

AUDITED COMBINED FINANCIAL
STATEMENTS AND OTHER FINANCIAL
INFORMATION

Windham Community Memorial Hospital, Inc., and Affiliates
Years Ended September 30, 2010 and 2009

Windham Community Memorial Hospital, Inc., and Affiliates

Audited Combined Financial Statements and Other Financial Information

Years Ended September 30, 2010 and 2009

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Report of Independent Auditors

Board of Trustees

Windham Community Memorial Hospital, Inc. and Affiliates

We have audited the accompanying combined balance sheets of Windham Community Memorial Hospital, Inc., and Affiliates (the Hospital) as of September 30, 2010 and 2009, and the related combined statements of operations and changes in net assets and cash flows for the year then ended. These combined financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these combined financial statements based on our audit. We did not audit the financial statements of The Hatch Hospital Corporation which statements reflect total assets of \$873,735 and \$816,375 as of September 30, 2010 and 2009, and total revenues of \$2,378,405 and \$1,879,625 for the years then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for The Hatch Hospital Corporation, is based solely on the report of the other auditors.

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

In our opinion, based on our audits and the report of the other auditors, the combined financial statements referred to above present fairly, in all material respects, the combined financial position of Windham Community Memorial Hospital, Inc. and Affiliates as of September 30, 2010 and 2009, and the combined results of their operations and changes in net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.



January 20, 2011

Windham Community Memorial Hospital, Inc., and Affiliates

Combined Balance Sheets

	September 30	
	2010	2009
Assets		
Current assets:		
Cash and cash equivalents	\$ 3,314,081	\$ 3,357,508
Current portion of assets whose use is limited	684,559	804,428
Accounts receivable, less allowances of approximately \$1,494,000 in 2010 and \$2,103,000 in 2009	14,090,656	13,116,037
Other receivables	1,032,229	2,334,406
Inventories of supplies	1,175,285	1,175,255
Prepaid expenses	280,392	671,383
Pledges receivable	165,043	372,884
Funds designated for debt service	424,886	919,441
Due from third-party reimbursement agencies	1,585,717	1,258,523
Total current assets	<u>22,752,848</u>	<u>24,009,865</u>
Other assets:		
Investments	347,049	322,070
Assets whose use is limited:		
Donor restricted investments	1,885,179	2,743,568
Beneficial interest in perpetual trusts	2,607,805	1,752,149
Investment in real estate, net of accumulated depreciation of approximately \$656,000 in 2010 and \$587,000 in 2009	880,317	946,499
Unamortized bond discount and issuance expense	432,208	448,118
Debt service reserve fund	1,673,374	1,674,179
Due from related party	32,000	-
Deposits and other assets	995,386	902,998
Total other assets	<u>8,853,318</u>	<u>8,789,581</u>
Property, plant and equipment, net of accumulated depreciation	<u>36,227,411</u>	<u>36,908,939</u>
Total assets	<u>\$ 67,833,577</u>	<u>\$ 69,708,385</u>

	September 30	
	2010	2009
Liabilities and net assets		
Current liabilities:		
Trade accounts payable	\$ 3,465,207	\$ 3,370,047
Salaries, wages, payroll taxes and amounts withheld from employees	840,849	1,276,413
Accrued vacation and holiday pay	1,088,949	1,459,086
Other accrued expenses	746,552	1,033,556
Accrued pension	3,965,000	1,133,000
Current portion of long-term debt and capital lease obligations	703,485	855,910
Total current liabilities	10,810,042	9,128,012
Long-term liabilities:		
Accrued pension and other liabilities	53,726,319	57,389,912
Long-term debt, less current portion	19,435,038	19,698,257
Interest rate swap obligation	3,185,469	2,585,845
Capital lease obligations, less current portion	612,432	1,077,681
Total liabilities	87,769,300	89,879,707
Net assets:		
Unrestricted	(25,203,815)	(25,502,905)
Temporarily restricted	1,538,289	2,104,204
Permanently restricted	3,729,803	3,227,379
Total net assets	(19,935,723)	(20,171,322)
Total liabilities and net assets	\$ 67,833,577	\$ 69,708,385

See accompanying notes.

Windham Community Memorial Hospital, Inc., and Affiliates
 Combined Statements of Operations and Changes in Net Assets

	Year Ended September 30	
	2010	2009
Unrestricted operating revenues:		
Net patient revenue	\$ 86,942,706	\$ 83,605,148
Other operating revenue	2,622,664	2,401,877
Total operating revenues	89,565,370	86,007,025
Operating expenses:		
Salaries	39,301,133	37,098,685
Employee benefits	14,575,223	12,646,534
Physician fees	932,425	910,707
Consulting, legal and auditing fees	657,860	764,944
Supplies	9,437,343	9,495,592
Insurance	1,043,977	1,200,994
Purchased services	6,445,484	6,177,714
Other nonsalary expenses	7,568,921	6,608,688
Provision for uncollectible accounts	5,459,445	4,595,065
Depreciation and amortization	4,522,902	4,418,804
Interest	1,557,105	1,483,430
Total operating expenses	91,501,818	85,401,157
(Loss) income from operations	(1,936,448)	605,868
Nonoperating income (loss):		
Interest income, net	96,303	152,507
Gifts and bequests	252,482	205,897
Net realized and unrealized gain on investments	20,260	1,992
Net loss from investment in real estate	(10,352)	(53,022)
Other nonoperating activities	(85,065)	(2,098,246)
Net nonoperating income (loss)	273,628	(1,790,872)
Deficiency of revenues over expenses	(1,662,820)	(1,185,004)

Continued on next page.

Windham Community Memorial Hospital, Inc., and Affiliates

Combined Statements of Operations and Changes in Net Assets (continued)

	Year Ended September 30	
	2010	2009
Unrestricted net assets:		
Deficiency of revenues over expenses	(1,662,820)	(1,185,004)
Change in pension funding and post retirement obligations	1,624,421	(33,873,622)
Net assets released from restriction for capital	239,353	11,387
Other	24,894	(13,922)
Transfer from other entity	73,242	–
Transfer from temporarily restricted net assets	–	74,511
Increase (decrease) in unrestricted net assets	299,090	(34,986,650)
Temporarily restricted net assets:		
Gifts and bequests	350,312	129,238
Investment income, net	45,236	25,969
Realized gain (loss) on investments	20,492	(35,866)
Unrealized gain on investments	91,812	95,348
Transfer to unrestricted net assets	–	(74,511)
Transfer to permanently restricted net assets	(394,647)	–
Net assets released from restrictions for operations	(439,767)	–
Net assets released from restriction for capital	(239,353)	(11,387)
(Decrease) increase in temporarily restricted net assets	(565,915)	128,791
Permanently restricted net assets:		
Gifts and bequests	691	
Investment loss income, net	(1,387)	(4,189)
Realized gain (loss) on investments	6,210	(41,490)
Unrealized gain on investments	6,058	38,950
Transfer from temporarily restricted net assets	394,647	
Change in fair value of perpetual trust	96,205	(39,566)
Increase (decrease) in permanently restricted net assets	502,424	(46,295)
Increase (decrease) in net assets	235,599	(34,904,154)
Net assets, beginning of year	(20,171,322)	14,732,832
Net assets, end of year	\$(19,935,723)	\$(20,171,322)

See accompanying notes.

