WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidated Financial Statements and Supplementary Information

June 30, 2013 and 2012

(With Independent Auditors' Report thereon)

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Table of Contents

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

Independent Auditors' Report

The Board of Directors
Western Maryland Health System Corporation:

We have audited the accompanying consolidated financial statements of Western Maryland Health System Corporation, which comprise the consolidated balance sheets as of June 30, 2013 and 2012, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Western Maryland Health System Corporation as of June 30, 2013 and 2012, and the results of its operations and its cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles

Emphasis of Matter

As discussed in note 2(u) to the consolidated financial statements, in 2013, the Health System adopted new accounting guidance, Accounting Standards Update 2011-07, *Health Care Entities (Topic 954), Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities.* Our opinion is not modified with respect to this matter.

Other Matter

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary information in Schedules 1-3 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

October 18, 2013

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidated Balance Sheets

June 30, 2013 and 2012

(Dollars in thousands)

Assets		2013	2012
Current assets:			
Cash and cash equivalents	$	51,953	44,573
Investments		43,528	31,951
Funds on deposit with trustee		15,476	15,303
Accounts receivable, less allowance for doubtful accounts of $5,093 in 2013 and $5,907 in 2012		40,847	41,515
Pledge receivable, net		605	941
Other receivables, less allowance for uncollectible accounts of $1,190 in 2013 and $2,022 in 2012		4,774	3,831
Inventories and other current assets		10,250	10,208
Total current assets		167,433	148,322
Funds on deposit with trustee		36,439	32,701
Board designated investments		5,465	945
Other long-term investments		405	636
Investments restricted by donor or grantor		4,604	2,221
Beneficial interest in trustee held Foundation assets		1,823	1,728
Property and equipment, net		332,336	354,451
Unamortized financing fees		3,997	4,258
Investments in affiliates		18,438	17,012
Other assets		5,228	4,241
Total assets	$	576,168	566,515
Liabilities and Net Assets			
Current liabilities:			
Current portion of long-term debt	$	8,229	7,863
Accounts payable and accrued liabilities		6,848	7,193
Accrued bond interest payable		7,691	7,858
Accrued salaries and benefits		14,209	15,099
Payable to third-party payors		6,956	8,050
Total current liabilities		43,933	46,063
Long-term debt, net of current portion		319,773	328,663
Pension benefits in excess of pension assets		39,047	60,202
Other liabilities		14,966	13,380
Total liabilities		417,719	448,308
Commitments and contingencies			
Net assets:			
Unrestricted:			
Unrestricted net assets		150,081	111,282
Noncontrolling interest in consolidated subsidiaries		1,510	2,094
Total unrestricted net assets		151,591	113,376
Temporarily restricted		4,790	2,862
Permanently restricted		2,068	1,969
Total net assets		158,449	118,207
Total liabilities and net assets	$	576,168	566,515

See accompanying notes to consolidated financial statements.

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidated Statements of Operations

Years ended June 30, 2013 and 2012

(Dollars in thousands)

	2013	2012
Unrestricted revenues, gains and other support:		
Patient service revenue (net of contractual allowances and charity)	$ 298,772	289,334
Provision for bad debts	(7,514)	(5,817)
Net patient service revenue	291,258	283,517
Other revenue	9,823	5,365
Total revenues, gains and other support	301,081	288,882
Expenses:		
Salaries and wages	104,097	109,711
Employee benefits	39,745	33,736
Professional fees	11,437	9,129
Purchased services	18,530	19,155
Supplies	55,023	61,169
Utilities	4,002	4,497
Insurance	4,932	4,761
Interest	15,457	15,788
Depreciation and amortization	27,257	28,774
Other	7,902	8,001
Total expenses	288,382	294,721
Operating income (loss)	12,699	(5,839)
Nonoperating income:		
Equity in income of affiliates	1,424	4,649
Investment income, including realized gains on trading portfolio	2,582	2,686
Unrealized gains on trading portfolio	628	619
Other	483	131
Total nonoperating income	5,117	8,085
Excess of revenues over expenses	$ 17,816	2,246

See accompanying notes to consolidated financial statements.

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidated Statements of Changes in Net Assets

Years ended June 30, 2013 and 2012

(Dollars in thousands)

	Unrestricted net assets	Temporarily restricted net assets	Permanently restricted net assets	Total net assets
Balance at June 30, 2011	$ 154,682	4,327	2,035	161,044
Excess of revenues over expenses	2,246	—	—	2,246
Investment income	—	5	—	5
Donations	—	112	—	112
Grants	—	735	—	735
Change in funded status of pension plan	(39,795)	—	—	(39,795)
Net assets released for operations	—	(1,509)	—	(1,509)
Net assets released for purchase of property and equipment	808	(808)	—	—
Change in beneficial interest of trustee-held Foundation assets	—	—	(66)	(66)
Distributions to noncontrolling interest in consolidated subsidiaries	(4,565)	—	—	(4,565)
Change in net assets	(41,306)	(1,465)	(66)	(42,837)
Balance at June 30, 2012	113,376	2,862	1,969	118,207
Excess of revenues over expenses	17,816	—	—	17,816
Investment loss	—	(7)	—	(7)
Donations	—	3,180	—	3,180
Grants	—	69	—	69
Change in funded status of pension plan	22,506	—	—	22,506
Net assets released for operations	—	(886)	—	(886)
Net assets released for purchase of property and equipment	428	(428)	—	—
Change in beneficial interest of trustee-held Foundation assets	—	—	99	99
Asbestos liability adjustment	345	—	—	345
Distributions to noncontrolling interest in consolidated subsidiaries	(2,880)	—	—	(2,880)
Change in net assets	38,215	1,928	99	40,242
Balance at June 30, 2013	$ 151,591	4,790	2,068	158,449

See accompanying notes to consolidated financial statements.

