

InterHealth Corp. and Affiliates

Consolidated Financial Statements as of and
for the Years Ended September 30, 2013 and 2012,
Supplementary Consolidating Schedules as of and
for the Year Ended September 30, 2013, and
Independent Auditors' Report

INTERHEALTH CORP. AND AFFILIATES

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
InterHealth Corp. and Affiliates:

We have audited the accompanying consolidated financial statements of InterHealth Corp. and affiliates (the "Company"), which comprise the consolidated balance sheets as of September 30, 2013 and 2012, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these 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.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company'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 Company'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 consolidated financial position of InterHealth Corp. and affiliates as of September 30, 2013 and 2012, and the results of their operations, changes in their net assets, and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Supplementary Consolidating Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary consolidating information on pages 37–43 is presented for the purpose of additional analysis of the consolidated financial statements rather than to present the financial position, results of operations, and cash flows of the individual companies, and is not a required part of the 2013 consolidated financial statements. These schedules are the responsibility of the Company's management and were derived from and relate directly to the underlying accounting and other records used to prepare the 2013 consolidated financial statements. Such schedules have been subjected to the auditing procedures applied in our audit of the 2013 consolidated financial statements and certain additional procedures, including comparing and reconciling such schedules directly to the underlying accounting and other records used to prepare the 2013 consolidated financial statements or to the 2013 consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, such schedules are fairly stated in all material respects in relation to the 2013 consolidated financial statements as a whole.

Deloitte & Touche LLP

January 22, 2014

INTERHEALTH CORP. AND AFFILIATES

CONSOLIDATED BALANCE SHEETS AS OF SEPTEMBER 30, 2013 AND 2012 (In thousands)

	2013	2012
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 24,775	\$ 9,085
Investments — short term (Note 4)	2,366	15,616
Patient accounts receivable — net of allowance for doubtful accounts of \$8,487 and \$9,368 in 2013 and 2012, respectively (Notes 3 and 12)	65,599	63,893
Inventory	5,137	3,726
Other receivables	6,956	5,002
Prepaid expenses and other assets (Note 2)	9,392	11,503
Other current assets — Hospital Fee Program (Note 15)	<u>7,598</u>	<u>10,549</u>
Total current assets	121,823	119,374
INVESTMENTS IN MUTUAL FUNDS AND OTHER INVESTMENTS (Note 4)	34,609	26,606
INVESTMENTS — Assets limited as to use (Note 4)	364,149	376,426
PROPERTY, PLANT, AND EQUIPMENT — Net (Note 6)	513,989	463,106
DEFERRED FINANCING COSTS — Net	2,561	3,399
GOODWILL — Net of accumulated amortization of \$2,182 in 2013 and 2012 (Note 5)	11,545	11,545
OTHER ASSETS (Note 2)	1,509	260
OTHER ASSETS — Downey (Notes 5 and 17)	<u>23,636</u>	<u> </u>
TOTAL	<u>\$ 1,073,821</u>	<u>\$ 1,000,716</u>

(Continued)

INTERHEALTH CORP. AND AFFILIATES

CONSOLIDATED BALANCE SHEETS AS OF SEPTEMBER 30, 2013 AND 2012 (In thousands)

	2013	2012
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	\$ 57,043	\$ 54,268
Estimated third-party payor settlements (Note 3)	1,207	1,424
Accrued interest	1,362	1,382
Current portion of long-term debt (Note 7)	7,940	7,725
Short-term loan borrowing	30,500	
Other current liability — Hospital Fee Program (Note 15)	3,684	14,019
Retention — self-insurance programs — current portion (Note 10)	<u>10,926</u>	<u>11,444</u>
Total current liabilities	112,662	90,262
DEFERRED COMPENSATION (Note 4)	15,036	14,186
INTEREST RATE SWAPS (Note 7)	35,919	53,054
LONG-TERM DEBT — Net of current portion (Note 7)	285,005	292,967
PENSION LIABILITY (Note 9)	46,764	75,646
RETENTION — Self-insurance programs — net of current portion (Note 10)	<u>15,930</u>	<u>14,636</u>
Total liabilities	<u>511,316</u>	<u>540,751</u>
COMMITMENTS AND CONTINGENCIES (Note 10)		
NET ASSETS:		
Unrestricted	557,266	453,414
Temporarily restricted (Note 8)	4,268	5,580
Permanently restricted (Note 8)	<u>971</u>	<u>971</u>
Total net assets	<u>562,505</u>	<u>459,965</u>
TOTAL	<u>\$ 1,073,821</u>	<u>\$ 1,000,716</u>

See notes to consolidated financial statements.

(Concluded)

INTERHEALTH CORP. AND AFFILIATES

CONSOLIDATED STATEMENTS OF OPERATIONS FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012 (In thousands)

