

CONSOLIDATED FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

Western Connecticut Health Network, Inc. and Subsidiaries
Years Ended September 30, 2012 and 2011
with Report of Independent Auditors

Ernst & Young LLP

 **ERNST & YOUNG**

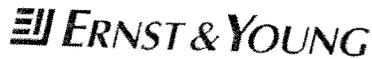
Western Connecticut Health Network, Inc. and Subsidiaries

Consolidated Financial Statements
and Supplementary Information

Years Ended September 30, 2012 and 2011

Contents

Report of Independent Auditors.....	1
Consolidated Financial Statements	
Consolidated Balance Sheets	2
Consolidated Statements of Operations and Changes in Net Assets	4
Consolidated Statements of Cash Flows.....	6
Notes to Consolidated Financial Statements.....	7
Supplementary Information	
Report of Independent Auditors on Supplementary Information	38
Consolidating Balance Sheet as of September 30, 2012.....	39
Consolidating Statement of Operations for the Year Ended September 30, 2012.....	40
Consolidating Balance Sheet as of September 30, 2011.....	41
Consolidating Statement of Operations for the Year Ended September 30, 2011.....	42



Ernst & Young LLP
Goodwin Square
225 Asylum Street
Hartford, CT 06103-1506
Tel: +1 860 247 3100
Fax: +1 860 725 6040
www.ey.com

Report of Independent Auditors

The Board of Directors
Western Connecticut Health Network, Inc.

We have audited the accompanying consolidated balance sheets of Western Connecticut Health Network, Inc. and Subsidiaries (the Network) as of September 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 financial statements are the responsibility of the Network's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of Western Connecticut Health Network Insurance Co., Ltd. (the Company), a subsidiary of The Danbury Hospital, which statements reflect total assets of 7% as of September 30, 2012 and 2011, and total revenues of 2% for the years then ended of the related consolidated totals. 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 Company, 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 Network'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 Network'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, and 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 other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Western Connecticut Health Network, Inc. and Subsidiaries at September 30, 2012 and 2011, and the consolidated results of their operations and changes in net assets and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

January 25, 2013

Western Connecticut Health Network, Inc. and Subsidiaries

Consolidated Balance Sheets

	September 30	
	2012	2011
Assets		
Current assets:		
Cash and cash equivalents	\$ 74,083,960	\$ 56,787,869
Current portion of assets limited as to use	2,100,896	2,780,279
Current portion of pledges receivable	3,008,962	1,768,111
Accounts receivable, less allowance for uncollectible accounts of approximately \$19,119,000 in 2012 and \$17,544,000 in 2011	79,495,132	74,395,713
Inventories	11,357,589	12,213,567
Prepaid expenses and other	17,443,644	16,364,779
Total current assets	187,490,183	164,310,318
Investments	185,848,424	159,792,485
Assets limited as to use:		
Funds restricted by donor	48,645,413	49,659,312
Board designated funds	8,639,352	7,461,876
Beneficial interest in trusts held by others	7,262,631	6,439,298
Construction funds	100,552,317	125,248,424
Investments in WCHNIC	59,508,868	50,837,322
Total noncurrent assets limited as to use	224,608,581	239,646,232
Other assets	14,361,331	13,551,622
Property, plant, and equipment:		
Land and land improvements	11,920,666	10,476,804
Buildings and building improvements	347,385,812	325,821,610
Equipment and other	304,269,720	291,542,729
Construction in progress (estimated cost to complete at September 30, 2012: \$122,195,000)	39,399,365	27,578,848
	702,975,563	655,419,991
Less accumulated depreciation	417,555,078	388,704,091
	285,420,485	266,715,900
Pledges receivable, less current portion	8,803,496	6,462,823
Bond issuance costs, net	4,628,949	5,779,765
Total assets	\$ 911,161,449	\$ 856,259,145

	September 30	
	2012	2011
Liabilities and net assets		
Current liabilities:		
Accounts payable	\$ 28,342,969	\$ 32,026,942
Payroll-related accruals	33,802,144	22,931,036
Due to third-party payors	12,492,073	15,337,343
Interest payable	1,624,480	1,803,683
Other accrued expenses	4,582,166	6,050,960
Current portion of long-term debt and capital lease obligations	2,050,090	3,024,773
Total current liabilities	<u>82,893,922</u>	<u>81,174,737</u>
Self-insurance liabilities	42,317,667	39,197,898
Accrued pension liabilities and other	191,481,514	133,967,350
Long-term debt and capital lease obligations, less current portion	250,593,765	253,514,718
Net assets:		
Unrestricted	277,089,185	286,369,831
Temporarily restricted	33,826,104	30,149,404
Permanently restricted	32,959,292	31,885,207
Total net assets	<u>343,874,581</u>	<u>348,404,442</u>
Total liabilities and net assets	<u>\$ 911,161,449</u>	<u>\$ 856,259,145</u>

See accompanying notes.

Western Connecticut Health Network, Inc. and Subsidiaries
Consolidated Statements of Operations and Changes in Net Assets

	Year Ended September 30	
	2012	2011
Unrestricted revenues:		
Net patient service revenue	\$ 736,921,369	\$ 720,525,178
Provision for bad debt <i>(see Note 1)</i>	24,771,952	26,465,527
Net patient service revenue less provision for bad debt	712,149,417	694,059,651
Net assets released from restriction	3,324,588	3,167,079
Other operating revenue	26,582,697	14,009,110
	742,056,702	711,235,840
Expenses:		
Salaries, benefits and fees	462,975,344	459,799,796
Supplies and other	204,378,809	199,184,231
Insurance	11,680,311	8,742,635
Depreciation and amortization	39,029,252	36,236,656
Interest	4,322,562	5,333,933
	722,386,278	709,297,251
Operating income before pension curtailment charge	19,670,424	1,938,589
Pension curtailment charge	(1,306,064)	(10,337,542)
Operating income (loss)	18,364,360	(8,398,953)
Income tax expense	501,000	1,000
Nonoperating gains (losses):		
Contributions	1,936,206	3,166,972
Investment income, net	2,445,895	9,355,429
Change in unrealized gains and losses on investments	22,674,214	(3,715,643)
Operating expenses of the New Milford Hospital Foundation, Inc. and Western Connecticut Health Network Foundation, Inc.	(2,407,222)	(3,213,974)
	24,649,093	5,592,784
Excess (deficiency) of revenues over expenses	42,512,453	(2,807,169)

Continued on next page.

Western Connecticut Health Network, Inc. and Subsidiaries

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

	Year Ended September 30	
	2012	2011
Unrestricted net assets:		
Excess (deficiency) of revenues over expenses (continued)	42,512,453	(2,807,169)
Change in fair value of interest rate swap	-	156,640
Net assets released from restrictions for property, plant and equipment	4,723,875	5,618,089
Transfer from temporarily restricted net assets	2,431,853	3,301,137
Change in pension funding obligation	(57,585,651)	44,064,249
Transfer to other entity	-	(10,213,352)
Acquisition of non-controlling interest in joint venture	(1,176,149)	-
Other	(187,027)	1,362,496
(Decrease) increase in unrestricted net assets	(9,280,646)	41,482,090
Temporarily restricted net assets:		
Contributions	7,922,288	7,333,773
Investment income, net	1,362,975	4,305,181
Change in unrealized gains and losses on investments	5,007,098	(2,596,384)
Net assets released from restriction	(3,324,588)	(3,167,079)
Net assets released from restrictions for property, plant and equipment	(4,723,875)	(5,618,089)
Transfer to unrestricted and permanently restricted net assets	(2,567,198)	(3,703,746)
Increase (decrease) in temporarily restricted net assets	3,676,700	(3,446,344)
Permanently restricted net assets:		
Increase (decrease) in beneficial interest in trusts held by others	823,333	(461,722)
Contributions	115,407	47,145
Transfer from temporarily restricted net assets	135,345	402,609
Increase (decrease) in permanently restricted net assets	1,074,085	(11,968)
(Decrease) increase in net assets	(4,529,861)	38,023,778
Net assets at beginning of year	348,404,442	310,380,664
Net assets at end of year	\$ 343,874,581	\$ 348,404,442

See accompanying notes.

Western Connecticut Health Network, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

	Year Ended September 30	
	2012	2011
Operating activities and other income		
(Decrease) increase in net assets	\$ (4,529,861)	\$ 38,023,778
Adjustments to reconcile (decrease) increase in net assets to net cash provided by operating activities and other income:		
Depreciation and amortization	39,029,252	36,236,656
Change in unrealized gains and losses on investments	(27,681,312)	6,312,027
Change in pension funding obligation	57,585,651	(44,064,249)
Change in other	187,027	(1,362,496)
Restricted contributions and investment income	(9,400,670)	(11,686,099)
Change in beneficial interest in trusts held by others	(823,333)	461,722
Provision for bad debt	24,771,952	26,465,527
Changes in operating assets and liabilities (<i>see Note 12</i>)	(28,743,341)	(8,275,809)
Net cash provided by operating activities and other income	<u>50,395,365</u>	<u>42,111,057</u>
Investing activities		
Additions to property, plant, and equipment, net	(57,733,837)	(71,526,718)
Decrease (increase) in investments, net and assets limited as to use	17,978,713	(94,212,508)
Net cash used in investing activities	<u>(39,755,124)</u>	<u>(165,739,226)</u>
Financing activities		
Change in bond issuance costs	1,150,816	(2,662,379)
Proceeds from long-term debt	39,880,000	175,105,000
Payments of long-term debt	(43,775,636)	(48,362,909)
Restricted contributions and investment income	9,400,670	11,686,099
Net cash provided by financing activities	<u>6,655,850</u>	<u>135,765,811</u>
Net increase in cash and cash equivalents	17,296,091	12,137,642
Cash and cash equivalents at beginning of year	56,787,869	44,650,227
Cash and cash equivalents at end of year	<u>\$ 74,083,960</u>	<u>\$ 56,787,869</u>

See accompanying notes.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

September 30, 2012

1. Summary of Significant Accounting Policies

Organization and Basis of Presentation

Western Connecticut Health Network, Inc. (the Network) was established under the statutes of the State of Connecticut and is the parent company of the following subsidiaries: The Danbury Hospital (Danbury Hospital); Western Connecticut Health Network Foundation, Inc. (WCHNF); Western Connecticut Health Network Affiliates, Inc. (WCHNA); Business System, Inc. (BSI); Western Connecticut Home Care, Inc. (WCHC); Regional Hospice of Western Connecticut (Hospice); the Foundation for Community Health Care (Foundation); The New Milford Hospital Inc. and Subsidiaries (New Milford Hospital) and Western Connecticut Medical Group, P.C. (WCMG).

