SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Consolidated Financial Statements and Other Financial Information

June 30, 2010 and 2009

(With Independent Auditors' Report Thereon)

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

Independent Auditors' Report

The Board of Trustees
Sheppard and Enoch Pratt Foundation, Inc.:

We have audited the accompanying consolidated balance sheet of Sheppard and Enoch Pratt Foundation, Inc. and subsidiaries (collectively, Foundation) as of June 30, 2010, and the related consolidated statements of operations, changes in net assets and cash flows for the year then ended. These consolidated financial statements are the responsibility of Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audit. The accompanying consolidated financial statements of Foundation as of June 30, 2009 were audited by other auditors, whose report thereon dated November 10, 2009, expressed an unqualified opinion on those statements.

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

In our opinion, the 2010 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Foundation at June 30, 2010, and the consolidated results of its operations and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

KPMG LLP

October 11, 2010

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

June 30, 2010 and 2009

Assets		**2010**	**2009**
Current assets:			
Cash and cash equivalents	$	40,342,845	25,967,174
Temporary investments		735,545	785,523
Investments limited or restricted as to use		2,978,971	3,597,810
Accounts receivable, net		29,117,328	28,190,391
Current portion of notes receivable		125,949	75,982
Prepaid expenses and other current assets		6,959,512	8,690,297
Total current assets		80,260,150	67,307,177
Investments limited or restricted as to use, less current portion		123,263,426	114,599,193
Notes receivable		2,865,469	2,931,729
Property and equipment, net		190,946,694	197,346,005
Other assets		6,585,194	6,064,441
Total assets	$	403,920,933	388,248,545
Liabilities and Net Assets			
Current liabilities:			
Current maturities of long-term debt	$	4,355,042	3,143,989
Current portion of obligations under capital leases		427,467	345,547
Note payable		—	16,900,000
Accounts payable		7,293,981	9,852,374
Accrued salaries, wages and employee benefits		19,218,715	16,256,839
Third-party payor settlements payable		3,871,279	4,325,534
Other accrued expenses		6,920,213	6,613,596
Total current liabilities		42,086,697	57,437,879
Long-term liabilities:			
Long-term debt, less current portion		109,555,839	98,906,881
Obligations under capitalized leases, less current portion		4,585,496	5,051,925
Self-insurance liabilities		4,688,915	4,710,462
Accrued pension liabilities		34,905,313	17,836,432
Other long-term liabilities		2,166,218	1,875,029
Total liabilities		197,988,478	185,818,608
Net assets:			
Unrestricted		196,455,886	192,383,617
Temporarily restricted		6,008,074	6,622,845
Permanently restricted		3,468,495	3,423,475
Total net assets		205,932,455	202,429,937
Total liabilities and net assets	$	403,920,933	388,248,545

See accompanying notes to consolidated financial statements.

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Consolidated Statements of Operations

Years ended June 30, 2010 and 2009

		2010	**2009**
Unrestricted revenues, gains, and other support:			
Net patient service revenue	$	118,174,102	112,943,644
Residential and educational service revenue		130,149,957	124,171,682
Net assets released from restrictions used for operations		1,221,420	918,340
Realized gain on disposal of assets		19,100	—
Other revenue		15,161,184	15,738,264
Total unrestricted revenues, gains, and other support		264,725,763	253,771,930
Expenses:			
Salaries and wages		143,408,801	138,147,804
Employee benefits		34,096,512	31,468,979
Expendable supplies		15,200,481	15,302,788
Purchased services		38,104,502	40,767,465
Interest		3,892,519	4,529,164
Repairs and minor alterations		6,583,953	5,861,939
Depreciation and amortization		14,889,995	14,548,396
Provision for doubtful accounts		7,544,158	5,333,455
Net realized loss on disposal of assets		—	36,937
Total expenses		263,720,921	255,996,927
Operating gain (loss)		1,004,842	(2,224,997)
Other (expense) income:			
Investment income		2,329,920	3,731,756
Net realized gain (loss) on investments		4,391,858	(7,201,497)
Change in net unrealized gain (loss) on investments		6,086,719	(11,636,277)
Other		490,397	457,491
Total other income (expense)		13,298,894	(14,648,527)
Excess (deficiency) of revenues over expenses		14,303,736	(16,873,524)
Other changes in net assets:			
Net assets released from restrictions used for purchases of property and equipment		317,155	1,102,681
Pension liability adjustment		(10,998,679)	(15,846,204)
Reclassification of net assets		450,057	—
Increase (decrease) in unrestricted net assets	$	4,072,269	(31,617,047)

See accompanying notes to consolidated financial statements.

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Consolidated Statements of Changes in Net Assets

Years ended June 30, 2010 and 2009

		2010	2009
Unrestricted net assets:			
Excess (deficiency) of revenues over expenses	$	14,303,736	(16,873,524)
Other changes in net assets:			
Net assets released from restrictions used for purchases of property and equipment		317,155	1,102,681
Pension liability adjustment		(10,998,679)	(15,846,204)
Reclassification of net assets		450,057	—
Increase (decrease) in unrestricted net assets		4,072,269	(31,617,047)
Temporarily restricted net assets:			
Gifts and grants		925,577	3,201,642
Investment income		98,629	165,598
Net gain (loss) on investments		349,655	(590,467)
Net assets released from restrictions for operations		(1,221,420)	(918,340)
Net assets released from restrictions for purchases of property and equipment		(317,155)	(1,102,681)
Reclassification of net assets		(450,057)	—
(Decrease) increase in temporarily restricted net assets		(614,771)	755,752
Permanently restricted net assets:			
Gifts		1,500	230,535
Investment income (expense)		43,520	(77,353)
Increase in permanently restricted net assets		45,020	153,182
Increase (decrease) in net assets		3,502,518	(30,708,113)
Net assets, beginning of year		202,429,937	233,138,050
Net assets, end of year	$	205,932,455	202,429,937

See accompanying notes to consolidated financial statements.

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended June 30, 2010 and 2009

	2010	2009
Cash flows from operating activities:		
Increase (decrease) in net assets	$ 3,502,518	(30,708,113)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:		
Depreciation and amortization	14,889,995	14,548,396
Pension liability adjustment	10,998,679	15,846,204
Provision for doubtful accounts	7,544,158	5,333,455
Restricted gifts and grants, net	294,343	(2,513,837)
Net realized (gain) loss on investments	(4,497,244)	7,410,121
Net unrealized gain (loss) on investments	(6,399,904)	12,018,120
Restricted investment income on restricted net assets	(142,149)	(88,245)
Unrealized (gain) loss on interest rate swaps	(57,430)	197,144
Net settlement on interest rate swaps	244,062	192,833
(Gain) loss on disposal of assets	(19,100)	36,937
Increase in accounts receivable, net	(8,471,095)	(6,583,277)
Decrease in prepaid expenses and other current assets	2,074,056	1,032,319
Increase in accounts payable and accrued expenses and other	805,067	5,143,306
(Decrease) increase in self-insurance liabilities	(21,547)	1,603,048
(Decrease) increase in third-party payor settlements payable	(454,255)	166,941
Increase (decrease) in accrued pension liability	6,070,202	(12,814,298)
Net cash provided by operating activities	26,360,356	10,821,054
Cash flows from investing activities:		
Purchases of property and equipment	(9,205,822)	(15,794,646)
Decrease in temporary investments	49,978	267,246
Increase in other assets	(779,999)	(184,187)
Decrease in notes receivable	16,293	120,163
Proceeds from sale of property and equipment	882,687	—
Decrease (increase) in investments limited or restricted as to use, net	2,991,405	(1,699,133)
Net settlement on interest rate swaps	(244,062)	(192,833)
Net cash used in investing activities	(6,289,520)	(17,483,390)
Cash flows from financing activities:		
Proceeds from debt	15,311,800	1,831,969
Payment of note payable	(16,900,000)	—
Payment of long-term debt principal	(3,428,113)	(3,670,476)
Payment on capital lease obligations	(384,509)	(344,458)
Restricted gifts and grants, net	(294,343)	2,513,837
Net cash (used in) provided by financing activities	(5,695,165)	330,872
Net increase (decrease) in cash and cash equivalents	14,375,671	(6,331,464)
Cash and cash equivalents, beginning of year	25,967,174	32,298,638
Cash and cash equivalents, end of year	$ 40,342,845	25,967,174

See accompanying notes to consolidated financial statements.

(1) Summary of Significant Accounting Policies

(a) Organization

Sheppard and Enoch Pratt Foundation, Inc. (Foundation or the Company), a not-for-profit, nonstock Company, was organized on June 15, 1984 to engage in activities necessary to provide medical services to the public through the planning and implementation of programs provided by its various subsidiaries. Subsidiary companies, controlled by Foundation, include Sheppard Pratt Health System, Inc. (Health System), Sheppard Pratt Physicians, P.A. (Physicians), Sheppard Pratt Investment, Inc. (Investment Company), Mosaic Community Services, Inc. (Mosaic), Way Station, Inc. (Way Station), Family Services, Inc. (Family Services), Turning Point of Washington County, Inc. (Turning Point), The North Baltimore Center, Inc. (North Baltimore) and Sheppard Pratt Preferred Resources, Inc. (Resources).

Health System is a not-for-profit, nonstock company that operates two inpatient hospitals, day hospitals, residential and educational services for children and adolescents, and outpatient programs.

Physicians is a professional company of licensed medical professionals organized on July 1, 1985 exclusively to carry out the charitable, educational and scientific purposes of Foundation and its affiliates. The common stock of Physicians is held by several individuals who are employed by a member of Foundation, Health System, or Physicians and are subject to the terms of a stock agreement. Under the terms of the agreement, the stockholders are required to consult with Foundation regarding its views on any matter with respect to which the stockholder is entitled to vote, and the stockholders may not transfer shares (by sale or gift) without the permission of Foundation. The stock agreement does not allow for Stockholders to receive dividends or any other benefit for having held the stock. If the stockholder ceases to be employed by Foundation, Health System, or Physicians, Physicians shall require the stockholder to sell and transfer all of the stock such stockholder owns to a person designated by Foundation. The purchase price for each share of stock of the Company is $1 per share.

Investment Company is a not-for-profit, nonstock company which manages the investments of certain subsidiaries.

Mosaic, Way Station, Family Services, Turning Point and North Baltimore (collectively, the Affiliates) are not-for-profit, nonstock Maryland companies which provide residential, rehabilitation, vocational, and outpatient mental health services across the state of Maryland.

Resources is a for-profit company that was formed for the purpose of providing employee assistance program services to other entities. Resources was inactive as an operating entity for the years ended June 30, 2010 and 2009.

(b) Basis of Presentation

The consolidated financial statements are prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles. All majority-owned and affiliated member entities are consolidated. All entities where the Company exercises significant influence but for which it does not have control are accounted for under the equity method. All other entities are accounted for under the cost method. All significant intercompany accounts and transactions have been eliminated.