Windham Community Memorial Hospital, Inc., and Affiliates

Combined Statements of Cash Flows

	Year Ended September 30	
	2010	2009
Cash flows from operating activities		
Change in net assets	\$ 235,599	\$ (34,904,154)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Noncash items:		
Depreciation and amortization	4,522,902	4,434,713
Change in unrealized gains and losses on investments	97,870	136,838
Change in unrealized gains and losses on investments on funds held in trust by others	96,205	39,566
Provision for uncollectible accounts	5,459,445	4,595,065
Change in net assets related to post retirement and pension plans	(1,624,421)	33,873,622
Change in fair value of interest rate swap agreements	599,624	930,655
Guarantee of swap	-	1,655,190
Restricted contributions, realized gains and losses, and investment income	(421,554)	(73,662)
Other changes in net assets:		
Changes in assets and liabilities, net	(5,173,474)	(6,752,464)
Net cash provided by operating activities	<u>3,792,196</u>	<u>3,935,369</u>
Cash flows from investing activities		
Net purchase of property, plant and equipment	(3,841,374)	(3,365,043)
Investment in real estate	66,182	(168,986)
(Purchase) sales of investments	(96,452)	(342,664)
Net cash used in investing activities	<u>(3,871,644)</u>	<u>(3,876,693)</u>
Cash flows from financing activities		
Payments on debt	(325,654)	(307,270)
Proceeds of debt service funds	495,360	1,200,993
Payment of capital leases	(555,239)	(446,557)
Restricted contribution, realized gains and losses, and investment income	421,554	73,662
Net cash provided by financing activities	<u>36,021</u>	<u>520,828</u>
Net (decrease) increase in cash and cash equivalents	<u>(43,427)</u>	<u>579,504</u>
Cash and cash equivalents at beginning of year	<u>3,357,508</u>	<u>2,778,004</u>
Cash and cash equivalents at end of year	<u>\$ 3,314,081</u>	<u>\$ 3,357,508</u>

See accompanying notes.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements

September 30, 2010

1. Significant Accounting Policies

The accounting policies that affect significant elements of Windham Community Memorial Hospital, Inc. and Affiliate's financial statements are summarized below and in Note 2.

Organization and Basis of Combination

Windham Community Memorial Hospital, Inc. (Windham) is a voluntary association incorporated under the General Statutes of the State of Connecticut, and as of March 2009, is an affiliate of Hartford Healthcare Corporation (HHC). The Board of Directors of Windham, appointed by HHC, controls the operations of Windham. The accompanying combined financial statements include Windham Community Memorial Hospital, Inc., The Hatch Hospital Corporation, and the Windham Hospital Foundation, Inc. (together, the Hospital). All material intercompany accounts and transactions have been eliminated in the accompanying combined financial statements.

Windham, located in Willimantic, Connecticut, is a nonprofit acute care hospital. Windham provides inpatient, outpatient and emergency care services for residents of Northeastern Connecticut.

The Hatch Hospital Corporation (Hatch) is a nonprofit organization incorporated under the General Statutes of the State of Connecticut. Its purpose is to promote, foster, aid, carry out and fulfill the aims, objectives and purposes of the trust created under the Tenth Clause of the will of George Hatch. Periodically, amounts are transferred from the trust to Hatch for expenses as the need arises.

Windham Hospital Foundation, Inc. (Foundation) is a nonprofit organization incorporated under the General Statutes of the State of Connecticut. Its purpose is to promote and solicit charitable support for the purposes of Windham.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. There is at least a reasonable possibility that certain estimates will change by material amounts in the near term. Actual results could differ from those estimates.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

1. Significant Accounting Policies (continued)

Regulatory Matters

The Hospital is required to file annual operating information with the State of Connecticut Office of Health Care Access (OHCA).

Fair Value of Financial Instruments

The carrying value of financial instruments classified as current assets and current liabilities approximate fair value. The fair values of other financial instruments are disclosed in the respective notes and/or in Note 5.

Cash and Cash Equivalents

Cash and cash equivalents are defined as highly liquid investments with maturities of 90 days or less. The Hospital maintains its cash and cash equivalents in bank deposit or brokerage accounts that, at times, may exceed federally insured limits. In addition, cash and cash equivalents may, at times, be invested in instruments not covered by federal insurance. The Hospital's deposits exceeded federal depository insurance limits as of September 30, 2010 and 2009. However, the Hospital has not experienced any losses in such accounts or instruments, and management believes the Hospital is not exposed to any significant credit risk on cash and cash equivalents.

Investments

The Hospital's investment portfolio is classified as trading, with unrealized gains and losses included in the deficiency of revenues over expenses.

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value at the balance sheet date. Alternative investments, those assets whose market value is not readily determinable, are stated at fair value as estimated in an unquoted market. Valuations of those investments and, therefore, the Hospital's holdings may be determined by the investment manager and are primarily based on the underlying securities.

Assets Whose Use is Limited

Assets whose use is limited includes assets that are set aside internally for nursing support and other health care services. Investments for restricted purposes are those restricted based on donors' intents.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

1. Significant Accounting Policies (continued)

Patient Accounts Receivable

Patient accounts receivable result from the health care services provided by the Hospital. Additions to the allowance for doubtful accounts result from the provision for bad debts. Accounts written off as uncollectible are deducted from the allowance for doubtful accounts.

The amount of the allowance for doubtful accounts is based upon management's assessment of historical and expected net collections, business and economic conditions, trends in Medicare and Medicaid health care coverage and other collection indicators. See Note 2 for additional information relative to third party payor programs.

The Hospital's primary concentration of credit risk is patient accounts receivable, which consist of amounts owed by various governmental agencies, insurance companies and private patients. The Hospital manages the receivables by regularly reviewing its patient accounts and contracts, and by providing appropriate allowances for uncollectible amounts.

Inventories

Inventory consists of medical supplies and instruments and is valued at the lower of cost or market. Cost is determined on a first-in, first-out basis.

Unamortized Bond Issuance Costs

Bond issuance costs associated with long-term debt for capital projects are amortized over a period consistent with the life of the debt.