The Network owns 100% of the capital stock of BSI. Western Connecticut Health Network, Inc. is the sole corporate member of Danbury Hospital, WCHNF, New Milford Hospital, WCHNA, and WCHC. As of December 1, 2010, the affiliation with Hospice was terminated.

The Network owned 100% of Ridgefield Surgical Center (RSC), a free-standing ambulatory surgical center located in Ridgefield, Connecticut, as of September 30, 2010. The operations of RSC became a department of Danbury Hospital in April 2011.

The Foundation is a corporation under the Nonstock Corporation Act of the State of Connecticut and requires contributions by the physician members. The Network is required to make contributions that match those made by the physician members. As of this date, no physicians have made contributions and the Foundation is currently inactive.

Danbury Hospital is a voluntary, nonprofit association incorporated under the General Statutes of the State of Connecticut, and is a wholly owned subsidiary of the Network. The Board of Danbury Hospital is appointed by the Network. The financial statements of Danbury Hospital include its wholly owned subsidiary, Western Connecticut Health Network Insurance Co., Ltd. (WCHNIC).

New Milford Hospital is a voluntary, not-for-profit, non-stock corporation established under the General Statutes of the State of Connecticut and is the sole corporate member of its subsidiaries, New Milford Hospital Foundation, Inc. and New Milford Visiting Nurse Association, Inc. (the VNA). During 2011, the affiliation with the VNA was terminated.

Effective October 28, 2009, New Milford Hospital formed a strategic partnership with Radcorp of New Milford, LLC. The partnership, New Milford MRI JV, LLC, offers MRI services located at New Milford Hospital. New Milford Hospital owned a 51% share of New Milford MRI JV, LLC with the remaining 49% owned by Radcorp of New Milford, LLC. In 2012,

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

New Milford Hospital purchased Radcorp of New Milford, LLC's ownership share and New Milford MRI JV, LLC became a department of New Milford Hospital. Prior to the acquisition of the remaining ownership interest, the partnership's capital accounts were in a deficit position.

WCMG is established under the general statutes of the State of Connecticut and provides physician services to patients primarily from Western Connecticut and Southeastern New York. WCMG also provides physician support to various Network affiliates.

The consolidated financial statements include the accounts of Western Connecticut Health Network, Inc., Danbury Hospital, WCHNF, New Milford Hospital, WCHNA, BSI, WCHC, WCMG, and Foundation. All material intercompany transactions have been eliminated in consolidation.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and related footnotes. 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.

Regulatory Matters

The Network is required to file annual operating information with the State of Connecticut Office of Health Care Access.

Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with maturities of three months or less at date of purchase other than amounts held in the investment portfolio and assets limited as to use. Cash and cash equivalents are maintained with domestic financial institutions with deposits that exceed federally insured limits. It is the Network's policy to monitor the financial strength of these institutions.

Investments

The Network's investment portfolio reported in the accompanying consolidated balance sheets is designated as trading, with realized and unrealized gains and losses included in the excess (deficiency) of revenues over expenses.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Investments in equity securities with readily determinable fair values and all investments in debt securities are recorded at fair value, based upon quoted market prices, on the consolidated balance sheets. Investment income or loss (including realized and unrealized gains and losses on investments, interest and dividends) is included in the excess (deficiency) of revenues over expenses unless the income or loss is restricted by donor or by law.

Alternative investments (nontraditional, not-readily-marketable assets), some of which are structured such that the Network holds limited partnership interests, are reported based upon net asset value and derived from the application of the equity method of accounting. Individual investment holdings within the alternative investments may, in turn, include investments in both nonmarketable and market-traded securities. Valuations of these investments and, therefore, the Network's holdings, may be determined by the investment manager or general partner, and for "fund of funds" investments are primarily based on financial data supplied by the underlying investee funds. Values may be based on historical cost, appraisals, or other estimates that require varying degrees of judgment. The Network accounts for these investments using the equity method of accounting, except for investments held by the defined benefit pension plan, and reports its share of the increase or decrease in the funds value as investment gain or loss. Alternative investments held by the defined benefit pension plan are held at fair value as estimated in an unquoted market. The financial statements of the investees are audited annually by independent auditors, although the timing for reporting the results of such audits does not coincide with the Network's annual consolidated financial statement reporting.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the Network has been limited by donors to a specific time frame or purpose. Temporarily restricted net assets primarily consist of contributions restricted for certain healthcare services. Permanently restricted net assets, which are primarily endowment gifts and assets held in trusts by others, have been restricted by donors, and are to be maintained in perpetuity.

Contributions

For financial statement purposes, the Network distinguishes between contributions of unrestricted assets, temporarily restricted assets, and permanently restricted assets.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Contributions for which donors have not stipulated restrictions, as well as contributions for which donors have stipulated restrictions, but which are met within the same reporting period, are reported as unrestricted support. Contributions, for which donors have imposed restrictions which limit the use of the donated assets, are reported as temporarily restricted net assets if the restrictions are not met in the same reporting period. When such donor imposed restrictions are met in subsequent reporting periods, temporarily restricted net assets are reclassified to unrestricted net assets and reported as net assets released from restrictions. Contributions of assets which donors have stipulated must be maintained in perpetuity, with only the income earned thereon available for current use, are classified as permanently restricted net assets.

Patient Accounts Receivable

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

The Network's estimation of the allowance for uncollectible accounts is based primarily upon the type and age of the patient accounts receivable and the effectiveness of the Network's collection efforts. The Network's policy is to reserve a portion of all self-pay receivables, including amounts due from the uninsured and amounts related to co-payments and deductibles, as these charges are recorded. On a monthly basis, the Hospital reviews its accounts receivable balances and various analytics to support the basis for its estimates. These efforts primarily consist of reviewing the following:

- Historical write-off and collection experience using a hindsight or look-back approach;
- Revenue and volume trends by payor, particularly the self-pay components;
- Changes in the aging and payor mix of accounts receivable, including increased focus on accounts due from the uninsured and accounts that represent co-payments and deductibles due from patients;
- Cash collections as a percentage of net patient revenue less the provision for bad debt; and
- Trending of days revenue in accounts receivable

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

The Network regularly performs hindsight procedures to evaluate historical write-off and collection experience throughout the year to assist in determining the reasonableness of its process for estimating the allowance for uncollectible accounts.

The Network's primary concentration of credit risk is patient accounts receivable, which consists of amounts owed by various governmental agencies, insurance companies and private patients. The Network manages the receivables by regularly reviewing its patient accounts and contracts, and by providing appropriate allowances for uncollectible amounts. Significant concentrations of gross patient accounts receivable include 42% and 11%, and 43% and 10%, for Medicare and Medicaid, respectively, at September 30, 2012 and 2011, respectively.

Assets Limited as to Use

Assets limited as to use represent investments with donor restrictions; assets set aside by the Board of Directors for the purpose of providing for future improvement, expansion and replacement of plant and equipment; assets held by trustees under indenture agreements related to financing activities with the State of Connecticut Health and Educational Facilities Authority (CHEFA); assets held in trusts by others in accordance with donor restrictions; cash designated for the Supplemental Executive Retirement Plans; and donated land held for sale; and investments held by WCHNIC. Board designated funds represent unrestricted funds set aside for specific purposes. Assets limited as to use are reported at fair value based upon quoted market prices. The portion of amounts required for funding current liabilities is included in current assets.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. The Network provides for depreciation of property, plant and equipment using the straight-line method in amounts sufficient to depreciate the cost of the assets over their estimated useful lives.

Conditional asset retirement obligations amounted to \$396,262 and \$464,904 as of September 30, 2012 and 2011, respectively. These obligations are recorded in other long-term liabilities in the accompanying consolidated balance sheets. There are no assets that are legally restricted for purposes of settling asset retirement obligations. During 2012 and 2011, retirement obligations incurred and settled were minimal.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Bond Issuance Costs

Discounts and deferred costs related to the issuance of bonds are amortized over the period the obligation is outstanding, using the bonds outstanding method. Accumulated amortization of discounts and deferred costs were \$1,569,849 and \$1,347,238 at September 30, 2012 and 2011, respectively.

Inventories

Danbury Hospital uses the first in, first out method, in the valuation of its inventory. Inventories, used in general operations of New Milford Hospital, are stated at average cost.

Nonoperating Gains (Losses)

Activities, other than in connection with providing health care services, are considered to be nonoperating. Nonoperating gains (losses) primarily consist of contributions, income on invested funds, realized and unrealized gains and losses on investments, and the operating expenses of the WCHNF and the New Milford Hospital Foundation.

Excess (Deficiency) of Revenues Over Expenses

The consolidated statements of operations and changes in net assets include excess (deficiency) of revenues over expenses as the performance indicator. Changes in unrestricted net assets, which are excluded from excess (deficiency) of revenues over expenses, include permanent transfers of assets for other than goods and services, contributions of long-lived assets, changes in pension funding obligation, changes in the fair value of interest rate swap, transfer to another entity in connection with the disaffiliation of the New Milford Hospital VNA and Hospice in fiscal year 2011, and the acquisition of non-controlling interest in joint venture in fiscal year 2012.

Transactions deemed by management to be ongoing, major or central to the provision of health care services are reported within income from operations.

Fair Value of Financial Instruments

The carrying value of financial instruments classified as current assets and current liabilities as of September 30, 2012 and 2011 approximate fair value based on current market conditions. The fair values of the Network's financial instruments are disclosed in the respective notes and/or in Note 4.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Investments include certificates of deposit with original maturities in excess of three months.

Income Taxes

The Network comprises not-for-profit corporations as described in 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 Network is also exempt from state and local taxes. WCHNIC, a subsidiary of Danbury Hospital, is a foreign corporation exempt from US taxation and is not subject to taxes under the Cayman Islands tax concessions law.

At September 30, 2012, the Network has losses from unrelated business activities of approximately \$39,784,000 which began expiring in 2009. A deferred tax asset for these losses of approximately \$15,914,000 is offset by a corresponding valuation allowance of the same amount due to the uncertainty of utilizing the deferred tax asset in future periods. The Network also has a net operating loss carryforward of approximately \$454,000 related to BSI and a 2012 tax liability of approximately \$500,000 for federal and state taxes.

Adoption of New Accounting Standards

In August 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-23, *Measuring Charity Care for Disclosure*. The new guidance requires that the level of charity care provided be presented based on the direct and indirect costs of the charity services provided. Separate disclosure of the amount of any cash reimbursements received for providing charity care must also be disclosed. The new disclosure requirements became effective for the Network on October 1, 2011 and are included in the accompanying consolidated financial statements for all periods presented (see Note 2).