Net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. The net assets of Foundation and changes therein are classified and reported as follows:

> *Unrestricted net assets* – Net assets that are not subject to donor-imposed stipulations. Board-designated funds are included within this category of net assets.
>
> *Temporarily restricted net assets* – Net assets whose use by the Company has been limited by donors to a specific time or purpose.
>
> *Permanently restricted net assets* – Net assets that have been restricted by donors to be maintained by Sheppard Pratt in perpetuity. Generally, the donors of these assets permit Foundation to use all or part of the income earned on related investments for general or specific purposes.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Contributions with no donor-imposed restrictions are recognized as revenues in the period received as increases in unrestricted net assets.

Unconditional promises to give cash and other assets to Foundation with donor-imposed restrictions are reported as increases in temporarily or permanently restricted net assets at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. When the donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

(c) Charity Care

Foundation provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because Foundation does not pursue collection of amounts determined to qualify for charity care, such amounts are not reported as revenue.

(d) Cash and Cash Equivalents

Cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less that are not limited or restricted as to use.

(e) Temporary Investments

Temporary investments include short-term investments with an original maturity greater than three months and less than one year that are not limited or restricted as to use.

(f) Allowance for Doubtful Accounts

Foundation’s policy is to write off all accounts that have been identified as uncollectible. An allowance for uncollectibles is recorded for accounts not yet written off that are anticipated to become uncollectible in future periods. Insurance coverage and credit information are obtained from patients when available. No collateral is obtained for accounts receivable. Accounts receivable from third-party payors have been adjusted to reflect the difference between charges and the estimated reimbursable amounts.

(g) Investments Limited as to Use

Investments limited as to use, primarily recorded at fair value, represent assets that have been designated by the board of trustees for special purposes and investments held by the bank trustees under the bond indenture and self-insurance trust arrangements. The principal, income and capital appreciation of the Moses Sheppard and Enoch Pratt bequests are legally unrestricted but are classified, for financial reporting purposes, as board-designated and limited as to use. Assets designated by the board of trustees for particular purposes are controlled by the board of trustees, who at their discretion, may subsequently use the assets for other purposes.

Investments of board-designated, temporarily restricted and permanently restricted funds are maintained in a combined investment pool. Related income, realized and unrealized gains and losses on sales of investments are apportioned on the basis of the shares held by each of the respective funds and in accordance with donor restrictions on the use of investment earnings.

Investments are recorded at fair value. Foundation classifies its investment portfolio as trading securities with unrealized gains and losses included in other income (expense), which is in the excess of revenues over expenses. Realized gains or losses are included in other income (expense) in the accompanying statements of operations. The investment portfolio is classified as current or noncurrent assets based on management’s intention as to use.

Hedge funds represent both subscriptions in private equity venture capital funds and subscriptions in funds-of-funds utilized to diversify the portfolio of Foundation. Annual audited financial statements for these funds are submitted to Foundation and reviewed by management. The funds’ financial statements are presented at fair value as estimated in an unquoted market. Foundation’s hedge fund investments are accounted for under the equity method of accounting. The investment balance is equal to Foundation’s proportionate interest in the fund’s net equity. Individual investment holdings within the investment may, in turn, include investments in both nonmarketable and market-traded securities. Valuations of these 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. Certain of these investments contain additional capital call requirements, based upon the provisions of the investment agreements.

(Continued)

(h) Pledges

Pledges, less an allowance for uncollectible amounts, are recorded as receivables in the year the pledge is made unless the pledge carries conditions that have not been met. Conditional pledges are recorded as contributions when the conditions of the pledge have been satisfied. The fair value of pledges receivable is recorded at fair value and is calculated using a discount rate of 5.0% at June 30, 2010 and 2009.

(i) Property and Equipment

Property and equipment acquisitions are recorded at cost (except donated property and equipment which are recorded at their fair market value at the date of receipt). Depreciation is computed on the straight-line method and charged to operations over estimated useful lives ranging from twenty to forty years for buildings and improvements and three to ten years for furniture, equipment, automobiles and trucks. Property and equipment under capital lease obligations are amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the property and equipment. Interest costs incurred on borrowed funds during the period of construction are 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 other changes in unrestricted net assets, and are excluded from the excess of revenues over expenses, 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 those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

(j) Costs of Borrowing

Deferred financing costs and debt premiums are amortized using the effective interest method and charged to operations as a component of interest expense over the term of the related debt.

(k) Estimated Self-Insurance Liability Claims

The estimated self-insured professional liability claims are reflected as a liability and include actuarially determined estimates of the ultimate costs for both reported claims and claims incurred but not reported. Costs under self-insurance programs for employee health benefits and workers' compensation include estimates for both reported claims and claims incurred but not reported, based on an evaluation of pending claims and past experience.

(l) Pension Benefits

Pension benefits are recorded in accordance with *Defined Benefit Plans-Pension* (ASC Subtopic 715-30), which requires the recognition of the funded status of pension plans within the accompanying balance sheets. As of June 30, 2010 and 2009, the funded status of the pension plan has been recorded within other long-term liabilities.

(m) Patient Service Revenue

Foundation has agreements with third-party payors that provide for payments to Foundation at amounts different from its established rates. Payment arrangements include prospectively determined rates per day, reimbursed costs, discounted charges and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with certain third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Differences between the estimated amounts and final settlements are reported in operations in the year of settlement.

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

(n) Residential and Educational Service Revenue

Foundation provides Educational Services to special needs children under arrangements with the Maryland State Department of Education (MSDE). On an annual basis, a prospective rate per student is set with MSDE based upon an approved operating budget. Subsequently, as services are provided, invoices are submitted to each student's local school district for payment on a monthly basis.

Foundation also operates two levels of Residential services for Adolescents: Residential Treatment Centers (RTCs) and Respite Care. Substantially all of the RTC services are reimbursed by the State of Maryland Medicaid Program on a cost basis subject to annual ceilings. Foundation receives an interim per diem rate during the year and ultimately settles final payment based upon an audited cost report filing. Respite Services are provided through a Purchase of Care Agreement with the Maryland Department of Human Resources. Services are provided and reimbursed on an interim per diem basis and are subject to cost settlement based upon an audit of the Program's operating expenses. Foundation accrues any difference between interim payments and estimates of expected cost settlement for both RTCs and Respite Care.

(o) Investment Income

Investment income from unrestricted cash equivalents, temporary investments, the self insurance trust and a portion of the debt service accounts maintained by bond trustees are reported as other operating revenue since such income is considered to be a part of Foundation's ongoing central operations of providing health care services.

Investment income and realized gains and losses from all other investments is reported as other income (expense), unless the income is restricted by donors which is reported as previously described above.

Unrealized gains and losses on trading securities are included as a component of other income (expense).

(p) Impairment of Long-Lived Assets

Management regularly evaluates whether events or changes in circumstances have occurred that could indicate an impairment in the value of long-lived assets. In accordance with the provisions of ASC Subtopic 360-10, *Property, Plant, and Equipment - Overall*, if there is an indication that the carrying amount of an asset is not recoverable, Foundation estimates the projected undiscounted cash flows, excluding interest, to determine if an impairment loss should be recognized. The amount of impairment loss is determined by comparing the historical carrying value of the asset to its estimated fair value. Estimated fair value is determined through an evaluation of recent and projected financial performance using standard industry valuation techniques.

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

In estimating the future cash flows for determining whether an asset is impaired and if expected future cash flows used in measuring assets are impaired, Foundation groups its assets at the lowest level for which there are identifiable cash flows independent of other groups of assets.

(q) Rental Income

Foundation has agreements with various organizations and individual clinicians to rent office space and land. Foundation recognizes the rent under the leases, using the straight-line method, net of an allowance for doubtful accounts, where necessary, in other income.

(r) Excess (Deficiency) of Revenues over Expenses

The consolidated statements of operations include a performance indicator, the excess (deficiency) of revenues over expenses. Changes in unrestricted net assets which are excluded from excess (deficiency) of revenues over expenses, consistent with industry practice, include changes in pension liability adjustments and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets).

(s) Income Taxes

Foundation and its subsidiaries, except for Resources, have been recognized as tax-exempt organizations under Section 501(a) as organizations described in Section 501(c)(3) of the Internal Revenue Code and are not subject to income taxes on related income pursuant to Section 501(a) of the Internal Revenue Code. The operations of Resources, a for-profit Company, are not significant to the consolidated financial statements.

(t) Derivative Instruments

Derivatives and Hedging – Overall (ASC Subtopic 815-10) establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, (collectively referred to as derivatives) and for hedging activities. ASC Subtopic 815-10 requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. Foundation's interest rate swaps do not qualify for hedge accounting under the provisions of ASC Subtopic 815-10; therefore, Foundation has accounted for these derivative instruments as speculative derivative instruments with the change in the fair value reflected in other income (expense) in the consolidated statements of operations in the period of change. The net settlement payments made or received during the life of the swap are recorded as an increase or decrease to other income. See note 10.

(u) Use of Estimates

The preparation of consolidated financial statements in conformity with United States generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures 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.

(v) Reclassifications

Certain reclassifications have been made to the prior year balances to conform to the current year presentation.

(2) New Accounting Pronouncements

In June 2009, the FASB issued guidance that eliminates the hierarchy of authoritative accounting and reporting guidance on nongovernmental GAAP and replaces it with a single authoritative source, the FASB Accounting Standards Codification (ASC). The ASC affects the way in which users refer to GAAP and perform accounting research, but does not change GAAP. This guidance is effective for reporting periods ending after September 15, 2009. The Company adopted the provisions of this guidance during the year ended June 30, 2010. The adoption did not have an impact on the Company's financial position or results of operations.

In January 2010, the FASB issued Accounting Standards Update No. 2010-06 (ASU 2010-06), *Improving Disclosures about Fair Value Measurements*. ASU 2010-06 amends ASC Topic 820, *Fair Value Measurements and Disclosures*, to require a number of additional disclosures regarding fair value measurements. Effective in fiscal year 2010, ASU 2010-06 requires disclosure of the amounts of significant transfers between Level I and Level II investments and the reasons for such transfers, the reasons for any transfers in or out of Level III investments, and disclosure of the policy for determining when transfers among levels are recognized. ASU 2010-06 also clarified that disclosures should be provided for each class of assets and liabilities and clarified the requirement to disclose information about the valuation techniques and inputs used in estimating Level II and Level III measurements. Effective in fiscal year 2011, ASU 2010-06 also requires that information in the reconciliation of recurring Level III measurements about purchases, sales, issuances and settlements be provided on a gross basis. The adoption of ASU 2010-06 only required additional disclosures and did not have an impact on the consolidated financial statements. As the Company does not have significant transfers between Levels, or any Level III measurements, no additional disclosures were necessary.

In December 2008, the FASB issued guidance related to *Employers' Disclosures about Postretirement Benefit Plan Assets* which amended previously issued guidance. The purpose of the guidance is to enhance disclosures and provide users' with information regarding the types of assets and associated risks in an employer's defined benefit pension or other postretirement plan and events in the economy and markets that could have a significant effect on the value of plan assets. The disclosures about plan assets required shall be provided for fiscal years ending after December 15, 2009. The Company adopted this disclosure requirement for the year ended June 30, 2010.

