Reading Health System

Consolidated Financial Statements and Supplementary Consolidating Information
June 30, 2013 and 2012

Reading Health System
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June 30, 2013 and 2012

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Independent Auditor's Report

To the Board of Directors of
Reading Health System

We have audited the accompanying consolidated financial statements of Reading Health System (the "System"), which comprise the consolidated balance sheets as of June 30, 2013 and 2012, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; 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.

Auditor's Responsibility

Our responsibility is to express an opinion on the 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 our 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, we consider internal control relevant to the System'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 System'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 Reading Health System at June 30, 2013 and 2012, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

October 21, 2013

Reading Health System
Consolidated Balance Sheets
June 30, 2013 and 2012

	2013	2012
Assets		
Current		
Cash and cash equivalents	$ 64,194,346	$ 191,713,225
Patient accounts receivable, less allowance for uncollectible accounts of $52,456,860 and $41,451,392 in 2013 and 2012, respectively	179,935,902	110,747,136
Other receivables	13,227,984	5,914,466
Receivable from affiliates	677,836	1,454,833
Inventories	14,821,977	12,175,915
Estimated third-party payor receivables	8,198,991	2,408,590
Prepaid expenses and other current assets	14,823,188	12,072,896
Assets whose use is limited - required for current liabilities		
Self-insurance funding arrangements	7,812,332	10,782,507
Revenue bond indentures - debt service requirements	2,878,958	7,252,138
Total current assets	306,571,514	354,521,706
Assets whose use is limited		
Self-insurance funding arrangements	20,032,628	19,640,559
Under regulatory requirements	2,912,455	2,912,455
By board for capital improvements	940,950,458	856,481,130
Total assets whose use is limited, net of current portion	963,895,541	879,034,144
Investments	20,115,778	17,741,189
Temporarily restricted funds	660,370	654,010
Property, plant and equipment, net	681,697,895	615,065,637
Deferred financing expense, net	4,815,161	4,996,857
Deferred compensation fund	2,873,977	3,023,129
Other assets	14,443,615	13,747,873
Total assets	$ 1,995,073,851	$ 1,888,784,545

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

Reading Health System
Consolidated Balance Sheets
June 30, 2013 and 2012

	2013	2012
Liabilities and Net Assets		
Current		
Current installments of long-term debt	$ 6,733,536	$ 7,680,255
Accounts payable	48,395,821	43,085,133
Estimated third-party payor settlements	4,555,158	8,068,145
Current portion of estimated self-insurance costs	10,791,791	10,877,737
Accrued expenses	31,374,720	29,276,477
Accrued vacation	21,784,242	20,537,858
Advance from third-party payor	3,832,000	3,832,000
Other current liabilities	16,014,939	7,985,863
Total current liabilities	143,482,207	131,343,468
Long-term debt, net of current portion and unamortized discount	596,948,921	603,758,661
Accrued pension liabilities	112,951,705	200,514,393
Deferred revenue	34,959,665	34,903,416
Deferred compensation	3,203,918	2,999,484
Gift annuities	579,100	586,343
Estimated self-insurance costs, net of current portion	43,781,001	40,574,001
Swap contracts	59,859,380	82,635,153
Total liabilities	995,765,897	1,097,314,919
Net assets		
Unrestricted	979,817,008	774,002,732
Temporarily restricted	660,886	654,010
Permanently restricted	18,830,060	16,812,884
Total net assets	999,307,954	791,469,626
Total liabilities and net assets	$ 1,995,073,851	$ 1,888,784,545

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

Reading Health System
Consolidated Statements of Operations
Years Ended June 30, 2013 and 2012

	2013	2012
Unrestricted revenues and other support		
Net patient service revenue	$ 914,062,738	$ 874,307,259
Provision for uncollectible accounts	(53,362,307)	(49,489,385)
Net patient service revenue less provision for uncollectible accounts	860,700,431	824,817,874
Residential revenue	19,941,623	19,875,080
Other revenue	32,402,118	28,536,854
Total revenues and other support	913,044,172	873,229,808
Expenses		
Salaries and benefits	515,466,808	480,444,099
Supplies	117,757,926	111,362,303
Utilities	12,215,580	12,853,524
Interest	15,715,462	20,443,050
Depreciation and amortization	75,024,450	64,965,124
Purchased services	79,528,886	70,323,048
Repairs and maintenance	22,743,187	19,421,008
Other	53,768,423	58,947,523
Total expenses	892,220,722	838,759,679
Income from operations	20,823,450	34,470,129
Nonoperating gains/(losses)		
Investment income	76,027,384	20,829,827
Loss on extinguishment of debt	-	(5,302,466)
Realized and unrealized (losses)/gains on swap contracts	14,200,002	(36,240,771)
Other losses	(1,509,780)	(727,167)
Nonoperating gains/(losses), net	88,717,606	(21,440,577)
Excess of revenue, gains and other support over expenses	$ 109,541,056	$ 13,029,552

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

Reading Health System
Consolidated Statements of Changes in Net Assets
Years Ended June 30, 2013 and 2012

	2013	2012
Unrestricted net assets		
Excess of revenues, gains and other support over expenses	$ 109,541,056	$ 13,029,552
Change in unrealized gains/(losses) on investments	(1,075,841)	(19,373,757)
Change in pension liability	98,966,619	(96,257,226)
Other net assets	(1,617,558)	404,072
Increase/(Decrease) in unrestricted net assets	205,814,276	(102,197,359)
Temporarily restricted net assets		
Contributions	9,065	-
Net assets released from restrictions - for operations	(2,189)	(18,461)
Increase/(Decrease) in temporarily restricted net assets	6,876	(18,461)
Permanently restricted net assets		
Contributions	1,271,841	29,254
Change in unrealized gains/(losses) on investments	598,300	-
Change in beneficial interest in trusts	147,035	(585,204)
Increase/(Decrease) in permanently restricted net assets	2,017,176	(555,950)
Change in net assets	207,838,328	(102,771,770)
Net assets		
Beginning of year	791,469,626	894,241,396
End of year	$ 999,307,954	$ 791,469,626

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

Reading Health System
Consolidated Statements of Cash Flows
Years Ended June 30, 2013 and 2012

	2013	2012
Cash flows from operating activities		
Change in net assets	$ 207,838,328	$ (102,771,770)
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Change in unrealized (losses)/gains on investments	477,541	19,373,757
Change in fair value of swap contracts	(22,775,773)	30,302,796
Loss on extinguishment of debt	-	5,302,466
Premium on issuance of bonds	-	6,882,971
Amortization of bond discount	77,683	136,815
Amortization of bond premium	(212,328)	-
Amortization of deferred financing expense	181,696	353,318
Change in pension liability, net	(87,562,688)	100,658,432
Depreciation	75,024,450	64,965,124
(Gain) Loss on disposal of fixed assets	(3,200)	605,118
Provision for uncollectible accounts	53,362,307	49,489,385
Realized gains on investments	(60,889,148)	(7,440,377)
Equity income of affiliates	(5,269,424)	(185,740)
Distribution from equity investees	4,471,325	-
Restricted contributions and investment income received	(1,280,906)	(29,254)
Change in cash due to changes in operating assets and liabilities		
Receivable from patients and others	(129,864,591)	(55,449,650)
Receivable from affiliates	776,998	(194,507)
Inventories	(2,646,062)	762,708
Prepaid expenses and other assets	(2,647,935)	(8,110,770)
Accounts payable and other expenses	(3,441,352)	26,889,819
Deferred compensation	353,586	(23,645)
Gift annuities	(7,243)	(65,738)
Deferred revenue	56,249	(749,264)
Net cash provided by operating activities	26,019,513	130,701,994
Cash flows from investing activities		
Acquisition of property, plant and equipment	(127,961,335)	(64,282,208)
Proceeds from sale of fixed assets	3,200	913
Return of capital from equity investee	-	1,773,740
Purchases and sales of investments and assets whose use is limited, net	(19,234,095)	(12,959,628)
Net cash used in investing activities	(147,192,230)	(75,467,183)
Cash flows from financing activities		
Restricted contributions and investment income received	1,280,906	29,254
Proceeds from issuance of new debt, net of bond discount	-	472,471,969
Repayment of bonds	-	(470,215,013)
Increase in deferred financing expense	-	(3,548,378)
Payments of long-term debt	(7,627,068)	(15,970,553)
Net cash used in financing activities	(6,346,162)	(17,232,721)
Net increase in cash and cash equivalents	(127,518,879)	38,002,090
Cash and cash equivalents		
Beginning of year	191,713,225	153,711,135
End of year	$ 64,194,346	$ 191,713,225
Supplemental cash flow information		
Cash paid during the year for interest	$ 15,519,042	$ 21,208,003
Fixed asset additions included in accounts payable	13,688,973	12,627,200

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

1. Organizational Structure and Nature of Operations

Reading Health System ("Parent") is a tax-exempt not-for-profit corporation under Section 501(c)(3) of the Internal Revenue Code. The Parent is located in West Reading, Pennsylvania and provides inpatient, outpatient and emergency care for residents of the greater Berks County area. Admitting physicians are primarily practitioners in the local area.

Controlled Entities and Subsidiaries of the Parent Include:

Reading Hospital ("Hospital"), a tax-exempt not-for-profit acute and post-acute care hospital;

Reading Professional Services ("RPS"), a tax-exempt entity established for charitable, educational and scientific purposes. RPS recruits physicians, provides physician billing and administrative services for the Hospital, including supervision and instruction for medical students completing their residency training;

MC Realty, Inc. ("MC Realty"), a wholly owned subsidiary, established to strategically acquire real estate in Berks County and the surrounding areas. MC Realty is consolidated into the Parent;

The Reading Hospital Medical Group ("TRHMG"), a not-for-profit entity, established on January 1, 2007 to assure access to high quality primary care physicians and specialty physicians in sufficient numbers to meet the community need; and

The Highlands at Wyomissing ("Highlands"), a not-for-profit corporation is a fully controlled entity of The Reading Hospital. The purpose of the Highlands is to operate a continuing care retirement community including residential, recreational, and health care facilities and services specially designed to meet the physical, social, and psychological needs of elderly persons. The Highlands facility is located in Wyomissing, Pennsylvania and its residents are principally from the Wyomissing, and Reading, Pennsylvania area. The facility contains 290 residential living units, an 80-bed skilled nursing unit and 66 personal care units. Certain members of the board of directors from the Hospital are also members of the board of directors of the Highlands.

