | —  | —                              | 1,996,105                     |
| Due to affiliates   | 247,947  | —  | —                              | 247,947                       |
| Total current liabilities   | 13,119,572   | —  | —                              | 13,119,572                    |
| Malpractice and other self-insurance liabilities                                    | 1,510,283  | —  | —                              | 1,510,283                     |
| Accrued pension obligations   | 1,406,432  | —  | —                              | 1,406,432                     |
| Other long-term liabilities   | 199,887  | —  | —                              | 199,887                       |
| Long-term debt, less current portion  | 6,290,000  | —  | —                              | 6,290,000                     |
| Total liabilities   | 22,526,174   | —  | —                              | 22,526,174                    |
| Net assets:   |  |  |                                |                               |
| Unrestricted  | 48,099,030   | 5,329,510  | (5,329,510)                    | 48,099,030                    |
| Temporarily restricted  | 7,882,651  | 7,643,296  | (7,643,296)                    | 7,882,651                     |
| Permanently restricted  | 825,171  | 825,171  | (825,171)                      | 825,171                       |
| Total net assets  | 56,806,852   | 13,797,977   | (13,797,977)                   | 56,806,852                    |
| Total liabilities and net assets  | \$ 79,333,026  | 13,797,977   | (13,797,977)                   | 79,333,026                    |

See accompanying independent auditors' report.

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Consolidating Balance Sheet Information

June 30, 2011

| <b>Assets</b>   | <b>Mt. Washington<br/>Pediatric<br/>Hospital, Inc.</b> | <b>Mt. Washington<br/>Pediatric<br/>Foundation, Inc.</b> | <b>Elimination<br/>entries</b> | <b>Consolidated<br/>total</b> |
|---|--|--|--------------------------------|-------------------------------|
| Current assets:   |  |  |                                |                               |
| Cash and cash equivalents   | \$ 15,507,758  | 2,221,189  | —                              | 17,728,947                    |
| Current portion of assets limited as to use   | 119,548  | —  | —                              | 119,548                       |
| Patient accounts receivable, less allowance for<br>doubtful accounts of \$1,865,402 | 5,682,019  | —  | —                              | 5,682,019                     |
| Other accounts receivable   | 56,201   | —  | —                              | 56,201                        |
| Inventories of supplies   | 122,165  | —  | —                              | 122,165                       |
| Prepaid expenses and other current assets   | 551,912  | 25,734   | (116,665)                      | 460,981                       |
| Total current assets  | 22,039,603   | 2,246,923  | (116,665)                      | 24,169,861                    |
| Investments   | 11,018,339   | 3,580,655  | —                              | 14,598,994                    |
| Assets limited as to use, less current portion:                                     |  |  |                                |                               |
| Board-designated funds  | 4,017,500  | —  | —                              | 4,017,500                     |
| Eliasberg Second Floor Construction Fund  | —  | 4,000,000  | —                              | 4,000,000                     |
| Funds restricted by donor   | 96,087   | 6,095,285  | —                              | 6,191,372                     |
| Self-insurance trust funds  | 1,323,147  | —  | —                              | 1,323,147                     |
|   | 5,436,734  | 10,095,285   | —                              | 15,532,019                    |
| Property and equipment, net   | 17,850,797   | —  | —                              | 17,850,797                    |
| Economic interest in net assets of the Foundation                                   | 15,806,198   | —  | (15,806,198)                   | —                             |
| Other assets  | 254,171  | —  | —                              | 254,171                       |
| Total assets  | \$ 72,405,842  | 15,922,863   | (15,922,863)                   | 72,405,842                    |
| <b>Liabilities and Net Assets</b>   |  |  |                                |                               |
| Current liabilities:  |  |  |                                |                               |
| Current portion of long-term debt   | \$ 260,000   | —  | —                              | 260,000                       |
| Trade accounts payable  | 2,294,411  | —  | —                              | 2,294,411                     |
| Accrued payroll benefits  | 3,098,217  | —  | —                              | 3,098,217                     |
| Advances from third-party payors  | 3,538,985  | —  | —                              | 3,538,985                     |
| Current portion of malpractice and other<br>self-insurance liabilities              | 82,283   | —  | —                              | 82,283                        |
| Due to affiliates   | 363,762  | 116,665  | (116,665)                      | 363,762                       |
| Total current liabilities   | 9,637,658  | 116,665  | (116,665)                      | 9,637,658                     |
| Malpractice and other self-insurance liabilities                                    | 740,546  | —  | —                              | 740,546                       |
| Accrued pension obligations   | 795,735  | —  | —                              | 795,735                       |
| Long-term debt, less current portion  | 6,570,000  | —  | —                              | 6,570,000                     |
| Total liabilities   | 17,743,939   | 116,665  | (116,665)                      | 17,743,939                    |
| Net assets:   |  |  |                                |                               |
| Unrestricted  | 44,079,465   | 5,476,833  | (5,401,312)                    | 44,154,986                    |
| Temporarily restricted  | 9,757,267  | 9,504,194  | (9,579,715)                    | 9,681,746                     |
| Permanently restricted  | 825,171  | 825,171  | (825,171)                      | 825,171                       |
| Total net assets  | 54,661,903   | 15,806,198   | (15,806,198)                   | 54,661,903                    |
| Total liabilities and net assets  | \$ 72,405,842  | 15,922,863   | (15,922,863)                   | 72,405,842                    |

See accompanying independent auditors' report.