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidated Statements of Cash Flows

Years ended June 30, 2013 and 2012

(Dollars in thousands)

	2013	2012
Cash flows from operating activities:		
Change in net assets	$ 40,242	(42,837)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	27,257	28,774
Amortization of bond premium	661	684
Change in funded status of pension plan	(22,506)	39,795
Provision for bad debts	7,514	5,817
Distributions to noncontrolling interest holder	2,880	4,565
Equity in (income) loss of affiliates	(1,424)	(4,649)
Realized and unrealized gains (losses) on investments	(1,526)	(1,725)
Change in beneficial interest in trustee held Foundation assets	(99)	66
Changes in assets and liabilities:		
Accounts receivable	(6,846)	(2,707)
Other receivables	(943)	1,137
Inventories and other current assets	(42)	2,325
Accounts payable and accrued liabilities, accrued bond interest payable and accrued salaries and benefits	(1,402)	2,097
Payable to third-party payors	(1,094)	1,999
Other assets, funded status of pension plan, and other liabilities	628	(1,513)
Net cash provided by operating activities	43,300	33,828
Cash flows from investing activities:		
Purchase of long-lived assets	(4,881)	(9,774)
Change in funds on deposit with trustee	(3,911)	(8,695)
Net change in investments	(16,484)	(7,660)
Distributions from unconsolidated entities	—	4,000
Net cash used in investing activities	(25,276)	(22,129)
Cash flows from financing activities:		
Repayments of long-term debt	(7,445)	(7,120)
Capital lease payments	(418)	(394)
Restricted investment income (loss)	99	(66)
Distributions to noncontrolling interest holder	(2,880)	(4,565)
Net cash used in financing activities	(10,644)	(12,145)
Net increase (decrease) in cash and cash equivalents	7,380	(446)
Cash and cash equivalents at beginning of year	44,573	45,019
Cash and cash equivalents at end of year	$ 51,953	44,573
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 15,336	15,699

See accompanying notes to consolidated financial statements.

(1) Mission and Organization

Western Maryland Health System Corporation (the Health System or WMHS) is a not-for-profit community health system. The mission of the Health System is to improve the health status and quality of life of the individuals and the communities served, especially those in need. The Health System provides patient and family centered services through responsible management of human and fiscal resources. The Health System is a values-driven health system that respects and supports life, preserves the dignity of each individual, and promotes a healthy and just society through collaboration with others who share the Health System's values.

The Health System accepts patients regardless of their ability to pay. Those patients who meet certain criteria under its charity care policies receive services at no charge or at an amount less than full charges. Essentially, these policies define charity services as those services for which no payment is anticipated. In addition to providing charity care, the Health System provides other programs and services for the general community. The Health System offers over 90 community health programs that include programs that target health education programs and health screenings to patients. A wide variety of health screenings are offered throughout the year for the general community that are free of charge or offered for a nominal fee. The Health System provides free education programs on a variety of health topics. The Health System also sponsors an annual community health fair, which provides health screenings, education and activities targeted to health and safety.

The Health System comprises the following wholly or partially owned, and controlled, consolidated subsidiaries in Cumberland, Maryland:

(a) Acute Care Hospital

Western Maryland Regional Medical Center – a full service community hospital located in Cumberland, Maryland, licensed for 275 acute care beds, owned and operated by the Health System.

(b) Long-Term Care

Frostburg Nursing and Rehabilitation Center (Frostburg)

(c) Other

Western Maryland Health System Foundation, Inc. (Foundation)

Western Maryland Insurance Company, Ltd. (WMIC)

Haystack Consolidated Services Inc. (Haystack)

Cumberland Properties, Inc.

Memorial Medical Center Services, Inc. (MMCS)

Johnson Heights Medical Building Partnership (Johnson Heights)

Haystack Imaging Services, LLC (Haystack Imaging)

In addition, the Health System has investments in several unconsolidated affiliates, which are accounted for on the cost or equity methods of accounting, as appropriate (see note 6).

(2) Summary of Significant Accounting Policies

(a) Principles of Consolidation

The consolidated financial statements are prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles, and include the accounts of the Health System and its subsidiaries and controlled entities. Significant intercompany accounts and transactions have been eliminated in consolidation. The Health System's consolidated financial statements reflect the respective interests of the minority investors in the joint ventures' net assets and changes in net assets.

(b) Investments in Affiliates

Investments in certain joint ventures, which are not controlled by the Health System, are accounted for using the cost or equity method of accounting as appropriate (see note 6). These investments are included as investments in affiliates in the accompanying consolidated balance sheets. The Health System's proportionate share of income or loss of the unconsolidated joint ventures is included in nonoperating income in the accompanying consolidated statements of operations.

(c) Cash Equivalents

Cash equivalents consist primarily of temporary investments with maturities of three months or less when purchased and certain overnight repurchase agreements. Overnight repurchases are principally unsecured and are subject to normal credit risk.

(d) Accounts Receivable

Patient accounts receivable are stated at estimated net realizable amounts from patients, third-party payors and other insurers when services are provided. The Health System bills the insurer directly for services provided. Insurance coverage and credit information is obtained from patients when available. No collateral is obtained for accounts receivable.

(e) Inventories

Inventories primarily consist of medical supplies and drugs and are carried at lower of cost or market. Cost is determined principally using the average cost method, which approximates the first-in first-out (FIFO) method.

(f) Investments

The Health System's investment portfolio, including board designated investments and investments restricted by donor or grantor, is considered a trading portfolio and is classified as current or noncurrent assets based on management's intention as to use. Accordingly, realized and unrealized gains and losses are included in investment income in the accompanying consolidated statements of

operations. Dividend and interest income, as well as realized gains on sales of securities, are included in investment income.

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the balance sheet. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in the excess of revenues over expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from the excess of revenues over expenses unless the investments are trading securities.

(g) Property and Equipment

Property and equipment are stated at cost or, if donated, at fair market value at date of gift. Depreciation is determined using a straight-line basis over the estimated useful lives of the related assets. Repairs and maintenance are expensed as incurred.

Gifts of long-lived assets, such as land, building or equipment, or cash gifts to be used for purchase of long-lived assets, are reported as unrestricted support, 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 reported are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as temporarily restricted net assets. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported as released from restrictions when the donated or acquired long-lived assets are placed in service.

The Health System opened a 275-bed, state-of-the-art hospital on November 21, 2009. Adjacent to the hospital is a 120,000-square-foot medical office building (MOB) previously owned and operated by a third-party medical office building developer until the purchase of the MOB by WMHS on February 17, 2011. The MOB includes both hospital services and physicians' office space.

(h) 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 Accounting Standards Codification (ASC) Subtopic 360-10, *Accounting for the Impairment or Disposal of Long-Lived Assets*, if there is an indication that the carrying amount of an asset is not recoverable, the Health System projects 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 discounted cash flows.