Property, Plant and Equipment

Land, buildings and equipment acquisitions that individually exceed \$500 (\$250 for technology) are capitalized at cost and depreciated on a straight-line basis over their estimated useful lives. Estimated useful lives are as follows:

Land and improvements	10-20 years
Building and leasehold improvements	5-75 years
Equipment	2-25 years

Amortization of equipment held under capital leases is included in depreciation expense.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

1. Significant Accounting Policies (continued)

Conditional asset retirement obligations recorded under the provisions of Accounting Standards Codification (ASC) 410-20, *Asset Retirement Obligations*, amounted to \$97,738 and \$151,482 as of September 30, 2010 and 2009, respectively. These obligations are recorded in other noncurrent liabilities in the accompanying combined balance sheets. There are no assets that are legally restricted for purposes of settling asset retirement obligations. During 2010 and 2009, retirement obligations incurred and settled were minimal.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those where use by the Hospital has been limited by donors, to a specific time frame or purpose. Temporarily restricted net assets are available to provide for the support of the new emergency room renovations, purchase of equipment, free care, nursing support, scholarships and various other special purposes. Permanently restricted net assets have been restricted by donors and are maintained by the Hospital in perpetuity. The Hospital is a partial beneficiary to various perpetual trust agreements. Assets recorded under these agreements are recognized at fair value. The investment income generated from these funds is expendable to support healthcare services and the assets are classified as permanently restricted.

Contributions, including unconditional promises to give, are recognized as revenue in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Unrestricted contributions are recorded, net of expenses, within other operating revenue.

Pledges receivable to be received beyond one year are discounted utilizing a discount rate commensurate with the related risks involved. Amortization of the discount is recognized as revenue and is reflected in accordance with donor-imposed restrictions, if any, on the contributions.

Donor-Restricted Gifts

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the combined statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are unrestricted contributions in the accompanying financial statements, except those relating to donations of long-lived assets.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

1. Significant Accounting Policies (continued)

Nonoperating Revenues

Activities, other than in connection with providing healthcare services, are considered to be nonoperating. Nonoperating gains consist primarily of income earned on invested funds, realized and unrealized gains and losses on unrestricted funds, change in fair value of interest rate swap agreements, and gifts and bequests.

Deficiency of Revenues over Expenses

The combined statements of operations and changes in net assets include deficiency of revenues over expenses as the performance indicator. Changes in unrestricted net assets which are excluded from deficiency of revenues over expenses include 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), changes in pension funding and postretirement obligations, and net asset transfers.

Professional Liability Insurance

Coverage for medical malpractice insurance is provided on a claims-made basis. The primary level of coverage is \$10,000,000 per claim and \$39,000,000 in the aggregate. The excess indemnity coverage is layered with four different insurance companies at \$15,000,000 per claim and \$15,000,000 in the aggregate per layer. The primary coverage is with CHS Insurance Limited, a captive insurance company.

The Hospital establishes reserves for unpaid losses with the assistance of consulting actuaries based on a combination of industry and hospital specific data. Future adjustments to the amounts recorded resulting from continual review processes, as well as differences between estimates and ultimate payments, will be reflected in the consolidated statement of operations of future years when such adjustments, if any, become known.

Interest Rate Swap Agreements

The Hospital utilizes interest rate swap agreements to reduce risks associated with changes in interest rates. The Hospital does not hold or issue derivative financial instruments for trading purposes. The Hospital is exposed to credit loss in the event of nonperformance by the counterparties to its interest rate swap agreements.

Interest rate swap agreements are reported at fair value. Changes in fair value are recognized in the performance indicator in the statements of operations and changes in net assets.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

1. Significant Accounting Policies (continued)

Income Taxes

Windham, Hatch and the Foundation are nonprofit corporations as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code.

Adoption of New Accounting Standards

In December 2008, the FASB issued additional authoritative guidance regarding an employer's disclosures about postretirement benefit plan assets, currently included in ASC 715. This guidance requires disclosure about the major classes of postretirement benefit plan assets, including a description of the inputs and valuation techniques used to measure those assets and the designation of such assets by level; how investment allocation decisions are made; the effect of fair value measurements using significant unobservable inputs on changes in plan assets for the period; and significant concentrations of risk within plan assets. See Note 5 for these additional disclosures for the year ended September 30, 2010. The adoption of this guidance did not have a significant impact on the Hospital's consolidated financial statements for the year ended September 30, 2010.

New Accounting Standards

In January 2010, the Financial Accounting Standards Board issued Accounting Standards Update 2010-06, *Improving Disclosures about Fair Value Measurements*, (ASU 2010-06). ASU 2010-06 amended ASC 820 to clarify certain existing fair value disclosures and require a number of additional disclosures. The guidance in ASU 2010-06 clarified that disclosures should be presented separately for each "class" of assets and liabilities measured at fair value and provided guidance on how to determine the appropriate classes of assets and liabilities to be presented. ASU 2010-06 also clarified the requirement for entities to disclose information about both the valuation techniques and inputs used in estimating Level 2 and Level 3 fair value measurements. In addition, ASU 2010-06 introduced new requirements to disclose the amounts (on a gross basis) and reasons for any significant transfers between Levels 1, 2 and 3 of the fair value hierarchy and present information regarding the purchases, sales, issuances and settlements of Level 3 assets and liabilities on a gross basis. With the exception of the requirement to present changes in Level 3 measurements on a gross basis, which is delayed until 2011, the guidance in ASU 2010-06 becomes effective for reporting periods beginning after December 15, 2009. Management is currently evaluating the effect that the provisions of ASU 2010-06 will have on the consolidated financial statements.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

1. Significant Accounting Policies (continued)

Subsequent Events

The Hospital evaluates the impact of subsequent events, which are events that occur after the balance sheet date but before the financial statements are issued, for potential recognition in the financial statements as of the balance sheet date for the year ended September 30, 2010. The Hospital evaluated subsequent events through January 20, 2011, which is the date the financial statements were issued. No events occurred that require disclosure or adjustment to the consolidated financial statements.

Reclassifications

Certain reclassifications have been made to the year ended September 30, 2009 balances previously reported in the combined balance sheets and statements of operations and changes in net assets in order to conform with the year ended September 30, 2010 presentation.