**MT. WASHINGTON PEDIATRIC HOSPITAL, INC.  
AND SUBSIDIARY**

Consolidating Statement of Operations and Changes in Net Assets Information

Year ended June 30, 2012

|  | <u>Mt. Washington<br/>Pediatric<br/>Hospital, Inc.</u> | <u>Mt. Washington<br/>Pediatric<br/>Foundation, Inc.</u> | <u>Elimination<br/>entries</u> | <u>Consolidated<br/>total</u> |
|--|--|--|--------------------------------|-------------------------------|
| Unrestricted revenue and other support:  |  |  |                                |                               |
| Net patient service revenue  | \$ 48,091,824  | —  | —                              | 48,091,824                    |
| Other revenue  | 713,729  | —  | (268,195)                      | 445,534                       |
| Total unrestricted revenue and other support   | <u>48,805,553</u>                                      | <u>—</u>   | <u>(268,195)</u>               | <u>48,537,358</u>             |
| Operating expenses:  |  |  |                                |                               |
| Salaries, wages, and benefits  | 32,855,597   | —  | —                              | 32,855,597                    |
| Purchased services   | 11,499,405   | —  | —                              | 11,499,405                    |
| Interest expense   | 61,785   | —  | —                              | 61,785                        |
| Depreciation   | 1,777,490  | —  | —                              | 1,777,490                     |
| Provision for bad debts  | 495,836  | —  | —                              | 495,836                       |
| Total operating expenses   | <u>46,690,113</u>                                      | <u>—</u>   | <u>—</u>                       | <u>46,690,113</u>             |
| Operating income   | 2,115,440  | —  | (268,195)                      | 1,847,245                     |
| Nonoperating income and expenses:  |  |  |                                |                               |
| Contributions  | 193,775  | —  | —                              | 193,775                       |
| Investment income  | 456,993  | 311,100  | —                              | 768,093                       |
| Change in fair value of investments  | (761,680)  | —  | —                              | (761,680)                     |
| Support from Mt. Washington Pediatric Foundation, Inc.   | —  | (2,219,494)  | 2,219,494                      | —                             |
| Total nonoperating income and expense  | <u>(110,912)</u>                                       | <u>(1,908,394)</u>                                       | <u>2,219,494</u>               | <u>200,188</u>                |
| Excess (deficiency) of revenues over expenses  | 2,004,528  | (1,908,394)  | 1,951,299                      | 2,047,433                     |
| Net unrealized losses on other-than-trading securities   | —  | (265,749)  | —                              | (265,749)                     |
| Net assets released from restrictions used for the purchase of property and equipment upon donor request | 3,120,322  | 2,026,820  | (2,026,820)                    | 3,120,322                     |
| Change in funded status of defined benefit plan  | (957,962)  | —  | —                              | (957,962)                     |
| Change in economic interest in the Foundation  | (147,323)  | —  | 147,323                        | —                             |
| Increase (decrease) in unrestricted net assets   | <u>4,019,565</u>                                       | <u>(147,323)</u>   | <u>71,802</u>                  | <u>3,944,044</u>              |
| Changes in temporarily restricted net assets:  |  |  |                                |                               |
| Contributions  | 3,553,785  | —  | (2,219,494)                    | 1,334,291                     |
| Investment income, net   | —  | 554,802  | —                              | 554,802                       |
| Net unrealized losses on temporarily restricted investments  | —  | (388,880)  | —                              | (388,880)                     |
| Change in economic interest in the Foundation  | (1,860,898)  | —  | 1,860,898                      | —                             |
| Net assets released from restrictions used for the purchase of property and equipment                    | (3,120,322)  | (2,026,820)  | 2,026,820                      | (3,120,322)                   |
| Net assets released from restrictions used for operations  | (447,181)  | —  | 268,195                        | (178,986)                     |
| Decrease in temporarily restricted net assets  | <u>(1,874,616)</u>                                     | <u>(1,860,898)</u>                                       | <u>1,936,419</u>               | <u>(1,799,095)</u>            |
| Total increase (decrease) in net assets  | 2,144,949  | (2,008,221)  | 2,008,221                      | 2,144,949                     |
| Net assets, beginning of year  | <u>54,661,903</u>                                      | <u>15,806,198</u>  | <u>(15,806,198)</u>            | <u>54,661,903</u>             |
| Net assets, end of year  | <u>\$ 56,806,852</u>                                   | <u>13,797,977</u>  | <u>(13,797,977)</u>            | <u>56,806,852</u>             |

See accompanying independent auditors' report.