In April 2009, the FASB issued guidance related to *Not-for-Profit Entities: Mergers and Acquisitions Including an Amendment of FASB Statement No. 142*. This guidance establishes principles and requirements for how a not-for-profit entity determines whether a combination is a merger or an acquisition and amends previously issued guidance related to *Intangibles - Goodwill and Other*, to make it fully applicable to not-for-profit entities. The guidance is effective for mergers for which the merger date is on or after the beginning of an initial reporting period beginning on or after December 15, 2009; therefore, effective for the Company on January 1, 2010. The guidance is effective for acquisitions for which the acquisition date is on or after the beginning of the first *annual* reporting period beginning on or after December 15, 2009; therefore, effective for the Company on July 1, 2010. It may not be applied to mergers or acquisitions before those dates.

In July 2010, the FASB issued guidance related to *Health Care Entities: Presentation of Insurance Claims and Related Insurance Recoveries*. The purpose of this guidance is to distinguish between common health care industry practice and proper auditing presentation standards. This guidance clarifies that netting receivables for expected insurance recoveries with liabilities accrued for medical malpractice and other similar claims on the balance sheet is inconsistent with other industries and current accounting guidance, namely ASC Subtopic 720-20, *Insurance Costs*. The guidance also explains that offsetting receivables for expected insurance recoveries against a recognized liability would not be appropriate unless certain criteria of ASC Topic 210 are met. The Company will adopt this guidance on July 1, 2011.

In July 2010, the FASB issued guidance related to *Health Care Entities: Measuring Charity Care for Disclosure*. This guidance serves to further standardize the required charity care disclosures. Effective in fiscal year 2012, the Company will be required to disclose charity care provided during the year measured using cost instead of its current, and the most prevalent, measurement of the total charges forgone. Any related reimbursements recorded should be separately disclosed. Retrospective application is required with this guidance and early adoption is permitted. The Company will adopt this guidance in 2012.

(3) Charity Care and Community Services

Foundation maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy and equivalent service statistics. The following information measures the estimated level of charity care provided during the years ended June 30:

		2010	2009
Charges foregone, based upon established rates	$	8,200,330	3,031,333
Percentage of charges foregone to gross patient service revenue		3.64%	1.49%

In addition to the direct charity care noted above, Foundation accepts all patients covered by the Medicare and Medicaid programs. These programs reimburse Foundation at amounts less than charges. The difference between the charges for health care services and the related reimbursement amounts for these and other third-party payors is as follows for the years ended June 30:

		2010	2009
Medicare	$	13,342,097	11,251,657
Medicaid		11,817,667	9,748,388
Other third-party payors		7,566,346	7,191,320
	$	32,726,110	28,191,365

Foundation provides the community with other healthcare services and programs, including teaching of psychiatric residents, providing programs and facilities for teaching other medical health professionals, providing behavioral health educational programs for the general public, and conducting research to improve treatment of behavioral health problems.

(4) Investments Limited or Restricted as to Use

Investments limited or restricted as to use, stated at fair value, except for the real estate investment, which is recorded at cost and investments in partnerships and hedge funds, which are recorded under the equity method include the following at June 30:

		2010	2009
Board-designated, unrestricted:			
Portion of pooled investments	$	96,099,110	86,461,905
Other investments		5,939,603	4,366,127
Held by trustees:			
Under self-insurance trusts		4,595,465	5,778,498
Under bond indenture		11,376,517	12,126,914
Donor-restricted:			
Temporarily restricted portion of pooled investments		1,801,509	1,621,370
Other temporarily restricted investments		2,961,698	3,721,435
Permanently restricted portion of pooled investments		2,904,154	2,902,654
Other permanently restricted investments		564,341	1,218,100
Total investments limited or restricted as to use		126,242,397	118,197,003
Current portion		2,978,971	3,597,810
Investments limited or restricted as to use, less current portion	$	123,263,426	114,599,193

(Continued)

Foundation manages a significant component of its investments limited or restricted as to use in a combined investment pool. The combined investment pool has been allocated based on donor restrictions, where applicable, as follows at June 30:

		2010	2009
Board-designated unrestricted	$	96,099,110	86,461,905
Temporarily restricted		1,801,509	1,621,370
Permanently restricted		2,904,154	2,902,654
Total	$	100,804,773	90,985,929

The combined investment pool is comprised of the following at June 30:

		2010	2009
Cash equivalents	$	808,333	1,429,687
Bonds and short-term commercial paper		12,154,453	13,320,922
Marketable equity securities		24,198,287	5,969,764
Mutual funds		46,361,020	52,045,375
Other (including hedge funds under equity method)		17,282,680	18,220,181
Total	$	100,804,773	90,985,929

Other board-designated investments consist of the following at June 30:

		2010	2009
Cash and cash equivalents	$	1,709,127	557,625
Real estate held for future development, at cost		3,038,410	3,045,451
Other receivables related to investment transactions		1,192,066	763,051
	$	5,939,603	4,366,127

The funds held by trustees under self-insurance trusts is comprised of the following at June 30:

		2010	2009
Cash and cash equivalents	$	6,663	26,916
Fixed income investments		3,605,066	3,396,611
Equity investments		983,736	2,354,971
	$	4,595,465	5,778,498

(Continued)

The funds held by trustees under bond indentures is comprised of the following at June 30:

		2010	2009
Interest Fund	$	958,478	932,608
Debt Service Reserve Fund		5,978,249	6,057,043
Debt Service Principal Fund for 2003 Bonds		1,860,014	1,805,010
MHHEFA Bond Proceeds		—	595,857
Prefunded Bonds, North Baltimore and Mosaic		2,459,863	2,621,136
Sinking Fund for Way Station Debt		119,913	115,260
	$	11,376,517	12,126,914

The funds held by trustees under bond indentures is comprised of the following at June 30:

		2010	2009
Cash and cash equivalents	$	6,115,799	3,332,253
Fixed income investments		5,260,718	8,794,661
	$	11,376,517	12,126,914

The total investment return, net of investment fees, including the return from the combined investment pool, is summarized as follows for the years ended June 30:

	2010	2009
Investment income:		
Unrestricted	$ 2,329,920	3,731,756
Temporarily restricted	98,629	165,598
Permanently restricted	43,520	(77,353)
	2,472,069	3,820,001
Net realized gains (losses) on sales of investments:		
Unrestricted	4,385,609	(7,017,589)
Temporarily restricted	111,635	(208,624)
	4,497,244	(7,226,213)
Net unrealized gains (losses) on investments (excluding self-insurance trust assets):		
Unrestricted	6,071,433	(11,581,242)
Temporarily restricted	238,020	(381,843)
Total unrealized losses	6,309,453	(11,963,085)
Total investment return on combined investment pool	13,278,766	(15,369,297)
Investment return on other unrestricted investments and cash and cash equivalents	602,945	576,166
Investment return on self-insurance trust assets (including unrealized gains of $90,451 in 2010 and losses of $55,035 in 2009, respectively)	398,578	(159,433)
Total investment return	$ 14,280,289	(14,952,564)

(5) Temporarily Restricted Assets

Temporarily restricted net assets consist of the following at June 30:

		2010	2009
Pledges receivable, net of unamortized discount of $130,000 at June 30, 2010 and $166,000 at June 30, 2009	$	1,563,423	1,977,059
Less allowance for uncollectible pledges		63,000	64,000
Net pledges receivable		1,500,423	1,913,059
Other investments		2,415,101	2,771,063
Portion of pooled investments (note 4)		1,801,509	1,621,370
Way Station restricted cash		204,624	149,245
Family Services restricted cash		—	42,756
Mosaic restricted investments		86,417	125,352
	$	6,008,074	6,622,845

The fair value of the unconditional pledges receivable at June 30, 2010 was calculated using an average discount rate of 5%. The net present value of pledges receivable and the expected collection period at June 30, 2010 are as follows:

2011	$	1,158,387
2012		273,885
2013		89,182
2014		25,916
2015		13,191
Thereafter		2,862
	$	1,563,423

(6) Note Receivable

In connection with the land lease described in note 7, Investment Company provided a loan and a line of credit to the Maryland Economic Development Company (MEDCO) to help finance the development of university student housing located on the campus of Foundation. The unsecured term loan of $3.75 million is payable in equal quarterly installments between the initial repayment date (January 2004) and June 30, 2031. MEDCO repaid approximately $132,000 and $127,000 during the years ended June 30, 2010 and 2009, respectively, which resulted in an outstanding balance of $2,799,976 and $2,931,729 at June 30, 2010 and 2009, respectively. The loan bears interest at the rate of 12% per annum. Foundation has included approximately $347,000 and $371,000 of interest income from the loan in investment income during the fiscal years ended June 30, 2010 and 2009, respectively.

(7) Property and Equipment

Property and equipment at June 30 are summarized as follows:

	2010	2009
Land	$ 10,453,832	10,422,795
Land improvements	8,708,454	6,366,801
Buildings and building improvements	231,501,539	230,526,022
Furniture and equipment	49,283,134	45,642,027
Vehicles	4,888,080	4,740,838
Construction in progress	2,708,234	3,358,080
	307,543,273	301,056,563
Less accumulated depreciation	116,596,579	103,710,558
	$ 190,946,694	197,346,005

Assets under capital lease, at June 30, 2010 and 2009, of $6,631,630 were included in building and building improvements and furniture and equipment in the table above. Accumulated depreciation of assets under capital leases totaled $1,945,059 and $1,322,834 at June 30, 2010 and 2009, respectively.

Certain land, buildings, improvements and equipment are pledged as collateral for the debt described in note 9.

Depreciation expense for the years ended June 30, 2010 and 2009 was $14,716,393 and $14,367,338, respectively.

In June 2001, the Health System entered into a 40-year ground lease with MEDCO, whereby MEDCO leases certain parcels of land from Foundation. The base year rental income, included in other revenue in the accompanying statements of operations is $885,500 and increases by 3% per annum over the life of the lease. MEDCO has constructed student housing on the leased parcels of land (the MEDCO lease). Unpaid accrued rent bears interest at 12.65% per annum.

The payment of ground rent is subordinate to the payment of debt on the MEDCO loan. Based on current cash flow projections, it is anticipated that the full amount of rent accruing will not be paid. Foundation has recorded an allowance for a portion of the unpaid accrued rent, and the related interest on the unpaid rents for fiscal years 2003 through 2009. A partial ground rent payment of $1,081,632 and $1,031,384 was accrued as a receivable at June 30, 2010 and 2009, respectively. As of June 30, 2010 and 2009, Foundation has recorded total ground rent receivable in prepaid expenses and other current assets in the accompanying consolidated balance sheets of $5,877,267 and $5,533,890, respectively, with a related reserve of $4,795,635 and $4,502,506, respectively.

In January 2008, the Health System acquired a property in Glyndon, Maryland for the Forbush School, the Health System's flagship educational facility. The property, which cost $17,250,000, consists of 44 acres and includes six buildings totaling 90,000 square feet. The acquisition was financed primarily through a $16,900,000 bank note payable which matured in November 2009 and was subsequently refinanced. The school was relocated from the Towson campus to the Glyndon location in June 2009. During fiscal year

(Continued)

2009, the Health System recorded additional depreciation expense of $172,000 for the assets that will no longer be used at the previous location.