	2013	2012
REVENUES:		
Net patient service revenue including Hospital Fee Program revenue of \$20,784 for 2013 and \$28,623 for 2012 (Notes 3, 12, and 15)	\$538,388	\$491,372
Provision for bad debts	<u>13,864</u>	<u>14,152</u>
Net patient service revenue less provision for bad debts	524,524	477,220
Capitation revenue (Note 3)	77,405	76,619
Other operating revenue	21,350	29,758
Net assets released from restrictions used for operations	<u>866</u>	<u>954</u>
Total revenues	<u>624,145</u>	<u>584,551</u>
EXPENSES (Note 14):		
Salaries and wages	199,868	182,167
Purchased services	86,858	89,857
Medical supplies and drugs	70,299	59,655
Employee benefits (Notes 9 and 10)	79,777	74,692
Professional fees	82,135	67,085
Depreciation and amortization	27,482	21,462
Other expenses	19,909	17,658
Interest — net (Note 7)	5,423	3,977
Insurance (Note 10)	5,147	5,076
Rent lease expense	3,033	2,189
Hospital Fee Program (Note 15)	<u>17,584</u>	<u>28,315</u>
Total expenses	<u>597,515</u>	<u>552,133</u>
EXCESS OF REVENUES OVER EXPENSES BEFORE LITIGATION SETTLEMENT	26,630	32,418
LITIGATION SETTLEMENT — Reversal of overaccrual	<u> </u>	<u>419</u>
EXCESS OF REVENUES OVER EXPENSES	<u>26,630</u>	<u>32,837</u>
OTHER GAINS (LOSSES) — Net:		
Net investment income (Note 4)	9,963	9,875
Realized gains on investments — net (Note 4)	13,722	1,836
Change in fair value of interest rate swap and interest expense (Note 7)	10,477	(9,877)
Loss on extinguishment of debt	<u>(1,416)</u>	<u> </u>
Other gains — net	<u>32,746</u>	<u>1,834</u>
EXCESS OF REVENUES OVER EXPENSES AND OTHER GAINS (LOSSES)— Net	59,376	34,671
CHANGE IN UNREALIZED GAINS ON INVESTMENTS — Net (Note 4)	4,011	32,999
PENSION-RELATED CHANGES OTHER THAN NET PERIODIC PENSION COST (Notes 2 and 9)	38,636	(18,521)
NET ASSETS RELEASED FROM RESTRICTIONS USED FOR LONG-LIVED ASSETS	1,993	46
OTHER LOSSES — Net (Note 10)	<u>(164)</u>	<u>(484)</u>
TOTAL INCREASE IN UNRESTRICTED NET ASSETS	<u>\$103,852</u>	<u>\$ 48,711</u>

See notes to consolidated financial statements.

INTERHEALTH CORP. AND AFFILIATES

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012 (In thousands)

	2013	2012
UNRESTRICTED NET ASSETS — Increase in unrestricted net assets	<u>\$ 103,852</u>	<u>\$ 48,711</u>
Change in unrestricted net assets	<u>103,852</u>	<u>48,711</u>
TEMPORARILY RESTRICTED NET ASSETS:		
Contributions and grants received	1,547	2,437
Net assets released from restrictions	<u>(2,859)</u>	<u>(1,000)</u>
Change in temporarily restricted net assets	<u>(1,312)</u>	<u>1,437</u>
CHANGE IN NET ASSETS	102,540	50,148
NET ASSETS — Beginning of year	<u>459,965</u>	<u>409,817</u>
NET ASSETS — End of year	<u>\$ 562,505</u>	<u>\$ 459,965</u>

See notes to consolidated financial statements.

INTERHEALTH CORP. AND AFFILIATES

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012 (In thousands)

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	\$ 102,540	\$ 50,148
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	27,482	21,462
Amortization of deferred financing costs	221	250
Provision for bad debts	13,864	14,152
Accretion of bond premium	(44)	(51)
Amortization of bond discount	22	21
Loss on disposal of equipment	155	462
(Gain) loss on interest rate swap	(17,135)	3,497
Loss on extinguishment of debt	1,416	
Net realized and unrealized gains on investments	(17,733)	(34,834)
Pension-related changes other than net periodic pension cost	(38,636)	18,521
Contributions restricted for purchase of long-lived assets	(182)	(636)
Changes in assets and liabilities:		
Patient accounts receivable	(15,570)	(8,762)
Inventory	(1,411)	(398)
Other receivables	(1,954)	(817)
Prepaid expenses and other assets	2,111	(574)
Other current assets — Hospital Fee Program	2,951	(4,245)
Other assets	(1,249)	1
Accounts payable and accrued expenses	2,987	(108)
Estimated third-party payor settlements	(217)	1,424
Accrued interest	(20)	(115)
Other current liability — Hospital Fee Program	(10,335)	4,007
Retention — self-insurance programs	776	692
Pension liability	9,754	5,789
Deferred compensation	850	138
Net cash provided by operating activities	<u>60,643</u>	<u>70,024</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of assets limited as to use	(119,122)	(53,415)
Proceeds from the sale of assets limited as to use	148,786	47,564
Purchase of investments in mutual funds and other investments	(14,618)	(15,183)
Proceeds from the sale of investments in mutual funds and other investments	20,212	12,529
Proceeds from sale of property, plant, and equipment	6	8
Purchase of property, plant, and equipment	(78,738)	(91,384)
Purchase of medical group assets		(329)
Downey acquisition	(23,636)	
Net cash used in investing activities	<u>(67,110)</u>	<u>(100,210)</u>

(Continued)

INTERHEALTH CORP. AND AFFILIATES

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012 (In thousands)

	2013	2012
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayment of long-term debt	\$ (155,725)	\$ (7,375)
Proceeds from issuance of long-term debt	148,000	
Proceeds from short-term borrowing	30,500	
Payment of bond issuance costs	(800)	(104)
Contributions restricted for purchase of long-lived assets	<u>182</u>	<u>636</u>
Net cash provided (used in) financing activities	<u>22,157</u>	<u>(6,843)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	15,690	(37,029)
CASH AND CASH EQUIVALENTS — Beginning of year	<u>9,085</u>	<u>46,114</u>
CASH AND CASH EQUIVALENTS — End of year	<u>\$ 24,775</u>	<u>\$ 9,085</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION — Cash paid for interest	<u>\$ 11,887</u>	<u>\$ 10,196</u>
SUPPLEMENTAL INFORMATION RELATING TO NONCASH INVESTING AND FINANCING ACTIVITIES —		
As of September 30, 2013 and 2012, accounts payable and accrued expenses include \$7,938 and \$8,150, respectively, related to purchases of property, plant, and equipment.		

See notes to consolidated financial statements.