In July 2011, the FASB issued ASU No. 2011-07, *Presentation and Disclosure of Patient Service Revenue Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*. The new guidance requires the Network to change the presentation of its statement of operations by reclassifying the provision for bad debt associated with patient service revenue (net of contractual allowances and discounts) from an operating expense to a deduction from patient service revenue. Additionally, the Network is required to provide enhanced disclosures about its policies for recognizing revenue and assessing bad debts, as well as qualitative and quantitative information about changes in the allowance for uncollectible accounts. The new guidance was adopted by the Network as of and for the year ended September 30, 2012 and retrospectively applied the presentation requirements for the year ended September 30, 2011.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

In August 2010, the FASB issued ASU No. 2010-24, *Health Care Entities (Topic 954): Presentation of Insurance Claims and Recoveries*, which provides clarification to companies in the health care industry on the accounting for professional liability and similar insurance. ASU 2010-24 states that insurance liabilities should not be presented net of insurance recoveries and that an insurance receivable should be recognized on the same basis as the liabilities, subject to the need for a valuation allowance for uncollectible accounts. ASU 2010-24 is effective for fiscal years beginning after December 15, 2010 and was adopted by the Network during 2012. The adoption of this standard increased other assets by \$475,000 and accrued pension liabilities and other by \$475,000 in the consolidated balance sheet as of September 30, 2012 as compared to September 30, 2011.

Reclassifications

Certain reclassifications have been made to the year ended September 30, 2011 balances previously reported in the consolidated balance sheets and consolidated statements of operations and changes in net assets in order to conform with the year ended September 30, 2012 presentation.

2. Net Patient Service Revenue and Charity Care

The following table summarizes net patient service revenue:

	Year Ended September 30	
	2012	2011
Gross patient service revenue	\$ 1,649,794,278	\$ 1,620,897,693
Deductions:		
Allowances	895,739,602	884,704,840
Charity care (at charges)	17,133,307	15,667,675
Net patient service revenue	912,872,909	900,372,515
Provision for bad debt	736,921,369	720,525,178
Net patient service revenue less provision for bad debt	24,771,952	26,465,527
	\$ 712,149,417	\$ 694,059,651

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

2. Net Patient Service Revenue and Charity Care (continued)

During 2012 and 2011, approximately 37% of net patient service revenue was received under the Medicare and Medicaid programs. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. 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. The Network believes it is in compliance with all applicable laws and regulations. Changes in the Medicare and Medicaid programs and the reduction of funding levels could have an adverse impact on the Network.

The Network has agreements with third-party payors that provide for payments 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 ongoing and 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 2012 and 2011, the Network recorded increases in net patient service revenue of approximately \$8,375,000 and \$2,300,000, respectively, related to changes in previously estimated third-party payor settlements.

The Network 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 Network specific data. Such amounts are included in the accompanying consolidated balance sheets.

Patient service revenue, net of contractual allowances and before the provision for bad debts, recognized in the period from major payor sources for the year ended September 30, 2012, is as follows:

Third-party payors	\$ 708,178,306
Self-pay patients	45,876,370
	<u>\$ 754,054,676</u>

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

2. Net Patient Service Revenue and Charity Care (continued)

It is the policy of the Network to provide necessary care to all persons seeking treatment without discrimination on the grounds of age, race, creed, national origin, or any other grounds unrelated to an individual's need for the service or the availability of the needed service at the Network. A patient is classified as a charity care patient by reference to established policies of the Network. Essentially, these policies define charity services as those services for which no payment is anticipated. In assessing a patient's inability to pay, the Network utilizes the generally recognized federal poverty income guidelines, but also includes certain cases where incurred charges are significant when compared to a responsible party's income. These charges are not included in net patient service revenues for financial reporting purposes.

The estimated cost of charity care provided was approximately \$7,962,000 and \$7,029,000 for the years ended September 30, 2012 and 2011, respectively. The estimated cost of charity care is based on the ratio of cost to charges, as determined by Network specific data.

3. Investments and Assets Limited as to Use

The composition of investments and assets limited as to use is set forth in the following table:

	September 30	
	2012	2011
Cash and cash equivalents	\$ 103,851,929	\$ 131,767,669
Common collective funds	104,698,546	86,113,308
Fixed income securities	57,471,300	51,993,062
Mutual funds	109,736,400	105,355,048
Commodities	1,076,854	533,890
Alternative investments (at equity method)	27,260,241	18,816,721
	<u>\$ 404,095,270</u>	<u>\$ 394,579,698</u>

Also included within assets limited as to use is \$1,200,000 of land held for sale as of September 30, 2012 and 2011 and trusts held by others of \$7,262,631 and \$6,439,298 as of September 30, 2012 and 2011, respectively.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

3. Investments and Assets Limited as to Use (continued)

Investment income included in non-operating gains (losses) for the year ended September 30, 2012 and 2011 consists of:

	<u>2012</u>	<u>2011</u>
Interest and dividend income	\$ 2,482,343	\$ 5,401,831
Realized gains and losses, net and equity income on alternative investments	<u>(36,448)</u>	<u>3,953,598</u>
	<u>\$ 2,445,895</u>	<u>\$ 9,355,429</u>

4. Fair Values of Financial Instruments

For assets and liabilities required to be measured at fair value, the Network measures fair value 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. Fair value measurements are applied based on the unit of account from the Network's perspective. The unit of account determines what is being measured by reference to the level at which the asset or liability is aggregated (or disaggregated) for purposes of applying other accounting pronouncements.

The Network follows a valuation hierarchy that is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

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 that 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 Network uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible and considers nonperformance risk in its assessment of fair value.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

4. Fair Values of Financial Instruments (continued)

Financial assets carried at fair value in the accompanying consolidated balance sheets, excluding assets invested in the Network's defined benefit pension plan, are classified in the table below in one of the three categories described above:

	September 30, 2012			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$ 74,083,960	\$ -	\$ -	\$ 74,083,960
Investments and assets limited as to use:				
Cash and cash equivalents	103,851,929	-	-	103,851,929
Mutual funds:				
Fixed income	109,736,400	-	-	109,736,400
Common collective funds:				
Domestic equity	-	71,269,667	-	71,269,667
International equity	-	30,705,225	-	30,705,225
Other	-	2,723,654	-	2,723,654
Securities:				
Fixed income	40,496,405	16,974,895	-	57,471,300
Real estate/commodities	-	1,076,854	-	1,076,854
Beneficial interest in trusts held by others:				
Cash and cash equivalents	337,967	-	-	337,967
Mutual funds:				
Domestic equity	964,503	-	-	964,503
International equity	399,466	-	-	399,466
Fixed income	882,911	-	-	882,911
Common collective funds:				
Domestic equity	-	1,824,408	-	1,824,408
International equity	-	668,411	-	668,411
Fixed income	-	948,416	-	948,416
Corporate and foreign bonds	-	10,019	-	10,019
Real estate/commodities	-	626,718	-	626,718
Other	-	599,812	-	599,812
	\$ 330,753,541	\$ 127,428,079	\$ -	\$ 458,181,620

Western Connecticut Health Network, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

4. Fair Values of Financial Instruments (continued)

	September 30, 2011			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$ 56,787,869	\$ -	\$ -	\$ 56,787,869
Investments and assets limited as to use:				
Cash and cash equivalents	131,767,974	-	-	131,767,974
Mutual funds:	-	-	-	-
Fixed income	105,355,048	-	-	105,355,048
Common collective funds:				
Domestic equity	-	57,538,708	-	57,538,708
International equity	-	19,429,089	-	19,429,089
Other	-	9,145,511	-	9,145,511
Securities:				
Fixed income	27,264,022	24,729,040	-	51,993,062
Real estate/commodities	-	533,890	-	533,890
Beneficial interest in trusts held by others:				
Cash and cash equivalents	129,233	-	-	129,233
Mutual funds:				
Domestic equity	2,436,708	-	-	2,436,708
International equity	846,776	-	-	846,776
Fixed income	1,914,353	-	-	1,914,353
Other	295,190	-	-	295,190
Common collective funds:				
Domestic equity	-	331,012	-	331,012
International equity	-	115,745	-	115,745
Fixed income	-	202,723	-	202,723
Real estate/commodities	-	141,297	-	141,297
Other	-	26,260	-	26,260
	<u>\$ 326,797,173</u>	<u>\$ 112,193,275</u>	<u>\$ -</u>	<u>\$ 438,990,448</u>

The amounts reported in the tables above do not include alternative investments totaling \$27,260,241 and \$18,816,721 as of September 30, 2012 and 2011, respectively, that are accounted for under the equity method of accounting.

The above tables do not include \$1,200,000 of land held for sale as of September 30, 2012 and 2011, respectively, included within the current portion of assets limited as to use.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

4. Fair Values of Financial Instruments (continued)

Financial assets carried at fair value included in the defined benefit pension plans are classified in the table below in one of the three categories described above:

	September 30, 2012			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$1,147,463	\$ -	\$ -	\$ 1,147,463
Mutual funds:				
Domestic equity	21,149,836	-	-	21,149,836
International equity	2,710,892	-	-	2,710,892
Fixed income	149,169,151	-	-	149,169,151
Other	2,713,995	-	-	2,713,995
Common collective funds:				
Domestic equity	-	160,036,331	-	160,036,331
International equity	-	40,913,821	-	40,913,821
Alternative investments	-	-	52,676,206	52,676,206
	<u>\$176,891,337</u>	<u>\$ 200,950,152</u>	<u>\$ 52,676,206</u>	<u>\$ 430,517,695</u>
	September 30, 2011			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$4,008,665	\$ -	\$ -	\$ 4,008,665
Mutual funds:				
Domestic equity	12,600,394	-	-	12,600,394
Fixed income	145,650,859	-	-	145,650,859
International equity	1,995,582	-	-	1,995,582
Other	2,085,655	-	-	2,085,655
Common collective funds:				
Domestic equity	-	110,465,006	-	110,465,006
International equity	-	49,180,804	-	49,180,804
Alternative investments	-	-	27,947,917	27,947,917
	<u>\$166,341,155</u>	<u>\$ 159,645,810</u>	<u>\$ 27,947,917</u>	<u>\$ 353,934,882</u>