Other Noncontrolled Related Entities Include:

Berkshire Health Partners ("BHP") is licensed by the Commonwealth of PA as a fully integrated, non-risk bearing preferred provider organization. A nonprofit corporation in PA, BHP was established by hospitals and physicians, and offers a provider network of physicians, hospitals, and ancillary providers and services. Certain members of the Hospital's Board of Directors are directors of BHP. In September 2011, BHP entered into a Membership Repurchase Agreement giving the Parent full ownership of the hospital side of BHP. The other 50% is owned by Reading Physicians Organization.

Medicus Resource Management ("MRM"), a wholly owned subsidiary of BHP, is a for-profit company for PA tax purposes that coordinates the utilization management process and provides precertification, case management, concurrent reviews, and short term disability reviews.

Reading Berks Physical Therapy LLC ("RBPT"), a limited liability corporation established to provide physical therapies at eight locations within the greater Berks County area. The Hospital maintains a 40% interest in RBPT under the equity method of accounting. This interest is included in other assets on the accompanying Balance Sheets;

The Reading Hospital Surgicenter at Springridge, LLC ("Springridge LLC"), a limited liability company, was established to provide ambulatory surgery services to the surrounding community. The Hospital maintains a 50% ownership under the equity method of accounting. In FY 2013, Reading Hospital received a distribution of $3,692,000. This interest is included in other assets on the accompanying Balance Sheets;

The Parent, along with several other acute care service hospitals throughout the central Pennsylvania area, contributed capital to form Central Pennsylvania Alliance Laboratories ("CPAL"), a joint venture to combine laboratory operations. The Parent maintains a 20% ownership interest in CPAL. This interest is recorded under the equity method of accounting and is included in other assets on the accompanying Balance Sheet;

The Parent's ownership of Central Pennsylvania Homecare, Inc. (d.b.a. Visiting Nurse Association, "VNA") is 44.1%. Additional owners include Lancaster General with 44.1% and Pinnacle with 11.8% shares. VNA provides visiting home nursing services to outpatients of the Hospital, and other healthcare providers in the surrounding community. This investment is recorded under the equity method of accounting and is included in other assets on the accompanying Balance Sheets;

The Parent is a 20% owner, along with Central Pennsylvania Healthcare Alliance ("CPHA") members: Ephrata Community Hospital, Lancaster General, Pinnacle Health System, Summit Health Alliance and WellSpan Health, of Quest Behavioral Health, Inc. ("Quest"). Quest is a not-for-profit corporation providing full service managed behavioral healthcare. This investment is recorded under the equity method of accounting and is included in other assets on the accompanying Balance Sheets; and

Horizon is a for-profit limited liability partnership which provides in-home infusion drug therapy to customers in central Pennsylvania. The ownership structure equals 25% ownership shares for each of four parties, including Lancaster General, Reading Hospital, Pinnacle Health, and Hershey Medical Center. In FY 2013, RH received a distribution of $775,000. The investment is recorded under the equity method of accounting and is included in other assets on the accompanying Balance Sheets.

2. Summary of Significant Accounting Policies

Basis of Accounting
These Financial Statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America ("US GAAP"). The significant accounting policies followed by Reading Health System (the "System") are as follows:

Principles of Consolidation
The Consolidated Financial Statements of the System include the accounts of the Parent, the Hospital, RPS, TRHMG, Highlands and MC Realty. All significant intercompany balances and transactions have been eliminated.

Use of Estimates
The preparation of 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 reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Financial Statements and the reported amounts of revenues and expenses during the reporting period. These significant estimates include the accounts

receivable allowance for doubtful accounts, contractual allowances, estimated third-party payor settlements, investments, accrued pension liabilities, accrued retirement costs and accrued insurance costs. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with an original maturity of three months or less. At June 30, 2013 and 2012, the System had cash balances in financial institutions that exceeded federal depository insurance limits. Management believes that the credit risk related to these deposits is minimal.

Net Patient Service Revenue and Patient Accounts Receivable

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, 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 and include estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

The Hospital recognizes patient service revenue associated with services provided to patients who have third-party payor coverage on the basis of contractual rates for the services rendered. For uninsured patients who do not qualify for charity care, The Hospital recognizes revenue based on established rates, subject to certain discounts as determined by The Hospital. An estimated provision for bad debts is recorded that results in net patient service revenue being reported at the net amount expected to be received. The Hospital has determined that patient service revenue is primarily recorded prior to assessing the patient’s ability to pay and as such, the entire provision for bad debts related to patient revenue is recorded as a deduction from patient service revenue in the accompanying Statements of Operations and changes in net assets. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), for the year ended June 30, 2013 from these two payor sources are as follows:

	Third-party Payors	Self-Pay	Total
Patient service revenue (net of contractual allowances and discounts)	95.5 %	4.5 %	100.0 %

Revenue from the Medicare and Medicaid programs accounted for approximately 33% and 7%, respectively, of Reading Hospital’s net patient service revenue for the year ended June 30, 2013 and 30% and 7%, respectively, for the year ended June 30, 2012. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The 2013 and 2012 net patient service revenue increased approximately $39,755,000 and $47,470,000, respectively, because of tentative settlements and final settlements for years that are no longer subject to audits, reviews, and investigations, as well as other changes in estimates.

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, the System analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, the System analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), The System records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Residential Revenue
The Highlands' entrance fees are refundable for a period of time up to 50 months. During this time, for refund purposes only, a resident's entrance fee is amortized at the rate of 2% per month for 50 months beginning on the date of occupancy. Entrance fees which are no longer refundable are recorded as deferred entrance fee revenue. Entrance fees are amortized to income using the straight-line method over the estimated remaining life expectancy of the resident. For all contracts entered into prior to January 1, 2005, a portion of the entrance fee, referred to as the health fund, equal to 30% of the total entrance fee, is reserved to be accounted for individually for each resident/couple. All health funds are refundable to the extent not amortized. Amortization of the health fund occurs when a resident utilizes health services (Nursing or Personal Care). The amortization rate is the incremental difference between the daily rate for health services and the monthly fee prorated on a daily basis.

Other Revenue
Significant components of other revenue include rental income on leased properties, tuition revenue for The Reading Hospital School of Health Sciences and cafeteria revenues.

Charity Care
The System provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Donor Restricted Gifts
Unconditional promises to give cash and other assets to the Hospital are reported at estimated fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at estimated fair value at the date the gift is received.

Contributions are reported as either temporarily or permanently restricted if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the Consolidated 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.

Compensated Paid Leave

The System records a liability for amounts due to employees for future paid leave which are attributable to services performed in the current and prior periods.

Excess of Revenues, Gains and Other Support Over Expenses

The Consolidated Statements of Operations include the excess of revenues, gains and other support over expenses. Changes in unrestricted net assets that are excluded from the excess of revenues, gains and other support over expenses, consistent with industry practice, include changes in unrealized gains and losses on investments other than certain not readily marketable investments, adjustments for defined benefit and other post-retirement benefits 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).

Assets Whose Use is Limited

Assets whose use is limited includes designated assets set aside by the Board of Directors for future capital improvements, assets held by trustees under indenture agreements and self insurance trust arrangements. The Board retains control over Board-restricted assets and may at its discretion subsequently use these assets for other purposes.

Assets whose use is limited includes cash and cash equivalents, marketable debt securities (including U.S. government and government agencies, corporate, state and local government), marketable equity securities (including common, preferred and foreign stock), exchange traded/listed mutual funds (including fixed income funds), hedge funds, private equity funds and limited partnerships. The Pennsylvania Continuing Care Provide Registration and Disclosure Act requires a statutory reserve equivalent to the greater of the total of debt service payments due during the next 12 months on account of any loan or 10% of the projected annual operating expenses of the facilities exclusive of depreciation, computed only on the proportional share of financing or operating expenses that is applicable to residents under entrance agreement contracts. For the System, this statutory requirement applies only to The Highlands at Wyomissing. This statutory reserve requirement is considered to be fulfilled from board-designated funds included within assets limited as to use.

The calculation of the 10% of the annual operating expenses for 2014 is as follows:

Budgeted operating expenses for 2014	$ 24,362,959
Less: Budgeted depreciation and amortization expense	(3,092,503)
Net budgeted operating expenses for 2013	21,270,456
Required reserve as of July 1, 2013 (10%)	$ 2,127,046

The principal and interest due in the next 12 month period for the long-term financing of the Highlands is the greater of the two options and is calculated as follows:

Principal due	$ 1,521,724
Interest due	1,549,741
Required reserve as of July 1, 2013	$ 3,071,465

Property, Plant and Equipment

Property, plant and equipment are carried at cost, less accumulated depreciation. Expenditures which substantially increase the useful lives of existing assets are capitalized. Routine maintenance and repairs are expensed as incurred. Depreciation is computed using the straight-line method over the estimated useful lives of each class of depreciable asset. Useful lives range as follows:

Land improvements	5-25 years
Buildings and building improvements	10-40 years
Fixed equipment	5-10 years
Movable equipment	3-7 years

Gains and losses resulting from the retirement or sale of property, plant and equipment are included in the Consolidated Statements of Operations. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Gifts of long-lived operating assets such as land, buildings or equipment are reported as unrestricted contributions and are, excluded from the excess of revenues, gains and other support over expenses, unless explicit donor stipulations specify how the donated asset 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.

Temporarily and Permanently Restricted Net Assets

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

Inventories

Inventories are stated at lower of cost determined by the (first-in, first-out method) or market. Physical inventory counts were conducted in February and May 2013 and adjustments recorded. In January 2013, $859,000 of inventory was recorded upon acquisition of Berks Hematology Oncology Associates.

Investments and Investment Income

Investment income earned on securities (interest and dividends) is reported in the non-operating income section of the Consolidated Statements of Operations within Investment income. Realized gains or losses related to the sale of investments, other than temporary impairments on other than trading investments and unrealized gains or losses on alternative investments, are included in the non-operating section of the Consolidated Statements of Operations in Investment income unless the income or loss is restricted by donor or law.

Investments in equity securities with readily determinable fair values and all investments in debt securities are recorded at fair value in the Consolidated Balance Sheets. These securities have been classified as other than trading, and net changes in unrealized gains (losses) on these instruments are included in the Consolidated Statements of Changes in Net Assets.

The fair value option for financial assets and liabilities permits the System to elect to measure eligible items at fair value on an instrument by instrument basis. If elected, this option requires the System to report the unrealized gains and losses on these instruments as part of the performance indicator. Once elected, the fair value option is irrevocable for that instrument. Alternative investments include investments in managed funds, which include hedge funds, private partnerships and other investments that do not have readily determinable fair values and may be subject to withdrawal restrictions. Investments in hedge funds, private partnerships, and other investments in managed funds (collectively “alternative investments”) are accounted for using the fair value option. The unrealized gains or losses from these alternative investments are included in the Consolidated Statements of Operations as part of non-operating gains/ (losses) within Investment income.