(8) Other Assets

The other assets balance is composed of the following at June 30:

		2010	2009
Goodwill	$	2,663,300	2,663,300
Deferred financing costs		3,524,894	3,279,807
Other intangible assets		1,307,000	1,307,000
Cash surrender value of life insurance and other		2,027,192	1,052,368
		9,522,386	8,302,475
Accumulated amortization		(2,937,192)	(2,238,034)
	$	6,585,194	6,064,441

(9) Long-Term Debt

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

		2010	2009
Maryland Health and Higher Education Facilities Authority (MHHEFA) Revenue Bonds, Series 2003	$	82,770,000	84,575,000
MHHEFA Series D pooled loan program		4,939,999	5,110,000
Maryland Industrial Development Financing Authority Revenue Bonds, Series C		495,000	715,000
Mortgages on real estate		8,583,827	8,476,949
Bank note payable		—	16,900,000
Bank financing agreement		14,000,000	—
Other debt		2,726,187	2,754,376
		113,515,013	118,531,325
Plus unamortized bond premium		395,868	419,545
		113,910,881	118,950,870
Less current portion		4,355,042	20,043,989
	$	109,555,839	98,906,881

In May 2003, Obligated Group, comprised of Sheppard and Enoch Pratt Foundation, Inc., Health System, Physicians, and Investment Company, issued tax-exempt Series 2003 Bonds in the original amount of $91,140,000 to finance the construction of a 192 bed inpatient hospital, and renovation of certain existing facilities and common areas which was completed in February 2006 (the Project) and to repay then existing debt. The Series 2003 Bonds were issued pursuant to a loan agreement and trust indenture between

MHHEFA and Obligated Group. Portions of the Series 2003 Bonds (Series A) in the original amount of $45,590,000, bear interest semi-annually at fixed rates ranging from 2.8% to 5.3%. The Series A Bonds are subject to annual mandatory sinking fund requirements commencing in 2029 through 2037. The Series B Bonds are subject to annual mandatory principal requirements commencing in 2007 through 2028. Principal payments vary in increasing amounts from $600,000 with the final installment of $3,425,000 in 2028. The Series B Bonds were originally issued as auction rate securities. Pursuant to the original governing documents, in February 2008, Foundation elected to convert the Series B Bonds from auction rate securities to variable rate demand bonds backed by a five-year bank letter of credit. The amount of Series B Bonds outstanding at June 30, 2010 and 2009 was $43,700,000 and $44,325,000, respectively. Draws under the letter of credit would be repayable over a five-year term, with the first payment 366 days from the draw date. The effective interest rate on the debt for 2010 and 2009 was approximately .7% and 2.1%, respectively.

The Series 2003 Bonds are secured by a trust indenture and Obligated Group has granted MHHEFA a security interest in its revenues. The Series B Bonds are also insured by a financial guaranty insurance policy issued by a commercial insurance company. The Series 2003 Bonds, the letter of credit and the financial guaranty insurance policy require Obligated Group to satisfy certain measures of financial performance as long as the Series 2003 Bonds are outstanding. Obligated Group was in compliance with such financial covenants as of June 30, 2010.

In September, 2006, Mosaic and North Baltimore Center jointly borrowed $5,420,000 through the MHHEFA Series D pooled loan program. This loan was used to defease certain bonds issued in 1996 by the Maryland Economic Development Company and certain bonds issued in 2001 by Baltimore County, Maryland for ReVisions, Inc. (an entity which subsequently merged with Mosaic) and for certain renovations and equipment purchases. The variable rate bonds, which are supported by a bank letter of credit, which expires in September 2011, are being amortized over twenty years. The effective interest rate on this debt was approximately 3.6% for 2010 and 2009. The defeased debt, which will be repaid through August 2011, is included in “other” debt in the table presented above and bore interest at an effective rate of 8.5% in 2010 and 2009. As of June 30, 2009, Mosaic and North Baltimore Center were not in compliance with a financial covenant contained in the Series D pooled loan agreement. The noncompliance related to a covenant that requires Mosaic and North Baltimore Center (on a combined basis) to maintain a minimum debt service coverage ratio (as defined) on a quarterly basis. In November 2009, Mosaic and North Baltimore Center obtained a waiver of the June 30, 2009 noncompliance and an amendment of the definition of the quarterly coverage ratio requirements for the year ending June 30, 2010. The amendment lowered the minimum coverage ratio and excluded certain amounts related to North Baltimore Center from the calculation through June 30, 2010. Mosaic and North Baltimore Center were in compliance with the amended covenant during the year ending June 30, 2010. However, management does not expect to comply with the covenants in fiscal year 2011, which could result in such debt being called if a waiver is not received.

In January 2008, Obligated Group, comprised of Sheppard and Enoch Pratt Foundation, Inc., Health System, Physicians, and Investment Company, entered into a line of credit agreement with Bank of America for $16,900,000 (Bank Note) to finance the purchase of property in Glyndon, Maryland for the Forbush School. The original term of the line of credit was through May 31, 2009 and interest was payable monthly at Interbank Offered Rate (LIBOR) plus 0.45%. In May 2009, the Bank Note was extended to

November 30, 2009 and in connection with the extension, the interest rate was changed to LIBOR plus 0.85%.

In December 2009, Obligated Group entered into a financing agreement with Bank of America for up to $30,000,000 to refinance the Bank Note and to provide funds for the potential purchase of land for future expansion in Howard County, Maryland. The term of the agreement is through December 2014. Interest is payable monthly at 65% of the Interbank Offered Rate (LIBOR) plus 1.55%. The effective rate of interest on the debt was approximately 1.7% for 2010. As of June 30, 2010, $14,000,000 has been drawn under this agreement and the proceeds, combined with an equity contribution, were used to refinance the Bank Note. Foundation is required to satisfy certain measures of financial performance as long as the loan is outstanding. Foundation was in compliance with such financial covenants as of June 30, 2010.

The Maryland Industrial Development Financing Authority Revenue Bonds, Series C (Way Station Bonds) are tax-exempt revenue bonds issued for the construction of the Way Station facility. The Way Station Bonds are due in monthly payments of principal and interest, bear interest at a fixed rate of 4.3%, are due January 2012 and are secured by the first deed of trust on Way Station Bonds are secured by an irrevocable direct pay letter of credit by a commercial bank. The letter of credit of approximately $1,742,000 will expire in January 2012.

Way Station has a mortgage on two properties in the Frederick, Maryland area with a total outstanding balance of $669,434 and $87,284 at June 30, 2010 and 2009, with interest rates of 4.25% and 2.0% and maturity dates of 2019 and 2031. In addition, Way Station has a noninterest bearing loan due in 2023 and is secured by a lien on one of its properties. As of June 30, 2010 and 2009, the outstanding balance was $61,000 and $66,000, respectively.

Family Services has mortgages on 21 properties in the Gaithersburg, Maryland area with a total outstanding balance of $5,194,991 and $5,512,483 at June 30, 2010 and 2009, respectively, with interest rates ranging from 4.2% to 7.0%, and maturity dates ranging from August 2010 to December 1, 2039.

Mosaic has mortgages on 23 properties in the Baltimore County and Carroll County areas with a total outstanding balance of $2,658,139 and $2,773,487 at June 30, 2010 and 2009, respectively, with interest rates ranging from 0.0% to 8.5%, and maturity dates ranging from 2014 to 2038.

Turning Point has mortgages on two properties in the Hagerstown area with a total outstanding balance of $61,263 and $103,695 at June 30, 2010 and 2009, respectively, with interest rates ranging of 6.0% and 7.5%, and maturity dates of July 2012 and January 2014.

In addition, Family Services has a variable rate line of credit with Bank of America in the amount of $400,000 which is secured by certain assets of Family Services. At June 30, 2010 and 2009, Family Services had an outstanding balance of $175,000 and $90,000, respectively.

In addition, Mosaic has a variable rate line of credit with Bank of America in the amount of $1,000,000 which is secured by certain assets of Mosaic. At June 30, 2010 and 2009, Mosaic had an outstanding balance of $174,000.

Repayment of long-term debt, including mandatory sinking fund redemptions, in each of the next five fiscal years is as follows:

2011	$	4,355,042
2012		4,381,811
2013		4,012,729
2014		3,721,524
2015		3,194,836
2016 and thereafter		93,849,071
	$	113,515,013

Interest payments were $3,353,434 and $3,799,923 in 2010 and 2009.

(10) Other Financial Instruments

On July 1, 2002, Family Services entered into an interest rate swap with the notional amount of $2,400,000 and a term of 20 years to fix the interest rate on its bonds at 4.16% over the life of the swap. The interest rate swap does not qualify for hedge accounting under the provisions of ASC Subtopic 815-10. Family Services paid approximately $71,019 and $55,195 during 2010 and 2009, respectively, in settlements to the counter party that have been recorded as other income (expense) in the consolidated statements of operations.

On September 26, 2006, Mosaic and North Baltimore Center entered into an interest rate swap in conjunction with the issuance of MHHEFA Series D Bonds with the notional amount of $5,420,000 and a term of five years to fix the interest rate at 3.6%. The interest rate swap does not qualify for hedge accounting under the provisions of ASC Subtopic 815-10. Mosaic and North Baltimore Center paid approximately $173,043 and $137,638 during 2010 and 2009 in settlements to the counter party that have been recorded as other income (expense) in the consolidated statements of operations.

As of June 30, 2010 and 2009, the aggregate fair value of the interest rate swaps outstanding was $466,714 and $524,144, respectively. Such amounts are recorded as a component of other long-term liabilities in the accompanying consolidated balance sheets. Changes in fair value of interest rate swaps of approximately $57,430 and $(197,144), respectively, have been recorded as a component of other income (expense) in the accompanying consolidated statements of operations and changes in net assets for 2010 and 2009, respectively.

During the year ended June 30, 2006, Foundation received a gift annuity from donors. Under the terms of such agreement, Foundation agreed to pay 6% annually of the contributed amount (approximately $1 million) on a quarterly basis over the remaining lives of the donors. Accordingly, as of June 30, 2010 and 2009, the net present value of the estimated remaining payments of approximately $652,000 and $682,000, respectively, have been recorded as an other long-term liability.

(11) Pension Plan, Employees' Thrift Plan and Life, Accident and Health Plan

Foundation has a noncontributory defined benefit pension plan which covers eligible employees of Health System and Physicians. The benefits are based on the employees' credited service and average compensation during the five consecutive years, taken from the last ten years of service before retirement, which produces the highest result. The funding policy is to contribute annually amounts actuarially determined to provide for benefits attributed to service to date and benefits expected to be earned in the future. Prior service cost is being amortized on a straight-line basis over the estimated term of employment of current employees.

