



PORTER HOSPITAL, INC.

FINANCIAL STATEMENTS

with

SUPPLEMENTARY INFORMATION

September 31, 2011 and 2010

With Independent Auditors' Report



September 30, 2011 and 2010

TABLE OF CONTENTS

	<u>Page</u>
Independent Auditors' Report	1
Financial Statements	
Balance Sheets	2
Statements of Operations	3
Statements of Changes in Net Assets	4
Statements of Cash Flows	5
Notes to Financial Statements	6 - 29
Supplementary Information	
Schedule of Required Financial Covenant Ratios	30
Note to Supplemental Schedule of Required Financial Covenant Ratios	31



INDEPENDENT AUDITORS' REPORT

Board of Directors
Porter Hospital, Inc.

We have audited the accompanying balance sheets of Porter Hospital, Inc. (the Hospital), a subsidiary of Porter Medical Center, Inc., as of September 30, 2011 and 2010, and the related statements of operations, changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Porter Hospital, Inc. as of September 30, 2011 and 2010, and the results of its operations, the changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying supplementary schedule of required financial covenant ratios is presented for purposes of additional analysis and is not a required part of the basic 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 basic financial statements. The supplementary schedule of required financial covenant ratios has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with U.S. generally accepted auditing standards. In our opinion, the supplementary schedule is fairly stated in all material respects in relation to the financial statements taken as a whole.

BerryDunn McNeil & Parker, LLC

Manchester, New Hampshire
January 10, 2012
Registration No. 92-0000278

PORTER HOSPITAL, INC.

Balance Sheets

September 30, 2011 and 2010

ASSETS

	<u>2011</u>	<u>2010</u>
Current assets		
Cash and cash equivalents	\$ 3,100,982	\$ 6,737,172
Assets limited as to use, trustee held funds under debt agreements	337,031	322,937
Patient accounts receivable, net	10,069,880	6,784,157
Other receivables, net	1,132,783	367,095
Current portion of note receivable, related party	3,103	2,922
Supplies	1,178,244	754,471
Prepaid expenses and other	594,316	394,536
Due from affiliates	<u>240,336</u>	<u>428,190</u>
Total current assets	16,656,675	15,791,480
Assets limited as to use, deferred compensation plan assets	412,630	302,984
Long-term investments	3,101,976	2,934,333
Property and equipment, net	28,812,904	26,686,903
Beneficial interest in perpetual trusts	2,851,219	2,952,405
Deferred financing costs, net	142,662	148,674
Notes receivable	212,567	17,637
Note receivable, related party - noncurrent	<u>34,794</u>	<u>37,896</u>
Total assets	<u>\$ 52,225,427</u>	<u>\$ 48,872,312</u>

The accompanying notes are an integral part of these financial statements.

LIABILITIES AND NET ASSETS

	<u>2011</u>	<u>2010</u>
Current liabilities		
Current portion of long-term debt	\$ 1,385,558	\$ 978,213
Accounts payable and accrued expenses	1,620,426	1,863,591
Accrued payroll and related liabilities	2,051,341	1,679,092
Estimated third-party settlements	1,183,000	600,000
Accrued vacation	2,176,110	1,864,519
Deferred revenue	22,508	112,592
Due to affiliates	<u>148,688</u>	<u>310,644</u>
Total current liabilities	8,587,631	7,408,651
Liability for pension benefits	2,515,825	2,418,302
Deferred compensation	412,630	302,984
Long-term debt, excluding current portion	<u>16,173,391</u>	<u>16,029,735</u>
Total liabilities	<u>27,689,477</u>	<u>26,159,672</u>
Commitments and contingencies (Notes 5, 14, 15 and 17)		
Net assets		
Unrestricted	21,283,161	19,271,048
Temporarily restricted	283,888	371,505
Permanently restricted	<u>2,968,901</u>	<u>3,070,087</u>
Total net assets	<u>24,535,950</u>	<u>22,712,640</u>
Total liabilities and net assets	<u>\$ 52,225,427</u>	<u>\$ 48,872,312</u>

PORTER HOSPITAL, INC.

Statements of Operations

Years Ended September 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Unrestricted revenues, gains and other support		
Patient service revenue (net of contractual allowances and discounts)	\$ 58,979,939	\$ 54,573,553
Less provision for bad debts	<u>2,326,120</u>	<u>3,102,565</u>
Net patient service revenue	56,653,819	51,470,988
Other operating revenue	1,806,096	2,130,935
Net assets released from restrictions used for operations	<u>79,302</u>	<u>120,399</u>
Total unrestricted revenues, gains and other support	<u>58,539,217</u>	<u>53,722,322</u>
Expenses		
Professional care of patients	32,161,266	31,369,208
General services	3,800,481	3,363,898
Administrative and fiscal services	14,965,041	15,562,142
Health care improvement tax	3,158,424	2,483,444
Depreciation and amortization	3,431,186	2,980,433
Interest	<u>314,456</u>	<u>223,858</u>
Total expenses	<u>57,830,854</u>	<u>55,982,983</u>
Operating income (loss)	<u>708,363</u>	<u>(2,260,661)</u>
Nonoperating gains		
Contributions	186,633	115,877
Other program income, net	1,428,863	-
Investment income	<u>134,040</u>	<u>370,521</u>
Nonoperating gains	<u>1,749,536</u>	<u>486,398</u>
Excess (deficiency) of revenues, gains and other support over expenses and nonoperating gains	2,457,899	(1,774,263)
Change in net assets to recognize funded status of pension plan	(347,098)	(377,283)
Net assets released from restrictions used for purchase of property and equipment	-	40,600
Transfer to affiliate	<u>(98,688)</u>	<u>-</u>
Increase (decrease) in unrestricted net assets	<u>\$ 2,012,113</u>	<u>\$ (2,110,946)</u>

The accompanying notes are an integral part of these financial statements.

PORTER HOSPITAL, INC.