2. Revenues from Services to Patients and Charity Care

Significant concentrations of net patient revenues are comprised of 41% Medicare, 8% Medicaid and 20% Blue Cross for the year ended September 30, 2010, and 41% Medicare, 9% Medicaid and 20% Blue Cross for the year ended September 30, 2009.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries are outstanding, compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties and exclusion from the Medicare and Medicaid programs. Changes in the Medicare and Medicaid programs and the reduction of funding levels could have an adverse impact on the Hospital.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

2. Revenues from Services to Patients and Charity Care (continued)

The following table summarizes the combined gross and net revenues from services to patients:

	Year Ended September 30	
	2010	2009
Gross revenues from patients:		
Inpatient:		
Routine services	\$ 16,998,211	\$ 16,619,235
Special services	56,486,569	55,826,977
	73,484,780	72,446,212
Outpatient	120,470,784	117,737,661
Gross revenues from patients	193,955,564	190,183,873
Deductions:		
Allowances	104,466,765	104,418,812
Charity care	2,546,093	2,159,913
	107,012,858	106,578,725
Net patient revenue	\$ 86,942,706	\$ 83,605,148

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. The difference is accounted for as allowances. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, fee-for-service, discounted charges and per diem payments. Net patient service revenue is affected by the State of Connecticut Disproportionate Share program and is reported at the estimated net realizable amounts due from patients, third-party payors and others for services rendered and includes estimated retroactive revenue adjustments due to future audits, reviews and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews and investigations. During fiscal 2010 and 2009 the Hospital recorded net changes in estimate of approximately \$473,000 and \$43,000, respectively, which primarily relate to better than previously estimated third party payor settlements.

The Hospital has established estimates based on information presently available, of amounts due to or from Medicare, Medicaid and third-party payors for adjustments to current and prior year payment rates, based on industry-wide and Hospital-specific data. Such amounts are included in the accompanying balance sheets.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

2. Revenues from Services to Patients and Charity Care (continued)

The Hospital has agreements with various health maintenance organizations (HMOs) to provide medical services to subscribing participants. Under these agreements, the HMOs make fee-for-service payments to the Hospital for certain covered services based upon discounted fee schedules.

The Hospital accepts all patients, regardless of their ability to pay. A patient is classified as a charity patient by reference to the established policies of the Hospital. Essentially, these policies define charity services as those services for which no payment is anticipated. In assessing a patient's inability to pay, the Hospital utilizes the generally recognized poverty income levels but also includes certain cases where incurred charges are significant when compared to incomes. These charges are not included in net patient service revenues for financial reporting purposes.

3. Net Assets

Temporarily restricted net assets are available for the following purposes at September 30:

	2010	2009
Purchase of equipment	\$ 119,261	\$ 80,043
Free care	51,269	1,388
Nursing support	745,578	950,386
Other purpose restrictions	622,181	1,072,387
Total temporarily restricted net assets	<u>\$ 1,538,289</u>	<u>\$ 2,104,204</u>

Permanently restricted net assets at September 30 are restricted for:

	2010	2009
Investments to be held in perpetuity, the income from which is expendable to support health care services	\$ 1,121,998	\$ 1,475,230
Restricted funds held in trust by others, the income from which is expendable to support health care services	2,607,805	1,752,149
	<u>\$ 3,729,803</u>	<u>\$ 3,227,379</u>

The Hospital's endowment consists of various funds established for a variety of purposes. The endowment includes donor-restricted endowment funds. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor imposed restrictions.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

3. Net Assets (continued)

The Board of Trustees of the Hospital has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Hospital classifies as permanently net restricted 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 direction of the applicable donor gift instrument at the time of 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 organization in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Hospital considers the following factors in making a determination to appropriate or accumulate donor-restricted funds:

- 1) The duration and preservation of the fund
- 2) The purposes of the Hospital 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) Other resources of the Hospital
- 7) The investment policies of the Hospital

The primary objective of the endowment fund is to provide long-term support for the Hospital's capital and operating programs. The Hospital's investment goals are to maximize total return (capital appreciation, dividends and interest) while also protecting the Hospital's inflation-adjusted value over time. The Hospital's assets are diversified across multiple assets classes (e.g., common stocks, bonds and cash) to achieve an optimal balance between risk and return between current income and capital appreciation. The investment program is structured to offer reasonably high probability of generating real return to protect the real inflation-adjusted value of assets and to meet the spending requirements. The investment committee reviews investment policies annually to determine if changes need to be made to changing market conditions or other factors.

Management evaluates endowment spending in light of capital replacement and expansion plans. The spending policy does not apply a prescribed rate of spending in a given year, but does consider expenditures based on need and current market conditions as well as long-term invest goals.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

3. Net Assets (continued)

Changes in endowment funds for the fiscal year ended September 30, 2010 and 2009 consisted of the following:

	2010		
	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets at beginning of year	\$ 1,448,238	\$ 1,475,230	\$ 2,923,468
Net asset reclassification	(394,647)	(364,804)	(759,451)
Endowment net assets after reclassification	1,053,591	1,110,426	2,164,017
Investment return:			
Investment income	45,236	(1,387)	43,849
Net (realized and unrealized)	112,304	12,268	124,572
Total investment return	157,540	10,881	168,421
Contributions	4,430	691	5,121
Appropriation of endowment assets for expenditure	(281,104)	–	(281,104)
Endowment net assets at end of year	\$ 934,457	\$ 1,121,998	\$ 2,056,455
	2009		
	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets at beginning of year	\$ 1,364,605	\$ 1,481,959	\$ 2,846,564
Net asset reclassification	20,353	–	20,353
Endowment net assets after reclassification	1,384,958	1,481,959	2,866,917
Investment return:			
Investment income	15,185	(4,189)	10,996
Net (realized and unrealized)	59,482	(2,540)	56,942
Total investment return	74,667	(6,729)	67,938
Contributions	–	–	–
Appropriation of endowment assets for expenditure	(11,387)	–	(11,387)
Endowment net assets at end of year	\$ 1,448,238	\$ 1,475,230	\$ 2,923,468

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

3. Net Assets (continued)

From time to time, the fair value of assets associated with individual donor-restricted endowments funds may fall below the level that the donor of UPMIFA requires the Hospital to retain as a fund of perpetual duration. These deficiencies result from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions and continued appropriation for certain programs that was deemed prudent by the Board of Trustees. There were no significant deficiencies of this nature which are reported in unrestricted net assets as of September 30, 2010 or 2009.

4. Assets Whose Use is Limited and Investments

Investments and assets whose use is limited are stated at fair value at September 30 are as follows:

	<u>2010</u>	<u>2009</u>
Cash and cash equivalents	\$ 684,559	\$ 804,428
Marketable equity securities	492,375	1,041,516
Corporate and government obligations	266,034	630,836
Mutual funds	1,473,818	1,393,286
	<u>\$ 2,916,787</u>	<u>\$ 3,870,066</u>

The Hospital is the income beneficiary of certain perpetual trusts. The market value of the Hospital's share of these trusts were \$2,607,805 and \$1,752,149 as of September 30, 2010 and 2009, respectively.