ASC Subtopic 715-30, *Defined Benefit Plans-Pension*, requires Foundation to recognize the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of its pension plan in the accompanying consolidated balance sheets, with a corresponding adjustment to unrestricted net assets. The pension liability adjustment to unrestricted net assets represents the change in net unrecognized actuarial losses and unrecognized prior service costs which have not yet been recognized as part of excess (deficiency) of revenues over expenses. Those amounts will be subsequently recognized as a component of net periodic pension cost pursuant to Foundation's historical accounting policy for amortizing such amounts.

The following are deferred pension costs which have not yet been recognized in periodic pension expense but instead are included as a component of unrestricted net assets, as of June 30, 2010 and 2009. Unrecognized actuarial losses represent unexpected changes in the projected benefit obligation and plan assets over time, primarily due to changes in assumed discount rates and investment experience. Unrecognized prior service cost is the impact of changes in plan benefits applied retrospectively to employee service previously rendered. Deferred pension costs are amortized into annual pension expense over the average remaining assumed service period for active employees.

		Amounts in unrestricted net assets to be recognized during the next fiscal year	Amounts recognized in unrestricted net assets at June 30, 2010	Amounts recognized in unrestricted net assets at June 30, 2009
Net prior service cost	$	736,772	1,629,890	2,366,662
Net actuarial loss		1,872,482	34,600,188	22,864,737
Total	$	2,609,254	36,230,078	25,231,399

The Plan's change in benefit obligations, the change in plan assets, current funded status and the components of net periodic pension cost as of and for the years ended June 30, 2010 and 2009 are as follows:

		2010	2009
Accumulated benefit obligation at the end of the year	$	126,280,732	103,529,191
Changes in benefit obligations:			
Projected benefit obligation at the beginning of the year	$	115,374,087	108,244,101
Service cost		4,544,847	4,608,647
Interest cost		7,387,992	7,091,814
Actuarial loss (gain)		17,791,837	(749,920)
Benefits paid		(4,036,017)	(3,820,555)
Projected benefit obligation at the end of the year		141,062,746	115,374,087
Changes in plan assets:			
Fair value of plan assets at beginning of the year		97,537,655	93,439,575
Actual return on plan assets		12,655,795	(10,186,193)
Contributions to the plan		—	18,104,828
Benefits paid		(4,036,017)	(3,820,555)
Fair value of plan assets at end of the year		106,157,433	97,537,655
Funded status		(34,905,313)	(17,836,432)
Accrued pension cost	$	(34,905,313)	(17,836,432)

Net periodic pension expense includes the following components for the years ended June 30:

		2010	2009
Service cost	$	4,544,847	4,608,647
Interest cost		7,387,992	7,091,814
Expected return on plan assets		(7,627,552)	(7,146,702)
Amortization of prior service cost		736,772	736,772
Amortization of net loss		1,028,143	—
Net pension expense	$	6,070,202	5,290,531

The following table presents the weighted average assumptions used to determine benefit obligations and net periodic benefit expense for the Plan for 2010 and 2009:

	2010	2009
Discount rates (benefit obligation)	5.50%	6.50%
Discount rates (benefit expense)	6.50	6.75
Rate of compensation increase	4.00	4.00
Expected long-term return on plan assets	8.00	7.50

(a) Determination of Expected Long-Term Rate of Return

In developing the expected long-term rate of return on assets assumption, Foundation considered the current level of expected returns on risk free investments (primarily government bonds), the historical level of the risk premium associated with the other asset classes in which the portfolio is invested, and the expectations for future returns of each asset class. The expected return for each asset class was then weighted based on the target allocation to develop the expected long-term rate of return on assets assumption for the portfolio. This process resulted in the selection of the 8% assumption.

(b) Investment Policy and Objectives

The investment policy and objectives are established by the trustees of Foundation. The plan objectives include maintaining fully funded status and maximizing returns with reasonable and prudent levels of risk. The investment policy is based on a long-term perspective. An investment advisory firm engaged by Foundation trustees reviews fund performance and asset allocation at each quarterly meeting. The percentage allocation to each asset class may vary depending upon market conditions.

A Foundation trustee serves as an investment manager for a portion of the pension portfolio and investment portfolio totaling approximately $29,800,000 and $27,700,000 as of June 30, 2010 and 2009, respectively.

(c) Plan Assets

Foundation's pension plan weighted average asset allocations at the measurement dates of June 30, 2010 and 2009 by asset category are as follows:

	Target Allocation	2010	2009
Equity securities	60%	77%	48%
Debt securities	20	15	30
Cash	—	4	13
Other	20	4	9
	100%	100%	100%

The Company's Board of Directors authorizes and approves investment activity for which the different investment managers are responsible for making specific investment decisions. The Company monitors the investment managers' performance and ensures adequate diversification by asset class to further mitigate the risks associated with the investment program. Management believes that its investments are invested in accordance with its overall investment policies at June 30, 2010 and June 30, 2009.

In accordance with ASC Subtopic 715-20, *Defined Benefit Plans-General-Disclosures*, nonpublic entities are required to report the fair value of each major category of pension plan asset within the fair value hierarchy. ASC Subtopic 820-10, *Fair Value Measurements and Disclosures-Overall*, provides guidance for the fair value hierarchy, which is as a valuation technique that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs. Refer to note 17, for descriptions of each of the three levels within the valuation hierarchy.

The table below presents the Company's pension plan investable assets as of June 30, 2010 aggregated by the three level valuation hierarchy:

	Level 1	Level 2	Level 3	Total
Assets:				
Cash and cash equivalents	$ 4,289,110	—	—	4,289,110
Government issued bonds	—	1,712,286	—	1,712,286
Corporate bonds	—	14,636,723	—	14,636,723
Mutual funds	42,163,934	13,414,268	—	55,578,202
Other equities	899,327	—	—	899,327
Common stocks	24,399,959	—	—	24,399,959
Alternative investments	—	861,577	3,780,249	4,641,826
Total assets	$ 71,752,330	30,624,854	3,780,249	106,157,433

The Company's pension plan invests in six alternative investments which are primarily hedge fund of funds and private equity funds. Such investments are typically carried at estimated fair value. The Company uses the practical expedient to report the net asset values of these funds as an estimate of fair value. Most of the funds have not had changes in the redemption policies during fiscal year 2010. However, one fund imposed restrictions on redemptions during fiscal year 2010 but the Company expects such restrictions to lapse during fiscal year 2011. Determination of fair value is performed on a quarterly basis by the General Partner(s) of the funds. Because of the inherent uncertainty of valuation, the determined values may differ significantly from the values that would have been used had a ready market for these investments existed.

(Continued)

ASC 715-20 also requires that nonpublic entities provide a reconciliation of the beginning and ending balances for the Level 3 plan assets. In accordance with this guidance, changes to the Company's level 3 plan assets, are summarized as follows:

		Alternative investments
Balance as of June 30, 2009	$	8,389,214
Additions:		
Contributions/purchases		735,829
Disbursements:		
Withdrawals/sales		(7,306,435)
Net change in value		1,961,641
Balance as of June 30, 2010	$	3,780,249

(d) Contributions

Foundation contributed approximately $18.1 million to its pension plan for the fiscal year ended June 30, 2009. For the year ending June 30, 2010, Foundation did not make any contributions to its pension plan. The Foundation expects to contribute $11.0 million to its pension plan for the fiscal year ended June 30, 2011.

(e) Estimated Future Benefit Payments

The following benefit payments, which reflect expected future employee service, as appropriate, are expected to be paid from the plan in each of the fiscal years as follows:

2011	$	4,839,939
2012		5,341,351
2013		5,862,481
2014		6,592,760
2015		7,009,374
2016 – 2019		41,884,448

The expected benefits to be paid are based on the same assumptions used to measure Foundation benefit obligation at June 30, 2010.

Effective July 1, 2006, Foundation elected to not allow employees hired on or after July 1, 2006 to participate in either the defined benefit pension plan or the current employees' thrift plan. Instead, such employees participate in a new employees' thrift plan. The new employee's thrift plan expense was approximately $1,158,000 and $778,000 in 2010 and 2009, respectively. The retirement benefits for employees hired on or prior to June 30, 2006 under the defined benefit plan and employees' thrift plan remain unchanged.

Foundation sponsors an employees' thrift plan for certain employees of Health System and Physicians. Foundation may provide a discretionary contribution to the employees' thrift plan. There were no contributions to the thrift plan in 2010 and 2009.

Foundation maintains a life, accident and health plan for employees of Health System and Physicians which provides for monthly contributions in amounts sufficient to cover the costs of (1) insurance purchased from commercial insurance companies, (2) basic hospital, surgical and diagnostic benefits and (3) administrative expenses. The life, accident and health plan expense was approximately $8,658,000 in 2010 and $8,239,000 in 2009.

Certain of the subsidiaries maintain various tax sheltered annuity accounts, defined contribution plans or other retirement benefit plans. These subsidiaries have the option to issue discretionary matching contributions to the plans. During the years ended June 30, 2010 and 2009, these subsidiaries contributed approximately $254,000 and $240,000, respectively, to the plans.

(12) Leases

Foundation leases office space under long-term operating leases which expire at various dates through 2015, some of which require increasing monthly payments expiring over the next several years. The following is a schedule of the future minimum lease payments under operating leases as of June 30, 2010 that have initial or remaining lease terms in excess of one year for each of the years ending June 30:

2011	$	3,900,940
2012		3,156,322
2013		2,466,930
2014		1,851,234
2015		1,576,055
Thereafter		3,598,116
Total minimum lease payments	$	16,549,597

Rent expense was approximately $5,963,117 and $6,420,015 in 2010 and 2009, respectively. Foundation also leases various equipment under short-term leases.

Foundation leases a school building and certain software and equipment related to its electronic medical records system which are recorded in the consolidated balance sheets as capital leases. The school building lease has an initial lease term of 10 years, and Foundation has the right to extend the lease term for two successive periods of five years each.

The following is a schedule of future minimum lease payments under capital leases as of June 30, 2010.

2011	$	682,048
2012		670,683
2013		315,829
2014		325,304
2015		335,063
Thereafter		5,389,933
Total minimum lease payments		7,718,860
Less amount representing interest		2,705,897
Present value of net minimum lease payments		5,012,963
Less obligations under capital leases, current portion		427,467
Obligations under capital leases, less current portion	$	4,585,496

(13) Self-Insurance Programs and Litigation

Foundation is from time to time subject to claims and suits arising in the ordinary course of business. In the opinion of management, the ultimate resolution of pending legal proceedings will not have a material effect on the consolidated financial statements. In this regard, Foundation maintains a self-insurance program for professional liability claims, and a related trust fund has been established for the purpose of setting aside assets based on actuarial funding recommendations. Under the trust agreement, the assets can only be used for the payment of professional and general liability claims, related expenses and the cost of administering the trust. Certain claims-made based professional and occurrence-based general liability insurance coverages have been purchased to provide protection for claims in excess of the self-insured amounts. The assets of the trust are classified as investments limited as to use in the accompanying consolidated balance sheets in the amount of $990,399 and $2,381,772 at June 30, 2010 and 2009, respectively. The related claims liabilities of $4,688,915 and $4,710,462 as of June 30, 2010 and 2009, respectively, are recorded on an undiscounted basis and represent estimates for asserted claims and unasserted claims arising from reported incidents and unreported incidents. Management believes that the provision for loss is adequate at June 30, 2010 and 2009; however, the ultimate liability may differ significantly.