Statements of Changes in Net Assets

Years Ended September 30, 2011 and 2010

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Balances, October 1, 2009	\$ <u>21,381,994</u>	\$ <u>432,864</u>	\$ <u>2,659,814</u>	\$ <u>24,474,672</u>
Deficiency of revenues, gains and other support over (under) expenses and nonoperating gains	(1,774,263)	-	-	(1,774,263)
Net assets released from restrictions used for operations	-	(120,399)	-	(120,399)
Net assets released from restrictions used for purchase of property and equipment	40,600	(40,600)	-	-
Change in net assets to recognize funded status of pension plan	(377,283)	-	-	(377,283)
Contributions	-	83,160	-	83,160
Investment income, net	-	16,480	-	16,480
Change in beneficial interest in perpetual trusts	-	-	410,273	410,273
Net (decrease) increase in net assets	<u>(2,110,946)</u>	<u>(61,359)</u>	<u>410,273</u>	<u>(1,762,032)</u>
Balances, September 30, 2010	<u>19,271,048</u>	<u>371,505</u>	<u>3,070,087</u>	<u>22,712,640</u>
Excess of revenues, gains and other support over expenses and nonoperating gains	2,457,899	-	-	2,457,899
Net assets released from restrictions used for operations	-	(79,302)	-	(79,302)
Change in net assets to recognize funded status of pension plan	(347,098)	-	-	(347,098)
Transfer to affiliate	(98,688)	-	-	(98,688)
Contributions	-	1,203	-	1,203
Investment income, net	-	(9,518)	-	(9,518)
Change in beneficial interest in perpetual trusts	-	-	(101,186)	(101,186)
Net increase (decrease) in net assets	<u>2,012,113</u>	<u>(87,617)</u>	<u>(101,186)</u>	<u>1,823,310</u>
Balances, September 30, 2011	<u>\$ 21,283,161</u>	<u>\$ 283,888</u>	<u>\$ 2,968,901</u>	<u>\$ 24,535,950</u>

The accompanying notes are an integral part of these financial statements.

PORTER HOSPITAL, INC.

Statements of Cash Flows

Years Ended September 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Cash flows from operating activities		
Change in net assets	\$ 1,823,310	\$ (1,762,032)
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Loss on disposal of property and equipment	20,022	99,272
Depreciation and amortization	3,431,186	2,980,433
Provision for bad debts	2,326,120	3,102,565
Net realized and unrealized loss (gain) on investments	92,069	(151,271)
Change in net assets to recognize funded statements of pension plan	347,098	377,283
Equity transfer to affiliate	98,688	-
Net unrealized loss (gain) on beneficial interest in perpetual trusts	101,186	(410,273)
(Increase) decrease in		
Patient accounts receivable	(5,611,843)	(2,328,093)
Due from affiliates	187,854	(101,851)
Supplies, prepaids and other current assets	(1,403,335)	(1,171)
Increase (decrease) in		
Accounts payable and accrued expenses	(243,165)	470,257
Accrued payroll and related liabilities	372,249	(206,600)
Estimated third party-settlements	583,000	(582,305)
Due to affiliates	(161,956)	(771,967)
Other current liabilities	(28,068)	(44,656)
Net cash provided by operating activities	<u>1,934,415</u>	<u>669,591</u>
Cash flows from investing activities		
Purchase of investments	(2,071,849)	(289,954)
Proceeds from sale of investments	1,812,137	32,872
Payments on note receivable from affiliates	2,921	2,754
Purchase of property and equipment	(3,851,570)	(2,665,355)
Notes receivable	(194,930)	-
Net cash used by investing activities	<u>(4,303,291)</u>	<u>(2,919,683)</u>
Cash flows from financing activities		
Equity transfer to affiliate	(98,688)	-
Proceeds from issuance of long-term debt	-	1,300,079
Principal payments on long-term debt	(1,168,626)	(1,113,091)
Net cash (used) provided by financing activities	<u>(1,267,314)</u>	<u>186,988</u>
Decrease in cash and cash equivalents	(3,636,190)	(2,063,104)
Cash and cash equivalents, beginning of year	<u>6,737,172</u>	<u>8,800,276</u>
Cash and cash equivalents, end of year	<u>\$ 3,100,982</u>	<u>\$ 6,737,172</u>
Supplemental cash flows information		
Interest paid	\$ 314,465	\$ 228,805
Capital lease obligation incurred for property and equipment	1,719,627	-

The accompanying notes are an integral part of these financial statements.

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

Nature of Operations

Porter Hospital, Inc. (the Hospital) is a Vermont not-for-profit corporation which operates a 25-bed short-term community oriented general hospital. The Hospital primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in Middlebury, Vermont, and the surrounding area. Porter Medical Center, Inc. (PMC) is the parent holding company of the Hospital. In its capacity as sole member of the Hospital, PMC has the right to appoint Hospital directors, approve major Hospital expenditures, and approve Hospital long-term borrowings. As a subsidiary of PMC, the Hospital is also related to the following organizations: Helen Porter Nursing Home, Inc. (HPNH), Porter Management Services, Inc. (PMS) and Porter Real Estate Holdings, LLC (PREH). These financial statements represent the operating results, financial position and cash flows of only the Hospital.

1. Summary of Significant Accounting Policies

Basis of Presentation

Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions in accordance with the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 958, *Not-For-Profit Entities*. Under FASB ASC 958, all not-for-profit organizations are required to provide a balance sheet, a statement of operations, and a statement of cash flows. The Statement requires reporting amounts for an organization's total assets, liabilities, and net assets in a balance sheet; reporting the change in an organization's net assets in a statement of operations; and reporting the change in its cash and cash equivalents in a statement of cash flows.

Use of Estimates

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

Cash and Cash Equivalents

Cash and cash equivalents include all liquid investments with original maturities of three months or less other than deferred compensation plan investments to be cash equivalents. At September 30, 2011 and 2010, cash equivalents consisted primarily of money market accounts with brokers and certificates of deposit.