**MT. WASHINGTON PEDIATRIC HOSPITAL, INC.  
AND SUBSIDIARY**

Consolidating Statement of Operations and Changes in Net Assets Information

Year ended June 30, 2011

|  | <u>Mt. Washington<br/>Pediatric<br/>Hospital, Inc.</u> | <u>Mt. Washington<br/>Pediatric<br/>Foundation, Inc.</u> | <u>Elimination<br/>entries</u> | <u>Consolidated<br/>total</u> |
|--|--|--|--------------------------------|-------------------------------|
| Unrestricted revenue and other support:  |  |  |                                |                               |
| Net patient service revenue  | \$ 50,087,871  | —  | —                              | 50,087,871                    |
| Other revenue  | 563,269  | —  | (268,487)                      | 294,782                       |
| Total unrestricted revenue and other support   | <u>50,651,140</u>                                      | <u>—</u>   | <u>(268,487)</u>               | <u>50,382,653</u>             |
| Operating expenses:  |  |  |                                |                               |
| Salaries, wages, and benefits  | 31,989,461   | —  | —                              | 31,989,461                    |
| Purchased services   | 12,124,000   | —  | —                              | 12,124,000                    |
| Interest expense   | 67,663   | —  | —                              | 67,663                        |
| Depreciation   | 1,790,107  | —  | —                              | 1,790,107                     |
| Provision for bad debts  | 482,381  | —  | —                              | 482,381                       |
| Total operating expenses   | <u>46,453,612</u>                                      | <u>—</u>   | <u>—</u>                       | <u>46,453,612</u>             |
| Operating income   | 4,197,528  | —  | (268,487)                      | 3,929,041                     |
| Nonoperating income and expenses:  |  |  |                                |                               |
| Contributions  | 138,188  | —  | —                              | 138,188                       |
| Investment income  | 1,078,127  | 588,867  | —                              | 1,666,994                     |
| Change in fair value of investments  | 3,959,332  | —  | —                              | 3,959,332                     |
| Support from Mt. Washington Pediatric Foundation, Inc.   | —  | (450,132)  | 450,132                        | —                             |
| Total nonoperating income and expense  | <u>5,175,647</u>                                       | <u>138,735</u>   | <u>450,132</u>                 | <u>5,764,514</u>              |
| Excess of revenues over expenses   | 9,373,175  | 138,735  | 181,645                        | 9,693,555                     |
| Net unrealized (losses) gains on other-than-trading securities   | (2,544,535)  | 449,315  | —                              | (2,095,220)                   |
| Net assets released from restrictions used for the purchase of property and equipment upon donor request | 1,839,202  | —  | (106,124)                      | 1,733,078                     |
| Change in funded status of defined benefit plan  | 576,710  | —  | —                              | 576,710                       |
| Change in economic interest in the Foundation  | 588,050  | —  | (588,050)                      | —                             |
| Increase in unrestricted net assets  | <u>9,832,602</u>                                       | <u>588,050</u>   | <u>(512,529)</u>               | <u>9,908,123</u>              |
| Changes in temporarily restricted net assets:  |  |  |                                |                               |
| Contributions  | 1,122,113  | —  | (450,132)                      | 671,981                       |
| Investment income, net   | —  | 953,145  | —                              | 953,145                       |
| Net unrealized gains on temporarily restricted investments   | —  | 723,764  | —                              | 723,764                       |
| Change in economic interest in the Foundation  | 1,676,909  | —  | (1,676,909)                    | —                             |
| Net assets released from restrictions used for the purchase of property and equipment                    | (1,839,202)  | —  | 106,124                        | (1,733,078)                   |
| Net assets released from restrictions used for operations  | (446,489)  | —  | 268,487                        | (178,002)                     |
| Increase in temporarily restricted net assets  | <u>513,331</u>   | <u>1,676,909</u>   | <u>(1,752,430)</u>             | <u>437,810</u>                |
| Total increase in net assets   | <u>10,345,933</u>                                      | <u>2,264,959</u>   | <u>(2,264,959)</u>             | <u>10,345,933</u>             |
| Net assets, beginning of year  | <u>44,315,970</u>                                      | <u>13,541,239</u>  | <u>(13,541,239)</u>            | <u>44,315,970</u>             |
| Net assets, end of year  | <u>\$ 54,661,903</u>                                   | <u>15,806,198</u>  | <u>(15,806,198)</u>            | <u>54,661,903</u>             |

See accompanying independent auditors' report.