(Concluded)

INTERHEALTH CORP. AND AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012 (Dollars in thousands)

1. ORGANIZATION

InterHealth Corp. (“InterHealth”) is a nonprofit California corporation located in Whittier, California. InterHealth is the sole member (as the term “member” is defined in California Corporations Code, Section 5056) of the following nine other nonprofit corporations:

- Presbyterian Intercommunity Hospital, Inc. (PIH or the “Hospital”)
- PIH Foundation
- IHC Management Corp. (IHMC)
- Bright Health Physicians (BHP) (see Note 5)
- InterHealth Home Health Care
- Med Site — Hacienda Heights
- PIH Insurance Company (PIC), a reciprocal risk retention group
- PIH Community Pharmacy, LLC (the “Retail Pharmacy”)
- PIH Health Care Solutions (PHCS)

These entities are collectively referred to as the “Company.” The accompanying consolidated financial statements include the accounts of these member corporations and affiliates. All intercompany transactions have been eliminated in consolidation.

On December 11, 2008, PIC applied for and received approval to operate as a captive insurance company within the state of Hawaii. Effective January 1, 2009, this entity began to underwrite the Company’s medical malpractice self-insurance program.

On December 3, 2008, the Company formed the Retail Pharmacy under the laws of the State of California. PIH is the sole member of the limited liability company whose business is to operate as a retail pharmacy. The Retail Pharmacy opened on February 1, 2010.

On November 20, 2012, PHCS was incorporated as a California nonprofit mutual benefit corporation. On July 31, 2013, PHCS filed an application to the California Department of Managed Health Care for a Knox-Keene license to provide and/or arrange for the provision of health care services to commercial enrollees. Currently, PHCS application is under review with the California Department of Managed Health Care.

The Company has an integrated delivery network that provides health care services to southeastern Los Angeles County and portions of the San Gabriel Valley and Orange County. The Hospital is a 548-bed regional hospital with a full range of health services. Additionally, the Company provides transitional care services, home health, and hospice services.

2. SUMMARY OF SIGNIFICANT ACCOUNTING AND REPORTING POLICIES

Basis of Accounting — The consolidated financial statements are prepared on the accrual basis of accounting.

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

Cash and Cash Equivalents — Cash and cash equivalents are short-term, highly liquid investments with maturities of three months or less at the time of purchase. Cash and cash equivalents exclude amounts whose use is limited by Board of Directors' (the "Board") designation, other arrangements under trust agreements, and certain overnight short-term investments that participate in a reinvestment program.

Patient Accounts Receivable — The Company has agreements with third-party payors that provide for payments at established rates. Patient accounts receivable and net patient service revenue are reported at the net realizable amounts from patients, third-party payors, and others for services rendered.

The Company provides care to patients even though they may lack adequate insurance or may participate in programs with negotiated or regulated amounts. The Company manages its collection risk by regularly reviewing its accounts and contracts, and by providing appropriate allowances.

Pledges Receivable — As of September 30, 2013 and 2012, pledges receivable expected to be realized in one year or less are \$44 and \$128, respectively, and are included in prepaid expenses and other assets, and between one and five years are \$155 for 2013 and 2012 (net of \$40 discount for 2013 and 2012), and are included in other assets in the accompanying consolidated balance sheets.

Investments — Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value and are classified as held-to-maturity securities. Investment income or loss, net of expenses, is included in other gains and losses, unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments, if any, are excluded from excess of revenues over expenses and other gains (losses).

Management assesses its intent to sell for all debt and equity investments. If such intent exists, and an unrealized loss is present, securities are considered other-than-temporarily impaired. Management also assesses if the Company may be required to sell the debt investments prior to the recovery of amortized cost, which may also trigger such a charge. If securities are considered other-than-temporarily impaired based on intent or ability, management assesses if the amortized costs of the securities can be recovered. If management anticipates recovery of an amount less than the security's amortized cost, an impairment charge is calculated based on the expected discounted cash flows of the securities. Any deficit between the amortized cost and the expected cash flows is recorded through realized losses. No impairment amount was recognized during the years ended September 30, 2013 and 2012.

Investment securities, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially differ from the amounts in the accompanying consolidated balance sheets.

Assets Limited as to Use — Investments classified as assets limited as to use are stated at fair value. Assets limited as to use include primarily (a) assets set aside by the Board for future capital improvements over which the Board retains control and may, at its discretion, subsequently use for other purposes and (b) investments held by trustees under indenture agreements.

Fair Value Measurements — The Company measures and reports the fair value of its investments and certain liabilities in accordance with Accounting Standards Codification (ASC) 820, *Fair Value Measurements and Disclosures*. The Company records and classifies the investments and liabilities based on the level of judgment associated with the inputs used to measure their fair value and the level of market price observability. The Company also estimates fair value when the volume and level of activity for the assets have significantly decreased or in those circumstances that indicate when a transaction is not orderly.

Investments and liabilities measured and reported at fair value using level inputs are classified and disclosed in one of the following categories:

Level 1 — Quoted prices are available in active markets for identical investments as of the reporting date. The types of investments included in Level 1 include listed equities and publicly traded mutual funds whose value is determined based on quoted market prices for such investments. As required by ASC 820, the Company does not adjust the quoted price for these investments, even in situations where it holds a large position and a sale could reasonably affect the quoted price.

Level 2 — Pricing inputs are other-than-quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies, which are based on an income approach. Specific pricing inputs include quoted prices for similar securities in both active and nonactive markets and other observable inputs, such as interest rates, yield curve volatilities, default rates, and inputs that are derived principally from or corroborated by other observable market data. Investments that are generally included in this category include U.S. Treasury securities, asset-backed securities, corporate bonds, municipal bonds, and interest rate swaps.

Level 3 — Pricing inputs are unobservable for the investment and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment or estimation. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. Management'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 investment. The Company did not hold any Level 3 investments as of September 30, 2013 or 2012.

Inventory — Inventory is stated at the lower of cost or market, determined using the weighted-average cost method on a first-in, first-out basis.