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

Investments and Investment Income

Investments in equity securities having a readily determinable fair value and all investments in debt securities are measured at fair value in the balance sheets. The Hospital adopted ASC 825, effective October 1, 2008, and has elected the fair value option relative to its investments which consolidates all investment performance activity within the nonoperating gains (losses) section of the statement of operations.

Investments are exposed to various risks, such as interest rate, credit, and overall market volatility. As such, it is reasonably possible that changes in the values of investments will occur in the near term and that such changes could materially affect the amounts reported in the balance sheets and statements of operations and changes in net assets.

Assets Limited as to Use

Assets limited as to use include assets held by trustees under debt agreements and deferred compensation plan assets.

Patient Accounts Receivable

Patient accounts receivable are stated at the amount management expects to collect for services rendered from third-party payors, patients and others. Management provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions. Accounts are considered delinquent and subsequently written off as uncollectible based on individual credit evaluation and specific circumstances of the account.

In evaluating the collectibility of accounts receivable, the Hospital analyzes past results and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, the Hospital analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts. For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Hospital records a provision for bad debts in the period of service based on past experience, which indicates that many patients are unable or unwilling to pay amounts for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated or eligible) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged against the allowance for doubtful accounts.

Supplies

The Hospital records supply inventories at the lower of cost, determined using the first-in, first-out method, or market.

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

Property and Equipment

Property and equipment acquisitions are recorded at cost, or, if contributed, at fair market value determined at the date of donation. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the asset's estimated useful life. Such amortization is included in depreciation and amortization in the financial statements. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support, and are excluded from the excess (deficiency) of revenue, gains, and other support over expenses and nonoperating gain, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Deferred Financing Costs

Deferred financing costs represent costs incurred in connection with the issuance of long-term debt. Such costs are being amortized over the term of the respective debt using the straight-line method.

Deferred Revenue

Deferred revenue represents amounts received for disproportionate share payments that are recognized in earnings ratably over the period the funds are earned.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the Hospital have been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Hospital in perpetuity.

Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and are adjusted in future periods as final settlements are determined.

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

Charity Care

The Hospital provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue.

Contributions

Unconditional promises to give cash and other assets are accrued at estimated fair value at the date each promise is received. Gifts received with donor stipulations are reported as either temporarily or permanently restricted support. When a donor restriction expires, that is, when a time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified and reported as an increase in unrestricted net assets. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions. Conditional contributions are reported as liabilities until the condition is eliminated or the contributed assets are returned to the donor.

Excess (Deficiency) of Revenues, Gains and Other Support Over Expenses and Nonoperating Gains

The statements of operations include excess (deficiency) of revenues, gains, and other support over expenses and nonoperating gains. Changes in unrestricted net assets, which are excluded from this measure consistent with industry practice, include defined benefit pension plan adjustments, permanent transfers of assets to and from affiliates for other than goods and services, and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purpose of acquiring such assets).

Income Taxes

The Hospital is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal income taxes on related income.

New Accounting Pronouncement

In July 2011, the FASB amended ASC 954, *Health Care Entities*, to require health care entities to change the presentation of the statement of operations by reclassifying the provision for bad debts associated with patient service revenue from an operating expense to a deduction from patient service revenue (net of contractual allowances and discounts). Additionally, enhanced disclosures are required about the policies for recognizing revenues and assessing bad debts. The amendments also require disclosure of qualitative and quantitative information about significant changes in the allowance for doubtful accounts. The amendments to ASC 954 are effective for public entities for the first annual period beginning after December 15, 2011. The Hospital elected to early adopt these amendments for fiscal year ending September 30, 2011.

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

Subsequent Events

For purposes of the preparation of these financial statements in conformity with GAAP, the Hospital has considered transactions of events occurring through January 10, 2012, which was the date the financial statement were issued.

Reclassifications

Certain amounts in the 2010 financial statements have been reclassified to conform to the current year's presentation.

2. Net Patient Service Revenue and Patient Accounts Receivable

Net Patient Service Revenue

Patient service revenue and contractual and other allowances consisted of the following for the years ended September 30:

	<u>2011</u>	<u>2010</u>
Patient services		
Inpatient	\$ 28,831,889	\$ 19,552,623
Outpatient	<u>74,322,048</u>	<u>74,522,054</u>
Gross patient service revenue	<u>103,153,937</u>	<u>94,074,677</u>
Less Medicare and Medicaid allowances	26,494,947	21,478,967
Less other contractual allowances	16,573,892	16,920,966
Less charity care and other discounts	<u>1,105,159</u>	<u>1,101,191</u>
	<u>44,173,998</u>	<u>39,501,124</u>
Patient service revenue (net of contractual allowances and discounts)	58,979,939	54,573,553
Less provision for bad debts	<u>2,326,120</u>	<u>3,102,565</u>
Net patient service revenue	<u>\$ 56,653,819</u>	<u>\$ 51,470,988</u>

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

Patient Accounts Receivable

Patient accounts receivable consisted of the following at September 30:

	<u>2011</u>	<u>2010</u>
Gross patient accounts receivable	\$ 20,101,989	\$ 13,752,544
Less: Estimated contractual allowances	6,871,589	3,495,569
Estimated allowance for doubtful accounts and charity care	<u>3,160,520</u>	<u>3,472,818</u>
Net patient accounts receivable	<u>\$ 10,069,880</u>	<u>\$ 6,784,157</u>

During 2011, the Hospital decreased its estimate from \$2,828,932 to \$2,267,426 in the allowance for doubtful accounts relating to self-pay patients and increased such estimate from \$643,887 to \$893,094 for doubtful accounts relating to third-party payors. During 2011, self-pay write-offs increased from \$2,177,218 to \$3,572,590. Such increases resulted from trends experienced in the collection of amounts from self-pay patients and third-party payors.

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. These payment arrangements include:

Medicare

On December 31, 2005, the Hospital became a Critical Access Hospital (CAH). As a CAH, the Hospital is reimbursed at 101% of reasonable allowable costs for its inpatient and outpatient services excluding ambulance services, provided to Medicare patients. The Hospital is reimbursed for cost reimbursable items at tentative rates, with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through September 30, 2009.