The composition and presentation of unrestricted investment income which is included in nonoperating income are comprised of the following for the years ended September 30:

	<u>2010</u>	<u>2009</u>
Nonoperating income:		
Interest income, net	\$ 96,303	\$ 152,507
Net realized and unrealized gain on investments	20,260	1,992
	<u>\$ 116,563</u>	<u>\$ 154,499</u>

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

4. Assets Whose Use is Limited and Investments (continued)

Investment in real estate at September 30 is as follows:

	<u>2010</u>	<u>2009</u>
Professional building	\$ 885,445	\$ 885,445
Coventry Medical Building	650,624	648,729
	<u>1,536,069</u>	1,534,174
Less accumulated depreciation	655,752	587,675
Net investment in real estate	<u>\$ 880,317</u>	<u>\$ 946,499</u>

5. Fair Values of Financial Instruments

As defined in ASC 820-10, fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, ASC 820-10 establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Observable inputs that are based on inputs not quoted in active markets, but corroborated by market data.

Level 3: Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. In determining fair value, the Hospital utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. The Hospital also considers counterparty credit risk in its assessment of fair value.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

5. Fair Values of Financial Instruments (continued)

Financial assets and liabilities carried at fair value as of September 30, 2010 are classified in the table below in one of the three categories described above:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 3,314,081	\$ –	\$ –	\$ 3,314,081
Assets whose use is limited:				
Cash and cash equivalents	684,559	–	–	684,559
Mutual funds	1,473,818	–	–	1,473,818
Corporate and government obligations	266,034	–	–	266,034
Marketable equity securities	492,375	–	–	492,375
Funds held in trust	–	2,607,805	–	2,607,805
Pension fund assets:				
Cash and cash equivalents	5,228,793	–	–	5,228,793
Mutual funds	57,352,518	–	–	57,352,518
Liabilities				
Interest rate swap agreements	–	3,185,469	–	3,185,469

Financial assets and liabilities carried at fair value as of September 30, 2009 are classified in the table below in one of the three categories described above:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 3,357,508	\$ –	\$ –	\$ 3,357,508
Assets whose use is limited:				
Cash and cash equivalents	804,428	–	–	804,428
Mutual funds	1,393,286	–	–	1,393,286
Corporate and government obligations	630,836	–	–	630,836
Marketable equity securities	1,041,516	–	–	1,041,516
Funds held in trust	–	1,752,149	–	1,752,149
Liabilities				
Interest rate swap agreements	–	2,585,845	–	2,585,845

Fair value for Level 1 is based upon quoted market prices while fair value for Level 2 securities were determined primarily through prices obtained from third party pricing sources.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

6. Property, Plant and Equipment

A summary of property, plant and equipment at September 30, is as follows:

	2010	2009
Land and improvements	\$ 5,215,610	\$ 5,215,610
Buildings and leasehold improvements	46,654,278	45,041,772
Equipment	46,575,979	44,204,964
Construction in progress	270,392	428,448
	98,716,259	94,890,794
Less accumulated depreciation	62,488,848	57,981,855
Net property, plant and equipment	\$ 36,227,411	\$ 36,908,939

The Hospital capitalized interest expense of \$91,923 and \$138,355 for the years ended September 30, 2010 and 2009.

7. Debt Arrangements

Debt arrangements at September 30, include the following:

	2010	2009
CHEFA 2007 Series D bonds repayable over a 29-year period ending July 1, 2037, bearing 7.5% interest, secured by the Hospital's real property	\$ 19,350,000	\$ 19,555,000
Promissory mortgage note with a bank bearing interest at 6%, payments are due in equal installments through November 1, 2032, secured by a mortgage on the related real property	288,550	294,189
Connecticut Hospital Association energy note due November 2010, noninterest bearing, monthly payments of \$7,900	15,800	110,603
Promissory mortgage note with a bank bearing interest at 5.9%, payments are due in equal installments through October 1, 2012, secured by a mortgage on the related real property	44,154	64,366
	19,698,504	20,024,158
Less current portion	263,466	325,901
Total long-term debt	\$ 19,435,038	\$ 19,698,257

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

7. Debt Arrangements (continued)

The future minimum principal payments of long-term debt are as follows:

Year Ending September 30:	
2011	\$ 263,466
2012	264,344
2013	262,028
2014	282,461
2015	302,922
Thereafter	18,323,283
	<u>\$ 19,698,504</u>

The Connecticut Health and Educational Facilities Authority (CHEFA) Revenue bonds Series D (Series D CHEFA Bonds) were issued on November 14, 2007 in the amount of \$19,745,000. These proceeds were advanced to the Hospital under the terms of a loan agreement between the Hospital and CHEFA. Proceeds from the issuance of the 2007 Series D CHEFA bonds were used to redeem Series C CHEFA Bonds, pay off various capital leases, and fund equipment and facility improvements.

The carrying value of the Series D CHEFA Bonds approximates fair value.

In conjunction with the issuance of the Series D CHEFA Bonds, the Hospital entered into two interest rate swap agreements with a financial institution, with an original notional amount of \$19,745,000, to fix the debt at a rate of 4.15%. The fair value of the swap agreements were \$3,185,469 and \$2,585,845 at September 30, 2010 and 2009, respectively, and are recorded in the accompanying balance sheets. Although the swap agreements represent economic hedges of the interest rate on the bonds, they do not qualify for hedge accounting. The changes in fair value of these agreements are reported in the accompanying statements of operations and changes in net assets as a component of other nonoperating activities along with the net cash receipts on the swap agreements.

The Series D CHEFA Bonds contain a covenant which includes the maintenance of a minimum debt service coverage ratio. As of September 30, 2010, the Hospital was in compliance with the covenant. In addition, the Hospital is required to set aside certain funds for the purposes of future debt payments.

The Hospital has an outstanding line of credit with a financial institution for \$5,000,000 which expires on June 1, 2011. Interest is set at prime, and there have been no drawings under this under the line of credit as of September 30, 2010 and 2009.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

8. Capital Leases

The Hospital has entered into numerous agreements to lease equipment that meet the requirements of a capital lease.