Health System and Physicians are also self-insured for unemployment claims and have established a letter of credit arrangement of approximately $1,207,000 in 2010 and $1,138,000 in 2009 in accordance with the requirements of the Maryland Department of Employment and Training. Also, Foundation is self-insured for workers' compensation claims up to $450,000. Investments of approximately $3,605,000 and $3,400,000 at June 30, 2010 and 2009, respectively, are being held in an account at a financial institution to secure the payment of claims. These investments are included in the balance of investments limited or restricted as to use. The related liabilities of $2,009,618 and $1,689,072 as of June 30, 2010 and 2009, respectively, are recorded in the accompanying consolidated balance sheets. Foundation records outstanding losses and loss expenses for workers' compensation liability claims based on the estimates of the amount of reported losses together with a provision for losses incurred but not reported, the recommendations of an independent actuary, and management's judgment using its past experience and industry experience. Foundation offers employees an option to participate in a self-insured health plan. Health claims under this plan are paid by Foundation as they are submitted to the health plan administrator. Foundation maintains an accrual for claims that have been incurred but not reported to the plan administrator. The accrued liability for claims incurred but not reported is based on the historical claim lag period and current payment trends of health insurance claims. The accrued liability for health claims is $1,705,000 and $591,000, respectively, as of June 30, 2010 and 2009. While management believes that the provision for claims on unemployment, workers' compensation and employee health benefits is adequate, at June 30, 2010 and 2009, the ultimate liability may be significantly different than the estimates.

(14) Net Assets

Net assets at June 30 are summarized as follows:

	2010	2009
Unrestricted:		
Undesignated	$ 105,863,744	110,137,778
Board-designated:		
Moses Sheppard bequest	28,877,128	25,726,312
Enoch Pratt bequest	18,417,418	16,663,034
Other	43,297,596	39,856,493
Total board-designated	90,592,142	82,245,839
Total unrestricted	$ 196,455,886	192,383,617

Temporarily restricted net assets are available for the purposes of providing indigent care, health and educational programs, the purchase of property and equipment, and the repayment of debt. Permanently restricted net assets are restricted in perpetuity, the income from which is expendable to provide health and educational programs.

(15) Rate Setting Matters and Business and Credit Concentrations

Foundation provides health care services through its inpatient and outpatient care facilities located throughout Maryland. Foundation grants credit to patients and generally does not require collateral or other security in extending credit; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits receivable under their health insurance programs, plans or policies (e.g., Medicare, Medicaid, Blue Cross/Blue Shield, health maintenance organizations (HMOs) and commercial insurance policies).

Net patient, residential and educational service revenue, by payor class, consisted of the following for the years ended June 30:

	2010	2009
Medicare	13%	14%
Medicaid	38	34
Commercial insurers and HMOs	16	19
Local government	18	19
Blue Cross/Blue Shield	8	9
Self-pay and others	7	5
	100%	100%

Patient charges of the Health System (other than Medicare and Medicaid) are recorded at rates established by the State of Maryland Health Services Cost Review Commission (HSCRC), reviewed on an annual basis and adjusted prospectively giving effect to, among other things, the anticipated impact of inflation on operating expenses, variances between actual volume of patient services and the volume budgeted for such services, and variances between actual unit rates and approved unit rates during the previous rate year. Such rate adjustments are reflected in revenue of Health System in the subsequent rate year, which coincides with Health System's fiscal year.

Certain services rendered to the Maryland Department of Human Resources, Medicare and Medicaid program beneficiaries are reimbursed based upon cost reimbursement methodologies. Effective July 1, 2001, the Maryland Medicaid program changed its reimbursement methodology to a prospective payment system for psychiatric inpatient services. Medical outpatient services continue to be reimbursed on a cost report basis. Effective July 1, 2005, the Medicare program changed its reimbursement methodology to a prospective payment system, which occurred over a four-year period. Health System has received either the final settlement or the notice of final settlement on Medicare cost reports through June 30, 2007 and on Medicaid cost reports through June 30, 2001. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is a reasonable possibility that recorded estimates will change in the near term. However, in the opinion of management, retroactive adjustments, if any, would not be material to the consolidated financial position or results of operations of Foundation.

Accounts receivable are as follows at June 30:

	2010	2009
Patient accounts receivable	$ 28,691,685	28,832,003
Residential and educational accounts receivable	8,018,544	6,361,772
	36,710,229	35,193,775
Less allowance for doubtful accounts	7,592,901	7,003,384
	$ 29,117,328	28,190,391

(Continued)

(16) Functional Expenses

Members of Foundation provide healthcare and educational services to the patients which they serve. Expenses related to providing these services, based on management's estimates of expense allocations, are as follows:

		2010	2009
Healthcare and educational services	$	229,437,450	224,011,127
General and administrative		34,283,757	31,985,800
	$	263,721,207	255,996,927

(17) Disclosures about Fair Value of Financial Instruments

On July 1, 2008, Foundation adopted ASC Subtopic 820-10 for its financial assets and liabilities, as discussed in note 2. ASC Subtopic 820-10 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles and expands disclosures about fair value measurements. Specifically, the guidance provides for the following:

- Defines fair value as 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, and establishes a framework for measuring fair value;
- Establishes a three-level hierarchy for fair value measurement;
- Requires consideration of the Company's nonperformance risk when valuing liabilities; and
- Expands disclosures about instruments measured at fair value.

The three-level valuation hierarchy for fair value measurements is based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. The three-level valuation hierarchy is defined as follows:

- Level 1 – Quoted prices for identical instruments in active markets;
- Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar investments in markets that are not active; and model derived valuations whose significant inputs are observable; and
- Level 3 – Instruments whose significant inputs are unobservable.

The table below presents the Company's investable assets and liabilities as of June 30, 2010, aggregated by the three-level valuation hierarchy:

	Level 1	Level 2	Level 3	Total
Assets:				
Cash and cash equivalents	$ 11,596,497	—	—	11,596,497
Equities:				
Common stocks	23,357,018	—	—	23,357,018
Mutual funds	41,706,326	3,573,285	—	45,279,611
Other	938,061	—	—	938,061
Fixed income:				
Corporate bonds	—	21,645,966	—	21,645,966
Government issued bonds	—	1,761,780	—	1,761,780
Pledge receivable	—	—	1,500,423	1,500,423
Total assets	$ 77,597,902	26,981,031	1,500,423	106,079,356
Liabilities:				
Interest rate swap	$ —	(446,714)	—	(446,714)
Total liabilities	$ —	(446,714)	—	(446,714)

The table below presents the Company's investable assets and liabilities as of June 30, 2009, aggregated by the three-level valuation hierarchy:

	Level 1	Level 2	Level 3	Total
Assets:				
Cash and cash equivalents	$ 7,443,802	—	—	7,443,802
Equities:				
Common stocks	6,766,823	—	—	6,766,823
Mutual funds	50,840,196	3,109,672	—	53,949,868
Real estate investment trust	79,970	—	—	79,970
Other	842,418	—	—	842,418
Fixed income:				
Corporate bonds	—	23,440,458	—	23,440,458
Government issued bonds	—	2,156,510	—	2,156,510
Pledge receivable	—	—	1,913,059	1,913,059
Total assets	$ 65,973,209	28,706,640	1,913,059	96,592,908
Liabilities:				
Interest rate swap	$ —	(518,795)	—	(518,795)
Total liabilities	$ —	(518,795)	—	(518,795)

(Continued)

Foundation's Level 1 securities primarily consist of common stock, U.S. Treasury securities, exchange-traded mutual funds and cash. Foundation determines the estimated fair value for its Level 1 securities using quoted (unadjusted) prices for identical assets or liabilities in active markets.

Foundation's Level 2 securities consist of corporate bonds, government issued bonds, mutual funds and derivative instruments, which are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active or model derived valuations whose significant inputs are observable. Valuation models require a variety of inputs, including contractual terms, market fixed prices, inputs from forward price yield curves, notional quantities, measures of volatility and correlations of such inputs.

Investments classified within Level 3 have significant unobservable inputs, as they trade infrequently or not at all. Level 3 instruments include pledges receivable which are typically valued based upon discounted cash flow models.

The classification of a financial instrument within Level 3 is based upon the significance of the unobservable inputs to the overall fair value measurement. The following table includes a rollforward of the amounts for the year ended June 30, 2010 for financial instruments measured at fair value on a recurring basis classified within Level 3.

	Pledges receivable
Balance at June 30, 2009	$ 1,913,059
Contributions	927,077
Collections	(1,339,713)
Balance at June 30, 2010	$ 1,500,423

The carrying amount of cash and cash equivalents, accounts receivable, third-party payor settlements receivable or payable, other current assets, accounts payable, accrued expenses approximates fair value because of the short-term maturity of these instruments. The fair value of Foundation's long-term debt, except for the Series A portion of the 2003 Bonds, is estimated to approximate the carrying amount because interest rates are variable and determined frequently based on prevailing market conditions. The estimated fair value of the Series A portion of the 2003 Bonds is approximately $35,252,000 and $31,008,000 at June 30, 2010 and 2009, respectively. The carrying value for these bonds is $39,070,000 and $40,250,000 at June 30, 2010 and 2009, respectively. Due to the subjective nature of the terms of the Foundation's notes receivable and capital lease obligations, their fair values cannot be estimated.

(18) Certain Significant Risks and Uncertainties

The Company provides psychiatric healthcare services in the State of Maryland. The Company and other healthcare providers are subject to certain inherent risks, including the following:

- Dependence on revenues derived from reimbursement by the Federal Medicare and state Medicaid programs;
- Regulation of hospital rates by the State of Maryland Health Services Cost Review Commission;

- Government regulation, government budgetary constraints and proposed legislative and regulatory changes, and;
- Lawsuits alleging malpractice or other claims.

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

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

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

The healthcare industry is subject to numerous laws and regulations from federal, state and local governments, and the government has aggressively increased enforcement of Medicare and Medicaid anti-fraud and abuse laws. The Company's compliance with these laws and regulations is subject to periodic governmental review, which could result in enforcement actions unknown or unasserted at this time. Management is aware of certain asserted and unasserted legal claims, none of which, in the opinion of management, is expected to result in losses in excess of insurance limits.

The federal government and many states have aggressively increased enforcement under Medicare and Medicaid anti-fraud and abuse laws and physician self referral laws (STARK law and regulation). Recent federal initiatives have prompted a national review of federally funded healthcare programs. In addition, the federal government and many states have implemented programs to audit and recover potential overpayments to providers from the Medicare and Medicaid programs.

As a result of recently enacted and pending federal health care reform legislation, substantial changes are anticipated in the United States health care system. Such legislation includes numerous provisions affecting the delivery of health care services, the financing of health care costs, reimbursement to health care providers and the legal obligations of health insurers, providers and employers. These provisions are currently slated to take effect at specified times over the next decade. This federal health care reform legislation does not affect the 2010 nor the 2009 consolidated financial statements.