Medicaid

Inpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates. The prospectively determined rates are not subject to retroactive adjustment. Outpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates and therefore are not subject to retroactive adjustments.

Other Arrangements

The Hospital has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

Approximately 55% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended September 30, 2011 and 2010. The Hospital has agreements with the Centers for Medicare and Medicaid Services (Medicare) and the Office of Vermont Health Access (Medicaid). Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation as well as significant regulatory action, including fines, penalties and exclusion from the Medicare and Medicaid programs. Differences between amounts previously estimated and amounts subsequently determined to be recoverable or payable are included in net patient service revenues in the year that amounts become known. In 2011, net patient service revenue increased by approximately \$95,000, and in 2010, net patient service revenue decreased by approximately \$281,000 due to removal of allowances or recognition of settlements no longer subject to audits, reviews and investigations.

The Hospital recognizes patient service revenue associated with services rendered to patients who have third-party payor coverage on the basis of contractual rates for such services. For uninsured patients that do not qualify for charity care, the Hospital recognizes revenue on the basis of its standard rates (or on the basis of discounted rates, if negotiated or provided by policy). Based on historical trends, a significant portion of the Hospital's uninsured patients will be unable or unwilling to pay for the services rendered. Thus, the Hospital records a provision for bad debts related to uninsured patients in the period the services are rendered. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized during fiscal year ended September 30, 2011 totaled \$58,979,939, of which \$55,772,535 was revenue from third-party payors and \$3,207,404 was revenue from self-pay patients. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized during fiscal year ended September 30, 2010 totaled \$54,573,553, of which \$51,724,053 was revenue from third-party payors and \$2,849,500 was revenue from self-pay patients.

3. Community Benefit

The Hospital provides services without charge, or at amounts less than its established rates, to patients who meet the criteria of its charity care policy. The criteria for charity care, which is granted on a sliding scale, consider gross income and family size as compared to the federal poverty guidelines (FPL). The maximum of 100% charity care will be granted if the gross income of the individual is up to 200% of FPL.

The net cost of charity care provided was approximately \$619,000 in 2011 and \$512,800 in 2010. The total cost estimate is based on an overall financial statement cost to charge ratio applied against gross charity care charges. In 2011 and 2010, 1.1% and 1.2%, respectively, of all services as defined by percentage of gross revenue was provided on a charity basis.

In 2011, of a total of 44 inpatients received their entire episode of service on a charity case basis. In 2010, of a total of 45 inpatients received their entire episode of service on a charity case basis.

In 2011, of a total of 975 outpatients received their entire episode of service on a charity case basis. In 2010, of a total of 1,072 outpatients received their entire episode of service on a charity case basis.

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

4. Investments and Investment Income

Assets limited as to use include the following at September 30:

	<u>2011</u>	<u>2010</u>
Held by trustee under debt agreement		
Cash and cash equivalents	\$ <u>337,031</u>	\$ <u>322,937</u>
Held by trustee - deferred compensation funding		
Cash and cash equivalents	\$ <u>412,630</u>	\$ <u>302,984</u>

Long-term investments include the following at September 30:

	<u>2011</u>	<u>2010</u>
Cash and cash equivalents	\$ 264,947	\$ 208,978
Mutual funds	295,672	311,982
Marketable equity securities	1,313,725	1,381,278
Corporate and taxable bonds	562,000	613,171
U.S. Government obligations and government securities	510,041	347,953
Government sponsored enterprises	<u>155,591</u>	<u>70,971</u>
	<u>\$ 3,101,976</u>	<u>\$ 2,934,333</u>

Total investment income is comprised of the following for the years ending September 30:

	<u>2011</u>	<u>2010</u>
Interest and dividend income	\$ 216,591	\$ 235,730
Net unrealized (losses) gains	(175,221)	89,849
Realized gains	<u>83,152</u>	<u>61,422</u>
	<u>\$ 124,522</u>	<u>\$ 387,001</u>

Total investment income is reflected in the statement of operations and changes in net assets as follows:

	<u>2011</u>	<u>2010</u>
Unrestricted net assets		
Other nonoperating income	\$ 134,040	\$ 370,521
Temporarily restricted net assets	<u>(9,518)</u>	<u>16,480</u>
	<u>\$ 124,522</u>	<u>\$ 387,001</u>

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

5. Property and Equipment

The major categories of property and equipment are as follows at September 30:

	<u>2011</u>	<u>2010</u>
Land and land improvements	\$ 2,146,053	2,130,386
Buildings and leasehold improvements	24,934,247	24,277,080
Equipment	18,675,744	13,132,529
Construction in progress	<u>120,744</u>	<u>1,453,258</u>
	45,876,788	40,993,253
Less accumulated depreciation	<u>17,063,884</u>	<u>14,306,350</u>
Property and equipment, net	<u>\$ 28,812,904</u>	<u>\$ 26,686,903</u>

Construction in progress as of September 30, 2011 and 2010, consists of costs related to an information technology system conversion. The project is expected to be completed by September 2012, with an estimated cost of completion of \$4,359,000. As of September 30, 2011, the Hospital has committed \$1,500,000 to complete the project.

6. Beneficial Interest in Perpetual Trusts

The Hospital is an income beneficiary of two perpetual trusts controlled by an unrelated third-party trustee. The beneficial interests in the assets of these trusts are included in the Hospital's financial statements as permanently restricted net assets. Income is distributed in accordance with the individual trust documents and is included in investment return. Trust income distributed to the Hospital for the years ended September 30, 2011 and 2010, was \$138,366 and \$141,645, respectively.