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, the Health System groups the assets at the lowest level for which there are identifiable cash flows independent of other groups of assets. If such assets are impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets.

(i) Financing Costs

Financing costs incurred in issuing long-term debt have been deferred and are shown separately on the balance sheet. These costs are being amortized using the effective interest method over the term of the related debt. The unamortized balances were $3,997 and $4,258 at June 30, 2013 and 2012, respectively.

(j) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are limited as to use by donors to a specific time period or purpose. Permanently restricted net assets are to be held in perpetuity at the instruction of the donor. Income from permanently restricted net assets is used as defined by the donor.

(k) Net Patient Service Revenue

On November 16, 2010, the Health System and the Health Services Cost Review Commission (HSCRC) agreed to a three-year contract for the Health System to implement the Total Patient Revenue (TPR) methodology, effective July 1, 2010. The TPR agreement establishes a prospective, fixed revenue base "TPR cap," for the upcoming year. This includes both inpatient and outpatient regulated services. Under TPR, the Health System's revenue for all HSCRC regulated services is predetermined for the upcoming year, regardless of changes in volume, service mix intensity, or mix of inpatient or outpatient services that occurred during the year. The TPR agreement allows the Health System to adjust unit rates, within certain limits, to achieve the overall revenue base for the Health System at year end. Any overcharge or undercharge versus the TPR cap is prospectively added to the subsequent year's TPR cap. Although the TPR cap does not adjust for changes in volume or service mix, the TPR cap is adjusted annually for inflation, and for changes in payor mix and uncompensated care. Beginning in year three of the three-year contract, the Health System will receive an annual adjustment to its cap for the change in population in the Health System's service area. TPR is designed to encourage hospitals to operate efficiently by reducing utilization and managing patients in the appropriate care delivery setting.

Contractual adjustments, which represent the difference between amounts billed as patient service revenue and amounts paid by third-party payors, are accrued in the period in which the related services are rendered. Because the Health System does not pursue collection of amounts determined to qualify as charity care, such amounts are not reported as revenue.

The Maryland Medicaid program is administered primarily through independent licensed managed care organizations. The State of Maryland has contracts with these independent managed care organizations to manage the care to eligible participants. Amounts due from the Medicaid program in Maryland are primarily due from the independent managed care organizations.

Under certain provisions of the American Recovery and Reinvestment Act of 2009 (ARRA), federal incentive payments are available to hospitals, physicians and certain other professionals (Providers) when they adopt, implement or upgrade (AIU) certified electronic health record (EHR) technology or become "meaningful users," as defined under ARRA, of EHR technology in ways that demonstrate improved quality, safety and effectiveness of care. Providers can become eligible for annual Medicare incentive payments by demonstrating meaningful use of EHR technology in each period over four periods. Medicaid providers can receive their initial incentive payment by satisfying AIU criteria, but must demonstrate meaningful use of EHR technology in subsequent years in order to qualify for additional payments. Hospitals may be eligible for both Medicare and Medicaid EHR incentive payments; however, physicians and other professionals may be eligible for either Medicare or Medicaid incentive payments, but not both. The Health System recognizes Medicare EHR incentive payments when it is reasonably assured that the Health System will successfully demonstrate compliance with the specified meaningful use criteria. The Health System satisfied the CMS AIU and/or meaningful use criteria. As a result, the Health System recognized approximately $4,744 of Medicare and Medicaid EHR incentive payments in other operating revenues in the consolidated statement of operations for the year ended June 30, 2013.

(l) Excess of Revenues over Expenses

The consolidated statement of operations includes the performance indicator, excess of revenues over expenses. Changes in unrestricted net assets, which are excluded from excess of revenues over expenses, include unrealized gains and losses on other than trading securities, change in funded status of the pension plan, permanent transfers of assets to and from affiliates for other than goods and services, and contributions of long-lived assets (including assets acquired using contributions, which by donor restriction were to be used for the purposes of acquiring such assets).

(m) Charity Care

The Health System, as an integral part of its mission, accepts and treats all patients without regard to their ability to pay. A patient is classified as a charity patient in accordance with established criteria. Charity care is the recognition of services rendered for which no payment is expected.

(n) Donations

Unconditional donations are included in income when pledged or received. Donations restricted as to use by the donor are reflected as additions to temporarily or permanently restricted net assets. Expenditures of temporarily restricted net assets are transferred to unrestricted net assets if for capital additions, or reported as other revenue if for operating purposes.

(o) Income Taxes

The Health System and substantially all of its affiliates are tax exempt organizations under section 501(c)(3) of the Internal Revenue Code (IRC) and are not subject to income taxes except to the extent it has taxable income from activities that are not related to its exempt purpose. No provision for income taxes was required to be made in the consolidated financial statements for these entities.

Johnson Heights is a general partnership and Haystack Imaging is a limited liability company and both are not directly subject to income taxes. The results of their operations are included in the tax returns of their partners. Haystack and MMCS are taxable for profit entities, which recognized an immaterial amount of taxable losses during 2013 and 2012.

The Health System and affiliates account for tax provisions in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Subtopic 740-10, *Accounting for Uncertainty in Income Taxes*, which creates a single model to address uncertainty in tax positions and clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. Under the requirements of ASC Subtopic 740-10, an entity could be required to record an obligation as the result of a tax position they have historically taken on various tax exposure items. The Health System and affiliates have determined that it did not have any uncertain tax positions as of June 30, 2013 and 2012.

(p) Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

(q) Western Maryland Health System Foundation

The Foundation is controlled by the Health System and thus its assets, liabilities, net assets and results of operations are consolidated within the Health System's financial statements.

(r) Beneficial Interest in Trustee Held Assets

The Health System records a beneficial interest in several trusts (the assets of which are to be held in perpetuity) for which a portion of the income is to be distributed to the Health System. These changes in the fair value of the trusts are recorded as unrealized gains/losses in permanently restricted net assets.

(s) Pension Plan

For employees hired prior to July 1, 2011, the Health System has a noncontributory defined benefit pension plan covering substantially all of its employees upon their retirement. Since 2008, the benefits are based on age, years of service and career average pay. Grandfathered employees prior to 2008 are based on age, years of service and final average pay based on their five highest paid years of their last 10 years of service. Effective July 1, 2011, employees hired or rehired will not participate in the plan. These employees will participate in a new defined contribution plan that has been developed.