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

4. Fair Values of Financial Instruments (continued)

Fair value for Level 1 assets is based upon quoted market prices. Fair value for Level 2 assets is based upon model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Inputs are obtained from various sources including market participants, dealers and brokers. Level 3 assets consist of alternative investments held by the defined benefit plans, the valuation for which is described in Note 1. Many of the investments classified in Levels 2 and 3 in the above tables consist of shares or units in investment funds, as opposed to direct interests in the funds' underlying holdings, which may be marketable. As the net asset value reported by each fund is used as a practical expedient to estimate the fair value of the Network's interest therein, its classification in Level 2 or 3 is based on the Network's ability to redeem its interest at or near the measurement date. If the interest can be redeemed in the near term, the investment is classified in Level 2. The methods described above may produce a fair value that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Network believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

For the year ended September 30, 2012, the changes in the fair value of assets measured using significant unobservable inputs (Level 3) comprised the following:

Beginning balance at October 1, 2011	\$ 27,947,917
Change in unrealized gains and losses	1,271,312
Realized gains	-
Purchases	23,456,977
Sales	-
Ending balance at September 30, 2012	<u>\$ 52,676,206</u>

For the year ended September 30, 2011, the changes in the fair value of assets measured using significant unobservable inputs (Level 3) were comprised of the following:

Beginning balance at October 1, 2010	\$ 27,989,880
Change in unrealized gains and losses	1,988,325
Realized gains	99,652
Purchases	13,000,000
Sales	(15,129,940)
Ending balance at September 30, 2011	<u>\$ 27,947,917</u>

Western Connecticut Health Network, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

5. Pledges Receivable

Pledges receivable include the following unconditional promises to give:

	September 30	
	2012	2011
Due within one year	\$ 3,142,311	\$ 2,100,559
Due within one to five years	9,626,656	7,506,255
Due within greater than five years	133,375	214,386
	12,902,342	9,821,200
Allowance and discount for uncollectible pledges	(1,089,884)	(1,590,266)
Present value of pledges receivable	\$ 11,812,458	\$ 8,230,934

The allowance recognizes the estimated uncollectible portion of pledges and the discount of pledges to net present value. Pledges are discounted using an average rate of 3% as of September 30, 2012 and 2011.

6. Long-Term Debt and Credit Facility

Long-term debt consisted of the following:

	September 30	
	2012	2011
Danbury Hospital revenue bonds financed with CHEFA:		
Series G	\$ -	\$ 39,700,000
Series H	39,615,000	41,560,000
Network revenue bonds financed with CHEFA:		
Series K	29,610,000	31,325,000
Series L	96,000,000	96,000,000
Series M	46,030,000	46,030,000
Series N	39,880,000	-
New Milford Hospital term loans	466,426	607,285
New Milford Hospital capital lease obligations	1,042,429	1,317,206
	252,643,855	256,539,491
Less current portion	2,050,090	3,024,773
	\$ 250,593,765	\$ 253,514,718

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt and Credit Facility (continued)

The following is a summary of the combined aggregate amount of maturities and sinking fund requirements of the aforementioned obligations at September 30, 2012 according to their long-term amortization schedule:

2013	\$ 2,050,090
2014	3,401,009
2015	5,415,495
2016	5,487,261
2017	5,700,000
Thereafter	<u>230,590,000</u>
	<u>\$ 252,643,855</u>

The fair value of the revenue bonds, as determined by the Network's investment advisor using a discount cash flow analysis, was approximately \$263,780,000 and \$248,699,000 at September 30, 2012 and 2011, respectively. The carrying value of all remaining long-term debt approximates fair value. The Network paid interest of \$8,373,470 and \$4,970,685 in 2012 and 2011, respectively. The Network has capitalized interest of approximately \$3,746,000 and \$863,000 in 2012 and 2011, respectively. Debt service funds held under bond indenture agreements for Series G Bonds, Series H Bonds and Series N Bonds were \$900,896 and \$1,273,013 at September 30, 2012 and 2011, respectively.

The Series G revenue bonds (Series G Bonds) were scheduled to mature from 2012 through 2029 at an average coupon rate of 5.63%. The proceeds of the Series G Bonds were used to construct a new Cancer Center and reimburse the Network for equipment purchases made during fiscal year 1999. The scheduled payment of principal and interest on the Series G Bonds was guaranteed by an insurance policy issued by a commercial insurer. In November 2011, the Series G Bonds were refunded by Western Connecticut Health Network Issue, Series N CHEFA revenue bonds (Series N Bonds).

The Series H revenue bonds (Series H Bonds) mature from 2030 through 2036 at an average coupon rate of 4.425%. The proceeds of the Series H Bonds were used for the construction, renovation and equipping of an outpatient diagnostic building with approximately 28,000 square feet of medical office space, a 381-space parking garage, a 264-space surface parking lot and to fund capitalized interest. The scheduled payment of principal and interest on the Series H Bonds when due is guaranteed by an insurance policy issued by a commercial insurer.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt and Credit Facility (continued)

Under the terms of the Series H Bonds financing arrangements between Danbury Hospital and the Western Connecticut Health Network Foundation, Inc. (the Obligated Group) and CHEFA, the proceeds of the revenue bonds were loaned to Danbury Hospital. Danbury Hospital is obligated to provide amounts sufficient to pay the principal and interest due on the Series H Bonds. The Master Indentures and Supplemental Master Indentures provide for the potential establishment and maintenance of a Debt Service Reserve Fund and a pledge of gross receipts, as defined. The Master Indentures also establish a debt service coverage ratio requirement and restricts the incurrence of certain indebtedness by the Obligated Group. No violations of financial covenants existed as of September 30, 2012 and 2011.

In 2011, the Network issued three series of bonds. The Obligated Group was expanded to also include Western Connecticut Health Network, Inc., New Milford Hospital, New Milford Hospital Foundation, Inc. and Western Connecticut Medical Group, P.C. All proceeds from the bonds were used to finance Danbury Hospital capital projects. All members of the Obligated Group are jointly and severally liable under the Master Indenture to make all payments required with respect to obligations under the Master Indenture. The bonds are reflected as intercompany debt in the schedule above and include:

The Series K revenue bonds (Series K Bonds) were issued in the amount of \$33,035,000. The Series K Bonds bear interest at the bank purchase rate (1.446% and 1.972% at September 30, 2012 and 2011, respectively) and mature serially from September 30, 2011 to September 30, 2036.

The Series M revenue bonds (Series M Bonds) were issued in the aggregate principle of \$46,030,000, with interest payable initially on January 1, 2012 and semiannually on each January 1 and July 1 thereafter. The Series M Bonds bear interest at rates ranging from 5.000% to 5.375% and are scheduled to mature from July 1, 2031 to July 1, 2041. The Series M Bonds are also subject to annual sinking fund installments commencing in 2024 through scheduled maturity. The Series L Revenue Bonds (Series L Bonds) of \$96,000,000 were issued concurrently with Series M Bonds and are subject to annual sinking fund installments commencing July 1, 2015 and continuing through final maturity on July 1, 2041. The Series L Bonds bear interest at the bank purchase rate (1.355% and 1.348% at September 30, 2012 and 2011, respectively). The proceeds of the Series L Bonds and Series M Bonds are being used for funding the planning, design, acquisition, construction, equipping and furnishing of Danbury Hospital's new patient tower, expansion of a parking garage, capital improvements and to fund capitalized interest.

Western Connecticut Health Network, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt and Credit Facility (continued)

In 2012, Western Connecticut Health Network, Inc. issued Series N Bonds in the amount of \$39,880,000 and bear interest at rates between 3% and 5%. The Series N Bonds mature serially from July 1, 2014 to July 1, 2029. The proceeds of the Series N Bonds were used to refund Danbury Hospital's Series G Bonds.

On June 11, 2010, New Milford Hospital entered into a leasing agreement with First Litchfield Leasing Corporation to lease a 64-slice CT Scanner in the amount of \$1,008,023. Lease payments of \$56,993 are due quarterly beginning July 1, 2010 through April 1, 2015, at which point New Milford Hospital has the option to purchase the machine for \$1. The equipment lease agreement bears interest at 1.33%. The outstanding balance of the capital lease obligation was \$579,539 and \$820,498 as of September 30, 2012 and 2011, respectively.

On October 7, 2010, New Milford Hospital entered into a leasing agreement with First Litchfield Leasing Corporation to lease a medical linear accelerator in the amount of \$722,405. Lease payments of \$40,845 are due quarterly beginning November 1, 2010 through August 1, 2015, at which point New Milford Hospital has the option to purchase the machine for \$1. The equipment lease agreement bears interest at 1.33% quarterly. The outstanding balance of the capital lease obligation was \$450,173 and \$479,893 as of September 30, 2012 and 2011, respectively.

On June 9, 2010, New Milford MRI JV, LLC entered into a loan agreement with Siemens Financial Services, Inc. in the amount of \$700,000 to help finance the construction and legal costs associated with the joint venture MRI project. Principal and interest are paid monthly in the amount of \$13,092 beginning in October 2010 through October 2015. The loan agreement bears interest at 4.63%. The outstanding balance as of September 30, 2012 and 2011 was \$439,239 and \$572,631, respectively. Substantially, all assets owned by New Milford Hospital are pledged as collateral for the term loans.

7. Commitments and Contingencies

Malpractice claims have been asserted against the Network by various claimants. The claims are in various stages of processing and some may ultimately be brought to trial. In addition, the Network is a party to various lawsuits incidental to its business. Management believes that the claims and lawsuits will not have a material adverse effect on the Network's financial position.

The Network has entered into several lease agreements for real estate and equipment. Certain of these leases have renewal options for periods up to five years and escalation clauses. Rent is payable in equal monthly installments. Rent expense was \$14,614,302 and \$11,867,542 for the years ended September 30, 2012 and 2011, respectively.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

7. Commitments and Contingencies (continued)

The future minimum lease payments for the years ending September 30 are as follows:

2013	\$ 15,105,340
2014	12,456,186
2015	11,359,488
2016	10,627,945
2017	10,392,437
Thereafter	28,000,897
	<u>\$ 87,942,293</u>

8. Pension Plans

The Network has two defined benefit pension plans, for which plan benefits are based on years of service and the employee's compensation (collectively referred to as the Plans). Effective May 26, 2011, the Board of Directors adopted a resolution to freeze the Network's retirement plan (the Network Plan) for non-union employees effective December 31, 2011 with certain employees continuing to accrue benefits based on age and vesting. Effective September 7, 2012, the Board of Directors adopted a second resolution to freeze benefits for all of those that had been continuing to accrue. As a result of these resolutions, the Plan liabilities were re-measured for all employees and non-union employees as of September 30, 2012 and 2011, respectively. All outstanding prior service cost related to these employees totaling \$1,306,064 and \$10,337,542 for the years ended September 30, 2012 and 2011, respectively, were expensed as of the date of the re-measurement. The curtailment charges are included in the consolidated statement of operations and changes in net assets. The New Milford Hospital retirement plan was frozen effective January 31, 2010.