7. Borrowings

Long-term debt consisted of the following as of September 30:

	<u>2011</u>	<u>2010</u>
Vermont Educational and Health Buildings Financing Agency (VEHBFA) Variable Rate Demand Hospital Revenue Bonds, 2005 Series A bonds with variable interest (.15% at September 30, 2011), payable in annual installments ranging from \$335,000 to \$890,000 through December 2035; collateralized by the gross receipts of the Hospital.	\$ 14,220,000	\$ 14,540,000

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Note payable at a fixed interest rate of 4.7%, monthly payments of \$24,400, due March 2015; collateralized by certain equipment.	928,113	1,201,070
Note payable at variable interest rate of (4% at September 30, 2011), monthly payments of \$1,743, with the remaining principal, due March 2019; collateralized by certain property.	207,292	221,292
Note payable at a fixed interest rate of 7.5%, monthly payments of \$1,329, paid in full at September 30, 2011.	-	38,971
Capital lease obligations at various rates with monthly payments ranging from \$349 to \$37,110, due 2012 through 2016; collateralized by leased equipment.	<u>2,203,544</u>	<u>1,006,615</u>
	17,558,949	17,007,948
Less current portion	<u>1,385,558</u>	<u>978,213</u>
	<u>\$ 16,173,391</u>	<u>\$ 16,029,735</u>

Letter of Credit

As part of the bond covenants, the Hospital is required to maintain a letter of credit. The letter of credit is issued by a bank in the amount of the outstanding principal balance plus 45 days interest calculated at 10%, which, in turn, is secured by the gross receipts of the Hospital. The current letter of credit expires September 30, 2013.

In connection with the letter of credit securing the 2005 Series A bonds, the Hospital is subject to certain financial covenants which include capitalization and debt service ratio coverage, restrictions on acquisition of new indebtedness, disposition of properties, consolidations or mergers and transfers of assets between affiliated companies. The Hospital is in compliance with all of these financial covenants.

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

Aggregate annual maturities of long-term debt and payments on capital lease obligations at September 30, 2011, are:

	Long-Term Debt (Excluding Capital Lease Obligations)	Capital Lease Obligations
2012	\$ 552,319	\$ 861,606
2013	637,000	784,545
2014	666,600	628,071
2015	549,700	88,512
2016	421,000	29,504
Thereafter	<u>12,528,786</u>	<u>-</u>
	<u>\$ 15,355,405</u>	2,392,238
Less amounts representing interest		<u>(188,694)</u>
		<u>\$ 2,203,544</u>

8. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available for the following purpose or periods:

	<u>2011</u>	<u>2010</u>
Health care services	\$ 44,721	\$ 58,843
Purchase of equipment	2,787	76,282
Indigent care	<u>236,380</u>	<u>236,380</u>
	<u>\$ 283,888</u>	<u>\$ 371,505</u>

Permanently restricted net assets are restricted to:

	<u>2011</u>	<u>2010</u>
Investments to be held in perpetuity, the income is restricted for indigent care	\$ 117,682	\$ 117,682
Beneficial interest in perpetual trusts, the income is unrestricted	<u>2,851,219</u>	<u>2,952,405</u>
	<u>\$ 2,968,901</u>	<u>\$ 3,070,087</u>

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

9. **Assets Held in Trust**

The Hospital is a contingent income beneficiary of various trusts. Because the Hospital has only a contingent interest in the assets of the trust, they are not included in the Hospital's financial statements. The fair value of the assets totaled approximately \$3,458,000 and \$3,581,000 on September 30, 2011 and 2010, respectively. Distributions of income are made at the discretion of the trustees. Income distributed to the Hospital by the trust is restricted for indigent care and amounted to \$186,633 in 2011 and \$171,793 in 2010.

10. **Other Operating Revenue**

Other operating revenue consisted of the following for the year ended September 30:

	<u>2011</u>	<u>2010</u>
Rental income	\$ 125,193	\$ 136,856
Cafeteria and coffee shop income	137,529	135,813
Miscellaneous revenue	275,437	137,834
Disproportionate Share Payments	1,158,110	1,085,929
Foundation revenue	-	495,507
Lifeline income	<u>109,827</u>	<u>138,996</u>
Total other revenue	<u>\$ 1,806,096</u>	<u>\$ 2,130,935</u>

11. **Other Program Income, net**

Other program income, net represents the net income resulting from the federal 340(b) Drug Pricing Program. The Program provides for discounts and reduced prices on medications because the Hospital as a qualified federal grantee (as a Critical Access Hospital). In addition to savings for medications used within the Hospital, the Hospital has also established contracts with five local pharmacies during 2011. Revenue from prescriptions filled by these contract pharmacies is recorded as "other program revenue." The Hospital paid all expenses for the drugs dispensed by the contract pharmacies at wholesaler cost. The Hospital also paid the contract pharmacies a dispensing fee for filling the prescriptions. These expenses are treated as "other expense" by the Hospital. The net of these three amounts resulted in net program income of \$1,428,863 for the year ended September 30, 2011.

12. **Functional Expenses**

The Hospital provides health care services primarily to residents within its geographic area. Expenses related to providing these services are as follows:

	<u>2011</u>	<u>2010</u>
Health care services	\$ 50,753,256	\$ 49,131,536
General and administrative	<u>7,077,598</u>	<u>6,851,447</u>
	<u>\$ 57,830,854</u>	<u>\$ 55,982,983</u>

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

13. **Concentration of Credit Risk**

The Hospital grants credit without collateral to its patients, most of whom are area residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at September 30, 2011 and 2010, is:

	<u>2011</u>	<u>2010</u>
Medicare	36 %	27 %
Medicaid	9	8
Commercial and other	28	31
Self-pay	<u>27</u>	<u>34</u>
	<u>100 %</u>	<u>100 %</u>

The Hospital maintains a substantial portion of its cash and cash equivalents in bank accounts which at times may exceed federally insured limits. The Hospital has not experienced any losses on such accounts. The Hospital believes it is not exposed to any significant risk on cash and cash equivalents.

14. **Commitments and Contingencies**

Medical Malpractice Claims

The Hospital purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. GAAP requires a health care provider to accrue the expense of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Hospital's claim experience, no such accrual has been made. It is reasonably possible that this estimate could change materially in the near term.