Property, Plant, and Equipment — Property, plant, and equipment are recorded at cost. Depreciation on property, plant, and equipment is computed using the straight-line method over the estimated useful life of each class of depreciable assets. Leasehold improvements are amortized on a straight-line basis over the shorter of the useful lives of the improvements or the term of the related lease. 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. The Company capitalized interest in the amount of \$1,444 and \$3,406 for the years ended September 30, 2013 and 2012, respectively.

Estimated useful lives by asset type are generally as follows:

Land improvements	15–20 years
Buildings and improvements	15–40 years
Equipment — fixed and major movable	5–15 years
Leasehold improvements	5–20 years
Information technology equipment and software	3–10 years

When property is sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting net gain or loss is included in the excess of revenues over expenses and other gains (losses) in the accompanying consolidated statements of operations. The costs of normal maintenance and repairs and minor replacements are charged to expense when incurred.

Asset Retirement Obligations — The Company recognizes the fair value of a liability for legal obligations associated with asset retirements in the period in which it is incurred. When the liability is initially recorded, the Company capitalizes the cost of the asset retirement obligation by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost associated with the retirement obligation is depreciated over the useful life of the related asset. Upon settlement of the obligation, any differences between the cost to settle the asset retirement obligation and the liability recorded is recognized as a gain or loss in the consolidated statements of operations.

Asset Impairment — The Company routinely evaluates the carrying value of its long-lived assets for impairment and assessment of useful lives. The Company performs an annual impairment test on its recorded goodwill as of September 30, or more frequently if there are changes in events or circumstances that indicate that the Company may not recover the carrying value of its assets. The evaluations address the estimated recoverability of the assets' carrying value, which is principally determined based on projected undiscounted net cash flows generated by the underlying tangible assets for long-lived assets other than goodwill. In evaluating goodwill for impairment, management performs a two-step process. The first step requires the Company to compare the fair value of its reporting unit to the respective carrying value, which includes goodwill. If the fair value of the reporting unit exceeds its carrying value, the goodwill is not considered impaired. If the carrying value is greater than the fair value, there is an indication that an impairment may exist and the second step is required. In step two, the implied fair value of the goodwill is calculated as the excess of the fair value of its reporting unit over the fair values assigned to its assets and liabilities. If the implied fair value of goodwill is less than the carrying value of the reporting unit's goodwill, the difference is recognized as an impairment loss. The impairment test process requires valuation of the Company's reporting unit, which it estimates using a blended analysis of the present value of future discounted cash flows and the market approach of valuation. The process of evaluating the potential impairment of goodwill is subjective because it requires the use of estimates and assumptions. The discounted cash flow method requires the Company to use estimates and judgments about the future cash flows. Although the cash flow forecasts are based on assumptions that are consistent with plans and estimates to manage the underlying operations, there is significant judgment in determining the cash flows. The market approach is based on a comparison of the Company to comparable companies in similar lines of business. The estimates and judgments used to determine comparable companies include such factors as size, growth, profitability, risk, and return on investment.

No asset impairment charges were recorded and no change in useful life was determined in 2013 or 2012.

Deferred Financing Costs — Deferred financing costs consist primarily of costs incurred in connection with the issuance of the 2012, 2011, and 2009 revenue bonds, which are amortized based on the interest method over the life of the bonds.

Interest Rate Swap — The Company accounts for derivative instruments in the consolidated balance sheets as either assets or liabilities measured at estimated fair value and recognizes any unrealized gains or losses in the consolidated statements of operations. In certain defined conditions, a derivative may be specifically designated as a hedge for a particular exposure. The accounting for derivatives depends on the intended use of the derivatives and the resulting designation. Management has not designated the interest rate swaps as hedges in accordance with ASC 815, *Derivatives and Hedging*.

The Company uses derivative financial instruments to manage its exposure to interest rate risk and to balance its variable rate long-term debt portfolio. Credit risk related to derivative financial instruments is considered minimal and is managed by requiring high credit standards for its counterparties.

Net Patient Service Revenue — The Company has agreements with third-party payors that provide for payments to the Company at amounts different from established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per-diem payments. Net patient service revenue is recognized in the period the related services are rendered and is reported at the estimated net realizable amounts due from patients, third-party payors, and others, including estimated retroactive adjustments under reimbursement agreements with third-party payors. These 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.

Capitation Revenue — The Company has agreements with various health maintenance organizations (HMO) to provide medical services to subscribing participants. Under these arrangements, the Company receives monthly capitation payments based on the number of each HMO's participants assigned to the Company, regardless of services performed by the Company. In addition, the HMOs make fee-for-service payments to the Company for certain covered services based upon discounted fee schedules, per-diem rates, and case rates.

Charity Care — The Company provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. The Company maintains records to identify and monitor the level of charity care it provides. Because the Company does not pursue collection of amounts determined to qualify as charity care, these charges are not reported as revenue. The estimated costs of providing charity services are based on a calculation, which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of costs to charges is calculated based on the Hospital's total expenses divided by gross patient service revenue. The cost of these benefits and services was approximately \$10,602 and \$10,615 for the fiscal years ended September 30, 2013 and 2012, respectively. The costs were partially offset by the payments in the amount of \$4,551 and \$3,984 for the fiscal years ended September 30, 2013 and 2012, respectively.

Contributed Services — Volunteers have donated significant amounts of time and services to the Hospital's operations. Contributed services are recognized if the services received, which create or enhance long-lived assets or require specialized skills, would have typically been purchased if not provided by donation. None of the services donated met these criteria, and accordingly, no volunteer time has been reflected in the accompanying consolidated financial statements.

Excess of Revenues over Expenses and Other Gains (Losses) — The consolidated statements of operations include the excess of revenues over expenses and other gains (losses). Changes in

unrestricted net assets, which are excluded from this total, include the change in unrealized gains (losses), contributions of long-lived assets (including assets acquired using contributions that by donor restriction were to be used for the purposes of acquiring such assets), pension-related changes other than net period pension costs, and other losses.