Capital lease obligations as of September 30 include the following:

	<u>2010</u>	<u>2009</u>
Capital lease obligations	\$ 1,052,451	\$ 1,607,690
Less current portion	440,019	530,009
Long-term capital lease obligations	<u>\$ 612,432</u>	<u>\$ 1,077,681</u>

The following is a schedule of future minimum lease payments under capital leases:

Year Ending September 30:	
2011	\$ 440,019
2012	375,100
2013	180,040
2014	57,293
Total minimum lease payments	<u>1,052,452</u>
Less amount representing interest	<u>113,328</u>
Present value of net minimum lease payments	<u><u>\$ 939,124</u></u>

9. Pension and Other Postretirement Benefits

The Hospital has a pension plan that provides for both a contributory and noncontributory defined benefit plan for eligible employees providing for retirement and certain death benefits. The benefits are based on years of service and the employee's compensation during the last five years of employment. The Hospital makes contributions in amounts sufficient to fund the pension plan's minimum funding requirements under the Employee Retirement Income Security Act.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

9. Pension and Other Postretirement Benefits (continued)

Effective January 1, 2004, Windham began sponsoring the Windham Community Memorial Hospital 401(k) Plan. Under the terms of the plan, eligible employees receive a basic contribution of 2%, and the Hospital matches 50% of the employee's salary contribution up to an additional 3% of the employee's compensation. Effective April 1, 2006, all nonunion employees hired prior to April 1, 2004 have ceased their participation in the defined benefit plan, and their pension accruals have been frozen as of that date. A second defined contribution plan known as the Windham Hospital Defined Contribution Plan was established for nonunion employees hired prior to April 1, 2004. Under the terms of the plan, eligible employees receive a basic contribution of 5% with no matching contribution. Effective January 1, 2010, all non-union employees in the 401(k) plan were transferred into the Defined Contribution Plan.

Expense for employer contributions was approximately \$1,409,000 and \$609,000 in 2010 and 2009, respectively.

The Hospital provides health care and life insurance benefits to its retired employees who meet certain eligibility requirements. The Hospital's policy is to fund the cost of postretirement benefits other than the pension costs as incurred.

The measurement date for determining the pension plan's assets and obligations and the other postretirement benefit plan's obligations is September 30.

The following table sets forth the funded status and amounts recognized in the combined balance sheets for the pension and postretirement benefits:

	Pension Benefits		Other Postretirement Benefits	
	2010	2009	2010	2009
Change in benefit obligation:				
Benefit obligation at beginning of year	\$ (89,794,378)	\$ (64,525,026)	\$ (26,094,217)	\$ (17,779,323)
Service cost	(533,849)	(1,225,710)	(128,936)	(144,708)
Interest cost	(4,857,481)	(4,792,080)	(1,320,267)	(1,315,638)
Participant contributions	(23,367)	(86,087)	(108,532)	(98,442)
Benefits paid	3,058,943	2,728,453	1,162,456	1,064,404
Plan amendments	-	-	2,363,881	-
Actuarial losses	(2,457,199)	(21,893,928)	(1,436,685)	(7,820,510)
Benefit obligation at end of year	(94,607,331)	(89,794,378)	(25,562,300)	(26,094,217)
Change in plan assets:				
Fair value of plan assets at beginning of year	57,446,683	56,601,562	-	-
Actual return on plan assets	5,493,803	(22,645)	-	-
Employer contributions	2,676,401	3,510,132	1,053,924	965,962
Participant contributions	23,367	86,087	108,532	98,442
Benefits paid	(3,058,943)	(2,728,453)	(1,162,456)	(1,064,404)
Fair value of plan assets at end of year	62,581,311	57,446,683	-	-
Unfunded status	\$ (32,026,020)	\$ (32,347,695)	\$ (25,562,300)	\$ (26,094,217)

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

9. Pension and Other Postretirement Benefits (continued)

The accumulated benefit obligations for the defined benefit pension plan and other postretirement benefit plan at September 30, 2010 and 2009 are \$94,607,331 and \$25,562,300, respectively.

The following table sets forth the unrecognized items impacting the pension and the postretirement plans as of September 30:

	Pension Benefits		Other Postretirement Benefits	
	2010	2009	2010	2009
Unrecognized net loss from past experience different from that assumed and effects of changes in assumptions	\$ 42,268,275	\$ 42,552,843	\$ 9,566,713	\$ 8,679,556
Unrecognized prior service cost	–	4,723	(1,319,847)	–
Unrecognized transition asset	–	–	–	747,400

Amounts included in unrestricted net assets at September 30, 2010 and expected to be recognized in net periodic benefit cost during the year ended September 30, 2011 are as follows:

Amortization of prior service cost	\$ (437,035)
Amortization of net loss	3,991,098
	<u>\$ 3,554,063</u>

	Pension Benefits		Other Postretirement Benefits	
	2010	2009	2010	2009
Components of net periodic benefit cost:				
Service cost	\$ 533,849	\$ 1,225,710	\$ 128,936	\$ 144,708
Interest cost	4,857,481	4,792,080	1,320,267	1,315,638
Return on plan assets	(5,315,175)	22,645	–	–
Net amortization and deferral	2,563,430	(4,283,751)	252,894	124,567
Additional amount due to settlement or curtailment	4,432	–	–	–
Benefit cost	\$ 2,644,017	\$ 1,756,684	\$ 1,702,097	\$ 1,584,913

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

9. Pension and Other Postretirement Benefits (continued)

The weighted-average discount rates used in determining the actuarial present value of the projected benefit obligation of the defined benefit plan was 5.08% and 5.58% in 2010 and 2009, respectively. The weighted-average discount rates used in determining net periodic benefit cost of the defined benefit plan was 5.58% and 7.55% in 2010 and 2009, respectively. The rate of compensation increase was a graded scale based on age ranging from 7% to 2.5% in 2010 and 2009. The expected long-term rate of return on plan assets was 9% in 2010 and 2009. The rate of return for fiscal year 2011 will be 8.25%. The expected long-term rate of return assumption is determined by adding expected inflation to expected long-term real returns of various asset classes, taking into account expected volatility and correlation between the returns of various asset classes.

The weighted-average annual assumed rate of increase in the per capita cost of covered benefits (i.e., health care cost trend rate) is assumed to grade from 8% per year in fiscal year 2010 to 4% in fiscal year 2018. This health care cost trend rate assumption has a significant effect on the amounts reported. To illustrate, a 1% point increase in the assumed health care cost trend rate would increase the accumulated postretirement benefit obligation and service and interest costs by \$2,920,658 and \$173,498, respectively, at September 30, 2010. A 1% point decrease in the assumed health care cost trend rate would decrease the accumulated postretirement benefit obligation and service and interest costs by \$2,477,785 and \$146,286, respectively, at September 30, 2010.