(19) Endowment Net Assets

The Company's endowments consist of both individual donor-restricted funds established for a variety of purposes and funds designated by the Board of Trustees to function as endowments. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

(a) Interpretation of Relevant Law

The Company has interpreted the State Prudent Management of Institutional Funds Act (SPMIFA) 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 Company classifies its permanently restricted net assets as (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 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 SPMIFA. In accordance with SPMIFA, the Company considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

(1) The duration and preservation of the fund

(2) The purposes of the Company 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 Company

(7) The investment policies of the Company.

(b) Net asset (deficit) classification by type of endowment as of June 30, 2010:

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Donor-restricted endowment funds	$ —	—	3,468,495	3,468,495
Board-designated endowment funds	90,592,142	—	—	90,592,142
	$ 90,592,142	—	3,468,495	94,060,637

Changes in endowment net assets for the year ended June 30, 2010:

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Endowment net assets beginning of year	$ 82,245,839	—	3,423,475	85,669,314
Investment return:				
Investment income	2,121,363	—	—	2,121,363
Net appreciation (realized and unrealized gains and losses)	8,879,620	—	43,520	8,923,140
Total investment return	11,000,983	—	43,520	11,044,503
Contributions	—	—	1,500	1,500
Appropriation of endowment assets for expenditure	(2,654,680)	—	—	(2,654,680)
	$ 90,592,142	—	3,468,495	94,060,637

(c) Net asset (deficit) classification by type of endowment as of June 30, 2009:

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Donor-restricted endowment funds	$ —	—	3,423,475	3,423,475
Board-designated endowment funds	82,245,839	—	—	82,245,839
	$ 82,245,839	—	3,423,475	85,669,314

(Continued)

Changes in endowment net assets for the year ended June 30, 2009:

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Endowment net assets beginning of year	$ 97,499,752	—	3,270,293	100,770,045
Investment return:				
Investment income	3,229,476	—	—	3,229,476
Net depreciation (realized and unrealized gains and losses)	(15,740,372)	—	(77,353)	(15,817,725)
Total investment return	(12,510,896)	—	(77,353)	(12,588,249)
Contributions	—	—	230,535	230,535
Appropriation of endowment assets for expenditure	(2,743,017)	—	—	(2,743,017)
	$ 82,245,839	—	3,423,475	85,669,314

(d) Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or SPMIFA requires the Company to retain as a fund of perpetual duration. These deficiencies resulted from unfavorable market fluctuations.

(e) Investment Strategies

The Company has adopted policies for corporate investments, including endowment assets that seek to maximize risk-adjusted returns with preservation of principal. Endowment assets include those assets of donor-restricted funds that the Company must hold in perpetuity or for a donor-specified period(s).The endowment assets are invested in a manner that is intended to hold a mix of investment assets designed to meet the objectives of the account. The Company expects its endowment funds, over time, to provide an average rate of return that generates earnings to achieve the endowment purpose.

To satisfy its long-term rate-of-return objectives, the Company 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 Company employs a diversified asset allocation structure to achieve its long-term return objectives within prudent risk constraints.

The Company monitors the endowment funds returns and appropriates average returns for use. In establishing this practice, the Company considered the long-term expected return on its endowment. This is consistent with the Company's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

(20) Subsequent Events

Subsequent events were evaluated through October 11, 2010, the date of issuance for the Company's audited financial statements as of and for the year ended June 30, 2010.

Effective July 1, 2010, Mosaic completed a statutory merger with North Baltimore, with Mosaic being the remaining entity. The Company maintained sole membership of the surviving corporation. Due to the common ownership, this transaction will be accounted for as an "as-if" pooling of interests.

The Company has committed to purchase a 44-acre parcel of land in Howard County at an approximate cost of $9,000,000 and is expected to draw on an existing bank financing agreement to complete the transaction.

OTHER FINANCIAL INFORMATION

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

Independent Auditors' Report on Other Financial Information

The Board of Trustees
Sheppard and Enoch Pratt Foundation, Inc.:

Our audit was conducted for the purpose of forming an opinion on the June 30, 2010 consolidated financial statements taken as a whole. The accompanying financial information is presented for purposes of additional analysis and is not a required part of the June 30, 2010 consolidated financial statements. Such information has been subjected to the auditing procedures applied in our audit of the June 30, 2010 consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the June 30, 2010 consolidated financial statements taken as a whole.

KPMG LLP

October 11, 2010

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Supplemental Consolidating Balance Sheet Information

June 30, 2010

Assets	Sheppard and Enoch Pratt Foundation, Inc.	Sheppard Pratt Health System, Inc.	Sheppard Pratt Investment, Inc.	Sheppard Pratt Physicians, P.A.	Obligated group combining eliminations	Combined obligated group subtotal
Current assets:						
Cash and cash equivalents	$ 129,338	29,233,990	—	1,411,352	—	30,774,680
Temporary investments	—	—	—	—	—	—
Investments limited or restricted as to use	132,505	2,299,932	—	—	—	2,432,437
Accounts receivable, net	—	22,314,331	—	1,175,596	—	23,489,927
Current portion of notes receivable	—	125,949	—	—	—	125,949
Due from affiliates	—	1,001,026	4,138,321	83,725	(4,274,406)	948,666
Prepaid expenses and other current assets	—	4,008,813	—	260,214	—	4,269,027
Total current assets	261,843	58,984,041	4,138,321	2,930,887	(4,274,406)	62,040,686
Investments limited or restricted as to use, less current portion	953,966	35,767,243	83,768,370	—	—	120,489,579
Interest in net assets of Foundation	—	200,208	—	—	(200,208)	—
Notes receivable	—	65,493	2,799,976	—	—	2,865,469
Property and equipment, net	—	161,565,449	—	—	—	161,565,449
Other assets	—	5,368,007	538,625	—	—	5,906,632
	$ 1,215,809	261,950,441	91,245,292	2,930,887	(4,474,614)	352,867,815
Liabilities and Net Assets						
Current liabilities:						
Current maturities of long-term debt	$ —	2,195,000	—	—	—	2,195,000
Current portion of obligations under capital leases	—	395,075	—	—	—	395,075
Accounts payable	—	5,440,700	—	594,834	—	6,035,534
Accrued salaries, wages, and employee benefits	—	11,654,955	—	2,667,639	—	14,322,594
Third-party payor settlements payable	—	3,871,279	—	—	—	3,871,279
Due to affiliates	86,548	4,143,988	271,624	43,869	(4,274,406)	271,623
Other accrued expenses	—	4,831,921	381,526	323,445	—	5,536,892
Total current liabilities	86,548	32,532,918	653,150	3,629,787	(4,274,406)	32,627,997
Long-term liabilities:						
Long-term debt, less current portion	—	94,970,868	—	—	—	94,970,868
Obligations under capitalized leases, less current portion	—	4,554,594	—	—	—	4,554,594
Self-insurance liabilities	—	4,688,915	—	—	—	4,688,915
Accrued pension liabilities	—	33,645,313	—	1,260,000	—	34,905,313
Other long-term liabilities	652,303	—	—	—	—	652,303
Total liabilities	738,851	170,392,608	653,150	4,889,787	(4,274,406)	172,399,990
Net assets (deficit):						
Unrestricted	61,369	84,155,363	90,592,142	(1,958,900)	—	172,849,974
Temporarily restricted	200,208	4,498,316	—	—	(200,208)	4,498,316
Permanently restricted	215,381	2,904,154	—	—	—	3,119,535
Total net assets	476,958	91,557,833	90,592,142	(1,958,900)	(200,208)	180,467,825
	$ 1,215,809	261,950,441	91,245,292	2,930,887	(4,474,614)	352,867,815

See accompanying independent auditors' report.

Schedule 1

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Supplemental Consolidating Balance Sheet Information

June 30, 2010

Assets	North Baltimore Center, Inc.	Family Services Agency, Inc.	Mosaic Community Services, Inc.	Turning Point of Washington County, Inc.	Way Station, Inc.	Consolidating eliminations	Consolidated totals
Current assets:							
Cash and cash equivalents	$ 178,488	503,439	3,386,119	584,745	4,915,374	—	40,342,845
Temporary investments	—	—	553,166	—	182,379	—	735,545
Investments limited or restricted as to use	125,000	—	121,417	—	300,117	—	2,978,971
Accounts receivable, net	776,869	1,438,869	1,875,068	—	1,536,595	—	29,117,328
Current portion of notes receivable	—	—	—	—	—	—	125,949
Due from affiliates	61,392	51,800	236,222	105,079	8,330	(1,411,489)	—
Prepaid expenses and other current assets	57,634	262,724	620,460	259	1,749,408	—	6,959,512
Total current assets	1,199,383	2,256,832	6,792,452	690,083	8,692,203	(1,411,489)	80,260,150
Investments limited or restricted as to use, less current portion	1,208,419	—	1,565,404	—	271,212	(271,188)	123,263,426
Interest in net assets of Foundation	—	—	—	—	—	—	—
Notes receivable	—	—	—	—	—	—	2,865,469
Property and equipment, net	3,131,408	7,057,740	10,533,236	1,019,782	7,639,079	—	190,946,694
Other assets	112,441	68,577	107,704		389,840	—	6,585,194
	$ 5,651,651	9,383,149	18,998,796	1,709,865	16,992,334	(1,682,677)	403,920,933
Liabilities and Net Assets							
Current liabilities:							
Current maturities of long-term debt	$ 132,020	1,344,452	407,823	13,769	261,978	—	4,355,042
Current portion of obligations under capital leases	—	32,392	—	—	—	—	427,467
Accounts payable	126,366	356,950	460,573	—	314,558	—	7,293,981
Accrued salaries, wages, and employee benefits	768,023	712,115	1,927,192	—	1,488,791	—	19,218,715
Third-party payor settlements payable	—	—	—	—	—	—	3,871,279
Due to affiliates	397,063	3,005	201,105	8,330	801,551	(1,682,677)	—
Other accrued expenses	478,127	285,056	38,869	—	581,269	—	6,920,213
Total current liabilities	1,901,599	2,733,970	3,035,562	22,099	3,448,147	(1,682,677)	42,086,697
Long-term liabilities:							
Long-term debt, less current portion	2,992,875	4,025,539	6,555,607	47,494	963,456	—	109,555,839
Obligations under capitalized leases, less current portion	—	30,902	—	—	—	—	4,585,496
Self-insurance liabilities	—	—	—	—	—	—	4,688,915
Accrued pension liabilities	—	—	—	—	—	—	34,905,313
Other long-term liabilities	407,453	272,365	405,086	—	429,011	—	2,166,218
Total liabilities	5,301,927	7,062,776	9,996,255	69,593	4,840,614	(1,682,677)	197,988,478
Net assets (deficit):							
Unrestricted	349,724	2,320,373	8,567,165	1,640,272	10,728,378	—	196,455,886
Temporarily restricted	—	—	86,416	—	1,423,342	—	6,008,074
Permanently restricted	—	—	348,960	—	—	—	3,468,495
Total net assets	349,724	2,320,373	9,002,541	1,640,272	12,151,720	—	205,932,455
	$ 5,651,651	9,383,149	18,998,796	1,709,865	16,992,334	(1,682,677)	403,920,933

See accompanying independent auditors' report.