Contributions to the Plans' are intended to provide for benefits attributed to services rendered to date. The Network makes contributions in amounts sufficient to meet the required benefits to be paid to the Plans' participants as they become due as required by the Employee Retirement Income Security Act of 1974.

The Network established defined contribution pension plans for all eligible employees after freezing the Plans'. Pension expense related to the defined contribution plans for the years ended September 30, 2012 and 2011 was \$9,346,756 and \$1,777,328, respectively.

The Network also maintains noncontributory, supplemental defined-benefit retirement plans (Supplemental Plans) for certain executive employees. As of September 30, 2012 and 2011, the projected benefit obligation for the Supplemental Plans amounted to \$2,057,976 and \$1,115,988,

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

8. Pension Plans (continued)

respectively, which was included in accrued pension liabilities and other in the accompanying consolidated balance sheets. The expenses incurred related to the Supplemental Plans amounted to \$1,154,096 and \$671,711 for the years ended September 30, 2012 and 2011, respectively. Effective October 1, 2009, the New Milford Hospital Supplemental Plan was frozen. Provisions have been made to “grandfather” those participants in the plan that are sixty years old and have at least ten years of service.

Included in unrestricted net assets at September 30, 2012 and 2011, are the following amounts that have not yet been recognized in net periodic pension cost: Unrecognized actuarial loss of \$203,177,545 and \$145,591,894, respectively. The actuarial loss included in unrestricted net assets at September 30, 2012 and expected to be recognized in net periodic pension cost during the year ending September 30, 2013 is \$5,847,217.

The following table presents a reconciliation of the beginning and ending balances of the Plans’ projected benefit obligation and the fair value of plan assets, as well as the funded status of the plans and accrued pension cost included in the consolidated balance sheets:

	September 30	
	2012	2011
Change in benefit obligation		
Benefit obligation at beginning of year	\$ (460,152,661)	\$ (470,711,462)
Service cost	(9,231,340)	(16,813,970)
Assumption changes	(12,459,379)	64,119
Interest cost	(25,752,057)	(26,762,028)
Benefits paid	12,999,925	11,613,929
Curtailement	14,244,269	31,748,565
Actuarial (loss) gain	(112,216,729)	10,708,186
Benefit obligation at end of year	<u>(592,567,972)</u>	<u>(460,152,661)</u>
Change in plan assets		
Fair value of plan assets at beginning of year	353,934,882	335,635,988
Contributions	27,300,905	24,873,882
Actual return on plan assets	62,281,833	5,038,941
Benefits paid	(12,999,925)	(11,613,929)
Fair value of plan assets at end of year	<u>430,517,695</u>	<u>353,934,882</u>
Underfunded status of the plans	<u>\$ (162,050,277)</u>	<u>\$ (106,217,779)</u>

Western Connecticut Health Network, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

8. Pension Plans (continued)

Components of net periodic benefit cost	Year Ended September 30	
	2012	2011
Service cost	\$ 9,231,340	\$ 16,813,970
Interest cost	25,752,057	26,762,028
Expected return on plan assets	(28,785,560)	(27,190,423)
Net amortization and deferral	16,029,912	10,546,672
Recognized net loss	1,544,439	1,444,829
Curtailment costs	1,306,064	10,337,542
Prior service cost	469,500	1,365,818
Benefit cost	<u>\$ 25,547,752</u>	<u>\$ 40,080,436</u>

The assumptions used to develop net periodic benefit cost and the projected benefit obligation for the Plans are as follows:

	September 30	
	2012	2011
Discount rate used for net periodic benefit cost	5.56-5.58%	5.55%
Discount rate used for projected benefit obligation	4.12-4.23%	5.56 – 5.58%
Expected long-term rate of return on plan assets	8.00%	8.00%
Average rate of increase in compensation	3.00%	3.00 – 3.50%

To develop the expected long-term rate of return on plan assets assumption, the Network considered the historical return and the future expectations for returns for each asset class, as well as the target asset allocation of the pension portfolio.

The accumulated benefit obligation for the Plans at September 30, 2012 and 2011 was \$590,724,718 and \$446,972,234, respectively.

Plan Assets

The Plans' investment objectives are to achieve long-term growth in excess of long-term inflation and to provide a rate of return that meets or exceeds the actuarial expected long-term rate of return on plan assets over a long-term time horizon. In order to minimize the risk, the Plans aim to minimize the variability in yearly returns. The Plans also aim to diversify holdings among sectors, industries, and companies. The target allocations for the Network Plan assets are 50% in equities, 35% in fixed income securities and 15% in alternative investments. The assets of the New Milford Hospital's plan are all held in mutual funds.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

8. Pension Plans (continued)

The weighted average asset allocations for the Plans' assets by category are as follows:

<u>Asset Category</u>	<u>September 30</u>	
	<u>2012</u>	<u>2011</u>
Equity securities	52%	51%
Debt securities	35	39
Other investments	13	10
	<u>100%</u>	<u>100%</u>

As discussed in the Fair Value Measurements note (Note 4), the Network follows a three-level hierarchy to categorize assets measured at fair value. In accordance with this hierarchy, as of September 30, 2012, 41%, 47% and 12% of the Plans' assets which are measured at fair value on a recurring basis were categorized as Level 1, Level 2 and Level 3 investments, respectively.

Contributions

The Network expects to contribute \$26,940,000 to its plans in fiscal year 2013.

Estimated Future Benefit Payments

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

<u>Fiscal Year</u>	<u>Pension Benefits</u>
2013	\$ 17,606,151
2014	19,646,289
2015	21,579,753
2016	23,352,151
2017	25,192,249
Years 2018 – 2022	155,459,954

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

9. Professional Liability Insurance

Effective October 1, 2004, the Network formed a captive insurance company, Western Connecticut Health Network Insurance Co., Ltd. (WCHNIC). WCHNIC is domiciled in the Cayman Islands and provides alternative professional liability insurance to the Network, as well as providing community doctors with a competitive professional liability insurance option.

Coverage for medical malpractice insurance is on a claims-made basis. The coverage limits are \$5,000,000 per claim and \$25,000,000 in the aggregate. The excess indemnity coverage is \$25,000,000 per claim and \$25,000,000 in the aggregate. Professional liability for New Milford Hospital was also provided under claims-made policies. The Network has recorded a liability of \$10,488,898 and \$9,111,700 at September 30, 2012 and 2011, respectively, based on discount rates ranging from 3.0 –3.5% as of September 30, 2012 and 2011, for incurred-but-not-reported claims, which is included in accrued pension liabilities and other on the accompanying consolidated balance sheets.

Assets held by WCHNIC approximate \$65,788,000 and \$56,572,000 as of September 30, 2012 and 2011, respectively, of which a majority is reflected as assets limited as to use in the accompanying consolidated balance sheets. Total liabilities recorded by WCHNIC approximate \$42,543,000 and \$39,372,000 as of September 30, 2012 and 2011, respectively, of which a majority is reflected as self-insurance liabilities in the accompanying consolidated balance sheets.

The reserve for losses and loss adjustment expenses for WCHNIC are included in self-insurance liabilities in the accompanying consolidated balance sheets. Activity in the reserve for losses and loss adjustment expenses for the years ended September 30, 2012 and 2011 is summarized as follows:

	<u>2012</u>	<u>2011</u>
Balance at the beginning of period	\$ 35,675,566	\$ 32,294,365
Incurred related to:		
Current period	7,922,650	8,782,963
Prior period	960,245	(2,689,921)
Total incurred	<u>8,882,895</u>	<u>6,093,042</u>
Paid related to:		
Current period	(21,742)	(92,030)
Prior period	(5,023,091)	(2,619,811)
Total paid	<u>(5,044,833)</u>	<u>(2,711,841)</u>
Net provision for losses and loss adjustment expenses	<u>\$ 39,513,628</u>	<u>\$ 35,675,566</u>

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

9. Professional Liability Insurance (continued)

ASC 944, *Financial Services – Insurance*, requires the application of deposit accounting for any policies or agreements that do not transfer insurance risk. To the extent that an insurance contract or a reinsurance contract does not, despite its form, provide for indemnification of the insured or the ceding company by the insurer or reinsurer against loss or liability, the premium paid less the amount of the premium to be retained by the insurer or reinsurer shall be accounted for as a deposit by the insurer or ceding company. Accordingly, a portion of WCHNIC activity is recorded using deposit accounting on the Network’s consolidated balance sheets.

Activity in the deposit liability for the years ended September 30, 2012 and 2011, included in self-insurance liabilities on the consolidated balance sheets, is summarized as follows:

	<u>2012</u>	<u>2011</u>
Balance at the beginning of period	\$ 3,355,509	\$ 2,533,888
Losses paid	(1,657,800)	(88,040)
Gain on deposit liability transferred to statement of income	937,723	909,661
Balance at the end of period	<u>\$ 2,635,432</u>	<u>\$ 3,355,509</u>

Also included in self-insurance liabilities as of September 30, 2012 and 2011 are unearned premiums of \$168,607 and \$166,823, respectively.

The actuary estimated the liability for unpaid losses based on industry data, as well as entity-specific data. Management considers the liability to be adequate as of September 30, 2012 and 2011; however, no assurance can be given that the ultimate settlement of losses may not vary materially from the liability recorded. Future adjustments to the amounts recorded resulting from the continual review process, as well as differences between estimates and ultimate payments, will be reflected in the consolidated statements of operations and changes in net assets of future years when such adjustments, if any, become known.

10. Net Assets

Temporarily restricted net assets of \$33,826,104 and \$30,149,404 as of September 30, 2012 and 2011, respectively, are available to the Network for health care services. Permanently restricted net assets total \$32,959,292 and \$31,885,207 as of September 30, 2012 and 2011, respectively, and are investments to be held in perpetuity and funds held in trust by others, the income from which is expendable to support health care services.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

11. Endowments

The Network endowment consists of approximately 32 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the Board of Directors to function as endowments. Net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported in the accompanying consolidated balance sheets based on the existence or absence of donor-imposed restrictions.

The Leadership of the Network has interpreted the Uniform Prudent Management of Institutional Funds Act (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 Network 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 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 Network 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 Network 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 Network
- (7) The investment policies of the Network

The Network has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Network must hold in perpetuity or for a donor-specific period(s) as well as board-designated funds. Under this policy, as approved by the Network's Board of Directors, the endowment assets are invested in a manner that is intended to produce a real return, net of inflation and investment management costs, of at least 5% over the long term. Actual returns in any given year may vary from this amount.