Guarantees

The Hospital guarantees certain third-party debts of an unconsolidated affiliated organization. The guarantee terms are for periods of 9 and 14 years. Should the Hospital be obligated to perform under the guarantee agreements, the Hospital may seek reimbursement from the related organization of amounts expended under the guarantees. At September 30, 2011 and 2010, the total outstanding balances on the guaranteed loans were approximately \$447,000 and \$517,500, respectively.

Self-Insurance

PMC is self-insured for employee health care benefits. PMC accrues a liability for employee health care by charging the statement of operations for certain known claims and reasonable estimates for incurred, but not reported, claims based on claims experience. The amount of actual losses incurred could differ materially from these estimates in the near term.

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

Litigation

In the normal course of business, the Hospital is, from time to time, subject to allegations that may or do result in litigation. The Hospital evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of counsel, management records an estimate of the amount of ultimate expected loss, if any, for each of these matters. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

15. Benefit Plans

Defined Contribution Plan

PMC has a 403(b) defined contribution pension plan covering substantially all Hospital employees. PMC makes an employer contribution to the plan. In order to receive the contribution, employees must meet certain eligibility requirements. PMC will make contributions between 3% and 6% of covered payroll based on the employee's years of service and employees' ages as of January 1, 2007.

The Hospital has estimated a liability of approximately \$794,000 and \$690,000 at September 30, 2011 and 2010, respectively, related to the 403(b) plan. This amount has been included in other accrued expenses. Contributions are calculated on a calendar year basis, and are paid following the end of the calendar year. Contributions to the plan were approximately \$935,000 and \$873,000 for calendar years 2011 and 2010, respectively.

Deferred Compensation Plan

The Hospital has a nonqualified deferred compensation plan established under section 457 of the Internal Revenue Code of 1986. These plans cover a key employee of the Hospital. The Hospital does not contribute to this plan.

Defined Benefit Plan

PMC has a noncontributory defined benefit pension plan covering all Hospital employees who meet the eligibility requirements. PMC's funding policy is to make the minimum annual contribution that is required by applicable regulations, plus such amounts as PMC may determine to be appropriate from time to time. PMC expects to contribute \$133,212 to the plan in 2012.

PMC has adopted FASB ASC 715, *Compensation-Retirement Benefits*. The defined benefit pension plan has been frozen since April 2007, therefore, the adoption of these provisions had no effect on the balance sheet and statement of operations and changes in net assets of PMC.

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

The Hospital's share of the net pension accrual was a pension liability of \$2,515,825 and \$2,418,302 at September 30, 2011 and 2010, respectively. The Hospital's share of the pension expense was \$162,051 and \$145,428 for the years ending September 30, 2011 and 2010, respectively. The Hospital contributed \$411,000 and \$100,000 to the plan in 2011 and 2010, respectively.

PMC uses a September 30, 2011 measurement date for the plan. Significant balances, costs and assumptions for the plan as a whole are:

	<u>2011</u>	<u>2010</u>
Benefit obligations	\$(10,942,491)	\$(10,690,102)
Fair value of plan assets	<u>7,679,106</u>	<u>7,646,052</u>
Funded status	<u>\$ (3,263,385)</u>	<u>\$ (3,044,050)</u>

The tables below present details about the Plan, including its funded status, components of net periodic benefit cost and certain assumptions used to determine the funded status and cost:

	<u>2011</u>	<u>2010</u>
Change in benefit obligation		
Benefit obligation at beginning of year	\$10,690,102	\$ 9,744,578
Interest cost	554,076	553,482
Actuarial (gain) loss	(24,710)	647,213
Benefits paid	<u>(276,977)</u>	<u>(255,171)</u>
Benefit obligation at end of year	<u>\$10,942,491</u>	<u>\$10,690,102</u>
Change in plan assets		
Fair value of plan assets at beginning of year	\$ 7,646,052	\$ 7,274,994
Actual return on plan assets	(101,595)	526,229
Employer contributions	411,626	100,000
Benefits paid	<u>(276,977)</u>	<u>(255,171)</u>
Fair value of plan assets at end of year	<u>\$ 7,679,106</u>	<u>\$ 7,646,052</u>
Components of net periodic benefit cost		
Interest cost	\$ 554,076	\$ 553,482
Expected return on plan assets	(516,972)	(490,199)
Amortization of net loss	<u>163,718</u>	<u>124,366</u>
Net periodic benefit cost	<u>\$ 200,822</u>	<u>\$ 187,649</u>

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Weighted average assumptions used to determine benefit obligation		
Discount rate	5.50 %	5.25 %
Weighted average assumptions used to determine benefit cost		
Discount rate	5.25	5.75
Expected return on assets	6.85	6.85

PMC has estimated the long-term rate of return on plan assets based primarily on historical returns on plan assets, adjusted for changes in target portfolio allocations and recent changes in long-term interest rates based on publicly available information.

The following benefit payments are expected to be paid as of September 30, 2011:

2011	\$ 325,864
2012	377,573
2013	396,178
2014	442,799
2015	475,394
2016 - 2020	2,985,271

Plan assets are held by a bank-administered trust fund, which invests the plan assets in accordance with the provisions of the plan agreement. The plan agreement permits investment in common stocks, corporate bonds and debentures, U.S. government securities, certain insurance contracts, real estate and other specified investments, based on certain target allocation percentages.

Asset allocation is primarily based on a strategy to provide stable earnings while still permitting the plans to recognize potentially higher returns through a limited investment in equity securities. Plan assets are rebalanced quarterly. At September 30, 2011 and 2010, plan assets by category are as follows:

	<u>2011</u>	<u>2010</u>
Equity securities	43.0 %	47.4 %
Debt securities	49.2	45.3
Other assets	<u>7.8</u>	<u>7.3</u>
	<u>100.0 %</u>	<u>100.0 %</u>

No amounts are expected to be recognized in the next year as components of net periodic benefit cost related to items previously recognized in unrestricted net assets. No plan assets are expected to be returned to PMC in 2012.