Donor-Restricted Gifts — Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received or when the conditions expire, whichever occurs first. The gifts are reported as either temporarily or permanently restricted support 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 to unrestricted net assets and reported in the consolidated statements of operations as net assets released from restrictions.

Temporarily and Permanently Restricted Net Assets — Temporarily restricted net assets are those whose use by the Company has been limited by donors to a specific time period or purpose. Permanently restricted net assets are those with donor-imposed restrictions that are to be maintained by the Company in perpetuity.

Pension Plan — The Company applies the provisions of ASC 715, *Compensation-Retirement Benefits*, which requires a not-for-profit organization to recognize the overfunded or underfunded status of a defined benefit postretirement plan (measured as the difference between the fair value of plan assets and the projected benefit obligation as of the date of the fiscal year end) as an asset or liability in its balance sheet and to recognize changes in that funded status in the year in which the changes occur through changes in unrestricted net assets.

Income Taxes — The Company measures liabilities for unrecognized tax uncertainties in accordance with ASC 740, *Income Taxes*, which prescribes a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that a company has taken or expects to take on a tax return. The Company has not recorded a liability for unrecognized tax uncertainties in 2013 or 2012.

Recent Accounting Pronouncements — In September 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2011-08, *Intangibles — Goodwill and Other (Topic 350): Testing Goodwill for Impairment*, which permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. ASU No. 2011-08 was effective for the fiscal year ended September 30, 2012. The adoption of ASU No. 2011-08 did not have a material effect on the Company's operating results or financial position.

In May 2011, the FASB issued ASU No. 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS*, which amends ASC 820. ASU No. 2011-04 also requires the categorization by level for items that are only required to be disclosed at fair value and information about transfers between Level 1 and Level 2. In addition, ASU No. 2011-04 provides guidance on measuring the fair value of financial instruments managed within a portfolio and the application of premiums and discounts on fair value measurements. ASU No. 2011-04 requires additional disclosure for Level 3 measurements regarding the sensitivity of fair value to changes in unobservable inputs and any interrelationships between those inputs. The new guidance is effective for the Company for the fiscal year ended September 30, 2013. The adoption of ASU No. 2011-04 did not have a material impact on the Company's consolidated financial statements.

In July 2011, the FASB issued ASU No. 2011-07, *Health Care Entities (Topic 954): Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*, which provides guidance on presentation and disclosure of patient service revenue and the related provision for bad debts and allowance for doubtful accounts. ASU No. 2011-07 requires an entity to present its provision for bad debts as a reduction of patient service revenue on a separate line item in its consolidated statements of operations, disclose its policy for assessing the timing and amount of uncollectible patient service revenue recognized as bad debts by major payor source, and provide qualitative and quantitative information about significant changes in the allowance for doubtful accounts. The Company adopted ASU No. 2011-07 retrospectively for all periods presented.

In October 2012, the FASB issued ASU 2012-05, *Statement of Cash Flows (Topic 230): Not-for-Profit Entities: Classification on the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows*. This guidance provides clarification on how entities classify cash receipts arising from the sale of certain donated financial assets in the statement of cash flows. This guidance is effective for the Company beginning October 1, 2013, with early adoption permitted. The Company does not expect this guidance to have a material impact on its consolidated statement of cash flows.

In January 2013, the FASB issued ASU No. 2013-01, *Clarifying the Scope of Disclosures About Offsetting Assets and Liabilities*. The objective of this update is to clarify that the scope of ASU No. 2011-11, *Disclosures about Offsetting Assets and Liabilities*, would apply to derivatives, including bifurcated embedded derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with Section 210-20-45 or Section 815-10-45 or are subject to a master netting arrangement or similar agreement. The Company is required to adopt ASU No. 2013-01 for the fiscal year ending September 30, 2014. The Company does not expect the adoption of ASU No. 2013-01 to have a material effect on its operating results or financial position.

In April 2013, the FASB issued ASU 2013-06, *Services Received From Personnel of an Affiliate (Topic 958): Not-for-Profit Entities*. This provides guidance on recognizing all services received from personnel of an affiliate that directly benefit the recipient Not-for-Profit and for which the affiliate does not charge the recipient Not-for-Profit. Those services should be measured at the cost recognized by the affiliate for the personnel providing those services. However, if measuring a service received from personnel of an affiliate at cost will significantly overstate or understate the value of that service, the recipient Not-for-Profit may elect to recognize that service at its fair value. This guidance is effective for the Company beginning October 1, 2015, with early adoption permitted. The Company does not expect this guidance to have a material impact on its consolidated financial statements.

3. NET PATIENT SERVICE REVENUE

The Company recognizes patient service revenue on the basis of contractual rates for the services rendered for those patients who have third-party coverage. For the uninsured patients who do not qualify for charity care, the Company recognizes revenue on the basis of its standard rates (or on the basis of discounted rates, if negotiated or provided by policy). Patients covered by insurance, but required to pay deductibles or co-payments, are considered to be uninsured for those portions. Based on historical experience, the Company believes that a significant portion of its patient accounts will be uncollectible. Thus, it records a significant provision for bad debts related to patient accounts in the period the services are provided.

The Company's allowance for doubtful accounts was \$8,487 as of September 30, 2013, compared to \$9,367 as of September 30, 2012, or 11.5% and 12.8% of patient accounts receivable as of September 30, 2013 and 2012, respectively. The Company has not changed its charity care or uninsured discount policies during the fiscal year ended September 30, 2013 or 2012.

The Company has agreements with third-party payors that provide for payments to the Company at amounts different from its established rates. The Company accrues for amounts that it believes may ultimately be due from Medicare and other third-party payors and reports such amounts in the accompanying consolidated financial statements. A summary of the payment arrangements with major third-party payors is as follows:

Medicare — Inpatient acute care 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. Certain outpatient services provided to Medicare beneficiaries are paid based on prospectively determined rates for covered outpatient hospital services using ambulatory payment classification groups (APCs). APCs compose a system covering outpatient services consisting of groups arranged so that services within each group are comparable clinically and with respect to the use of resources. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through September 30, 2010.