Fair Value Measurements
The System follows the provisions of Financial Accounting Standards Board (“FASB”) ASC 820, Fair Value Measurement (“ASC 820”), which defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants at the measurement date. ASC 820 also establishes a framework for measuring fair value using valuation techniques such as the market approach, cost approach and income approach, and making disclosures about fair value measurements.

ASC 820 emphasizes that fair value is a market-based measurement, not an entity specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing an asset or liability. As a basis for considering market participant assumption in fair value measurements, ASC 820 defines a three-Level fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity and the reporting entity’s own assumptions about market participants. The fair value hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

Level 1 – Inputs utilized quoted market prices in active markets for identical assets or liabilities that the System has the ability to access.

Level 2 – Inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset and liability (other than quoted prices) such as interest rates, foreign exchange rates and yield curves that are observable at commonly quoted intervals.

Level 3 – Inputs are unobservable inputs for the asset or liability, which is typically based on an entity’s own assumptions, as there is little, if any, related market activity.

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the Level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest Level input that is significant to the fair value measurement in its entirety. The System’s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

Where quoted prices are available in an active market, investments are classified in Level 1 of the valuation hierarchy. Investments in Level 1 include cash, exchange-traded equity securities and mutual funds with a published daily net asset value or its equivalent (“NAV”). Investments in Level 2 include financial instruments valued based on quoted market prices for identical securities in markets that are not active, quoted prices for similar securities in markets that are active, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. If quoted prices are not available, other accepted valuation methodologies, such as interest rates, observable yield curves and spreads may be used to determine fair value. This Level includes investments in marketable corporate debt securities, U.S. government and agency debt securities, and certain mutual funds that permit daily redemptions but whose NAV is not published. Level 2 also includes investments in certain private entities that calculate NAV per share, or its equivalent, if the System has the ability to redeem its investment with the investee at the stated NAV at the measurement date or shortly thereafter. Investments in Level 3 include investments in auction rate securities and other nonreadily marketable alternative investments, such as investments in private equity funds and hedge funds where the System's investments are subject to lock up periods and other longer-term liquidity restrictions and are reported at fair value based on the use of inputs that are unobservable in the public market.

The fair values of Level 3 investments have been estimated by management based on all available data, including information provided by third-party pricing vendors, fund managers and general partners. Auction rate securities are estimated using the income approach. This approach uses estimation techniques to determine the estimated future cash flows of the respective asset or liability expected by a market participant and discounts those cash flows back to present value. Alternative investments are recorded at fair value based on the NAV as a practical expedient, as provided by the respective general partner or fund administrator of the individual alternative investment funds. The System believes the fair value of alternative investments in the Consolidated Balance Sheets is a reasonable estimate of its ownership interest in the alternative investment funds. As part of the System's overall valuation process, management evaluates these third-party methodologies to ensure that they are representative of exit prices in the security's principal markets.

These valuation methods may produce a fair value estimate that may not be reflective of future fair values. Furthermore, while the System believes that its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine fair value could result in a materially different estimate of fair value at the reporting date. See Note 5 for additional details related to the System's investments.

The System uses investment advisors to assist in managing their investment portfolios. One advisor is authorized to execute transactions to the Pension Fund. For the System's Long Term Capital Funds, the System has engaged an investment consultant and four new investment advisors who assist in managing the Long Term Capital funds. This full discretionary investment mandate, guided by the System's Board adopted Investment Policy Statement, was transitioned to the new advisors in October 2012. System Treasury staff coordinate with the investment consultant and advisors and a Board Committee, the Capital Resources Committee meet regularly with Advisors to discuss operations and performance of the investment portfolios.

Deferred Financing Expense

Deferred financing expense is amortized over the period the debt is outstanding using the straight-line method, which approximates the effective interest method. Amortization of deferred financing costs totaled $181,696 and $353,318 at June 30, 2013 and 2012, respectively.

Bond Premiums / (Discounts)

Bond premiums/(discounts) are reported as direct additions/(reductions) of the carrying values of the related debt instruments from which the discounts arose. Bond premiums/(discounts) are amortized over the period during which the debt is outstanding using the straight-line method, which approximates the effective interest method, with current period adjustments included as a component of interest expense.

Estimated Self-Insurance Costs
The provision for estimated self-insured claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported. The System self-insures its medical malpractice, general liability, and workers' compensation risks. Reserve estimates are subject to the impact of changes in claim trends as well as prevailing social, economic, and legal conditions. The ultimate net cost of settling these liabilities may vary from the estimated amounts. Accordingly, reserve estimates are continually reviewed and updated and any resulting adjustments are reflected in the current Financial Statements. Insurance recoveries are recognized at the same time as related claims liabilities.

Derivative Instruments
The System follows accounting guidance on derivative financial instruments that is based on whether the derivative instrument meets the criteria for designation as cash flow or fair value hedges. The criteria for designating a derivative as a hedge includes the assessments of the instruments effectiveness in risk reduction, matching the derivative instrument to its underlying transactions, and the assessment of the probability that the underlying transaction will occur. All of the System's derivative financial instruments are interest rate swap agreements without hedge accounting designation.

Entering into interest rate swap agreements involves, to varying degrees, elements of credit, default, prepayments, and market risk in excess of the amounts recognized on the Consolidated Balance Sheets. Such risks involved the possibility that there will be no liquid market for these arrangements, the counterpart to these arrangements may default on its obligations to perform and there may be unfavorable changes in interest rates. The System does not hold derivative instruments for the purpose of managing credit risk and enters into derivative transactions with high quality counterparties.

The fair value interest rate swap agreements entered into by the System is adjusted to market value quarterly at the close of the accounting period based upon quotations from market makers. The change in market value is recorded in the Statement of Operations within excess of revenues, gain and other support over expenses.

Income Taxes
The System is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. On such a basis, the exempt entities do not incur liability for federal income taxes, except in the case of unrelated business income.

The Company evaluates uncertain tax positions using a two-step approach for recognizing and measuring tax benefits taken or expected to be taken in an unrelated business activity tax return and disclosures regarding uncertainties in tax positions. No adjustments to the Financial Statements were required as a result of this evaluation.

Deferred Revenue
The Highlands has deferred revenue pertaining to refundable entrance fees of $15,798,000 and $17,078,000 at June 30, 2013 and 2012, respectively, and deferred entrance fee revenue of $17,634,000 and $16,821,000 at June 30, 2013 and 2012, respectively. Entrance fees are refundable for a period of time up to 50 months before they are transferred to deferred entrance fee revenue. The deferred entrance fee revenue is amortized to income using the straight-line method over the estimated remaining life expectancy of the resident.

Deferred Compensation
The System was a party to a deferred compensation plan that provided retirement benefits to certain individuals employed by the System. Assets were deposited pursuant to this agreement such that the market value of the assets approximates the related accrued deferred compensation liability. The plan is no longer active. No new participants or any additional contributions are allowed. The original contributions were funded entirely by the participating employees through payroll deferral.

Recently Issued Accounting Pronouncements
In July 2011, the FASB issued Accounting Standards Update ("ASU") 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 health care entities to change the presentation in 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 allowances and discounts). For nonpublic entities, the amendments are effective for Fiscal Years ("FY") and interim periods within those FY's beginning after December 15, 2012, with early adoption permitted. While this standard will have no impact on the Hospital's financial position or results of operations, it will require reclassification of the provision for doubtful accounts from operating expenses to a component of net revenues beginning with the first quarter of 2013, with retrospective application required.

The FASB has issued ASU No. 2011-04, Fair Value Measurements (Topic 820), "Amendments to Achieve Common Fair Value measurement and Disclosures Requirements in U.S. GAAP and IFRSs" (ASU 2011-04). The amendments in ASU 2011-04 change the wording used to describe many of the requirements in U.S. generally accepted accounting principles for measuring fair value and for disclosing information about fair value measurements. ASU 2011-04 is effective for FY's, and interim periods within those FY's, beginning after December 15, 2011. The System has adopted the provisions of ASU 2011-04 and made all required disclosures in the Consolidated Financial Statements.

Reclassifications
Certain reclassifications to amounts previously reported have been made to conform with the current period presentation.

Uncompensated Care and Community Service
The System provides services to patients who meet the criteria of its charity service policy without charge or at amounts less than the established rates. Criteria for charity care consider the patient's family income, family size, and ability to pay. Individuals who qualify for charity care do not have insurance or other coverage. In addition, accounts that remain unpaid after all attempts of collections have been exhausted are written off to uncompensated care.

The System maintains records to identify and monitor the level of charity care and community service it provides. These records include the amount of charges foregone based on established rates for services, and supplies furnished under its charity care, community service policies, and the estimated cost of those services.

Charges foregone for uncompensated care as determined in accordance with the System's policies were approximately $73,776,000 and $70,657,000 in 2013 and 2012, respectively. Direct and indirect costs to provide these services were approximately $24,383,000 and $23,352,000 for the years ended 2013 and 2012, respectively. The estimated costs were based on a calculation which multiplied the cost to charge ratio by the gross charges associated with providing uncompensated care to patients. The cost to charge ratio was obtained from our most recently filed Medicare Cost report.

Additionally, the System sponsors certain other service programs and charity services, which provide substantial benefit to the broader community. Such programs include services to needy populations requiring special services and support, community service programs and charity services, as well as, health promotion and education.

The System's community service includes the Medical Assistance program which makes payment for services provided to families with dependent children, the aged, the blind, and the permanently and totally disabled, whose income and resources are insufficient to meet the costs of necessary medical services. Payments from the Medical Assistance program are generally less than the System's charge of providing the service.

In addition, community service represents the cost to deliver services to the community, net of any payment received for those services. Included in these services are the System's subsidies of outpatient clinics, education of medical professionals who work with various health care providers in the community upon graduation, and community mental health programs. The System also sponsors health fairs and other wellness programs throughout the community.

3. Net Patient Service Revenue

The System has agreements with third-party payors that provide for payments at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows.

Medicare

Inpatient acute care and rehabilitation services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Outpatient services are reimbursed by Medicare under the Ambulatory Payment Classification System. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary. The Hospital's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization under contract with Medicare. The Hospital's Medicare cost reports have been closed and settled by the Medicare fiscal intermediary through June 30, 2007.