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

Risks

The Plan invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported.

16. Health Care Improvement Tax

Effective July 1, 1991, a health care improvement tax was imposed on medical centers, nursing homes and home health agencies as part of a program to upgrade services in Vermont. The State of Vermont pays the Hospital with funds received from the health care improvement trust fund and federal matching funds. The assessment rate for subsequent years will be determined annually by the General Assembly. A foundation associated with the Vermont Association of Hospitals and Health Systems redistributes amounts from hospitals who receive state funds in excess of their Medicaid assessment. The following tax was paid and funds received by the Hospital:

	<u>2011</u>	<u>2010</u>
Medicaid assessment	\$ 3,158,424	\$ 2,483,444
Disproportionate Share Payments	<u>(1,158,110)</u>	<u>(1,085,929)</u>
	2,000,314	1,397,515
Foundation revenue, included in other revenue	<u>-</u>	<u>(495,507)</u>
	<u>\$ 2,000,314</u>	<u>\$ 902,008</u>

17. Operating Leases

Noncancelable operating leases for primary care outpatient offices expire in various years through May 2013. These leases generally contain renewal options for periods ranging from three to six years and require the Hospital to pay all executory costs.

Future minimum lease payments at September 30, 2011, were:

2012	\$ 801,000
2013	613,000
2014	444,000
2015	444,000
2016	<u>304,000</u>
	<u>\$ 2,606,000</u>

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

18. Related Party Transactions

Revenues and Expenses

The Hospital contracts for services and provides services to related parties. A description of the services provided and amounts recorded as revenue (expense) by the Hospital is as follows during the years ended September 30:

	<u>2011</u>	<u>2010</u>
HPNH		
Medical Director	\$ 15,444	\$ 15,447
Employee physicals	31,419	16,268
Speech therapy services	(8,988)	(11,275)
Resident medical testing	69,436	107,935
PMS		
Management services	(594,312)	(1,855,628)
Administrative services	(1,107,456)	(1,217,601)
Fiscal services	-	(94,875)
Employee physicals	901	6,809
PREH		
Facility rent	(108,970)	(142,320)
Interest income	2,370	2,539

Accounts Receivable

Accounts receivable from related parties were as follows as of September 30:

	<u>2011</u>	<u>2010</u>
HPNH	\$ 102,114	\$ 60,781
PREH	66,926	3,457
PMS	70,516	352,707
PMC	<u>780</u>	<u>11,245</u>
	<u>\$ 240,336</u>	<u>\$ 428,190</u>

PORTER HOSPITAL, INC.
Notes to Financial Statements
September 30, 2011 and 2010

Accounts Payable

Accounts payable to related parties were as follows as of September 30:

	<u>2011</u>	<u>2010</u>
HPNH	\$ 1,650	\$ 1,188
PMS	146,775	309,274
PMC	<u>263</u>	<u>182</u>
	<u>\$ 148,688</u>	<u>\$ 310,644</u>

Note Receivable

Note receivable from PREH is as follows as of September 30:

	<u>2011</u>	<u>2010</u>
6% unsecured note receivable, monthly payments of \$441 including principal and interest, due February 21, 2021	\$ 37,897	\$ 40,818
Less current portion	<u>3,103</u>	<u>2,922</u>
	<u>\$ 34,794</u>	<u>\$ 37,896</u>

19. Fair Value Measurements

FASB ASC 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, and other inputs that are observable or can be corroborated by observable market data.

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

Level 3: Significant unobservable inputs that reflect an entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Assets and liabilities measured at fair value on a recurring basis are summarized below.

	<u>Fair Value Measurements at September 30, 2011</u>			
	<u>Total</u>	<u>Quoted Prices In Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Assets:				
Investments				
Cash and cash equivalents	\$ 264,927	\$ 264,927	\$ -	\$ -
Corporate and taxable bonds	562,000	-	562,000	-
U.S. Treasury obligations and government securities	510,041	510,041	-	-
Government sponsored enterprises	155,591	-	155,591	-
Marketable equity securities	-	-	-	-
Basic materials	28,845	28,845	-	-
Communication services	39,013	39,013	-	-
Consumer staple	142,096	142,096	-	-
Consumer discretionary	126,126	126,126	-	-
Energy	149,719	149,719	-	-
Financial services	169,501	169,501	-	-
Healthcare	170,202	170,202	-	-
Industrials	121,547	121,547	-	-
Technology	233,005	233,005	-	-
Utilities	30,679	30,679	-	-
Miscellaneous	<u>102,992</u>	<u>102,992</u>	-	-
Total marketable equity securities	<u>1,313,725</u>	<u>1,313,725</u>	-	-
Mutual funds	-	-	-	-
Growth funds	87,789	87,789	-	-
Equity funds	158,604	158,604	-	-
Bond funds	15,197	15,197	-	-
International funds	<u>34,082</u>	<u>34,082</u>	-	-
Total mutual funds	<u>295,672</u>	<u>295,672</u>	-	-
Deferred compensation plan assets:				
cash and cash equivalents	412,630	412,630	-	-
Beneficial interest in perpetual trusts	<u>2,851,219</u>	-	-	<u>2,851,219</u>
Total assets	<u>\$ 6,365,805</u>	<u>\$ 2,796,995</u>	<u>\$ 717,591</u>	<u>\$ 2,851,219</u>

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

	<u>Total</u>	<u>Quoted Prices In Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Pension assets:				
Cash and cash equivalents	\$ 591,426	\$ 591,426	\$ -	\$ -
Mutual funds	-	-	-	-
Growth funds	972,862	972,862	-	-
Equity funds	2,330,897	2,330,897	-	-
Bond funds	<u>3,777,562</u>	<u>3,777,562</u>	-	-
Total mutual funds	<u>7,081,321</u>	<u>7,081,321</u>	-	-
Accrued interest	<u>6,359</u>	<u>6,359</u>	-	-
Total pension assets	<u>\$ 7,679,106</u>	<u>\$ 7,679,106</u>	<u>\$ -</u>	<u>\$ -</u>