Medi-Cal — Inpatient services rendered to Medi-Cal program beneficiaries are paid at negotiated per-diem rates. The per-diem rates are not subject to retrospective adjustment. Outpatient services are paid based on prospectively determined rates per procedure provided. Beginning on July 1, 2013, the California Medi-Cal program transitioned away from negotiated, per diem contracts to a fee schedule based on the patient's final, determined diagnosis (known as diagnosis-related groupings or APR-DRGs). Under APR-DRGs, reimbursement is scaled to patient acuity and complexity.

Capitation Revenue — BHP also contracts with various HMOs to provide health care services to HMO enrollees. Under the various contracts, BHP receives monthly capitation payments based on the number of enrollees, regardless of physician services actually performed by BHP. Capitation payments are recognized as revenue based on the period the Company is obligated to provide services. As of September 30, 2013 and 2012, estimated liabilities of \$5,756 and \$5,547, respectively, for services provided to enrollees by providers other than the Company are included in accounts payable and accrued expenses in the accompanying consolidated financial statements.

Other — The Company has also entered into payment agreements with certain commercial insurance carriers, HMOs, and preferred provider organizations. The basis for payment under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates. In January 2012, the Company received a \$13 million one-time bonus payment pursuant to an agreement with one of its insurance carriers. This amount was included in Other operating revenue.

Patient service revenues, net of contractual and other allowances (but before the provision for bad debts), recognized during the years ended September 30, 2013 and 2012, are as follows:

	2013	2012
Medicare	\$ 83,526	\$ 81,164
Medi-Cal	69,670	65,529
HMO	207,187	188,815
PPO	135,392	118,102
Other third party and self-payors	<u>42,613</u>	<u>37,762</u>
Total	<u>\$ 538,388</u>	<u>\$ 491,372</u>

A summary of net patient service revenue before provision for bad debts for the years ended September 30, 2013 and 2012, is as follows:

	2013	2012
Gross charges:		
Inpatient	\$ 1,677,098	\$ 1,448,915
Outpatient and other	<u>1,400,872</u>	<u>1,270,908</u>
Gross patient service revenue	3,077,970	2,719,823
Less:		
Contractual and other allowances	(2,524,960)	(2,215,793)
Charity care	<u>(14,622)</u>	<u>(12,658)</u>
Net patient service revenue before provision for bad debts	<u>\$ 538,388</u>	<u>\$ 491,372</u>

4. INVESTMENTS AND ASSETS LIMITED AS TO USE

Investments — Short-term investments are stated at fair value and amounted to \$2,366 and \$15,616 as of September 30, 2013 and 2012, respectively. Such investments are composed of U.S. Treasury bills, debt securities, and commercial paper.

Investments in Mutual Funds and Other Investments — The Company has nonqualified deferred compensation plans that provide for deferred compensation at various minimum levels, based on employment status. The plans are available to certain physician, supervisory, and executive personnel. The Company has invested the deferred amounts in mutual funds and other investments that are stated at fair value. Such amounts, while segregated in the accompanying consolidated financial statements, are available to satisfy the Company's obligations to the general creditors, if necessary. Additionally, the Company has a flexible benefit plan that provides for life insurance coverage for certain executive personnel. Investments in mutual funds and other investments were \$34,609 and \$26,606, of which \$4,534 and \$4,043 were related to the flexible benefit plan for executives, as of September 30, 2013 and 2012, respectively.

Assets Limited as to Use — The composition of assets limited as to use at fair value as of September 30, 2013 and 2012, is as follows:

	2013	2012
Cash and cash equivalents	\$ 10,543	\$ 50,305
Fixed-income securities	62,802	61,959
Equity securities	67,490	43,685
Mutual funds	210,775	209,067
Real estate equity investments	<u>12,539</u>	<u>11,410</u>
Investments — assets limited as to use	<u>\$ 364,149</u>	<u>\$ 376,426</u>

Assets limited as to use at fair value as of September 30, 2013 and 2012, consist of amounts designated as follows:

	2013	2012
Board designated for building and equipment	\$ 358,346	\$ 331,575
Held by trustee under bond indenture (Note 7):		
Bond Reserve Fund	5,803	5,801
Swap Cash Collateral	<u> </u>	<u>39,050</u>
Investments — assets limited as to use	<u>\$ 364,149</u>	<u>\$ 376,426</u>

The unrealized losses and fair value of the Company's investments with unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of September 30, 2013 and 2012, are as follows:

	Unrealized Losses				Total	
	Less than 12 Months		12 Months or Greater			
	Market Value	Unrealized Losses	Market Value	Unrealized Losses	Market Value	Unrealized Losses
September 30, 2013						
Equity investments (includes mutual funds)	\$ 24,006	\$ (1,012)	\$ 9,145	\$ (1,861)	\$ 33,151	\$ (2,873)
Fixed income	<u>41,479</u>	<u>(1,339)</u>	<u>4,573</u>	<u>(220)</u>	<u>46,052</u>	<u>(1,559)</u>
Total	<u>\$ 65,485</u>	<u>\$ (2,351)</u>	<u>\$ 13,718</u>	<u>\$ (2,081)</u>	<u>\$ 79,203</u>	<u>\$ (4,432)</u>
	Unrealized Losses				Total	
	Less than 12 Months		12 Months or Greater			
	Market Value	Unrealized Losses	Market Value	Unrealized Losses	Market Value	Unrealized Losses
September 30, 2012						
Equity investments (includes mutual funds)	\$ 4,010	\$ (505)	\$ 25,044	\$ (1,271)	\$ 29,054	\$ (1,776)
Fixed income	<u>10,157</u>	<u>(113)</u>	<u>1,241</u>	<u>(57)</u>	<u>11,398</u>	<u>(170)</u>
Total	<u>\$ 14,167</u>	<u>\$ (618)</u>	<u>\$ 26,285</u>	<u>\$ (1,328)</u>	<u>\$ 40,452</u>	<u>\$ (1,946)</u>

The unrealized losses on the Company's investments in debt and equity securities were caused by interest rate increases and current market volatility. The Company has the ability and intent to hold these debt and equity securities until a recovery of fair value (which may be maturity).