The Hospital's pension plan weighted-average asset allocations by asset category are as follows:

	<u>2010</u>	<u>2009</u>
Mutual funds (equities)	66%	60%
Mutual funds (fixed income)	26	32
Immediate participation guarantee contract	8	8
	<u>100%</u>	<u>100%</u>

The asset mix was determined by evaluating the expected return against the plan's long-term objectives. Performance is monitored on a monthly basis, and the portfolio is rebalanced back to target levels to ensure the targets are within range. The investment policy describes which securities are allowed in the portfolios and the financed objectives of the plan which the Investment Committee of the Hospital Board oversees. The Investment Committee monitors the investment performance annually to determine the continued feasibility of achieving the investment objectives and the appropriateness of the investment policy.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

9. Pension and Other Postretirement Benefits (continued)

Contributions

The Hospital expects to contribute approximately \$2,900,000 to its pension plan beginning October 1, 2010. The Hospital funds its other postretirement plan for actual expenses incurred.

Estimated Future Benefit Payments

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

	Pension Benefits	Other Postretirement Benefits
2011	\$ 2,768,000	\$ 1,197,000
2012	3,017,000	1,298,000
2013	3,249,000	1,399,000
2014	3,519,000	1,513,000
2015	3,908,000	1,628,000
2016-2020	24,597,000	9,219,000

10. Pledges Receivable

Pledges receivable as of September 30, are expected to be collected as follows:

	2010	2009
Within one year	\$ 292,155	\$ 709,066
Less reserve for uncollectible pledges	(127,112)	(336,182)
Net pledges receivable	\$ 165,043	\$ 372,884

11. Commitments and Contingencies

Various lawsuits and claims arising in the normal course of operations are pending or are in progress against the Hospital. Such lawsuits and claims are either specifically covered by insurance as explained in Note 1 or are deemed to be immaterial. While the outcomes of the lawsuits cannot be determined at this time, management believes that any loss which may arise from these actions will not have a material adverse effect on the financial position or changes in net assets of the Hospital.

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

11. Commitments and Contingencies (continued)

Operating Leases

The Hospital rents certain equipment under terms of leases that qualify as operating leases. Rental and lease expense amounted to \$862,383 and \$722,322 for the years ended September 30, 2010 and 2009, respectively.

The minimum lease commitments under all noncancelable operating leases with initial or remaining terms of more than one year are as follows:

Year Ending September 30:	
2011	\$ 379,334
2012	390,473
2013	394,744
2014	397,869
2015	257,465
Thereafter	927,251
	\$ 2,747,135

12. Supplemental Cash Flow Information

The changes in assets and liabilities are as follows:

	September 30	
	2010	2009
	<i>(in thousands)</i>	
Increase in accounts receivable	\$ (6,434,064)	\$ (5,714,550)
Decrease (increase) in other receivables	1,302,177	(523,564)
Decrease in pledge receivables	207,841	69,688
Decrease in inventories of supplies and prepaid expenses	390,961	519,175
(Increase) decrease in estimated third-party payor settlements	(327,194)	908,171
Increase in deposits and other assets	(108,478)	(147,881)
Increase in accounts payable	95,160	86,753
Decrease in salaries, wages, payroll taxes and amounts withheld from employees and accrued vacation	(805,701)	(105,421)
Decrease in other accrued expenses	(287,004)	(491,338)
Increase (decrease) in accrued pension	792,828	(1,353,497)
	\$ (5,173,474)	\$ (6,752,464)

Windham Community Memorial Hospital, Inc., and Affiliates

Notes to Combined Financial Statements (continued)

13. Related Parties

During 2008, a letter of intent between the Hospital and HHC was executed. As part of this letter of intent, HHC agreed to guarantee the termination value of the Hospital's interest rate swap agreements in the event of either nonperformance by the counterparty or an election to terminate the interest rate swap agreements. In connection with the executed affiliation agreement with HHC in 2009, the original amount of the guarantee was reversed and included in the nonoperating activities in the accompanying statement of operations.

14. Functional Expenses

Windham provides short-term general health care services to acute-care patients. Hatch provides care, treatment and rehabilitation to patients convalescing from acute or chronic illness or injury. Expenses related to providing these services for the years ended September 30, 2010 and 2009, are as follows:

	<u>2010</u>	<u>2009</u>
Health care services	\$ 48,457,157	\$ 46,457,609
General and administrative	43,044,661	38,943,549
	<u>\$ 91,501,818</u>	<u>\$ 85,401,157</u>

Report of Independent Auditors on Other Financial Information

Board of Trustees
Windham Community Memorial Hospital, Inc. and Affiliates

Our audits were conducted for the purpose of forming an opinion on the combined financial statements taken as a whole. The combining details appearing in conjunction with the combined financial statements are presented for purposes of additional analysis and are not a required part of the combined financial statements of the Hospital. Such information has been subjected to the auditing procedures applied in our audits of the combined financial statements and, in our opinion, is fairly stated in all material respects in relation to the combined financial statements taken as a whole.

Ernst & Young LLP

January 20, 2011

Windham Community Memorial Hospital, Inc., and Affiliates

Combining Balance Sheets

September 30, 2010

	Windham Community Memorial Hospital, Inc.	The Hatch Hospital Corporation	Windham Hospital Foundation, Inc.	Eliminations	Combined	September 30 2009 Combined
Assets						
Current assets:						
Cash and cash equivalents	\$ 3,181,245	\$ 11,594	\$ 121,242		\$ 3,314,081	\$ 3,357,508
Current portion of assets whose use is limited	677,311	7,248			684,559	804,428
Accounts receivable, less allowances of approximately \$1,494,000	14,090,656				14,090,656	13,116,037
Other receivables	1,032,229				1,032,229	2,334,406
Due from affiliate	50,137			\$ (50,137)		
Inventories of supplies	1,175,285				1,175,285	1,175,255
Prepaid expenses	279,980		412		280,392	671,383
Pledges receivable	127,113		37,930		165,043	372,884
Funds designated for debt service	424,886				424,886	919,441
Due from third-party reimbursement agencies	1,585,717				1,585,717	1,258,523
Total current assets	22,624,559	18,842	159,584	(50,137)	22,752,848	24,009,865
Other assets:						
Investments	51,205	295,844			347,049	322,070
Assets limited as to use:						
Donor restricted investments	1,856,358	28,821			1,885,179	2,743,568
Beneficial interest in perpetual trust	2,077,581	530,224			2,607,805	1,752,149
Investments in real estate, net of accumulated depreciation of approximately \$656,000	880,317				880,317	946,499
Unamortized bond discount and issuance expense	432,208				432,208	448,118
Debt service reserve fund	1,673,374				1,673,374	1,674,179
Due from related party			32,000		32,000	
Deposits and other assets	995,386				995,386	902,998
Total other assets	7,966,429	854,889	32,000		8,853,318	8,789,581
Property, plant and equipment, net of accumulated depreciation	36,227,407	4			36,227,411	36,908,939
Total assets	\$ 66,818,395	\$ 873,735	\$ 191,584	\$ (50,137)	\$ 67,833,577	\$ 69,708,385
Liabilities and net assets						
Current liabilities:						
Trade accounts payable	\$ 3,454,752		\$ 10,455		\$ 3,465,207	\$ 3,370,047
Salaries, wages, payroll taxes and amounts withheld from employees	840,849				840,849	1,276,413
Accrued vacation and holiday pay	1,088,949				1,088,949	1,459,086
Other accrued expenses	736,752	\$ 9,800			746,552	1,033,556
Accrued pension	3,965,000				3,965,000	1,133,000
Due to affiliate			50,137	\$ (50,137)		
Current portion of long-term debt and capital lease obligation	703,485				703,485	855,910
Total current liabilities	10,789,787	9,800	60,592	(50,137)	10,810,042	9,128,012
Accrued pension and other liabilities	53,726,319				53,726,319	57,389,912
Long-term debt, less current portion	19,435,038				19,435,038	19,698,257
Interest rate swap obligation	3,185,469				3,185,469	2,585,845
Capital lease obligations, less current portion	612,432				612,432	1,077,681
Total liabilities	87,749,045	9,800	60,592	(50,137)	87,769,300	89,879,707
Net assets:						
Unrestricted	(25,515,325)	307,442	4,068		(25,203,815)	(25,502,905)
Temporarily restricted	1,385,096	26,269	126,924		1,538,289	2,104,204
Permanently restricted	3,199,579	530,224			3,729,803	3,227,379
Total net assets	(20,930,650)	863,935	130,992		(19,935,723)	(20,171,322)
Total liabilities and net assets	\$ 66,818,395	\$ 873,735	\$ 191,584	\$ (50,137)	\$ 67,833,577	\$ 69,708,385