Medicaid

Historically, inpatient and outpatient services rendered to Medicaid program beneficiaries were paid at prospectively determined rates with inpatient services being reimbursed on a rate-per-discharge basis and outpatient services on a predetermined fee schedule basis.

On December 29, 2010, the Pennsylvania Department of Public Welfare ("DPW") received approval from the Centers for Medicare & Medicaid Services for the state plan amendments pursuant to Act 49 of 2010, passed by the Pennsylvania General Assembly on July 3, 2010, that established a new inpatient hospital fee for service payment system, new supplemental payments and the waiver to establish the statewide Quality Care Assessment. DPW also received approval on final language for the DPW contracts with managed care organizations. The estimated net impact on the Hospital for the year ended June 30, 2013 was $8,239,000 (based on total payment adjustments of $19,148,000 offset by assessments of $10,909,000).

Capital Blue Cross

Beginning July 1, 2010, inpatient services rendered to Capital Blue Cross subscribers are reimbursed at negotiated case rates and per diem rates. Previously, inpatient services had been reimbursed on a negotiated percentage of covered charges. The prospectively determined rates are not subject to retroactive adjustment. The Hospital continues to be reimbursed for outpatient services at a negotiated percentage of covered charges.

Workers' Compensation

The payment method by which all employers and/or insurers of workers' compensation policies will pay for the services provided by health care providers to employees covered by workers' compensation is a percentage of the Medicare payment for these services.

Other Contractual Arrangements

The System has various payment agreements with preferred provider organizations and health maintenance organizations. The basis for payment under these agreements includes discounts from established charges.

Revenue received under agreements with third-party payors is subject to audit and retroactive adjustment. Adjustments related to tentative and final settlements with third-party payors are included in the determination of the excess of revenues, gains and other support over expenses in the year in which such adjustments become known. Such adjustments relating to prior years increased net patient service revenues by approximately $13,703,000 in 2013 and 2012 by $7,446,000.

The health care industry is subject to numerous laws and regulations of federal, state and local governments. Compliance with these laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at the time. Recently, government activity has increased with respect to investigations and allegations concerning possible violations by health care providers of fraud and abuse statutes and regulations, which could result in the imposition of significant fines and penalties as well as significant repayments for patient services previously billed.

4. Investments

	2013	2012
Deferred compensation		
Cash and cash equivalents	$ 452	$ 469
Mutual funds	2,873,525	3,022,660
Total deferred compensation	$ 2,873,977	$ 3,023,129

Assets whose uses are limited and that are required for obligations classified as current liabilities are reported as current assets. The composition of assets, whose uses are limited at June 30, 2013 and 2012, is set forth in the following tables.

	2013	2012
Under self-insurance funding arrangements		
Professional liability		
Cash and cash equivalents	$ 7,459,976	$ 9,066,781
U.S. Government securities	4,781,009	7,625,681
Corporate bonds	5,940,652	4,221,267
Mutual funds	91,242	78,752
	18,272,879	20,992,481
Workers' compensation		
Cash and cash equivalents	469,987	742,031
U.S. Government securities	3,870,122	4,015,106
Corporate bonds	3,442,871	2,995,656
Mutual funds	1,789,101	1,677,792
	9,572,081	9,430,585
Total assets whose use is limited under self-insurance funding arrangements	$ 27,844,960	$ 30,423,066

	2013	2012
Under revenue bond indenture agreements - held by trustee		
Cash and cash equivalents	$ 2,878,958	$ 7,252,138
Total assets whose use is limited under revenue bond indenture agreements	$ 2,878,958	$ 7,252,138
By board for capital improvement		
Cash and cash equivalents	$ 26,774,873	$ 190,763,607
U.S., State and Muni Government securities	9,717,067	40,404,646
Corporate and foreign bonds	5,174,213	-
Common, preferred and foreign stocks	4,514,752	1,092,580
Mutual funds	365,941,617	133,339,800
Fixed income funds	341,575,138	281,138,349
Hedge, Private Equity, Common Trust Funds	190,165,252	222,097,808
Total assets whose use is limited by the board for capital improvements	$ 943,862,912	$ 868,836,790
Temporarily restricted funds		
Cash and cash equivalents	$ 660,370	$ 654,010
Investments		
Beneficial interest in trusts	$ 13,288,593	$ 12,671,566
Cash and equivalents	103,364	152,048
Common, foreign and preferred stock	3,185,599	3,038,983
Mutual funds	891,025	-
Corporate and foreign bonds	877,760	563,550
U.S. Government securities	1,769,437	1,315,042
Total assets whose use is permanently restricted as to use	$ 20,115,778	$ 17,741,189

A summary of the System's total investment return for the years ended June 30, 2013 and 2012 as reflected in the Consolidated Statements of Operations and Changes in Net Assets are as follows:

	2013	2012
Investment income	$ 76,027,384	$ 20,829,827
Change in unrealized gains/(losses) on investments	(477,541)	(19,373,757)

The System's investments are managed by institutional investment advisors, fund managers and bank trust departments. Because the System's investments include a variety of financial instruments, the related values as presented in the Consolidated Financial Statements are subject to various market fluctuations which include changes in the equity markets, interest rate environment and general economic conditions.

In mid FY2012, the Capital Resources Committee, which is responsible for the oversight of the Investments and Debt of the System, began a process to outsource discretionary investment management of the Long Range Capital portfolio. This was started after deliberate process to develop a comprehensive Investment Policy Statement (IPS) that was approved early in FY2012 and later refreshed in mid FY2013. The Committee and System staff met, and interviewed, multiple investment banks and institutional managers as well as investment consultants.

At the end of FY2012, the Committee engaged an Investment Consultant and four investment Advisors to manage the Long Range Capital investment portfolio under the guidance of the IPS. The four investment managers were all selected based on their specific investment expertise and strengths. Each was assigned a specific investment mandate based on these criteria. In October 2012, once Advisor Investment Management Agreements (IMAs) were finalized, new investment allocations were calculated and preparations with the Investment Custodian finalized. The daily liquidity investments were liquidated and transferred to each of the respective new Advisors for deployment under each respective IMA.

During FY2013, $810.5 million of original Long Range Capital legacy investments were deployed under the new investment mandates, with $40.6 million remaining to be liquidated. On June 30, 2013, the total of all Long Term Capital portfolio and the legacy Long Range Capital portfolio are fully invested and are valued at $900.8 million.

The System performs an annual impairment analysis; no impairments were identified in Fiscal Year 2013 and 2012. There were 109 investments with a fair value of $301.1 million that were in an unrealized loss position totaling $19.6 million as of June 30, 2013. The unrealized losses on these investments were caused by interest rate increases and general market conditions. For investments in an unrealized loss position, the System does not have the intent or requirement to sell them, therefore, the System does not consider these investments to be other-than-temporarily impaired as of June 30, 2013.

The following table presents cost and fair value of investments for June 30, 2013 and June 30, 2012:

	Fair Value	**Cost**	**Fair Value**	**Cost**
Cash and Equiv	$ 38,347,980	$ 38,347,980	$ 208,631,105	$ 208,631,105
State and Local Govt Sec.	9,717,067	9,711,764	9,639,052	9,997,656
US Government Securities	10,420,568	10,283,813	43,721,423	41,079,255
Mutual Funds	371,586,510	353,263,428	138,119,003	130,643,211
Equities - Common Stock	7,700,351	6,450,034	4,131,563	3,498,856
Corporate and Foreign Bonds	15,435,495	15,540,603	7,780,474	7,451,332
Fixed Income Funds	341,575,141	344,051,702	281,138,349	276,192,389
Hedge Funds and PE Funds	190,165,252	176,707,121	222,097,807	206,185,628
Beneficial Interest in Trusts	13,288,592	11,985,975	12,671,566	11,876,337
Total	**$ 998,236,956**	**$ 966,342,420**	**$ 927,930,342**	**$ 895,555,769**

The following tables represent the fair value measurement levels for all assets and liabilities, which the System has recorded at fair value:

		Fair Value Measurement Using		
	June 30, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Assets				
Cash and cash equivalents	$ 38,347,980	$ 38,347,980	$ -	$ -
State and Local Govt Sec.	9,717,067	-	-	9,717,067
Corporate and foreign bonds	15,435,495	-	15,435,495	-
Common, preferred and foreign stock	7,700,351	7,700,351	-	-
U.S. Government securities	10,420,568	-	10,420,568	-
Mutual funds	371,586,510	335,472,405	36,114,105	-
Fixed income funds	341,575,141	335,353,344	6,221,797	-
Beneficial interests in trusts	13,288,592	-	-	13,288,592
Hedge, Private Equity, Common Trust Funds	190,165,252	-	6,676,991	183,488,261
Total investments	$ 998,236,956	$ 716,874,080	$ 74,868,956	$ 206,493,920
Liabilities				
Swap contracts	$ 59,859,380	$ -	$ 59,859,380	$ -

		Fair Value Measurement Using		
	June 30, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Assets				
Cash and cash equivalents	$ 208,631,105	$ 208,631,105	$ -	$ -
State and Local Govt Sec.	9,639,052	-	-	9,639,052
Corporate and foreign bonds	7,780,474	-	7,780,474	-
Common, preferred and foreign stock	4,131,563	4,131,563	-	-
U.S. Government securities	43,721,423	-	43,721,423	-
Mutual funds	138,119,003	138,119,003	-	-
Fixed income funds	281,138,349	281,138,349	-	-
Beneficial interests in trusts	12,671,566	-	-	12,671,566
Hedge, Private Equity, Common Trust Funds	222,097,807	-	77,248,808	144,848,999
Total investments	$ 927,930,342	$ 632,020,020	$ 128,750,705	$ 167,159,617
Liabilities				
Swap contracts	$ 82,635,153	$ -	$ 82,635,153	$ -

Following is the summary of the inputs and valuation techniques as of June 30, 2013 and 2012 for valuing Level 2 and Level 3 financial instruments:

Financial Instrument	Input	Valuation Technique
Cash Equivalents	Broker/Dealer	Market
U.S. Government Agencies	Broker/Dealer	Market
Corporate	Broker/Dealer	Market
Interest Rate Swaps agreements	Broker/Dealer	Market
Exchange traded/mutual funds	NAV	Market/Income
Auction Rate Securities	Broker/Dealer	Income
Hedge Funds	NAV	Market/Income
Limited Partnership/companies	NAV	Market/Income

The following table represents the non-readily marketable investments and auction rate securities for which fair value was measured under Level 3:

	Hedge Funds	Interests in Trusts	Government Securities	Equity Securities
Fair value at July 1, 2012	$ 110,376,934	$ 12,671,566	$ 9,639,052	$ 34,472,065
Purchases	97,252,579	-	-	8,688,990
Sales	(81,123,771)	-	(285,000)	(6,674,668)
Realized gains/(losses)	16,543,643	-	-	-
Net change in unrealized gains/(losses)	288,721	617,026	363,015	3,663,768
Fair value at June 30, 2013	$ 143,338,106	$ 13,288,592	$ 9,717,067	$ 40,150,155

	Hedge Funds	Beneficial Interests in Trusts	State and Local Government Securities	State and Local Government Securities
Fair value at July 1, 2011	$ 123,372,469	$ 13,248,119	$ 10,295,179	$ 29,252,340
Purchases	-	-	-	8,016,687
Sales	(11,774,209)	-	(100,000)	(4,796,321)
Realized gains/(losses)	2,872,165	-	-	1,999,359
Net change in unrealized gains/(losses)	(4,093,491)	(576,553)	(556,127)	-
Fair value at June 30, 2012	$ 110,376,934	$ 12,671,566	$ 9,639,052	$ 34,472,065

As shown above, the System's significant Level 3 measurements which employ unobservable inputs that are readily quantifiable pertain to auction rate securities. At June 30, 2013, the System held investments in auction rate securities from four different issuers having an original principal amount of $10,215,000. The following table presents the significant assumptions used to determine the fair values of the System's auction rate securities at June 30, 2013 and 2012:

Financial Instrument	Valuation Technique	Input	Range
Auction Rate Securities	Discounted Cash Flow	Discount rates	5.59%-7.19%
		Maximum rate	L+200%-205%
		Workout period	6-11 years

L - one-month LIBOR *(The London InterBank Offered Rate)*

Disclosure - Fair Value Measurements of Investments in Certain Entities that Calculate Net Asset Value per Share (or its Equivalent):

	Fair Value ($Millions)	Unfunded Committements	Redemption Frequency (If Eligible)	Redemption Notice Period
Equity Long/Short Hedge Funds - a	$ 15.0	$ -	Quarterly, Annually	30-90 Days
Event Driven Hedge Funds - b	9.9	-	Quarterly, Annual Rolling	60 Days
Global Opportunities Hedge Funds - c	2.9	-	Quarterly	45 Days
Multi Strategy Hedge Funds - d	89.7	-	Quarterly, Semi-Annually, Annually, Bi Annually on Anniversary	60 - 120 Days
Real Assets - e	6.3	-	Annually	90 Days
Real Estate Funds - f	27.2	13.5	N/A	N/A
Private Equity Funds - g	32.5	15.1	N/A	N/A
Total	**$ 183.5**	**$ 28.6**		

a. This class includes investments in hedge funds that invest both long and short in U.S. and foreign common stocks. Management of the hedge funds has the ability to shift investments from value to growth strategies, from small to large capitalization stocks, and from a net long position to a net short position. The fair values of the investments in this class have been estimated using the net asset value per share of the investments as a practical expedient.

b. This class includes investments in hedge funds that invest in equities and bonds to profit from economic, political, and government driven events. A majority of the investments are targeted at economic policy decisions. The fair values of the investments in this class have been estimated using the net asset value per share of the investments as a practical expedient.

c. This class includes investments in hedge funds that hold investments in U.S. and non-U.S. common stocks in the healthcare, energy, information technology, utilities, and telecommunications sectors. The fair values of the investments in this class have been estimated using the net asset value per share of the investments as a practical expedient.

d. This class invests in hedge funds that pursue multiple strategies to diversify risks and reduce volatility. The fair values of the investments in this class have been estimated using the net asset value per share of the investments as a practical expedient. Investments representing approximately 17 percent of the value of the investments in this class are biannually redeemed and sell orders have been placed. These will be redeemed in Sept. 2014 and May 2015. The remaining restriction period for these investments ranges from quarterly to annually.

e. This class includes funds with direct investments in base and precious metals and investment securities of miners, and associated mining equipment. This fund has a 90 day redemption notice period, which 1/3 of the fund will pay out with the remaining 2/3 paying out in the second and third year respectively.

f. This class includes real estate funds that invest in U.S. and non-U.S. residential and commercial as well as distressed real estate. The fair values of the investments in this class have been estimated using the net asset value of the System's ownership interest in partners' capital as a practical expedient. $15 million of these funds have a 90 day redemption notice, but the fund manager can only accommodate redemption requests as liquid assets allow. The remaining funds will receive distributions from each fund as the underlying investments of the funds are liquidated. It is estimated that the underlying assets of these funds will be liquidated over the next 7 to 10 years, although these funds may liquidate early in the event of purchase by a third party, or initial public offering.

g. This class includes private equity funds. These investments cannot be redeemed with the funds. Instead, the nature of the investments in this class is that distributions are received through the liquidation of the underlying assets of the fund. These funds are managed by one of the System's advisors with particular private equity experience in secondary market dealing. These funds could be subject to redemption to a third party buyer, but at June 30, 2013, no funds were currently being evaluated this way. The fair values of the investments in this class have been estimated using the net asset value of the System's ownership interest in partners' capital as a practical expedient.

5. Property, Plant and Equipment

Property, plant and equipment and related accumulated depreciation at June 30, 2013 and 2012 consist of:

	2013	2012
Land and land improvements	$ 65,272,375	$ 62,907,873
Buildings and improvements	537,217,113	524,663,808
Fixed equipment	267,538,143	266,202,182
Movable equipment	403,795,604	279,426,761
Property, plant, equipment before depreciation and AIP	1,273,823,235	1,133,200,624
Less: Accumulated depreciation	$ (646,293,982)	(570,689,459)
Property, plant, equipment before AIP, net of depreciation	627,529,253	562,511,165
AIP Non Equipment (EPIC & Construction Projects)	$ 54,168,642	52,554,472
Net property, plant and equipment	$ 681,697,895	$ 615,065,637

Depreciation expense was approximately $75,024,000 and $64,965,000 for the years ended June 30, 2013 and 2012, respectively.

6. Long-Term Debt

Long-term debt at June 30, 2013 and 2012 consist of:

	2013		2012	
	Carrying Value	**Fair Value (Level 2)**	**Carrying Value**	**Fair Value (Level 2)**
Berks County Municipal Authority Hospital Revenue Bond Series of 2012, net of unamortized discount and premium	$ 478,725,089	$ 475,014,687	$ 479,354,940	$ 480,768,793
Berks County Municipal Authority Hospital Revenue Bond Series of 2009, net of unamortized discount	117,946,613	134,321,792	121,438,220	140,138,046
Berks County Municipal Authority Hospital Revenue Bond Series of 1999, net of unamortized discount	-	-	1,204,746	1,226,344
Berks County Municipal Authority Hospital Revenue Bond Series of 1993,	4,770,000	4,963,431	6,965,000	7,355,191
Term loans	2,240,755	2,240,755	2,476,010	2,476,010
Total long-term debt	603,682,457	616,540,665	611,438,916	631,964,384
Less: Amounts due within one year	6,733,536		7,680,255	
Long-term debt, net of current portion	$ 596,948,921		$ 603,758,661	

Under the terms of the various debt agreements, the System is required to maintain certain deposits with a trustee. Such deposits are included with assets whose use is limited in the Consolidated Financial Statements. The various agreements also place limits on the incurrence of additional borrowings and require that the System satisfy certain measures of financial performance as long as the debt is outstanding. The System was in compliance with these covenants at June 30, 2013 and 2012.

Scheduled principal repayments on long-term debt are as follows for the years ending June 30, 2013:

2014	$ 6,733,536
2015	7,074,468
2016	5,274,162
2017	5,528,648
2018	5,751,432
Thereafter	568,648,509
Total long-term debt	599,010,755
Plus: Unamortized Net Premium	4,618,515
Long term-debt, net of unamortized discount	$ 603,629,270

Berks County Municipal Authority Hospital Revenue Bond Series of 2012
On June 28, 2012, The Berks County Municipal Authority (“Authority”) issued $473,275,000 (notional) of Revenue Bonds in four series, 2012 A, B, C and D.

The Authority issued $160,065,000 of Fixed Rate Serial Revenue Bonds (“2012 A”) for the purpose of refunding the Dauphin Country General Authority Hospital Revenue Bond Series 1994A, Berks County Bond Series 1998 and 2008.

Mandatory annual principal redemptions by the System for the 2012 A bonds due November 1, 2039 through November 1, 2044 range from $7,590,000 to $33,555,000 with final maturity on November 1, 2044. Effective interest rate of the bonds range from 4.23% to 4.50%.

The Authority issued $91,775,000 of Variable Rate Serial Revenue bonds ("2012 B") for the purpose of refunding the Authority Series 2009 A-5.

Mandatory annual principal redemptions by the System for the 2012 B bonds due November 1, 2035 through November 1, 2039 range from $3,225,000 to $24,955,000 with final maturity on November 1, 2039. Interest on these bonds is calculated on a SIFMA Municipal Index rate plus a fixed spread of 1.50%. The SIFMA rate at June 30, 2013 was .06%.

The Authority issued a $47,235,000 Floating Rate Bond ("2012 C") used to refund the Series 2009 A-4 and a $174,000,000 Floating Rate Bond ("2012 D") used to Refund the Series 2009 A-1 and A-2. Both Series 2012 C and 2012 D were privately placed with commercial banks.

Mandatory monthly principal redemptions by the System for the 2012 C bonds commence August 1, 2012 through July 1, 2022 and range from $39,363 to $128,823 with final maturity date on July 1, 2022. Interest on these bonds is calculated using a one month London Interbank Offered Rate Index rate (LIBOR) plus a fixed spread of 1.20% times an Applicable Factor of 70.0%. The one month LIBOR rate at June 30, 2013 was .19%.

Mandatory annual principal redemptions by the System for the 2012 D bonds due November 1, 2022 through November 1, 2035 range from $8,625,000 to $21,120,000 with final maturity on November 1, 2035. Interest on these bonds is calculated on a SIFMA Municipal Index rate plus a fixed spread of .70%. The SIFMA rate at June 30, 2013 was .06%.

Berks County Municipal Authority Hospital Revenue Bond Series of 2009
Series 2009 A-1, A-2, A-4 and A-5 were refunded on June 28, 2012 with the aforementioned Bond Series 2012. The 2009 A-3 bond remains outstanding.