Schedule 2, (Continued)

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Supplemental Consolidating Statement of Operations Information

Year ended June 30, 2010

	Sheppard and Enoch Pratt Foundation, Inc.	Sheppard Pratt Health System, Inc.	Sheppard Pratt Investment, Inc.	Sheppard Pratt Physicians, P.A.	Obligated group combining eliminations	Combined obligated group subtotal
Unrestricted revenues, gains, and other support:						
Net patient service revenue	$ —	100,939,386	—	17,276,299	—	118,215,685
Residential and educational service revenue	—	66,614,944	—	—	—	66,614,944
Net assets released from restrictions used for operations	—	485,087	—	—	—	485,087
Gain(loss) on disposal of assets	—	(9,903)	—	—	—	(9,903)
Other	6	9,358,048	—	10,131,554	(12,348,499)	7,141,109
Total unrestricted revenues, gains, and other support	6	177,387,562	—	27,407,853	(12,348,499)	192,446,922
Expenses:						
Salaries and wages	—	84,553,497	—	17,254,876	—	101,808,373
Employee benefits	—	22,782,124	—	2,834,552	—	25,616,676
Expendable supplies	—	12,281,943	—	—	—	12,281,943
Purchased services	2,983	31,334,635	—	7,210,673	(12,611,942)	25,936,349
Interest	—	3,020,442	—	—	—	3,020,442
Repairs and minor alterations	—	4,785,444	—	—	—	4,785,444
Depreciation and amortization	—	12,645,787	—	—	—	12,645,787
Provision for doubtful accounts	—	3,390,459	—	2,313,110	—	5,703,569
Total expenses	2,983	174,794,331	—	29,613,211	(12,611,942)	191,798,583
Operating gain (loss)	(2,977)	2,593,231	—	(2,205,358)	263,443	648,339
Other income (expense):						
Investment income	—	364,979	2,157,531	—	(263,443)	2,259,067
Realized gains on sale of investments	—	655,904	3,729,705	—	—	4,385,609
Change in net unrealized gain on trading securities	—	1,030,207	5,041,226	—	—	6,071,433
Other	—	438,309	72,521	—	—	510,830
Total other income (expense)	—	2,489,399	11,000,983	—	(263,443)	13,226,939
Excess (deficiency) of revenues over expenses	(2,977)	5,082,630	11,000,983	(2,205,358)	—	13,875,278
Other changes in net assets:						
Net assets released from restrictions used for purchases of property and equipment	—	278,443	—	—	—	278,443
Transfer to affiliates	—	2,654,680	(2,654,680)	—	—	—
Pension liability adjustment	—	(10,998,679)	—	—	—	(10,998,679)
Reclassification of net assets	—	—	—	—	—	—
Increase (decrease) in unrestricted net assets	$ (2,977)	(2,982,926)	8,346,303	(2,205,358)	—	3,155,042

See accompanying independent auditors' report.

Schedule 2

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Supplemental Consolidating Statement of Operations Information

Year ended June 30, 2010

	North Baltimore Center, Inc.	Family Services Agency, Inc.	Mosaic Community Services, Inc.	Turning Point of Washington County, Inc.	Way Station, Inc.	Consolidating eliminations	Consolidated totals
Unrestricted revenues, gains, and other support:							
Net patient service revenue	$	—	—		—	(41,583)	118,174,102
Residential and educational service revenue	13,414,769	12,049,868	20,261,796		17,808,580	—	130,149,957
Net assets released from restrictions used for operations	2,500	42,756	15,258		675,819	—	1,221,420
Gain(loss) on disposal of assets	100	34,064	(5,161)	—	—	—	19,100
Other	42,295	608,526	2,636,282	123,400	5,834,347	(1,224,775)	15,161,184
Total unrestricted revenues, gains, and other support	13,459,664	12,735,214	22,908,175	123,400	24,318,746	(1,266,358)	264,725,763
Expenses:							
Salaries and wages	7,690,863	6,216,682	13,135,056	—	14,557,827	—	143,408,801
Employee benefits	1,249,555	2,256,013	2,134,856	—	2,839,412	—	34,096,512
Expendable supplies	583,497	536,239	692,632	—	1,106,170	—	15,200,481
Purchased services	3,445,278	2,096,031	4,387,155	123,400	3,382,647	(1,266,358)	38,104,502
Interest	192,897	202,794	416,814	5,997	53,575	—	3,892,519
Repairs and minor alterations	498,956	158,648	658,673	—	482,232	—	6,583,953
Depreciation and amortization	229,354	451,188	1,020,371	39,124	504,171	—	14,889,995
Provision for doubtful accounts	938,458	541,819	190,094	—	170,218	—	7,544,158
Total expenses	14,828,858	12,459,414	22,635,651	168,521	23,096,252	(1,266,358)	263,720,921
Operating gain (loss)	(1,369,194)	275,800	272,524	(45,121)	1,222,494	—	1,004,842
Other income (expense):							
Investment income	60,062	—	—	4,196	6,595	—	2,329,920
Realized gains on sale of investments	—	—	—	—	6,249	—	4,391,858
Change in net unrealized gain on trading securities	—	—	—	—	15,286	—	6,086,719
Other	37,368	(114,199)	56,398	—	—	—	490,397
Total other income (expense)	97,430	(114,199)	56,398	4,196	28,130	—	13,298,894
Excess (deficiency) of revenues over expenses	(1,271,764)	161,601	328,922	(40,925)	1,250,624	—	14,303,736
Other changes in net assets:							
Net assets released from restrictions used for purchases of property and equipment	—	—	—	—	38,712	—	317,155
Transfer to affiliates	—	—	—	—	—	—	—
Pension liability adjustment	—	—	—	—	—	—	(10,998,679)
Reclassification of net assets	—	—	—	—	450,057	—	450,057
Increase (decrease) in unrestricted net assets	$ (1,271,764)	161,601	328,922	(40,925)	1,739,393	—	4,072,269

See accompanying independent auditors' report.

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Supplemental Consolidating Statement of Changes in Net Assets Information

Year ended June 30, 2010

		Sheppard and Enoch Pratt Foundation, Inc.	Sheppard Pratt Health System, Inc.	Sheppard Pratt Investment, Inc.	Sheppard Pratt Physicians, P.A.	Obligated group combining eliminations	Combined obligated group subtotal
Unrestricted net assets:							
Excess (deficiency) of revenues over expenses	$	(2,977)	5,082,630	11,000,983	(2,205,358)	—	13,875,278
Other changes in net assets:							
Net assets released from restrictions used for purchases of property and equipment		—	278,443	—	—	—	278,443
Transfer from (to) subsidiaries		—	2,654,680	(2,654,680)	—	—	—
Change in unrealized gains and losses for pension liabilities		—	(10,998,679)	—	—	—	(10,998,679)
Reclassification of net assets		—	—	—	—	—	—
Increase (decrease) in unrestricted net assets		(2,977)	(2,982,926)	8,346,303	(2,205,358)	—	3,155,042
Temporarily restricted net assets:							
Gifts and grants		(13,582)	302,193	—	—	—	288,611
Investment income		—	94,888	—	—	—	94,888
Net gain (loss) on investments		—	349,655	—	—	—	349,655
Interest in net assets of Foundation		—	(95,052)	—	—	95,052	—
Transfer from (to) subsidiaries		(81,469)	38,229	—	—	—	(43,240)
Net assets released from restrictions		—	(763,530)	—	—	—	(763,530)
Reclassification of net assets		—	—	—	—	—	—
Increase (decrease) in temporarily restricted net assets		(95,051)	(73,617)	—	—	95,052	(73,616)
Permanently restricted net assets:							
Gifts		—	1,500	—	—	—	1,500
Investment income		48,877	—	—	—	—	48,877
Reclassification of net assets		—	—	—	—	—	—
Increase (decrease) in permanently restricted net assets		48,877	1,500	—	—	—	50,377
Increase (decrease) in net assets		(49,151)	(3,055,043)	8,346,303	(2,205,358)	95,052	3,131,803
Net assets (deficit), beginning of year		526,109	94,612,876	82,245,839	246,458	(295,260)	177,336,022
Net assets (deficit), end of year	$	476,958	91,557,833	90,592,142	(1,958,900)	(200,208)	180,467,825

See accompanying independent auditors' report.

Schedule 3

SHEPPARD AND ENOCH PRATT FOUNDATION, INC. AND SUBSIDIARIES

Supplemental Consolidating Statement of Changes in Net Assets Information

Year ended June 30, 2010

	North Baltimore Center, Inc.	Family Services Agency, Inc.	Granite House, Inc.	Mosaic Community Services, Inc.	Turning Point of Washington County, Inc.	Way Station, Inc.	Consolidating eliminations	Consolidated totals
Unrestricted net assets:								
Excess (deficiency) of revenues over expenses	$ (1,271,764)	161,601	—	328,922	(40,925)	1,250,624	—	14,303,736
Other changes in net assets:								
Net assets released from restrictions used for purchases of property and equipment	—	—	—	—	—	38,712	—	317,155
Transfer from (to) subsidiaries	—	—	—	—	—	—	—	—
Change in unrealized gains and losses for pension liabilities	—	—	—	—	—	—	—	(10,998,679)
Reclassification of net assets	—	—	—	—	—	450,057	—	450,057
Increase (decrease) in unrestricted net assets	(1,271,764)	161,601	—	328,922	(40,925)	1,739,393	—	4,072,269
Temporarily restricted net assets:								
Gifts and grants	—	—	—	(38,059)	—	675,025	—	925,577
Investment income	—	—	—	3,741	—	—	—	98,629
Net gain (loss) on investments	—	—	—	—	—	—	—	349,655
Interest in net assets of Foundation	—	—	—	—	—	—	—	—
Transfer from (to) subsidiaries	2,500	—	—	10,640	—	30,100	—	—
Net assets released from restrictions	(2,500)	(42,756)	—	(15,258)	—	(714,531)	—	(1,538,575)
Reclassification of net assets	—	—	—	—	—	(450,057)	—	(450,057)
Increase (decrease) in temporarily restricted net assets	—	(42,756)	—	(38,936)	—	(459,463)	—	(614,771)
Permanently restricted net assets:								
Gifts	—	—	—	—	—	—	—	1,500
Investment income	—	—	—	(5,357)	—	—	—	43,520
Increase (decrease) in permanently restricted net assets	—	—	—	(5,357)	—	—	—	45,020
Increase (decrease) in net assets	(1,271,764)	118,845	—	284,629	(40,925)	1,279,930	—	3,502,518
Net assets (deficit), beginning of year	1,621,488	2,201,528	—	8,717,912	1,681,197	10,871,790	—	202,429,937
Net assets (deficit), end of year	$ 349,724	2,320,373	—	9,002,541	1,640,272	12,151,720	—	205,932,455

See accompanying independent auditors' report.