Windham Community Memorial Hospital, Inc., and Affiliates

Combining Statements of Operations and Changes in Net Assets

Year Ended September 30, 2010

	Windham Community Memorial Hospital, Inc.	The Hatch Hospital Corporation	Windham Hospital Foundation, Inc.	Eliminations	Combined	Year Ended September 30 2009 Combined
Unrestricted operating revenues:						
Net patient revenue	\$ 84,728,827	\$ 2,213,879			\$ 86,942,706	\$ 83,605,148
Other operating revenue	2,458,138	164,526			2,622,664	2,401,877
Total operating revenue	87,186,965	2,378,405			89,565,370	86,007,025
Operating expenses:						
Salaries	38,194,606	1,002,179	\$ 104,348		39,301,133	37,098,685
Employee benefits	14,163,903	371,668	39,652		14,575,223	12,646,534
Physician fees	908,648	23,777			932,425	910,707
Consulting, legal and auditing fees	641,085	16,775			657,860	764,944
Supplies	9,196,226	240,652	465		9,437,343	9,495,592
Insurance	1,017,356	26,621			1,043,977	1,200,994
Purchased services	6,262,121	164,360	19,003		6,445,484	6,177,714
Other nonsalary expenses	7,359,322	193,007	16,592		7,568,921	6,608,688
Provision for uncollectible accounts	5,320,229	139,216			5,459,445	4,595,065
Depreciation	4,407,568	115,334			4,522,902	4,418,804
Interest	1,517,399	39,706			1,557,105	1,483,430
Total operating expenses	88,988,463	2,333,295	180,060		91,501,818	85,401,157
(Loss) income from operations	(1,801,498)	45,110	(180,060)		(1,936,448)	605,868
Gain transferred to Windham	45,110	(45,110)				
Nonoperating income (loss):						
Investment income, net	86,921	6,922	2,460		96,303	152,507
Gifts and bequests			252,482		252,482	205,897
Net realized and unrealized gains (loss) on investments	3,503	16,860	(103)		20,260	1,992
Net loss from investment in real estate	(10,352)				(10,352)	(53,022)
Other nonoperating activities	(71,456)	(13,609)			(85,065)	(2,098,246)
Total nonoperating income (loss)	8,616	10,173	254,839		273,628	(1,790,872)
(Deficiency) excess of revenues over expenses	(1,747,772)	10,173	74,779		(1,662,820)	(1,185,004)

Continued on next page.

Windham Community Memorial Hospital, Inc., and Affiliates

Combining Statements of Operations and Changes in Net Assets (continued)

	Year Ended September 30, 2010					Year Ended September 30 2009 Combined
	Windham Community Memorial Hospital, Inc.	The Hatch Hospital Corporation	Windham Hospital Foundation, Inc.	Eliminations	Combined	
Unrestricted net assets:						
Deficiency of revenues over expenses	\$ (1,747,772)	\$ 10,173	\$ 74,779		\$ (1,662,820)	\$ (1,185,004)
Change in pension funding and post retirement obligations	1,624,421				1,624,421	(33,873,622)
Net assets released from restriction for capital		10,350	229,003		239,353	11,387
Other			24,894		24,894	(13,922)
Transfer from other entity	73,242				73,242	
Transfer from temporarily restricted net assets						74,511
Transfer from (to) Foundation	376,054		(376,054)			
Increase (decrease) in unrestricted net assets	325,945	20,523	(47,378)		299,090	(34,986,650)
Temporarily restricted net assets:						
Gifts and bequests	4,430		345,882		350,312	129,238
Investment income, net	30,041	15,195			45,236	25,969
Realized gain (loss) on investments	20,492				20,492	(35,866)
Unrealized gain on investments	91,812				91,812	95,348
Transfer to unrestricted net assets						(74,511)
Transfer to permanently restricted net assets	(394,647)				(394,647)	
Net assets released from restriction for operations	(402,278)		(37,489)		(439,767)	
Net assets released from restriction for capital		(10,350)	(229,003)		(239,353)	(11,387)
(Decrease) increase in temporarily restricted net assets	(650,150)	4,845	79,390		(565,915)	128,791
Permanently restricted net assets:						
Gifts and bequests	691				691	
Investment loss, net	(1,387)				(1,387)	(4,189)
Realized loss on investments	6,210				6,210	(41,490)
Unrealized gains on investments	6,058				6,058	38,950
Transfer from temporarily restricted net assets	394,647				394,647	
Change in fair value of perpetual trust	74,013	22,192			96,205	(39,566)
Increase (decrease) in permanently restricted net assets	480,232	22,192			502,424	(46,295)
Increase (decrease) in net assets	156,027	47,560	32,012		235,599	(34,904,154)
Net assets, beginning of year	(21,086,677)	816,375	98,980		(20,171,322)	14,732,832
Net assets, end of year	\$ (20,930,650)	\$ 863,935	\$ 130,992	\$	\$ (19,935,723)	\$ (20,171,322)