The 2009 A-3 bonds were issued on July 15, 2009. The Authority issued $133,665,000 of Fixed Rate Revenue Bonds, Series 2009 A-3 for the primary purpose of redeeming $115,520,000 of 2001 Bonds and $14,965,000 for major renovation projects.

The 2009 A-3 bonds are comprised of $44,285,000 of serial bonds and $89,380,000 of term bonds. The serial bonds are due in installments payable November 1, 2009 through 2019, with payments ranging from $120,000 to $4,895,000. The term bonds are due on November 1 of 2024, 2031 and 2039, with payments ranging from $820,000 to $9,380,000. The effective interest rate on the serial bonds ranges from 3% to 5% and 5.25% to 5.75% for the term bonds.

Berks County Municipal Authority Hospital Revenue Bond Series of 1999
On November 1, 1999, the Authority issued $45,805,000 of Hospital Revenue Bonds, Series 1999 ("1999 Bonds") for the primary purpose of providing funds for the cost of certain capital projects relating to the facilities, buildings, and equipment of the Hospital (the "project"), and to include payment of costs incurred with the issuance of the 1999 Bonds. The project consists of certain improvements to the Hospital's campus, the construction of new facilities, the renovation of existing facilities, and the acquisition of certain medical equipment. The System granted to the Authority a security interest in certain assets and substantially all revenues as collateral for its obligation under the indenture. The Series 1999 Bond matured in November 2012 with the final payment of $1,210,000 plus accrued interest.

Berks County Municipal Authority Hospital Revenue Bond Series of 1993
On June 1, 1993, the Authority issued Hospital Revenue Bonds, Series of 1993 ("1993 Bonds") for the primary purpose of providing funds for the advance refunding of the Berks County Municipal Authority Hospital Revenue Bonds Series of 1986 ("1986 Bonds"), the retirement of certain other indebtedness, and the funding of certain medical and computer equipment to be located on Hospital premises.

Remaining mandatory annual principal redemptions by the Hospital for the 1993 Bonds are $2,320,000 in FY2013 and $2,450,000 in FY2014 when the Bond matures. All mandatory redemptions are at par value. The Hospital granted to the Authority a security interest in certain assets and substantially all revenues as collateral for its obligation under the indenture.

The stated interest rates of the 1993 Bonds at June 30, 2013 are 5.70%.

Term Loans
Effective retroactive to January 1, 2004, the Hospital replaced NMG Limited Partnership as the borrower on three promissory notes. The Hospital was previously the guarantor for the notes. The original notes were issued as follows: $2,100,000 due March 31, 2020, $2,000,000 due December 31, 2019 and $165,000 due March 31, 2006. In conjunction with the assumption of debt, the Hospital received assets which have been purchased with the proceeds from the debt.

Mandatory annual principal redemptions by the Hospital for the notes for the 2012-2019 period range from $219,000 to $411,000 in 2019. The interest rate is calculated based upon the one month LIBOR plus a spread of 1.70%. This LIBOR rate was .19% at June 30, 2013.

Line of Credit
At June 30, 2013, the System had available a line of credit of $10,500,000 with M&T Bank. The amounts outstanding on the available letters of credit at June 30, 2013 and 2012, equaled $3,992,500 for both periods.

7. Interest Rate Swaps

The System has, in the past used derivative instruments, such as interest rate swaps, to manage certain interest rate exposures. Derivative instruments are viewed as risk management tools by the System and are not used for trading and speculative purposes.

When quoted market prices are not available, the valuation of derivative instruments is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of each leg of the derivative. This analysis reflects the contractual terms of the derivatives, including interest rate curves and implied volatilities. The estimates of fair value valuation are made by swap counterparties using a standardized methodology based on observable market inputs. As part of the System's overall valuation process, management evaluates this counterparty valuation methodology to ensure that it is representative of exit prices in the principal markets. These future net cash flows, however, are susceptible to change primarily due to fluctuations in interest rates. As a result, the estimated values of these derivatives will change over time as cash is received and paid, and as interest rates change. As these changes occur, they may have a positive or negative impact on estimated valuations.

The System has classified its interest rate swap in Level 2 of the fair value hierarchy, as the significant inputs to the overall valuations are based on market-observable data or information derived from or corroborated by market-observable data. For over-the-counter derivatives that trade in liquid markets such as interest rate swaps, model inputs (i.e. contractual terms, market prices, yield curves, credit curves, and measures of volatility) can generally be verified, and model selection does not involve significant management judgment.

The fair market value of the swap contracts and the related realized and unrealized gains/(losses) were as follows, as of June 30, 2013 and 2012:

Classification of derivatives in Balance Sheets	**Fair market value 2013**	**Fair market value 2012**
Derivatives not designated as hedging instrument:		
2008 Bond Issuance	$ 147,064	$ 191,717
2005 Bond Issuance	(5,006,891)	(7,149,360)
2002 Bond Issuance	(22,950,621)	(31,355,502)
2001 Bond Issuance	(30,041,409)	(41,389,318)
1997 Bond Issuance	(421,865)	(623,313)
1992 Bond Issuance	(1,082,389)	(1,620,320)
Term loans	(503,269)	(689,057)
Total swap contracts	$ (59,859,380)	$ (82,635,153)

Classification of derivatives gain/(loss) in Statements of Operations	**Amount of gain/(loss) recognized in excess of revenue over expenses 2013**	**Amount of gain/(loss) recognized in excess of revenue over expenses 2012**
Derivatives not designated as hedging instrument:		
Unrealized gain/(loss) on swap contracts	$ 22,775,774	$ (30,302,796)
Realized gain/(loss) on swap contracts	(8,575,772)	(5,937,975)
Realized and unrealized gains (losses) on swap contracts	$ 14,200,002	$ (36,240,771)

In connection with the 2008 bond issuance, the System entered into an interest rate swap agreement with a third party. The swap economically converted the fixed rate obligation of the 2008 bonds from a fixed rate of 7.5% to variable rates. Notional amount of the swap is $100 million and this swap matured in November 2012.

In connection with the 2008 bond issuance, the System entered into two basis swaps by which the System pays SIFMA and receives an average of .85% of three month LIBOR. Notional amount of these basis swaps is $175.4 million and the three month LIBOR rate at June 30, 2013 was .27%.

In connection with the 2005 bond issuance, the System entered into an interest rate swap agreement with a third party. The swap economically converts the variable rate obligation of the 2005 bonds to a fixed rate of 3.584%. Notional amount of the swap is $39 million.

In connection with the 2001 and 2002 bonds issuances, the System entered into two interest rate swap agreements with a third party. The swaps economically convert the variable rate obligations of the 2001 and 2002 bonds to a fixed rate of 4.30% and 4.69%, respectively. Notional amounts of the swaps are $143.6 million and $75.1 million.

On June 26, 2006, the System entered into an interest rate swap agreement on the 2001, 2002 and 2005 bond issuances which were effective as of August 4, 2006. The swap has a variable effective interest rate at 68% of the LIBOR.

In connection with the 2002 bond issuance, the System entered into two interest rate swap agreements. The swaps effectively convert the variable rate obligation of the Series A and B Bonds to fixed rates of 4.69% and 6.28%, respectively. Notional amounts of the swaps are $4.6 million and $8.2 million.

In connection with the 1997 bond issuance, the System entered into an interest rate swap agreement which was effective as of May 26, 2005. The swap effectively converts the variable rate obligation of the Bonds to a fixed rate of 3.397%. Notional amount of the swap is $5.9 million.

In connection with the 1992 bond issuance, the System entered into an interest rate swap agreement which was effective as of May 26, 2005. The swap effectively converts the variable rate obligation of the Bonds to a fixed rate of 3.607%. Notional amount of the swap is $8.1 million.

In connection with the term loans, the System assumed two interest rate swap agreements with a third party. The swaps effectively convert the variable obligations to fixed rates of 9.13% for the $2,100,000 note and 9.06% for the $2,000,000 note. The fair value of the interest rate swap agreements is the amount at which they would be settled based on estimates of market rates, which was a liability of $503,000 at June 30, 2013 and $689,000 at June 30, 2012.

The change in the value of the interest rate swap agreements and the interest expense associated with these swaps are recorded in other non-operating gains/(losses) on the Statements of Operations.

8. Accounting for Defined Benefit Plan

Substantially all employees of the System are covered under a qualified noncontributory defined benefit pension plan. Pension costs are funded as accrued except when not permitted by regulations, such as full funding limitations. Unfunded prior service costs are amortized over an initial term of thirty years.

The System follows the FASB standards over employer's accounting for defined benefit pension and other post-retirement plans. Included in these standards is a requirement for an entity to recognize in its Balance Sheet, the overfunded or underfunded status of its defined benefit postretirement plans measured as the difference between the fair value of the plan assets, and the benefit obligation. For a pension plan, this would be the projected benefit obligation; for any other post-retirement plan, the benefit obligation would be the accumulated post-retirement benefit obligation. These standards also require measurement dates for the pension plan obligation to be measured as of the date of the entity's Balance Sheet.

The System will be transitioning for the current defined benefit plan structure. Employees hired on or after July 1, 2013 will be enrolled in a defined contribution plan. Current employees will continue to accrue benefits in the existing defined plan until June 30, 2016. On July 1, 2016 the benefits will remain accrued and employees will begin to accumulate dollars under a defined contribution plan.

Obligations and Funded Status at June 30 for the Plan

	2013	2012
Change in projected benefit obligation		
Benefit obligation at beginning of year	$ 478,052,596	$ 378,415,249
Service cost	20,221,748	15,919,894
Interest cost	23,509,010	21,595,137
Actuarial loss/(gain)	(9,184,898)	73,636,234
Benefits paid	(11,789,340)	(11,513,918)
Curtailment	(70,273,670)	-
Benefit obligation at end of year	$ 430,535,446	$ 478,052,596
Change in plan assets		
Fair value of plan assets at beginning of year	$ 277,861,737	$ 278,882,822
Actual return on assets	32,764,023	(3,907,167)
Employer contributions	19,070,855	14,400,000
Benefits paid	(11,789,340)	(11,513,918)
Fair value of plan assets at end of year	$ 317,907,275	$ 277,861,737

The accrued liability of the plan at June 30, 2013 and 2012 consists of the following components:

	2013	2012
Funded status	$ (112,628,174)	$ (200,190,859)

The accumulated benefit obligations totaled $423,957,000 and $408,166,000 at June 30, 2013 and 2012, respectively, for the Plan.