Western Connecticut Health Network, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

11. Endowments (continued)

To satisfy its long-term rate-of-return objectives, the Network 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 Network targets a diversified asset allocation to achieve its long-term objective within prudent risk constraints. Each year, the Network's Board of Directors will approve an endowment and similar fund spending rate. The objectives of the portfolio are the enhancement of capital and real purchasing power while limiting exposure to risk of loss. The endowment spending rate will be calculated on the 13 quarter trailing average market value of each portfolio as of the prior May 31. The computed value may be adjusted for large contributions, withdrawals or market value swings as necessary. A default spending cap on appreciation of seven percent in any given year is currently in effect. The Network Board abides by these regulations and will adjust this rate accordingly.

Endowment net asset composition by type of fund as of September 30, 2012, consisted of the following:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ 13,820,607	\$ 25,696,661	\$ 39,517,268
Board-designated endowment funds	8,357,137	-	-	8,357,137
Endowment net assets at end of year	<u>\$ 8,357,137</u>	<u>\$ 13,820,607</u>	<u>\$ 25,696,661</u>	<u>\$ 47,874,405</u>

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

11. Endowments (continued)

Changes in endowment funds for the fiscal year ended September 30, 2012, consisted of the following:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets at beginning of the year	\$ 7,218,125	\$ 14,345,583	\$ 25,445,909	\$ 47,009,617
Investment return:				
Investment income, net	210,135	1,000,507	-	1,210,642
Change in unrealized gains and losses	928,877	4,578,012	-	5,506,889
Total investment return	1,139,012	5,578,519	-	6,717,531
Contributions	-	266,310	115,407	381,717
Net asset reclassification- net change in loss on endowments	-	(28,482)	-	(28,482)
Appropriation of endowment assets for expenditures	-	(6,205,978)	-	(6,205,978)
Other changes:				
Transfers to permanently restricted endowment	-	(135,345)	135,345	-
Endowment net assets at end of year	<u>\$ 8,357,137</u>	<u>\$ 13,820,607</u>	<u>\$ 25,696,661</u>	<u>\$ 47,874,405</u>

Endowment net asset composition by type of fund as of September 30, 2011, consisted of the following:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ 14,345,583	\$ 25,445,909	\$ 39,791,491
Board-designated endowment funds	7,218,125	-	-	7,218,125
Endowment net assets at end of year	<u>\$ 7,218,125</u>	<u>\$ 14,345,583</u>	<u>\$ 25,445,909</u>	<u>\$ 47,009,617</u>

Western Connecticut Health Network, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

11. Endowments (continued)

Changes in endowment funds for the fiscal year ended September 30, 2011, consisted of the following:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets at beginning of the year	\$ 12,020,250	\$ 18,999,710	\$ 24,996,155	\$ 56,016,115
Investment return:				
Investment income, net	1,156,098	3,898,117	-	5,054,215
Change in unrealized gains and losses	(513,521)	(2,459,072)	-	(2,972,593)
Total investment return	642,577	1,439,045	-	2,081,622
Contributions	-	274,835	47,145	321,980
Net asset reclassification- net change in loss on endowments	-	24,840	-	24,840
Appropriation of endowment assets for expenditures	(5,444,702)	(6,212,604)	-	(11,657,306)
Other changes:				
Transfers to permanently restricted endowment	-	(180,243)	402,609	422,366
Endowment net assets at end of year	<u>\$ 7,218,125</u>	<u>\$ 14,345,583</u>	<u>\$ 25,445,909</u>	<u>\$ 47,209,617</u>

From time to time, the fair value of assets associated with individual donor-restricted endowments funds may fall below the level fund of the corpus that UPMIFA requires the Network 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 Directors. There was \$28,482 in deficiencies of this nature which are reported in unrestricted net assets as of September 30, 2011 (none at September 30, 2012).

Also included within permanently restricted net assets is \$7,262,631 and \$6,439,298 of beneficial interests in trusts held by others as of September 30, 2012 and 2011, respectively.

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

12. Changes in Components of Operating Assets and Liabilities

	Year Ended September 30	
	2012	2011
(Increase) decrease in operating assets:		
Pledges receivable	\$ (3,581,524)	\$ (3,551,957)
Accounts receivable, net	(29,871,371)	(24,158,591)
Inventories	855,978	(1,379,603)
Prepaid expenses and other assets	(1,888,574)	(6,928,558)
	<u>(34,485,491)</u>	<u>(36,018,709)</u>
Increase (decrease) in operating liabilities:		
Accounts payable	(3,683,973)	6,133,200
Payroll-related accruals	10,871,108	(1,869,415)
Due to third-party payors	(2,845,270)	455,018
Interest payable	(179,203)	735,967
Other accrued expenses	(1,468,794)	(5,358,260)
Self-insurance liabilities	3,119,769	4,213,901
Accrued pension liabilities and other	(71,487)	23,432,489
	<u>5,742,150</u>	<u>27,742,900</u>
Decrease in operating assets and liabilities	<u>\$ (28,743,341)</u>	<u>\$ (8,275,809)</u>

13. Functional Expenses

The Network provides general health care services to residents within its geographic location. Expenses related to providing these services, including the operating expenses of the Western Connecticut Health Network Foundation, Inc., are as follows:

	Year Ended September 30	
	2012	2011
Healthcare services	\$ 596,089,430	\$ 595,459,794
General and administrative	127,602,912	124,174,999
Fundraising	2,407,222	3,213,974
	<u>\$ 726,099,564</u>	<u>\$ 722,848,767</u>

Western Connecticut Health Network, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

14. Subsequent Events

The Network 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, 2012, the Network evaluated subsequent events through January 25, 2013, which represents the date the consolidated financial statements were issued. On April 3, 2012, an initial letter of intent was signed between the Network and Norwalk Health Systems Corporation, followed by a summary of terms. The letter of intent was signed to document a potential affiliation between Norwalk Health Systems Corporation and the Network. On January 22, 2013, a definitive agreement was signed between the Network and Norwalk Health Systems Corporation based on the approval of each entity's board of directors.

No other events have occurred that require disclosure in or adjustment to the consolidated financial statements.



Ernst & Young LLP
Goodwin Square
225 Asylum Street
Hartford, CT 06103-1506
Tel: +1 860 247 3100
Fax: +1 860 725 6040
www.ey.com

Report of Independent Auditors on Supplementary Information

The Board of Directors
Western Connecticut Health Network, Inc.

We have audited the consolidated financial statements of Western Connecticut Health Network, Inc. and Subsidiaries (the Network) as of and for the years ended September 30, 2012 and 2011, and have issued our report thereon dated January 25, 2013, which contained an unqualified opinion on those consolidated financial statements. Our audits were performed for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating balance sheets and statements of operations are presented for the purposes of additional analysis and are 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. In our opinion, based on our audits and the report of other auditors, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Ernst & Young LLP

January 25, 2013

Western Connecticut Health Network, Inc. and Subsidiaries
Consolidating Balance Sheet