For the defined benefit pension plan, the Health System records annual amounts relating to its pension plan based on calculations that incorporate various actuarial and other assumptions including, discount rates, mortality, assumed rates of return, compensation increases, turnover rates

(Dollars in thousands)

and healthcare cost trend rates. The Health System reviews its assumptions on an annual basis and makes modifications to the assumptions based on current rates and trends when it is appropriate to do so. The Health System believes that the assumptions utilized in recording its obligations under its plans are reasonable based on its experience and market conditions.

(t) Reclassifications

Certain prior year amounts in note (17) Functional Expenses have been reclassified to reflect the effects of the Accounting Pronouncement discussed in note 2(u). The result reduced the 2012 Healthcare Services expenses by the provision for bad debts of $5,817.

(u) New Accounting Pronouncements

In July 2011, the FASB issued ASU No. 2011-07, *Health Care Entities (Topic 954), Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*, which requires a healthcare entity to change the presentation of their statement of operations by reclassifying the provision for bad debts associated with patient service revenue from an operating expense to a deduction from patient service revenue (net of contractual allowance and discounts). Additionally, enhanced disclosures about an entity's policies for recognizing, assessing bad debts, as well as qualitative and quantitative information about changes in the allowance for doubtful accounts are required. As permitted, the Health System adopted ASU No. 2011-07 beginning July 1, 2012. As such the Health System reclassified the provision for uncollectible, $7,514 and $5,817 for the years ended 2013 and 2012, respectively, from operating expenses to a reduction of patient service revenue in the statement of operations. In addition, the required disclosures related to the Health System's sources of patient service revenue and changes in the allowance for doubtful accounts can be found at note 3.

(3) Accounts Receivable, Allowance for Doubtful Accounts and Business Concentrations

During fiscal years 2013 and 2012, net patient service revenue was received from the following payors:

	2013	2012
Medicare	55%	55%
Medicaid	14	13
Blue Cross	12	13
Self-pay	4	3
Other	15	16
	100%	100%

(Dollars in thousands)

Gross accounts receivable at June 30, 2013 and 2012 consisted of the following payors:

	2013	2012
Medicare	43%	42%
Medicaid	11	12
Blue Cross	14	13
Self-pay	19	18
Other	13	15
	100%	100%

Patient accounts receivable are reduced by allowances for bad debts. In evaluation the collectability of accounts receivable, the Health System analyzes historical collections and write-offs and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for bad debts and provision for uncollectible accounts. Management regularly reviews its estimate and evaluates the sufficiency of the allowance for bad debts. The Health System analyzes contractual amounts due from patients who have third-party coverage and provides and allowance for doubtful accounts and a provision for bad debts. For patient accounts receivable associated with self-pay patients, which includes those patients without insurance coverage exists for a portion of the bill, the Health System records a significant provision for bad debts for patients that are unable or unwilling to pay for the portion of the bill representing their financial responsibility. Account balances are charged off against the allowance for doubtful accounts after all means of collection has been exhausted.

The activity in the allowance for bad debts is summarized as follows for the years ended June 30:

		2013	2012
Beginning balance as of July 1	$	5,907	7,539
Provision for uncollectible accounts		7,514	5,817
Less write offs		(8,328)	(7,449)
Ending balance as of June 30	$	5,093	5,907

(Continued)

(Dollars in thousands)

(4) Investments

Investments, which include Funds on deposit with trustees, Board designated investments and Investments restricted by donor or grantor, consist of the following as of June 30:

		2013	2012
U.S. government obligations	$	14,014	6,346
Money market funds		24,411	2,695
Corporate stocks and other		13,897	12,056
Fixed income securities		53,595	62,660
	$	105,917	83,757

Investments have been classified in the accompanying consolidated balance sheets as follows as of June 30:

		2013	2012
Short-term investments	$	43,528	31,951
Funds on deposit with trustee		51,915	48,004
Board designated investments		5,465	945
Other long-term investments		405	636
Investments restricted by donor or grantor		4,604	2,221
	$	105,917	83,757

Investment income and gains for assets limited as to use, cash equivalents, and other investments comprise the following for the years ended June 30:

		2013	2012
Income:			
Investment income	$	1,684	1,580
Realized gains on trading investment portfolio		898	1,106
Unrealized gains on trading investment portfolio		628	619
	$	3,210	3,305

(Continued)

(Dollars in thousands)

(5) Property and Equipment

Property and equipment and estimated useful lives (in years) are summarized as follows as of June 30:

		2013	2012
Land and land improvements (2–25 years)	$	14,363	16,191
Buildings and improvements (5–40 years)		333,319	400,563
Equipment (3–20 years)		174,550	171,357
Construction in progress		911	109
		523,143	588,220
Less accumulated depreciation		190,807	233,769
Property and equipment, net	$	332,336	354,451

Depreciation expense for the year ended June 30, 2013 was $26,996. Depreciation expense for the year ended June 30, 2012 was $28,464 including an impairment of long-lived assets for $2,125.

(6) Investments in Affiliates

Investments in affiliates and equity in income (loss) of affiliates are as follows as of and for the years ended June 30:

Name	Interest	Business	Investment		Equity in income (loss)	
			2013	2012	2013	2012
Maryland Physicians Care, Inc.	25.00%	State of Maryland Medicaid managed care	$ 18,235	16,752	1,482	4,887
Other affiliates	0.21% to 33.33%	Supply purchasing and medical equipment	203	260	(58)	(238)
			$ 18,438	17,012	1,424	4,649

(Continued)

(Dollars in thousands)

(7) Long-Term Debt

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

		2013	2012
Maryland Health and Higher Educational Facilities Authority (MHHEFA) Series 2006, Series A and B Revenue (FHA Insured) Bonds, interest rate 4.0 to 5.0%	$	317,915	325,360
Capital leases		559	977
Net unamortized bond premium		9,528	10,189
Long-term debt		328,002	336,526
Less current portion of long-term debt		8,229	7,863
Long-term debt less current portion	$	319,773	328,663

Scheduled principal repayments on long-term debt for the years ending June 30 are as follows:

2014	$	8,229
2015		8,300
2016		8,565
2017		8,975
2018		9,365
Thereafter		275,040

In November 2006, proceeds from issuance of $348,650 and $2,180 Maryland Health and Higher Education Facilities Authority Series 2006, Series A and B bonds were obtained for the purpose of (1) financing the costs of acquisition, construction and equipping of the Western Maryland Regional Medical Center (see note 1) and (2) to refund prior debt issuances. The Health System redeemed $11,360 of the Series 2006A bonds in conjunction with their final endorsement in 2010.