Fair Value Measurements — The information about the Company's assets and liabilities measured at fair value on a recurring basis and the fair value hierarchy of the valuation techniques utilized by management to determine such fair values as of September 30, 2013 and 2012, are as follows:

As of September 30, 2013	Level 1	Level 2	Total
Assets			
Investments — short term:			
Cash and cash equivalents	\$ 285	\$ -	\$ 285
Fixed-income securities:			
U.S. government and agency		1,303	1,303
Corporate debt instruments		552	552
Mortgages and asset backed		75	75
State and municipal		151	151
Total investments — short term	<u>\$ 285</u>	<u>\$ 2,081</u>	<u>\$ 2,366</u>
Investments in mutual funds and other investments:			
Cash and cash equivalents	<u>\$ 48</u>	<u>\$ -</u>	<u>\$ 48</u>
Fixed-income securities:			
U.S. government and agency		3,579	3,579
Corporate debt instruments		3,566	3,566
Mortgages and asset backed		968	968
State and municipal		70	70
Total fixed-income securities	<u>-</u>	<u>8,183</u>	<u>8,183</u>
Mutual funds:			
Balanced funds	235		235
Bond funds	1,262		1,262
Equity funds	13,196		13,196
Total mutual funds	<u>14,693</u>	<u>-</u>	<u>14,693</u>
Investments in fixed-income annuity and cash surrender value		11,685	11,685
Total investments in mutual funds and other investments	<u>\$ 14,741</u>	<u>\$ 19,868</u>	<u>\$ 34,609</u>
Investments — assets limited as to use:			
Cash and cash equivalents	<u>\$ 10,543</u>	<u>\$ -</u>	<u>\$ 10,543</u>
Fixed-income securities:			
U.S. government and agency		19,455	19,455
Corporate debt instruments		22,904	22,904
Mortgages and asset backed		15,783	15,783
State and municipal		4,660	4,660
Total fixed-income securities	<u>-</u>	<u>62,802</u>	<u>62,802</u>
Equity securities:			
Consumer discretionary	12,159		12,159
Consumer staples	6,482		6,482
Energy	2,699		2,699
Financials	13,355		13,355
Health care	4,393		4,393
Industrials	8,383		8,383
Information technology	12,245		12,245
Materials	5,114		5,114
Telecommunication services	2,056		2,056
Utilities	604		604
Total equity securities	<u>67,490</u>	<u>-</u>	<u>67,490</u>
Mutual funds:			
Balanced funds	53,499		53,499
Bond funds	64,034		64,034
Equity funds	73,195	20,047	93,242
Total mutual funds	<u>190,728</u>	<u>20,047</u>	<u>210,775</u>
Real estate equity investment — limited partnership		12,539	12,539
Total investments — assets limited as to use	<u>\$ 268,761</u>	<u>\$ 95,388</u>	<u>\$ 364,149</u>
Liabilities			
Interest rate swap liability	<u>\$ -</u>	<u>\$ 35,919</u>	<u>\$ 35,919</u>

As of September 30, 2012	Level 1	Level 2	Total
Assets			
Investments — short term:			
Cash and cash equivalents	\$ 14,181	\$ -	\$ 14,181
Fixed-income securities:			
U.S. government and agency		890	890
Corporate debt instruments		417	417
State and municipal		128	128
Total investments — short term	<u>\$ 14,181</u>	<u>\$ 1,435</u>	<u>\$ 15,616</u>
Investments in mutual funds and other investments:			
Fixed-income securities:			
U.S. government and agency	\$ -	\$ 4,048	\$ 4,048
Corporate debt instruments		2,049	2,049
Mortgages and asset backed		694	694
State and municipal		225	225
Total fixed-income securities	<u>-</u>	<u>7,016</u>	<u>7,016</u>
Mutual funds:			
Balanced funds	24		24
Bond funds	188		188
Equity funds	7,965		7,965
Total mutual funds	<u>8,177</u>	<u>-</u>	<u>8,177</u>
Investments in fixed-income annuity and cash surrender value		11,413	11,413
Total investments in mutual funds and other investments	<u>\$ 8,177</u>	<u>\$18,429</u>	<u>\$ 26,606</u>
Investments — assets limited as to use:			
Cash and cash equivalents	<u>\$ 50,305</u>	<u>\$ -</u>	<u>\$ 50,305</u>
Fixed-income securities:			
U.S. government and agency		18,279	18,279
Corporate debt instruments		18,192	18,192
Mortgages and asset backed		20,268	20,268
State and municipal		5,220	5,220
Total fixed-income securities	<u>-</u>	<u>1,959</u>	<u>61,959</u>
Equity securities:			
Consumer discretionary	7,293		7,293
Consumer staples	1,869		1,869
Energy	5,748		5,748
Financials	8,064		8,064
Health care	5,281		5,281
Industrials	3,397		3,397
Information technology	9,552		9,552
Materials	2,108		2,108
Real estate	373		373
Total equity securities	<u>43,685</u>	<u>-</u>	<u>43,685</u>
Mutual funds:			
Balanced funds	42,779		42,779
Bond funds	65,218		65,218
Equity funds	83,872	17,198	101,070
Total mutual funds	<u>191,869</u>	<u>17,198</u>	<u>209,067</u>
Real estate equity investment — limited partnership		11,410	11,410
Total investments — assets limited as to use	<u>\$285,859</u>	<u>\$90,567</u>	<u>\$376,426</u>
Liabilities			
Interest rate swap liability	<u>\$ -</u>	<u>\$53,054</u>	<u>\$ 53,054</u>

A summary of the fair value measurements of investment in assets limited as to use that calculate net asset value (NAV) per share (or its equivalent) is as follows:

	As of September 30	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Commingled funds (a)	2013	\$ 20,047	\$ -	Daily	1 day
Commingled funds (b)	2013	12,539		Monthly	30 days
Commingled funds (a)	2012	17,198		Daily	1 day
Commingled funds (b)	2012	11,410		Monthly	30 days

(a) This category includes investments in a pooled vehicle that invest in equity securities of large capitalization companies. The fair value of this investment has been estimated using the NAV per share of the fund.