September 30, 2012

Assets	Danbury Hospital	Western Connecticut Health Foundation, Inc.	Western Connecticut Health Network, Inc.	New Milford Hospital	Western Connecticut Medical Group, P.C.	Eliminations	Obligated Group	Foundation For Community Healthcare	Western Connecticut Health Network Affiliates, Inc.	Business System, Inc.	Western Connecticut Home Care, Inc.	Eliminations	Total
Cash and cash equivalents	\$ 54,460,115	\$ 844,986	\$ 374,361	\$ 6,281,016	\$ 6,037,216	\$ -	\$ 67,997,694	\$ 1,000	\$ 1,556,174	\$ 2,881,203	\$ 1,647,889	\$ -	\$ 74,083,960
Current portion of assets limited as to use	900,896	-	-	1,200,000	-	-	2,106,896	-	-	-	-	-	2,106,896
Current portion of pledges receivable	60,638,935	2,108,331	-	900,631	-	-	3,408,962	-	-	-	-	-	3,408,962
Accounts receivable, less allowance for uncollectible accounts of \$19,119,000	8,730,837	-	-	8,601,320	6,470,327	-	75,110,382	-	3,006,434	650,265	721,831	-	79,495,132
Current portion of due from related parties:	9,133,372	-	-	1,645,080	16,655	(5,633,038)	3,714,454	-	-	-	-	(3,714,454)	-
Inventories	14,340,018	-	-	900,544	256,552	-	11,235,004	-	-	-	122,585	-	11,357,589
Prepaid expenses and other	148,404,173	2,963,819	1,024,782	19,528,591	13,754,178	(3,411,121)	16,533,292	-	73,806	766,706	116,665	(43,125)	17,441,444
Total current assets	173,599,412	9,542,874	-	2,706,138	-	(5,974,159)	179,701,384	1,000	4,636,434	4,304,174	2,408,970	(3,761,779)	187,490,183
Investments	-	-	-	-	-	-	185,848,424	-	-	-	-	-	185,848,424
Assets limited as to use:	-	-	-	-	-	-	-	-	-	-	-	-	-
Funds restricted by donor	-	48,116,221	-	421,160	-	-	48,537,381	-	-	-	106,032	-	48,643,413
Board designated funds	-	8,639,352	-	-	-	-	8,639,352	-	-	-	-	-	8,639,352
Beneficial interest in trusts held by other	-	3,128,085	-	4,134,546	-	-	7,262,631	-	-	-	-	-	7,262,631
Construction funds	100,552,317	-	-	-	-	-	100,552,317	-	-	-	-	-	100,552,317
Investments in WCHNIC	59,508,868	-	-	-	-	-	59,508,868	-	-	-	-	-	59,508,868
Total noncurrent assets limited as to use	160,061,185	59,883,658	-	4,555,706	-	-	224,500,549	-	-	-	108,032	-	224,608,581
Other assets	156,420	-	7,694,603	4,541,461	4,407,304	(2,438,457)	14,361,331	-	-	-	-	-	14,361,331
Interest in Western Connecticut Health Network Foundation, Inc.	78,906,131	-	-	-	-	(78,906,131)	-	-	-	-	-	-	-
Due from related parties	8,172,413	-	-	-	-	(8,172,413)	-	-	-	-	-	-	-
Property, plant, and equipment	9,904,877	471,593	-	1,544,196	-	-	11,920,666	-	-	-	-	-	11,920,666
Land and land improvement	286,763,195	706,417	11,789	49,484,944	7,243,533	-	344,209,898	-	3,172,079	26,818	705,834	-	347,885,812
Buildings and building improvement	229,444,069	211,022	-	56,864,547	9,667,271	-	296,186,809	-	7,353,994	26,818	701,999	-	304,269,730
Equipment and other	39,100,951	-	-	298,414	-	-	39,399,365	-	-	-	-	-	39,399,365
Less accumulated depreciation	(563,213,092)	(1,389,032)	(11,789)	(108,192,101)	(16,910,824)	-	(691,716,838)	-	(10,526,073)	(26,818)	(705,834)	-	(702,975,363)
Net book value	(224,225,095)	(1,078,730)	(4,620)	(32,440,675)	(7,943,851)	-	(283,617,471)	-	(8,794,338)	(21,486)	(697,387)	-	(284,439,781)
Pledges receivable, less current portion	4,628,949	6,201,303	-	2,602,193	-	-	8,803,496	-	-	-	-	-	8,803,496
Bond issuance costs, net	(816,163,778)	(79,670,384)	(8,724,003)	(66,374,764)	(26,077,333)	(95,491,160)	(901,519,104)	1,000	6,368,169	(4,309,586)	(2,725,449)	(3,761,779)	(4,628,949)
Total assets	\$ 25,455,839	\$ -	\$ 1,368	\$ 3,081,591	\$ (331,544)	\$ (347,897)	\$ 27,859,357	\$ -	\$ 383,995	\$ -	\$ 99,617	\$ -	\$ 28,342,969
Liabilities and net assets	20,868,119	46,337	-	3,202,850	9,124,342	-	33,241,648	-	252,377	167,940	140,179	-	33,802,144
Current liabilities:	9,985,351	-	-	2,463,714	-	-	12,447,065	-	-	-	45,008	-	12,492,073
Accounts payable	1,624,480	-	-	5,057,706	109,568	(5,632,887)	-	-	623,873	2,740,137	397,769	(3,761,779)	-
Payroll-related accruals	3,553,987	251,695	28,434	460,952	151,257	-	4,446,325	-	(361,071)	497,512	-	-	4,624,480
Due to third-party payors	63,042,776	763,645	29,802	14,759,593	9,053,623	(5,980,784)	81,668,965	-	896,374	3,405,389	682,573	(3,761,779)	82,803,922
Interest payable	42,317,667	-	-	-	-	-	42,317,667	-	-	-	-	-	42,317,667
Other accrued expenses	16,602,276	608	146,499,045	26,239,675	4,765,095	(2,926,469)	191,180,190	-	2,759	-	298,565	-	191,481,514
Current portion of long-term debt and capital lease obligation	-	-	-	3,815,518	4,340,270	(8,165,788)	-	-	-	-	-	-	-
Total current liabilities	249,580,000	-	-	1,013,765	-	-	250,593,765	-	-	-	-	-	250,593,765
Self-insurance liabilities	-	-	-	-	-	-	-	-	-	-	-	-	-
Accrued pension liabilities and other	-	-	-	-	-	-	-	-	-	-	-	-	-
Accrued pension liabilities and other	-	-	-	-	-	-	-	-	-	-	-	-	-
Due to related parties	-	-	-	-	-	-	-	-	-	-	-	-	-
Long-term debt and capital lease obligations, less current portion	-	-	-	-	-	-	-	-	-	-	-	-	-
Net assets:	-	-	-	-	-	-	-	-	-	-	-	-	-
Unrestricted	386,002,265	20,287,298	(157,804,842)	12,487,373	7,908,345	(19,799,386)	269,081,155	1,000	5,466,836	903,917	1,636,279	-	277,089,185
Temporarily restricted	29,794,088	29,794,087	-	3,923,984	-	(29,794,087)	33,718,072	-	-	-	-	-	33,718,072
Permanently restricted	28,834,216	28,834,246	-	4,134,546	-	(28,834,246)	33,929,292	-	-	-	108,032	-	33,929,292
Total net assets	444,630,569	78,906,131	(137,804,842)	20,545,903	7,908,345	(28,818,119)	335,738,517	1,000	5,466,836	903,917	1,744,311	(3,761,779)	313,874,361
Total liabilities and net assets	\$ 816,163,778	\$ 79,670,384	\$ 8,724,003	\$ 66,374,764	\$ 36,077,333	\$ (95,491,160)	\$ 301,319,103	\$ 1,000	\$ 6,368,169	\$ 4,309,586	\$ 2,725,449	\$ (3,761,779)	\$ 313,874,361

Western Connecticut Health Network, Inc. and Subsidiaries

Consolidating Statement of Operations

Year Ended September 30, 2012

	Danbury Hospital	Western Connecticut Health Network, Inc.	New Milford Hospital	Western Connecticut Medical Group, P.C.	Western Connecticut Health Network Affiliates, Inc.	Business System, Inc.	Western Connecticut Home Care, Inc.	Eliminations	Total
Unrestricted revenues:									
Net patient service revenue	\$ 521,836,000	\$ -	\$ 81,236,073	\$ 104,940,347	\$ 14,974,831	\$ 10,630,596	\$ 4,422,720	\$ (309,448)	\$ 736,921,369
Provision for bad debt	19,413,218	(24,553)	3,125,172	1,769,388	405,650	63,438	19,739		24,771,952
Net patient service revenue less provision for bad debt	502,422,782	24,587	78,110,901	103,171,059	14,569,181	10,567,158	4,402,981	(509,448)	712,149,417
Net assets released from restriction	3,156,468	-	66,843	-	-	-	101,277	-	3,324,588
Other operating revenues	26,682,322	-	1,034,489	58,842,786	3,253,311	-	129,192	(465,851)	26,383,097
	532,361,572	25,868	79,212,233	162,013,845	18,822,492	3,010,078	4,633,450	(975,299)	742,056,702
Expenses:									
Salaries, benefits and fees	313,980,347	-	51,817,496	138,444,987	7,093,837	2,028,467	3,351,506	(3,265)	462,975,344
Supplies and other	141,577,637	-	25,778,114	22,023,818	5,862,240	9,885,844	1,531,287	(847,798)	204,378,809
Insurance	11,680,311	-	1,643,424	2,750,952	85,932	12,774	23,530	(124,236)	11,680,311
Depreciation and amortization	31,663,499	1,180	5,526,925	1,324,333	38,513,937	12,183	10,884	-	39,029,252
Interest	4,156,059	-	419,014	43,402	4,322,562	-	-	-	4,322,562
Operating income before pension curtailment charge	303,057,853	(4,072,281)	85,184,973	164,587,492	13,756,257	11,939,268	4,919,207	(975,299)	722,386,278
Pension curtailment charge	29,203,719	(4,046,413)	(5,972,740)	(2,573,647)	946,875	1,637,968	(285,757)	-	19,670,424
Operating income (loss)	273,854,134	(8,118,694)	79,212,233	162,013,845	14,702,382	10,301,300	4,633,450	(975,299)	742,056,702
Income tax expense	-	-	-	-	-	-	-	-	-
Nonoperating gains (losses):									
Contributions	-	-	-	-	-	-	-	-	-
Investment income, net	-	-	-	-	-	-	-	-	-
Change in unrealized gains and losses on investments	1,690,407	902,614	1,009,077	3,235	-	-	24,515	-	1,976,306
Change in equity interest in unrestricted net assets of the Western Connecticut Health Network Foundation, Inc.	19,910,410	797,854	429,853	3,241	3,241	-	49,859	-	2,445,895
Operating expenses of the New Milford Hospital Foundation, Inc. and Western Connecticut Health Network Foundation, Inc.	2,571,725	-	-	-	-	-	72,035	-	22,674,214
	24,172,542	(1,832,722)	(654,269)	79,769	(2,407,222)	-	-	-	(2,407,222)
Excess (deficiency) of revenues over expenses	\$ 35,376,261	\$ (2,571,721)	\$ (5,200,285)	\$ (2,570,412)	\$ (2,083,708)	\$ (40,563,967)	\$ (139,348)	\$ -	\$ (42,512,455)

Western Connecticut Health Network, Inc. and Subsidiaries
Consolidating Balance Sheet