Principal payments on the Series 2006A revenue bonds commence on July 1, 2010, and are due semi-annually through January 1, 2035. Interest payments are due semi-annually commencing July 1, 2007. The total outstanding balance on the Series 2006B revenue bonds was paid on July 1, 2010. Interest on the Series 2006A bonds accrues at a rate of 4.0% to 5.0% per annum.

The Federal Housing Authority (FHA) has issued a commitment for mortgage insurance with respect to the project. The financing document contains quantitative and qualitative covenants (measured quarterly). The quantitative covenants include a debt service coverage ratio, a day's cash on hand requirement, current ratio requirement, a net days in accounts receivable requirement, and restrictions on operating losses and revenue over expenses.

In 2009, the Health System amended their line of credit agreement with a bank that permits the Health System to borrow up to $1,000,000. There is no expiration date on the line of credit and the interest rate as

of June 30, 2013 was 4.5%. The line of credit primarily supports a letter of credit agreement in the amount of $700,000. There was no outstanding balance as of June 30, 2013.

(8) Charity Care

The Health System utilizes a cost to charge ratio methodology to convert charity care to cost. Costs incurred are estimated based on the ratio of total operating expenses to gross charges applied to charity care charges. The amount of charges foregone for services and supplies furnished under the Health System's Charity Care policy aggregated approximately $17,478 and $15,949 for the years ended June 30, 2013 and 2012, respectively. The total direct and indirect costs to provide the care amounted to approximately $13,458 and $13,078 for the years ended June 30, 2013 and 2012, respectively.

(9) Retirement Plans

The WMHS Retirement Plan (the Plan) is a noncontributory defined benefit plan, which covers substantially all full-time employees who meet certain age and service requirements. The Plan's funding policy is to contribute, annually, the pension costs as determined by the Plan's actuary, subject to adjustment for full funding limitations as defined by the IRC.

The Health System's investment policy, established by the Investment Committee of the Finance Committee and approved by the Health System's Board of Directors, is to ensure current and future benefit obligations are adequately funded in a cost effective manner. The investment guidelines are based on a time horizon of greater than five years. In establishing the risk tolerances, the ability to withstand short and intermediate term variability with some interim fluctuations in market value and rates of return may be tolerated in order to achieve the longer-term objectives.

The measurement date of the Plan is June 30.

(Continued)

(Dollars in thousands)

The component of the Plan's funded status, net periodic benefit costs and actuarial assumptions used in accounting for defined benefit plans for the years ended June 30, 2013 and 2012 are as follows:

		2013	2012
Change in projected benefit obligation:			
Projected benefit obligation at beginning of year	$	208,348	163,136
Service cost		7,095	5,447
Interest cost		8,446	9,139
Assumptions		(17,609)	36,369
Actuarial loss		—	829
Benefits paid		(7,139)	(6,572)
Projected benefit obligation at end of year		199,141	208,348
Change in plan assets:			
Plan assets at fair value at beginning of year		148,146	141,634
Actual return		10,087	5,084
Employer contributions		9,000	8,000
Benefits paid		(7,139)	(6,572)
Fair value of plan assets at end of year		160,094	148,146
Funded status at end of year	$	(39,047)	(60,202)

		2013	2012
Components of net periodic benefit costs:			
Service cost	$	7,095	5,447
Interest cost		8,446	9,139
Expected return on plan assets		(10,136)	(9,680)
Recognized prior service cost		(721)	(593)
Recognized net loss		5,667	2,593
Net periodic pension cost	$	10,351	6,906

(Continued)

(Dollars in thousands)

Deferred pension costs, which have not yet been recognized in periodic pension expense but are accrued in unrestricted net assets, are $52,385 and $74,891 at June 30, 2013 and 2012, respectively. Deferred pension costs represents unrecognized actuarial losses or 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 costs, which is the impact of changes in plan benefits applied retrospectively to employee service previously rendered. The amount of deferred pension costs expected to be recognized as a component of net period pension costs during the year ending June 30, 2014 is $3,290.

	2013	2012
Weighted average assumptions – benefit obligations:		
Discount rate	4.79%	4.12%
Salary scale	2.00	2.00
Return on assets	7.00	7.00
Weighted average assumptions – net periodic expense:		
Discount rate	4.12%	5.69%
Salary scale	2.00	2.00
Return on assets	7.00	7.00

The accumulated benefit obligation for the defined benefit pension plan was $195,232 and $202,432 at June 30, 2013 and 2012, respectively.

The Health System's pension plan weighted average asset allocations at the measurement dates of June 30, 2013 and 2012, by asset category, are as follows:

	Percentage of plan assets		
	Target allocation	2013	2012
Asset class:			
Equities	40%	43%	38%
Fixed	60	57	62

The Health System expects to contribute $8,000 to the Plan for the fiscal year ending June 30, 2014.

(Continued)

(Dollars in thousands)

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

2014	$	7,302
2015		7,871
2016		8,204
2017		8,875
2018		9,941
2019–2021		65,206

The expected benefits to be paid are based on the same assumptions used to measure the Health System's benefit obligation as of June 30, 2013.

Effective July 1, 2011, employees hired or rehired will not participate in the Plan. These employees will participate in a new defined contribution plan that has been developed, which allows employees to contribute amounts tax-deferred up to certain limits allowable under Internal Revenue Service (IRS) guidelines. The Health System has not contributed to the defined contribution plan during the year ended June 30, 2013 or 2012 but has accrued $225 in anticipation of a 100% match of employee contributions up to 3% of employee salaries for the current fiscal year and $109 for fiscal year 2012, to be contributed during 2014.

The Health System also sponsors a defined contribution retirement plan in accordance with Section 403(b) of the IRC. The Health System's expense related to this plan for the years ended June 30, 2013 and 2012 was $1,802 and $1,853, respectively, and is included in employee benefits in the accompanying consolidated statements of operations.