Amounts recognized in the Balance Sheet consist of:

	2013	2012
Accrued pension	$ 112,628,171	$ 200,190,859
Total accrued liability	$ 112,628,171	$ 200,190,859
Amounts recognized in net assets consist of:		
Net actuarial loss	$ 81,869,184	$ 179,386,937
Prior service cost	-	1,448,866
Pension cost charged to net assets	$ 81,869,184	$ 180,835,803

Net periodic benefit cost components include the following:

	2013	2012
Service cost - benefits earned during the period	$ 20,221,748	$ 15,919,894
Interest cost on projected benefit obligation	23,509,010	21,595,137
Expected return on plan assets	(23,199,274)	(22,446,051)
Amortization of prior service cost	161,972	215,963
Amortization of net gain	8,494,436	3,516,263
Effect of curtailment	1,286,894	-
Net periodic pension cost Charged to operations	$ 30,474,786	$ 18,801,206

Other changes in plan assets and benefit obligations recognized in unrestricted net assets:

	2013	2012
Net loss (gain)	$ (18,749,647)	$ 99,989,452
Amortization of prior service cost	(161,972)	(215,963)
Amortization of net loss	(8,494,436)	(3,516,263)
Effect of curtailment	(71,560,564)	-
Total recognized in unrestricted net assets	$ (98,966,619)	$ 96,257,226
Total recognized in net periodic benefit cost and unrestricted net assets	$ (68,491,833)	$ 115,058,432

The amounts expected to be amortized from unrestricted net asset to net periodic pension costs during fiscal year 2014 are a net loss of $1,176,000 and a prior service cost of $0.

Weighted-average assumptions used to determine benefit obligations at June 30:

	2013	2012
Discount rate	5.32 %	5.00 %
Rate of compensation increase	3.00 %	3.00 %
Measurement date	6/30/2013	6/30/2012

Weighted-average assumptions used to determine net periodic benefit cost for years ended June 30:

	2013	2012
Discount rate	5.00%/4.75%	5.78 %
Expected long-term return on plan assets	8.00 %	8.00 %
Rate of compensation increase	3.00 %	3.00 %

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

Plan Assets

Reading Hospital Pension Plan weighted-average asset allocations at June 30, 2013 and 2012, by asset category are as follows:

	Plan Assets at June 30	
	2013	**2012**
Asset category		
Cash and cash equivalents	8.2 %	1.7 %
Mutual funds	19.0	19.8
Fixed income	13.5	20.4
Equity investments	3.8	3.6
Alternate investments	55.5	54.5
	100.0 %	100.0 %

The overall investment objective of the Plan is to provide a return on investment consistent with the Plan's spending needs and to prevent erosion of purchasing power by inflation. Achievement of the return will be sought from an investment strategy that provides an opportunity for superior returns within acceptable levels of risk and volatility of returns.

The following tables represent the fair value measurement levels for all assets and liabilities, which the Hospital has recorded at fair value:

		Fair Value Measurement Using		
	June 30, 2013	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Other Unobservable Inputs (Level 3)**
Assets				
Cash and cash equivalents	$ 25,940,319	$ 25,940,319	$ -	$ -
State and local government securities	8,875,000	-	-	8,875,000
Mutual funds	60,121,164	60,121,164	-	-
Equities	12,213,662	12,213,662	-	-
Fixed income funds	34,146,523	34,146,523	-	-
Hedge funds	176,610,607	-	45,081,258	131,529,349
Total investments	$ 317,907,275	$ 132,421,668	$ 45,081,258	$ 140,404,349

		Fair Value Measurement Using		
	June 30, 2012	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Other Unobservable Inputs (Level 3)**
Assets				
Cash and cash equivalents	$ 4,592,602	$ 4,592,602	$ -	$ -
State and local government securities	9,175,000	-	-	9,175,000
Mutual funds	55,052,978	55,052,978	-	-
Equities	9,941,823	9,941,823	-	-
Fixed income funds	47,585,136	47,585,136	-	-
Hedge funds	151,514,197	-	31,725,966	119,788,231
Total investments	$ 277,861,736	$ 117,172,539	$ 31,725,966	$ 128,963,231

The following table represents the nonreadily marketable investments and auction rate securities for which fair value was measured under Level 3:

	Hedge Funds	State and Local Government Securities
Fair value at July 1, 2012	$ 119,788,232	$ 9,175,000
Purchases	17,670,006	-
Sales	(20,537,938)	(300,000)
Realized gains/(losses)	1,158,266	-
Net change in unrealized gains/(losses)	13,450,783	-
Fair value at June 30, 2013	$ 131,529,349	$ 8,875,000

	Hedge Funds	State and Local Government Securities
Fair value at July 1, 2011	$ 127,862,288	$ 9,450,000
Purchases	25,427,940	-
Sales	(33,959,960)	(275,000)
Realized gains/(losses)	1,001,636	-
Net change in unrealized gains/(losses)	(543,672)	-
Fair value at June 30, 2012	$ 119,788,232	$ 9,175,000

Cash Flows

Contributions (Unaudited)

The Reading Hospital expects to contribute the minimum required contribution during the 2014 fiscal year to the Plan, which is estimated to be $19,000,000.

Estimated Future Benefit Payments (Unaudited)

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

Years Ending June 30,	
2014	$ 13,050,670
2015	14,155,110
2016	15,967,127
2017	18,591,094
2018	20,549,088
2019–2023	130,342,149

9. Related Party Transactions

Other receivables from affiliated organizations at June 30, 2013 and 2012 consist of:

	2013	2012
Springridge, LLC	$ 589,168	$ 1,302,269
Berkshire Health Partners	108,745	144,255
Central Pennsylvania Homecare Inc	5,350	8,309
Total receivables from affiliated organizations	$ 703,263	$ 1,454,833

These amounts are all noninterest bearing with no stated repayment terms.

Included in other assets are the following investments in affiliates at June 30, 2013 and 2012:

	2013	2012
CPAL	$ 350,373	$ 350,373
Quest	19,717	13,594
Springridge, LLC	1,851,041	1,728,372
RBPT	237,864	332,774
Horizon	655,569	803,319
VNA Community Care Services	6,444,261	5,653,051
BHP	1,044,782	920,400
Total investments in affiliated organizations	$ 10,603,607	$ 9,801,883

10. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets at fair value are available for the following purposes at June 30, 2013 and 2012:

	2013	2012
Various health care services	$ 660,370	$ 654,010

Permanently restricted net assets at fair value at June 30, 2013 and 2012 are restricted to:

	2013	2012
Permanent endowment funds, the interest and dividend income from which is expendable to support health care services	$ 5,541,468	$ 4,127,781
Funds held in trust by others	13,288,592	12,685,103
Total permanently restricted net assets	$ 18,830,060	$ 16,812,884

11. Insurance Arrangements

The System participates in the Pennsylvania Medical Care Availability and Reduction of Error Fund or Mcare Fund established under the Commonwealth of Pennsylvania. The Mcare Fund presently provides coverage excess of up to $500,000 to the System's primary per occurrence retention (which is currently $500,000) with annual aggregate coverage of $1,500,000.

The System established a self-insurance trust fund to provide protection against professional liability claims. The trust is actuarially funded on an annual basis to provide single limit professional liability coverage of $500,000 per occurrence and $2,500,000 in the annual aggregate for the Hospital and certain employees. For incidents occurring since April 30, 2009, the System purchased commercial insurance to provide coverage on a claims-made basis in an amount up to $25,000,000 in excess of a total retention of $3,000,000 ($500,000 primary; $500,000 Mcare excess and a $2,000,000 self-insured buffer). The adoption of the ASU 2010-24 Pronouncement had no impact on the System's financial performance or cash flows. Claim liabilities are no longer netted by insurance recoveries. For the years ended June 30, 2013 and 2012, the insurance recoverable amounts were $4,500,000, and $5,600,000, respectively, which is included in other assets on the Consolidated Balance Sheets. Funding requirements of the plan are subject to increase depending on the plan's claim experience. Premium payments for the Mcare Fund are based upon each individually licensed healthcare provider's rating with the Joint Underwriters Association and the amount of the surcharge to be assessed is determined by the Mcare Fund on an annual basis. The System's annual surcharge premiums for participation in the Mcare Fund were $1,706,000 and $1,445,000 for the years ended June 30, 2013 and 2012, respectively.

Additionally, the System self-insures its workers' compensation and minor general liability risks. The System's self-insurance plan has been reviewed and approved by the Commissioner of Insurance of Pennsylvania.

The System purchases excess workers' compensation insurance for all controlled entities of the hospital with statutory limits over a self-retention of $1,000,000 per occurrence subject to a policy maximum of $1,000,000 for the policy period. The System has established a trust fund for the payment of workers' compensation benefits.

Reserves for self-insurance claims at June 30, 2013 and 2012 are summarized as follows:

	2013	2012
Professional liability claims payable	$ 40,602,000	$ 37,489,000
Workers' compensation	13,970,751	13,962,738
Total self-insurance claims reserve	54,572,751	51,451,738
Less: Current portion	10,791,751	10,877,737
Self-insurance claims reserve, net of current portion	$ 43,781,000	$ 40,574,001

12. Commitment and Contingencies

Operating Leases

The System leases equipment and facilities under operating leases expiring at various dates through May 2026. Total rental expense under all operating leases was $12,271,000 and $12,187,000 for the years ended June 30, 2013 and 2012, respectively.

The following table summarizes future minimum rental commitments under noncancellable operating leases with initial or remaining terms of more than one year:

Years Ending June 30,	
2014	$ 7,570,500
2015	6,178,521
2016	4,383,520
2017	3,433,824
2018 and thereafter	17,882,598

EPIC

On September 9, 2011, Reading Hospital entered into a sale and purchase agreement ("SPA") with EPIC Systems Corporation to purchase, install, and implement EPIC software for a consideration of $22 million of which $8,579,000 in payments ("Meaningful Use Funds") have been received. As of June 30, 2013, Reading Hospital has paid a sum of $16.0 million to EPIC Systems Corporation. Additional services and costs will be incurred toward the entire project scope, expecting to total $130 million in additional capital costs and $23 million in operating costs.

Obligation to Provide Future Services

The Highlands annually calculates the present value of the estimated net cost of future services and use of facilities to be provided to current residents and compares that amount with the balance of deferred entrance fee revenue. If the present value of the net cost of future services and use of facilities exceeds the deferred revenue, a liability is recorded with the corresponding charge to income. As of June 30, 2013 and 2012, the estimated present value of the net cost of future services and use of facilities is less than the deferred entrance fee revenue; thus, no liability has been recorded.