Significant activity for the year ended September 30, 2011 for assets measured at fair value on a recurring basis using unobservable inputs (Level 3) is as follows:

Level 3 investments at October 1, 2010	\$ 2,952,405
Net appreciation of beneficial interest in perpetual trusts	<u>(101,186)</u>
Level 3 investments at September 30, 2011	<u>\$ 2,851,219</u>

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

	Fair Value Measurements at September 30, 2010			
	Total	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Investments				
Cash and cash equivalents	\$ 208,978	\$ 208,978	\$ -	\$ -
Corporate and taxable bonds	613,171	-	613,171	-
U.S. Treasury obligations and government securities	347,953	347,953	-	-
Government sponsored enterprises	70,971	-	70,971	-
Marketable equity securities	-	-	-	-
Basic materials	48,228	48,228	-	-
Communication services	51,011	51,011	-	-
Consumer discretionary	96,574	96,574	-	-
Consumer staple	183,759	183,759	-	-
Energy	164,989	164,989	-	-
Financial services	195,901	195,901	-	-
Healthcare	171,296	171,296	-	-
Industrials	204,857	204,857	-	-
Technology	224,008	224,008	-	-
Utilities	40,655	40,655	-	-
Total marketable equity securities	<u>1,381,278</u>	<u>1,381,278</u>	<u>-</u>	<u>-</u>
Mutual funds				
Growth funds	85,196	85,196	-	-
Equity funds	170,869	170,869	-	-
Bond funds	14,663	14,663	-	-
International funds	41,254	41,254	-	-
Total mutual funds	<u>311,982</u>	<u>311,982</u>	<u>-</u>	<u>-</u>
Deferred compensation plan assets:				
cash and cash equivalents	302,984	302,984	-	-
Beneficial interest in perpetual trust	<u>2,952,405</u>	<u>-</u>	<u>-</u>	<u>2,952,405</u>
Total assets	<u>\$ 6,189,722</u>	<u>\$ 2,553,175</u>	<u>\$ 684,142</u>	<u>\$ 2,952,405</u>

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

	<u>Total</u>	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Pension assets:				
Cash and cash equivalents	\$ 522,812	\$ 522,812	\$ -	\$ -
Corporate bonds	1,018,165	-	1,018,165	-
US Treasury obligations and government securities	2,445,736	2,445,736	-	-
Marketable equity securities	-	-	-	-
Basic materials	85,416	85,416	-	-
Communication services	75,636	75,636	-	-
Consumer discretionary	300,304	300,304	-	-
Consumer staples	145,996	145,996	-	-
Energy	253,184	253,184	-	-
Financial services	357,617	357,617	-	-
Healthcare	275,245	275,245	-	-
Industrials	293,684	293,684	-	-
Technology	432,420	432,420	-	-
Utilities	<u>88,185</u>	<u>88,185</u>	-	-
Total equities	<u>2,307,687</u>	<u>2,307,687</u>	-	-
Mutual funds				
Growth funds	381,854	381,854	-	-
Equity funds	<u>932,163</u>	<u>932,163</u>	-	-
Total mutual funds	<u>1,314,017</u>	<u>1,314,017</u>	-	-
Accrued interest	<u>37,635</u>	<u>37,635</u>	-	-
Total pension assets	<u>\$ 7,646,052</u>	<u>\$ 6,627,887</u>	<u>\$ 1,018,165</u>	<u>\$ -</u>

Significant activity for the year ended September 30, 2010, for assets measured at fair value on a recurring basis using unobservable inputs (Level 3) is as follows:

Level 3 investments at October 1, 2009	\$ 2,542,132
Net appreciation of beneficial interest in perpetual trusts	<u>410,273</u>
Level 3 investments at September 30, 2010	<u>\$ 2,952,405</u>

The fair value of Level 2 assets is primarily based on quoted market prices of underlying assets or comparable securities. The fair value of Level 3 assets is based on the Medical Centers share of underlying assets of the trust. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

PORTER HOSPITAL, INC.

Notes to Financial Statements

September 30, 2011 and 2010

The Hospital's financial instruments consist of cash and cash equivalents, marketable securities, trade accounts receivable and payable, estimated third-party payor settlements and long-term debt. The fair values of all financial instruments approximate their carrying values at September 30, 2011 and 2010.

SUPPLEMENTARY INFORMATION

PORTER HOSPITAL, INC.

Schedule of Required Financial Covenant Ratios

Year Ended September 30, 2011

Debt Service Coverage Ratio

Income available for debt service:	
Increase in unrestricted net assets	\$ 2,012,113
Net unrealized losses on investments	175,221
Depreciation and amortization	3,431,186
Interest expense	314,456
Change in net assets to recognize funded status of pension plan	<u>347,098</u>
Income available for debt service	<u>\$ 6,280,074</u>
Interest expense	\$ 314,456
Current portion of long-term debt	<u>1,385,558</u>
Annual debt service	<u>\$ 1,700,014</u>
Debt service coverage ratio required to be no less than 1.5	3.69

Debt to Total Capitalization

Long-term debt	<u>\$ 17,558,949</u>
Long-term debt	\$ 17,558,949
Unrestricted net assets	21,283,161
Temporarily restricted net assets	<u>283,888</u>
Total capitalization	<u>\$ 39,125,998</u>
Debt to total capitalization required to be less than 60%	45 %

PORTER HOSPITAL, INC.

Note to Supplemental Schedule of Calculations of Required Financial Covenant Ratios

Year Ended September 30, 2011

Basis of Accounting

The accompanying Supplemental Schedule of Required Financial Covenant Ratios has been prepared in accordance with Section 5.09 of the Letter of Credit Reimbursement Agreement dated June 1, 2005, between Porter Hospital, Inc. and TD Bank. The Debt Service Coverage Ratio and Debt to Total Capitalization have been derived from the financial statements of Porter Hospital, Inc. for the year ended September 30, 2011.