(10) Self-Insurance Programs

(a) General and Professional Liability (GLPL)

On December 14, 2004, the Health System formed a new wholly owned insurance subsidiary, Western Maryland Insurance Company, Ltd. (WMIC), an exempted company under the Companies Law of the Cayman Islands, to provide GLPL insurance to the Health System and certain affiliates. Effective January 1, 2005, this subsidiary insures the Health System for its GLPL risks under a claims-made policy with a limit of $1,000 per claim and $8,000 in the aggregate. Claims in excess of $1,000 per claim and $8,000 in the aggregate, up to a limit of $25,000, have been reinsured with Zurich American Insurance Company, an independent third-party insurance company. The Health System's retained self-insurance risk under these policies is $1,000 per occurrence.

Management's estimate of the liability for GLPL claims, including incurred but not reported claims, is principally based on actuarial estimates performed by an independent third-party actuary. The Health System's estimated liability for GLPL claims, including incurred but not reported claims, totaled $14,247 and $12,377 as of June 30, 2013 and 2012, respectively. These amounts are included in other noncurrent liabilities in the accompanying consolidated financial statements. While management believes that this liability is adequate as of June 30, 2013, the ultimate liability may

(Dollars in thousands)

exceed the amount recorded. Additionally, the Health System has recorded an additional insurance recoveries receivable of $4,844 and $3,854 as of June 30, 2013 and 2012, respectively, included in other noncurrent assets.

(b) Workers' Compensation Insurance

In 2013 and 2012, the Health System participated in a self-insured plan for workers' compensation claims. Stop-loss coverage has been purchased through a commercial carrier for claims in excess of $400.

The Health System has accrued a liability of $2,346 and $2,586 as of June 30, 2013 and 2012, respectively, for known and incurred but not reported claims. Management believes this accrual is adequate to provide for all workers' compensation claims that have been incurred through June 30, 2013. Additionally, there are no material insurance recoveries related to workers' compensation as of June 30, 2013.

(c) Health Insurance

The Health System is self-insured for employee health claims. Under these self-insurance plans, the Health System has accrued a liability of $1,957 and $1,699 as of June 30, 2013 and 2012, respectively, for known claims and incurred but not reported claims. Management believes this accrual is adequate to provide for all employee health claims that may have been incurred through June 30, 2013. Additionally, there are no material insurance recoveries related to employee health claims as of June 30, 2013.

(11) Lease Commitments

Future minimum payments under noncancelable operating leases with terms in excess of one year or more for the years ending June 30 are as follows:

2014	$	3,488
2015		2,693
2016		2,235
2017		2,076
2018		1,860
Thereafter		458
Total	$	12,810

Rental expense under operating leases amounted to $2,591 and $2,748 for the years ended June 30, 2013 and 2012, respectively.

(Continued)

(Dollars in thousands)

(12) Temporarily and Permanently Restricted Net Assets

Temporarily and permanently restricted net assets as of June 30, 2013 and 2012 are available for the following purposes:

	2013	2012
Temporary restrictions:		
Specific support of healthcare services	$ 4,790	2,862
Permanent restrictions:		
Trustee held assets to be held in perpetuity, the income from which primarily is expendable to support health care services	2,068	1,969

(13) Fair Value of Financial Instruments

(a) Fair Value of Financial Instruments

The following methods and assumptions were used by the Health System in estimating the fair value of their financial instruments:

Cash and cash equivalents, investments, funds on deposit with trustee, board designated investments, patient accounts receivable, other assets, accounts payable, and accrued liabilities, payable to third-party payors, and other long term liabilities – The carrying amounts reported in the consolidated balance sheets approximate the related fair values.

The fair value of a financial instrument is the amount 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. Those fair value measurements maximize the use of observable inputs. However, in situations where there is little, if any, market activity for the asset or liability at the measurement date, the fair value measurement reflects the Health System's own judgments about the assumptions that market participants would use in pricing the asset or liability. Those judgments are developed by the Health System based on the best information available in the circumstances.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and cash equivalents, accounts receivable, due from affiliates, other assets, line of credit, accounts payable, advances from third-party payors, due to affiliates, and accrued expenses – The carrying amounts, at face value or cost plus accrued interest, approximate fair value because of the short maturity of these instruments.

Board designated and other investments – Equity and debt securities classified as trading are measured using quoted market prices at the reporting date multiplied by the quantity held.

(Continued)

(b) Long-Term Debt

The Series 2006 Bonds bear interest at fixed rates and, accordingly, had a carrying amount of $317,915 and a fair value of $326,368 as of June 30, 2013 and a carrying amount of $325,360 and a fair value of $344,886 as of June 30, 2012.

The fair value of the Health System's long-term debt is measured using quoted offered-side prices when quoted market prices are available. If quoted market prices are not available, the fair value is determined by discounting the future cash flows of each instrument at rates that reflect, among other things, market interest rates and the Health System's credit standing. In determining an appropriate spread to reflect its credit standing, the Health System considers credit default swap spreads, bond yields of other long-term debt offered by the Health System, and interest rates currently offered for similar debt instruments of comparable maturities by the Health System's bankers as well as other banks that regularly compete to provide financing to the Health System.

(c) Fair Value Hierarchy

The Health System adopted ASC Topic 820, *Fair Value Measurement*, on July 1, 2008 for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the consolidated financial statements on a recurring basis. ASC Topic 820 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Health System has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable inputs for the asset or liability.

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

(Dollars in thousands)

The table below presents assets that are measured at fair value as of June 30, 2013 aggregated by the three level valuation hierarchy:

	2013			
	Level 1	**Level 2**	**Level 3**	**Total**
Assets:				
U.S. government obligations	$ 14,014	—	—	14,014
Money market funds	24,411	—	—	24,411
Corporate stocks and other	13,897	—	—	13,897
Fixed income securities	—	53,595	—	53,595
Total assets	$ 52,322	53,595	—	105,917

The table below presents assets that are measured at fair values as of June 30, 2012 aggregated by the three level valuation hierarchy:

	2012			
	Level 1	**Level 2**	**Level 3**	**Total**
Assets:				
U.S. government obligations	$ 6,346	—	—	6,346
Money market funds	2,695	—	—	2,695
Corporate stocks and other	12,056	—	—	12,056
Fixed income securities	—	62,660	—	62,660
Total assets	$ 21,097	62,660	—	83,757

For the years ended June 30, 2013 and June 30, 2012, there were no significant transfers between levels 1, 2 or 3.