Litigation

The System and its controlled entities are involved in certain litigation which involves professional and general liability. In the opinion of management and legal counsel, the ultimate liability, if any, will not have a material effect on the consolidated financial condition of the Parent and its controlled entities.

Regulatory Compliance

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The System believes that it is in compliance with all applicable laws and regulations through the years ended June 30, 2013 and 2012. Compliance with such laws and regulations can be subject to government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

13. Functional Expenses

The System provides general health care services to residents within its geographic location. Expenses related to providing these services are as follows:

	2013	2012
Health care services	$ 674,531,174	$ 686,010,429
General and administrative	217,689,548	152,749,250
Total functional expenses	$ 892,220,722	$ 838,759,679

14. Concentrations of Credit Risk

Financial instruments which potentially subject the System to concentrations of credit risk consist primarily of cash, cash equivalents, investments, and accounts receivable.

Management periodically evaluates the credit standing of the financial institutions with which they maintain their cash, cash equivalents, and investments. Amounts held in its accounts often exceed the federally insured levels.

The fair value of the System's investments is subject to various market fluctuations which include changes in the interest rate environment and general economic conditions.

The System grants credit to its patients and other third-party payors, primarily Medicare, Medical Assistance, Blue Cross and various commercial insurance companies. The System maintains reserves for potential credit losses and such losses have historically been within management's expectations. The mix of receivables from patients and third-party payors at June 30, 2013 and 2012, was as follows:

	2013	**2012**
Medicare	32%	29%
Medical Assistance	14%	18%
Blue Cross	14%	17%
Commercial insurance	28%	17%
Self-pay	10%	17%
Other	2%	2%
	100%	100%

15. Subsequent Events

The Company has evaluated subsequent events through October 21, 2013. Management reviews and identifies subsequent events through participation at meetings of the Board of Directors and their subcommittees.

In July 2013, after two years of work on design and infrastructure, the Board of Trustees of the Reading Health System approved the 7th Avenue Project for a total cost of $354,000,000. The project includes a state of the art perioperative center, five all-private room nursing units and additional space for the Emergency Department and Trauma Center. There is no expansion of licensed beds included in this project.

Supplementary Consolidating Information

Report of Independent Auditors on
Supplementary Consolidating Information

To The Board of Directors of
Reading Health System

We have audited the consolidated financial statements of Reading Health System as of June 30, 2013 and for the year then ended and our report thereon appears on page 1 of this document. That audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The supplementary consolidating information is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. The 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 taken as a whole.

PricewaterhouseCoopers LLP

October 21, 2013

Reading Health System
Consolidating Balance Sheet
Year Ended June 30, 2013

Schedule I

	Parent	Hospital	RPS	TRHMG	Highlands	Consolidating and Eliminating Entries	Reading Health System
Current assets							
Cash and cash equivalents	$ -	$ 61,781,109	$ 23,424	$ 72,745	$ 2,317,068	$ -	$ 64,194,346
Patient accounts receivable, less allowance for uncollectible accounts of $52,456,860	-	171,175,301	4,231,911	1,944,218	2,584,472	-	179,935,902
Other receivables	1,788,580	10,830,652	550,108	57,940	704	-	13,227,984
Receivable from affiliates	8,145,493	2,613,524	(11,610)	43,565	-	(10,113,136)	677,836
Inventories	-	14,442,833	-	-	379,144	-	14,821,977
Estimated third-party payor receivables	-	8,198,991	-	-	-		8,198,991
Prepaid expenses and other current assets	-	14,164,667	-	413,091	245,430	-	14,823,188
Assets whose use is limited - required for current liabilities							
Self-insurance funding arrangements	-	7,812,332	-	-	-	-	7,812,332
Revenue bond indentures - debt service	-	2,878,958	-	-	-	-	2,878,958
Total current assets	9,934,073	293,898,367	4,793,833	2,531,559	5,526,818	(10,113,136)	306,571,514
Assets whose use is limited							
Self-insurance funding arrangements	-	20,032,628	-	-	-	-	20,032,628
Under regulatory requirements	-	-	-	-	2,912,455	-	2,912,455
By board for capital improvements	900,699,219	133,563	-	-	40,117,676	-	940,950,458
Total assets whose use is limited, net of current portion	900,699,219	20,166,191	-	-	43,030,131	-	963,895,541
Investments	-	20,115,778	-	-	-	-	20,115,778
Temporarily restricted funds	-	627,847	(258)	-	32,781	-	660,370
Long-term receivables from affiliates	523,014,508	-	-	-	-	(523,014,508)	-
Property, plant and equipment, net	40,194,230	582,640,305	-	7,110,415	51,752,945	-	681,697,895
Deferred financing expense, net	4,815,161	-	-	-	-	-	4,815,161
Deferred compensation fund	-	2,873,977	-	-	-	-	2,873,977
Other assets	8,514,701	5,961,437	258	-	(32,781)	-	14,443,615
Total assets	$ 1,487,171,892	$ 926,283,902	$ 4,793,833	$ 9,641,974	$ 100,309,894	$ (533,127,644)	$ 1,995,073,851

Reading Health System
Consolidating Balance Sheet
Year Ended June 30, 2013

Schedule I

	Parent	Hospital	RPS	TRHMG	Highlands	Consolidating and Eliminating Entries	Reading Health System
Current liabilities							
Current installments of long-term debt	$ 4,157,350	$ 2,576,186	$ -	$ -	$ -	$ -	$ 6,733,536
Current installments of long-term affiliated payables	-	4,157,350	-	-	5,955,786	(10,113,136)	-
Current portion of estimated self-insurance costs	-	10,596,040	-	-	195,751	-	10,791,791
Accounts payable	-	44,783,037	566,300	1,929,774	1,116,710	-	48,395,821
Estimated third-party settlements	-	4,555,158	-	-	-	-	4,555,158
Accrued expenses	2,981,259	18,132,199	6,438,002	3,032,730	790,530	-	31,374,720
Accrued vacation	-	17,039,602	3,201,890	1,099,952	442,798	-	21,784,242
Advance from third-party payor	-	3,832,000	-	-	-	-	3,832,000
Other current liabilities	-	15,293,996	-	3,411	717,532	-	16,014,939
Total current liabilities	7,138,609	120,965,568	10,206,192	6,065,867	9,219,107	(10,113,136)	143,482,207
Long-term debt, net of current portion and unamortized discount	592,514,352	4,434,569	-	-	-	-	596,948,921
Long-term affiliates payables, net of current portion	-	484,952,763	-	-	38,061,745	(523,014,508)	-
Accrued pension costs, net of current portion	-	112,628,171	-	-	323,534	-	112,951,705
Deferred revenue	-	3,203,918	-	-	-	-	3,203,918
Deferred compensation	-	1,527,412	-	-	33,432,253	-	34,959,665
Gift annuities	-	-	-	-	579,100	-	579,100
Estimated self-insurance costs, net of current portion	-	43,781,001	-	-	-	-	43,781,001
Swap contracts	59,356,111	503,269	-	-	-	-	59,859,380
Total liabilities	659,009,072	771,996,671	10,206,192	6,065,867	81,615,739	(533,127,644)	995,765,897
Net assets							
Unrestricted	828,162,820	134,829,325	(5,412,617)	3,576,107	18,661,373	-	979,817,008
Temporarily restricted	-	627,847	258	-	32,781	-	660,886
Permanently restricted	-	18,830,060	-	-	-	-	18,830,060
Total net assets	828,162,820	154,287,232	(5,412,359)	3,576,107	18,694,154	-	999,307,954
Total liabilities and net assets	$ 1,487,171,892	$ 926,283,903	$ 4,793,833	$ 9,641,974	$ 100,309,893	$ (533,127,644)	$ 1,995,073,851

Reading Health System
Consolidating Statement of Operations
Year Ended June 30, 2013

Schedule II

	Parent	Hospital	RPS	TRHMG	Highlands	Consolidating and Eliminating Entries	Reading Health System
Unrestricted revenues							
Net patient service revenue	$ -	$ 826,106,667	$ 40,133,209	$ 43,785,756	$ 4,037,106	$ -	$ 914,062,738
Provision for uncollectible accounts	-	(48,424,699)	(3,423,545)	(1,514,063)	-	-	(53,362,307)
Net patient service revenue less provision for uncollectible accounts	-	$ 777,681,968	$ 36,709,664	$ 42,271,693	$ 4,037,106	-	$ 860,700,431
Residential revenue	-	-	-	-	19,941,623	-	19,941,623
Other revenue	1,548,965	26,932,872	3,125,033	1,941,159	629,997	(1,775,908)	32,402,118
Total revenues and other support	1,548,965	804,614,840	39,834,697	44,212,852	24,608,726	(1,775,908)	913,044,172
Expenses							
Salaries and benefits	-	391,388,510	58,943,836	53,228,280	11,906,182	-	515,466,808
Supplies	-	111,411,510	1,136,822	3,122,464	2,087,130	-	117,757,926
Utilities	-	10,054,052	83,077	1,020,904	1,057,547	-	12,215,580
Interest	-	14,295,289	-	-	1,420,173	-	15,715,462
Depreciation	-	69,798,968	343,788	1,847,111	3,034,583	-	75,024,450
Purchased services	2,004,000	63,806,204	7,604,903	4,015,326	2,098,453	-	79,528,886
Repairs and maintenance	-	21,576,515	123,321	618,859	424,492	-	22,743,187
Other	-	42,296,214	5,386,325	6,078,256	1,783,536	(1,775,908)	53,768,423
Total expenses	2,004,000	724,627,262	73,622,072	69,931,200	23,812,096	(1,775,908)	892,220,722
Income (loss) from operations	(455,035)	79,987,578	(33,787,375)	(25,718,348)	796,630	-	20,823,450
Meaningful Use Funds	-	7,586,912	-	-	-	-	7,586,912
EPIC expense offset	-	(7,586,912)	-	-	-	-	(7,586,912)
Nonoperating gains/(losses)							
Investment income	73,623,405	562,345	-	-	1,841,634	-	76,027,384
Other (losses)/gains	-	(2,123,821)	-	-	614,041	-	(1,509,780)
Loss on extinguishment of debt	-	-	-	-	-	-	-
Realized and unrealized loss on interest rate swaps	14,098,501	101,501	-	-	-	-	14,200,002
Nonoperating gains, net	87,721,906	(1,459,975)	-	-	2,455,675	-	88,717,606
Excess (deficiency) of revenue, gains and other support over expenses	$ 87,266,871	$ 78,527,603	$ (33,787,375)	$ (25,718,348)	$ 3,252,305	$ -	$ 109,541,056