September 30, 2011

	Danbury Hospital	Western Connecticut Health Foundation, Inc.	Western Connecticut Health Network, Inc.	New Milford Hospital	Western Connecticut Medical Group, P.C.	Eliminations	Obligated Group	Foundation For Community Healthcare	Western Connecticut Health Affiliates, Inc.	Business System, Inc.	Western Connecticut Home Care, Inc.	Regional Hospice of Western Connecticut, Inc.	Eliminations	Total
Assets														
Current assets:														
Cash and cash equivalents	\$ 36,610,270	\$ 498,362	\$ 1,099,901	\$ 12,675,086	\$ 3,213,882	\$ -	\$ 54,097,501	\$ 1,000	\$ 760,628	\$ 271,934	\$ 1,656,806	\$ -	\$ -	\$ 56,787,869
Current portion of assets limited as to use	1,275,013	-	-	1,507,266	-	-	2,780,279	-	-	-	-	-	-	2,780,279
Current portion of pleads receivable	-	1,690,451	-	117,660	-	-	1,768,111	-	-	-	-	-	-	1,768,111
Accounts receivable, less allowance for uncollectible accounts of \$17,545,42	53,313,528	-	11,785	10,457,444	6,609,543	-	70,392,300	-	2,326,583	1,061,436	613,374	-	(2,035,984)	74,395,713
Current portion of due from related parties	6,009,891	-	-	1,000,027	1,000,027	(5,083,934)	2,025,984	-	-	-	-	-	-	4,000,000
Inventory	8,853,966	-	-	1,944,478	243,785	-	11,042,229	-	-	962,796	208,342	-	-	12,213,567
Prepaid expenses and other	15,544,259	-	124,299	1,415,605	298,675	(227,860)	17,153,038	-	54,652	18,164	144,023	-	(1,007,098)	16,364,779
Total current assets	121,604,927	2,148,813	1,235,985	28,117,539	11,465,912	(5,311,734)	159,261,442	1,000	3,141,863	2,314,330	2,624,745	-	(3,033,082)	164,310,318
Investments	151,523,870	8,068,873	-	199,742	-	-	159,792,485	-	-	-	-	-	-	159,792,485
Assets limited as to use:														
Funds restricted by donor	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Board designated funds	-	46,477,328	-	3,081,975	-	-	49,559,303	-	-	-	100,009	-	-	49,659,312
Beneficial interest in trusts held by other	-	7,461,876	-	-	-	-	7,461,876	-	-	-	-	-	-	7,461,876
Construction funds	125,248,424	2,752,457	-	3,686,841	-	-	6,439,298	-	-	-	-	-	-	6,439,298
Investments in WCHNC	50,857,322	-	-	-	-	-	125,248,424	-	-	-	-	-	-	125,248,424
Total noncurrent assets limited as to use	176,085,746	56,691,661	-	6,768,816	-	-	239,546,223	-	-	-	100,009	-	-	239,646,232
Other assets	-	-	6,098,277	1,095,567	6,357,818	-	13,551,622	-	-	-	-	-	-	13,551,622
Interest in Western Connecticut Health Network Foundation, Inc.	73,125,721	-	-	-	-	(73,125,721)	-	-	-	-	-	-	-	-
Due from related parties	5,905,152	-	-	-	-	(5,905,152)	-	-	-	-	-	-	-	-
Property, plant, and equipment	8,456,354	471,593	-	1,546,857	-	-	10,476,804	-	-	-	-	-	-	10,476,804
Land and land improvement	265,771,375	706,417	11,789	50,178,336	5,986,586	-	322,654,503	-	3,129,272	34,000	3,835	-	-	328,831,610
Buildings and building improvement	218,210,465	191,760	-	54,763,793	10,156,128	-	283,422,146	-	7,231,117	187,467	701,999	-	-	291,542,729
Equipment and other	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Construction in progress (estimated cost to complete as of September 30, 2011: \$ 137,976,704)	27,578,848	-	-	-	-	-	27,578,848	-	-	-	-	-	-	27,578,848
Less accumulated depreciation	(520,119,042)	(1,369,770)	(11,789)	(106,488,986)	(16,142,714)	-	(644,132,301)	-	(10,360,389)	(221,467)	(705,834)	-	-	(655,419,991)
Pledges receivable, less current portion	(299,833,683)	(251,969)	(5,989)	(71,743,955)	(7,709,054)	-	(379,544,590)	-	(8,304,090)	(108,908)	(686,503)	-	-	(388,704,091)
Bond insurance costs, net	220,283,359	1,117,861	5,800	34,745,031	8,433,660	-	264,587,711	-	2,056,299	52,559	19,331	-	-	266,715,900
Total assets	5,779,765	6,306,675	-	156,148	-	-	6,462,823	-	-	-	-	-	-	6,462,823
	\$ 754,310,540	\$ 74,333,883	\$ 7,340,022	\$ 71,082,843	\$ 26,257,390	\$ (84,342,607)	\$ 848,982,071	\$ 1,000	\$ 5,198,162	\$ 2,366,800	\$ 2,774,085	\$ -	\$ (3,033,082)	\$ 856,259,145
Liabilities and net assets														
Current liabilities:														
Accounts payable	\$ 27,363,171	\$ -	\$ 1,448	\$ 4,262,947	\$ -	\$ (227,820)	\$ 31,399,746	\$ -	\$ 285,633	\$ -	\$ 341,563	\$ -	\$ -	\$ 32,026,942
Accrued interest	12,263,559	68,525	-	2,329,129	7,770,453	-	22,431,666	-	276,989	52,633	169,748	-	-	22,911,036
Due to third-party payors	11,107,547	-	-	4,184,788	-	-	15,292,335	-	-	-	45,008	-	-	15,337,343
Current portion of due to related parties:														
Interest payable	1,803,683	765,775	-	4,028,167	294,100	(5,088,042)	-	-	408,534	2,543,248	81,300	-	(3,033,082)	1,803,683
Other accrued expenses	4,070,796	361,446	28,853	1,116,330	771,078	-	1,803,683	-	(302,372)	4,829	-	-	-	6,050,960
Current portion of long-term debt and capital lease obligation	59,123,756	1,195,746	30,301	16,431,134	8,835,631	(5,315,862)	80,300,706	-	668,784	2,600,710	637,619	-	(3,033,082)	81,174,737
Total current liabilities	39,197,898	12,416	94,177,011	17,644,845	6,242,282	-	133,723,862	-	12,658	-	230,830	-	-	39,197,898
Self-insurance liabilities	15,647,308	-	-	-	-	-	-	-	-	-	-	-	-	15,647,308
Accrued pension liabilities and other	-	-	-	5,203,150	697,874	(5,901,024)	-	-	-	-	-	-	-	-
Due to related parties	252,100,000	-	-	1,414,718	-	-	253,514,718	-	-	-	-	-	-	253,514,718
Long-term debt and capital lease obligations, less current portion	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net assets:														
Unrestricted	332,255,763	17,139,907	(86,867,290)	24,440,209	10,481,603	(17,139,907)	280,310,285	1,000	4,516,720	(233,801)	1,775,627	-	-	286,369,831
Temporarily restricted	27,787,449	-	-	2,261,946	-	(27,787,449)	30,049,595	-	-	-	-	-	-	30,149,404
Permanently restricted	28,198,366	28,198,366	-	3,686,841	-	(28,198,366)	31,885,207	-	-	-	100,009	-	-	31,885,207
Total net assets	388,231,578	73,125,721	(86,867,290)	30,386,996	10,481,603	(73,125,721)	342,244,887	1,000	4,516,720	(233,801)	1,875,656	-	-	348,604,442
Total liabilities and net assets	\$ 754,310,540	\$ 74,333,883	\$ 7,340,022	\$ 71,082,843	\$ 26,257,390	\$ (84,342,607)	\$ 848,982,071	\$ 1,000	\$ 5,198,162	\$ 2,366,800	\$ 2,774,085	\$ -	\$ (3,033,082)	\$ 856,259,145

Western Connecticut Health Network, Inc. and Subsidiaries

Consolidating Statement of Operations

Year Ended September 30, 2011

	Western Connecticut Health Network Foundation, Inc.	Western Connecticut Health Network, Inc.	New Milford Hospital	Western Connecticut Medical Group, P.C.	Eliminations	Obligated Group	Western Connecticut Health Network Affiliates, Inc.	Business System, Inc.	Western Connecticut Home Care, Inc.	Regional Hospice of Western Connecticut, Inc.	Eliminations	Total
Unrestricted revenues:												
Net patient service revenue	\$ 497,720,490	\$ 2,746,465	\$ 90,888,107	\$ 96,212,442	\$ (493,239)	\$ 686,774,245	\$ 15,492,962	\$ 13,311,707	\$ 4,088,750	\$ 1,366,962	\$ (509,448)	\$ 720,525,178
Provision for bad debt	18,183,085	127,402	2,545,989	5,256,573	—	26,113,049	291,310	8,886	48,657	3,625	—	26,465,527
Net patient service revenue less provision for bad debt	479,537,405	2,619,063	88,442,118	90,955,869	(493,239)	660,661,196	15,201,652	13,302,821	4,040,093	1,363,337	(509,448)	694,059,651
Net assets released from restriction	2,894,766	—	204,673	—	3,099,439	—	—	—	67,640	—	—	3,167,079
Other operating revenue	16,951,609	11,852	2,623,754	42,752,573	(48,516,363)	13,823,425	129,589	446,766	165,802	—	(654,472)	14,009,110
	499,383,780	2,630,915	90,870,545	133,708,442	(49,009,622)	677,584,060	15,331,241	13,749,587	4,271,535	1,363,337	(1,063,920)	711,235,840
Expenses:												
Salaries, benefits and fees	308,540,688	2,723,282	53,344,078	123,223,653	(41,783,413)	446,048,288	7,240,578	1,887,198	3,477,917	1,153,460	(7,645)	459,799,796
Supplies and other	130,649,238	2,836,058	29,943,027	19,836,126	(2,489,054)	180,775,995	5,976,212	11,872,667	1,125,964	355,020	(921,627)	199,184,231
Insurance	8,742,635	—	1,611,492	3,155,388	(4,766,880)	8,742,635	92,800	11,236	29,340	1,272	(134,648)	8,742,635
Depreciation and amortization	27,569,949	426,703	3,855,136	1,279,271	—	34,931,059	1,256,413	12,027	22,756	14,421	—	36,236,656
Interest	4,387,742	234,265	511,926	49,870	(49,870)	5,333,933	54,067	—	—	—	(54,967)	5,333,933
Operating income before pension curtailment charge	479,890,232	6,220,308	91,266,259	147,544,308	(49,089,217)	675,831,910	14,912,380	13,792,014	4,704,614	1,534,173	(1,118,887)	709,297,851
Pension curtailment charge	19,493,528	(3,589,393)	(395,714)	(13,835,866)	79,595	1,752,150	418,961	(42,427)	(433,079)	(160,836)	54,967	1,938,389
Operating income (loss)	460,396,704	(10,337,542)	89,870,973	133,708,442	(48,293,622)	674,079,760	14,493,419	13,749,587	4,271,535	(1,063,920)	54,967	707,359,464
Income tax expense	—	(750)	—	(13,835,866)	79,595	(8,385,392)	418,961	(42,427)	(433,079)	(160,836)	54,967	(8,398,953)
Nonoperating gains (losses):												
Contributions	—	(750)	—	—	—	(750)	—	(250)	—	—	—	(1,000)
Investment income, net	—	1,255,318	—	1,516,643	—	2,792,161	—	—	35,168	339,643	—	3,166,972
Change in unrealized gains and losses on investments	6,100,396	3,280,259	(101,324)	235,285	(151,510)	9,366,852	3,830	—	16,955	22,759	(54,967)	9,355,429
Change in equity interest in unrestricted net assets of the Western Connecticut Health Network Foundation, Inc.	(1,979,439)	(1,777,338)	—	3,746	(3,696,877)	—	—	—	(8,766)	—	—	(3,715,643)
Operating expenses of the New Milford Hospital Foundation, Inc.	71,435	—	—	—	(71,435)	—	—	—	—	—	—	—
Western Connecticut Health Network Foundation, Inc.	(2,746,901)	—	(538,988)	—	71,915	(3,215,974)	—	—	—	—	—	(3,213,974)
Excess (deficiency) of revenues over expenses	4,192,392	71,438	(101,324)	3,746	(151,030)	5,248,162	3,830	(42,677)	33,357	362,402	(54,967)	5,992,784
	23,685,920	71,438	837,226	(13,833,120)	(71,435)	(3,337,980)	422,791	(42,677)	(399,722)	301,566	—	(2,807,169)

Ernst & Young LLP

Assurance | Tax | Transactions | Advisory

About Ernst & Young

Ernst & Young is a global leader in assurance, tax, transaction and advisory services. Worldwide, our 167,000 people are united by our shared values and an unwavering commitment to quality. We make a difference by helping our people, our clients and our wider communities achieve their potential.

For more information, please visit www.ey.com

Ernst & Young refers to the global organization of member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. This Report has been prepared by Ernst & Young LLP, a client serving member firm located in the United States.