The table below presents the pension plan's investable assets as of June 30, 2013 aggregated by the three level valuation hierarchy:

	2013			
	Level 1	**Level 2**	**Level 3**	**Total**
Assets:				
Money market funds	$ 453	—	—	453
Mutual funds	38,329	—	—	38,329
Fixed income securities	—	34,051	—	34,051
Other funds	—	80,041	7,220	87,261
Total assets	$ 38,782	114,092	7,220	160,094

(Continued)

(Dollars in thousands)

The table below presents the pension plan's investable assets as of June 30, 2012 aggregated by the three level valuation hierarchy:

	2012			
	Level 1	**Level 2**	**Level 3**	**Total**
Assets:				
Money market funds	$ 7,430	—	—	7,430
Mutual funds	126,680	—	—	126,680
Fixed income securities	—	6,365	—	6,365
Other funds	—	7,671	—	7,671
Total assets	$ 134,110	14,036	—	148,146

During fiscal year 2013 transfers of $80,041 were made between Level 1 and Level 2 and transfers of $7,220 were made between Level 2 and Level 3 related to changes in liquidity.

(14) Commitments and Contingencies

(a) Litigation

From time to time, the Health System and its subsidiaries are involved in litigation and regulatory investigations arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the Health System's future financial position or results from operations.

(b) Other Matters

The Health System has contracts with various physician groups to provide certain emergency, obstetric, and surgical services. Those contracts include certain income guarantee levels, which eliminate as volumes related to services provided increase. The Health System paid $1,872 and $1,854 related to the guarantee provisions of the contracts in 2013 and 2012, respectively.

(15) Regulation and Reimbursement

The Health System provides health care services primarily through one general acute care hospital. The Health System and other healthcare providers in Maryland 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 HSCRC;
- Government regulation, government budgetary constraints and proposed legislative and regulatory changes; and
- Lawsuits alleging malpractice and related claims.

Such inherent risks require the use of certain management estimates in the preparation of the Health System'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 Health System's revenues and the Health System'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 Health System.

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

The current rate of reimbursement for services to patients under the Medicare and Medicaid programs is based on an agreement between the Center for Medicaid and Medicare Services (CMS) and the HSCRC. This agreement is based upon a waiver from Medicare prospective pay system reimbursement principles granted to the State of Maryland under Section 1814(b) of the Social Security Act and will continue as long as all third-party payors elect to be reimbursed in Maryland under this program and the rate of increase for costs per hospital inpatient admission in Maryland is below the national average.

On November 16, 2010, the Health System and the HSCRC agreed to a three-year contract for the Health System to implement the TPR methodology, effective July 1, 2010. The TPR agreement establishes a prospective, fixed revenue base "TPR cap," for the upcoming year. This includes both inpatient and outpatient regulated services. Under TPR, the Health System's revenue for all HSCRC regulated services is predetermined for the upcoming year, regardless of changes in volume, service mix intensity, or mix of inpatient or outpatient services that occurred during the year. The TPR agreement allows the Health System to adjust unit rates, within certain limits, to achieve the overall revenue base for the Health System at year end. Any overcharge or undercharge versus the TPR cap is prospectively added to the subsequent year's TPR cap. Although the TPR cap does not adjust for changes in volume or service mix, the TPR cap is adjusted annually for inflation, and for changes in payor mix and uncompensated care. Beginning in year three of the three-year contract, the Health System will receive an annual adjustment to its cap for the change in population in the Health System's service area. TPR is designed to encourage hospitals to operate efficiently by reducing utilization and managing patients in the appropriate care delivery setting.

(Continued)

(Dollars in thousands)

(16) Noncontrolling Interest

Effective June 30, 2012, the Health System adopted accounting guidance that requires a not-for-profit reporting entity to account for and present noncontrolling interests in a consolidated subsidiary as separate component of the appropriate class of consolidated net assets (equity). The reconciliation of noncontrolling interest reported in unrestricted net assets is as follows:

		WMHS Corporation	Noncontrolling interest	Unrestricted net assets
Balance at June 30, 2011	$	152,651	2,031	154,682
Operating income		(10,467)	4,628	(5,839)
Nonoperating income		8,085	—	8,085
Excess of revenues over expenses		(2,382)	4,628	2,246
Change in funded status of pension plan		(39,795)	—	(39,795)
Net assets released for purchase of property and equipment		808	—	808
Distributions to noncontrolling interest in consolidated subsidiaries		—	(4,565)	(4,565)
Change in net assets		(41,369)	63	(41,306)
Balance at June 30, 2012		111,282	2,094	113,376
Operating income		10,403	2,296	12,699
Nonoperating income		5,117	—	5,117
Excess of revenues over expenses		15,520	2,296	17,816
Change in funded status of pension plan		22,506	—	22,506
Net assets released for purchase of property and equipment		428	—	428
Distributions to noncontrolling interest in consolidated subsidiaries		—	(2,880)	(2,880)
Asbestos liability adjustment		345	—	345
Change in net assets		38,799	(584)	38,215
Balance at June 30, 2013	$	150,081	1,510	151,591

(Continued)

(Dollars in thousands)

(17) Functional Expenses

The Health System considers healthcare services and general and administrative to be its primary functional categories for purposes of expense classification. The Health System's operating expenses by functional classification are as follows for the years ended June 30:

		2013	2012
Healthcare services	$	256,948	261,418
General and administrative		31,434	33,303
	$	288,382	294,721

(18) Subsequent Events

Management evaluated all events and transactions that occurred after June 30, 2013 and through October 18, 2013. The Health System did not have any material recognizable subsequent events during this period.

Schedule 1

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidating Balance Sheet Information

June 30, 2013

(Dollars in thousands)

Assets	Western Maryland Health System Corporation	Frostburg Nursing & Rehabilitation Center	Haystack Consolidated Services, Inc.	Western Maryland Health System Foundation Inc.	Eliminations	Consolidated
Current assets:						
Cash and cash equivalents	$ 42,220	6,465	1,431	1,837	—	51,953
Short-term investments	39,022	—	674	3,832	—	43,528
Funds on deposit with trustee	15,476	—	—	—	—	15,476
Accounts receivable, net	39,076	1,771	—	—	—	40,847
Pledge receivable, net	—	—	—	605	—	605
Other receivables, net	5,063	—	571	7	(867)	4,774
Inventories and other current assets	12,891	1	—	5	(2,647)	10,250
Total current assets	153,748	8,237	2,676	6,286	(3,514)	167,433
Funds on deposit with trustee	36,439	—	—	—	—	36,439
Board designated investments	5,465	—	—	—	—	5,465
Other long-term investments	78	—	—	327	—	405
Investments restricted by donor or grantor	334	—	—	4,270	—	4,604
Beneficial interest in trustee held and Foundation's assets	—	—	—	1,823	—	1,823
Property and equipment, net	332,025	311	—	—	—	332,336
Unamortized financing fees	3,997	—	—	—	—	3,997
Investments in affiliates	18,375	—	63	—	—	18,438
Other assets	5,228	—	—	—	—	5,228
Total assets	$ 555,689	8,548	2,739	12,706	(3,514)	576,168

(Continued)

Schedule 1

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidating Balance Sheet Information

June 30, 2013

(Dollars in thousands)

Liabilities and Net Assets	Western Maryland Health System Corporation	Frostburg Nursing & Rehabilitation Center	Haystack Consolidated Services, Inc.	Western Maryland Health System Foundation Inc.	Eliminations	Consolidated
Current liabilities:						
Current portion of long-term debt	$ 8,229	—	—	—	—	8,229
Accounts payable and accrued liabilities	6,500	1,394	1,603	865	(3,514)	6,848
Accrued bond interest payable	7,691	—	—	—	—	7,691
Accrued salaries and benefits	13,931	278	—	—	—	14,209
Payable to third-party payors	6,956	—	—	—	—	6,956
Total current liabilities	43,307	1,672	1,603	865	(3,514)	43,933
Long-term debt, net of current portion	319,773	—	—	—	—	319,773
Pension benefits in excess of pension assets	39,047	—	—	—	—	39,047
Other liabilities	14,966	—	—	—	—	14,966
Total liabilities	417,093	1,672	1,603	865	(3,514)	417,719
Net assets:						
Unrestricted:						
Unrestricted net assets	136,752	6,876	1,136	5,317	—	150,081
Noncontrolling interest in consolidated subsidiaries	1,510	—	—	—	—	1,510
Total unrestricted net assets	138,262	6,876	1,136	5,317	—	151,591
Temporarily restricted	89	—	—	4,701	—	4,790
Permanently restricted	245	—	—	1,823	—	2,068
Total net assets	138,596	6,876	1,136	11,841	—	158,449
Total liabilities and net assets	$ 555,689	8,548	2,739	12,706	(3,514)	576,168

See accompanying independent auditors' report.

Schedule 2

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidating Statement of Operations Information

Year ended June 30, 2013

(Dollars in thousands)

	Western Maryland Health System Corporation (see note 1)	Frostburg Nursing & Rehabilitation Center	Haystack Consolidated Services, Inc.	Western Maryland Health System Foundation Inc.	Eliminations	Consolidated
Unrestricted revenues, gains and other support:						
Patient service revenue (net of contractual allowances and charity)	$ 291,542	7,230	—	—	—	298,772
Provision for bad debts	(6,920)	(594)	—	—	—	(7,514)
Net patient service revenue	284,622	6,636	—	—	—	291,258
Other revenue	10,213	10	—	—	(400)	9,823
Total revenues, gains and other support	294,835	6,646	—	—	(400)	301,081
Expenses:						
Salaries and wages	100,731	3,366	—	—	—	104,097
Employee benefits	38,643	1,102	—	—	—	39,745
Professional fees	11,367	70	—	—	—	11,437
Purchased services	17,779	751	—	343	(343)	18,530
Supplies	54,416	607	—	3	(3)	55,023
Utilities	3,824	178	—	—	—	4,002
Insurance	4,929	3	—	2	(2)	4,932
Interest	15,457	—	—	—	—	15,457
Depreciation and amortization	27,195	62	—	—	—	27,257
Other	7,153	683	8	110	(52)	7,902
Total expenses	281,494	6,822	8	458	(400)	288,382
Operating income (loss)	13,341	(176)	(8)	(458)	—	12,699

(Continued)

Schedule 2

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidating Statement of Operations Information

Year ended June 30, 2013

(Dollars in thousands)

	Western Maryland Health System Corporation	Frostburg Nursing & Rehabilitation Center	Haystack Consolidated Services, Inc.	Western Maryland Health System Foundation Inc.	Eliminations	Consolidated
Nonoperating income:						
Equity in income of affiliates	$ 1,479	—	(55)	—	—	1,424
Investment income	2,370	7	19	186	—	2,582
Unrealized gains (losses) on trading portfolio	190	—	(6)	444	—	628
Other	287	—	—	196	—	483
Total nonoperating income	4,326	7	(42)	826	—	5,117
Excess (deficiency) of revenues over (under) expenses	$ 17,667	(169)	(50)	368	—	17,816

See accompanying independent auditors' report.

Schedule 3

WESTERN MARYLAND HEALTH SYSTEM CORPORATION

Consolidating Statement of Changes in Net Assets Information

Year ended June 30, 2013

(Dollars in thousands)

	Western Maryland Health System Corporation	Frostburg Nursing & Rehabilitation Center	Haystack Consolidated Services, Inc.	Western Maryland Health System Foundation Inc.	Consolidated
Unrestricted net assets:					
Balance at June 30, 2012	$ 100,196	7,045	1,186	4,949	113,376
Excess of revenues over expenses	17,667	(169)	(50)	368	17,816
Change in funded status of pension plan	22,506	—	—	—	22,506
Net assets released for purchase of property and equipment	428	—	—	—	428
Asbestos liability adjustment	345	—	—	—	345
Distributions to noncontrolling interest in consolidated interest	(2,880)	—	—	—	(2,880)
Balance at June 30, 2013	138,262	6,876	1,136	5,317	151,591
Temporarily restricted net assets:					
Balance at June 30, 2012	492	—	—	2,370	2,862
Investment income				(7)	(7)
Donations	406	—	—	2,774	3,180
Grants	43	—	—	26	69
Net assets released from restrictions used for operations	(424)	—	—	(462)	(886)
Net assets released for purchase of property and equipment	(428)	—	—	—	(428)
Balance at June 30, 2013	89	—	—	4,701	4,790
Permanently restricted net assets:					
Balance at June 30, 2012	241	—	—	1,728	1,969
Change in beneficial interest of trustee-held assets	4			95	99
Balance at June 30, 2013	245	—	—	1,823	2,068
Net assets at June 30, 2013	$ 138,596	6,876	1,136	11,841	158,449

See accompanying independent auditors' report.