(b) This category includes investments in a pooled fund that invests in publicly-traded real estate securities (REITS). The fair value of this investment has been estimated using the NAV per share of the fund.

The Company's policy is to classify investments with quoted prices from active markets for identical assets as Level 1. During the year ended September 30, 2013, management identified \$20,102 of U.S. government securities in the Company's investment portfolios as of September 30, 2012, that trade over the counter which had previously been classified as Level 1 and should have been classified as Level 2. Accordingly, the amount has been reclassified from Level 1 to Level 2 to correct the error.

There were no significant transfers between Level 1 and Level 2 during the year ended September 30, 2013, and there were no Level 3 securities held by the Company during the years ended September 30, 2013 or 2012.

Investment Income (Expenses) and Gains (Losses) — Income, expenses, gains, and losses related to investments for the years ended September 30, 2013 and 2012, are composed of the following:

	2013	2012
Net investment income — interest income	\$ 9,963	\$ 9,875
Realized gains on investments	13,722	1,836
Change in fair value of interest rate swap and interest expense	10,477	(9,877)
Change in unrealized gains on investments	<u>4,011</u>	<u>32,999</u>
Total	<u>\$ 38,173</u>	<u>\$ 34,833</u>

5. ACQUISITIONS

Transactions with Downey Regional Medical Center — On June 14, 2013, the Company and Downey Regional Medical Center (DRMC), a nonprofit California corporation located in Downey, CA, entered into a Management Services Agreement (MSA) for the Company to provide management, administrative, and support services in the day-to-day operations of DRMC for a period of up to two years, with options to extend for up to two one-year terms. The fees for these services are based on a sliding scale as outlined in the MSA. Throughout the course of the MSA, the Board of DRMC controls DRMC and all significant decisions must be approved by the Board of DRMC.

Additionally, on June 14, 2013, the Company and DRMC entered into a Hospital Operations Assistance Loan Agreement (the “Assistance Loan”) whereby the Company agreed to lend up to \$10,000 to provide working capital and other financial assistance for DRMC’s hospital operations. Interest on the Assistance Loan is calculated at a rate equal to the *Wall Street Journal* Prime Rate plus two percent per annum on the unpaid balance accruing from the date each payment is made by DRMC until paid in full, with a maturity date of June 12, 2015. Subsequent to the origination of the Assistance Loan, the Company increased the loan amount and provided total proceeds of \$23,636 to DRMC as of September 30, 2013. These amounts are shown as Other Assets — Downey in the accompanying consolidated balance sheets.

The Company did not record or accrue any management fees or interest receivable on these agreements for the year ended September 30, 2013, as the collectability of these amounts was not assured. See Note 17 for subsequent events related to DRMC.

Acquisitions — Effective February 1, 2008, the Company, through its wholly owned affiliate Presbyterian Health Physicians (now known as BHP), acquired most of the assets of Bright Medical Associates, Inc., a California professional corporation; Bright Administrative Services LP, a California limited partnership; and Integrated Medical Management, Inc., a California corporation (collectively, BMA). BMA is a multispecialty medical group which provides medical services under managed care contracts with licensed health care service plans. Goodwill of \$11,576 was recorded in conjunction with the acquisition and was being amortized over 20 years; however, in accordance with ASU No. 2010-07, the amortization of goodwill was discontinued effective October 1, 2010.

In May 2012, BHP purchased the assets of Digestive Health Services, a California medical general partnership, and Colon Cancer Prevention Alliance, a California corporation. Goodwill of \$797 and certain property and equipment were recorded in conjunction with the acquisition.

The Company routinely evaluates the carrying value of its long-lived assets and goodwill for impairment and assessment of useful lives. The evaluations address the estimated recoverability of the assets’ carrying value, which is principally determined based on projected undiscounted net cash flows generated by the underlying tangible assets at the consolidated level. No asset impairment charges were recorded in 2013 or 2012.

6. PROPERTY, PLANT, AND EQUIPMENT

Property, plant, and equipment as of September 30, 2013 and 2012, comprise the following:

	2013	2012
Buildings and equipment	\$ 550,280	\$ 325,233
Land and land improvements	37,984	33,168
Leasehold improvements	89,191	83,157
Construction in progress	<u>21,689</u>	<u>181,983</u>
Total property, plant, and equipment	699,144	623,541
Less accumulated depreciation	<u>(185,155)</u>	<u>(160,435)</u>
Property, plant, and equipment — net	<u>\$ 513,989</u>	<u>\$ 463,106</u>

During the year ended September 30, 2013, the Company wrote off property, plant, and equipment totaling \$2,952 in gross carrying value and \$2,791 in related accumulated depreciation resulting in a \$155 loss on disposal of equipment, which is net of \$6 in proceeds.

During the year ended September 30, 2012, the Company wrote off property, plant, and equipment totaling \$8,688 in gross carrying value and \$8,622 in related accumulated depreciation resulting in a \$58 loss on disposal of equipment, which is net of \$8 in proceeds. In addition, the Company recognized a loss on disposal of buildings of \$404 due to the demolition of improvements at one of its properties.

Construction in progress consists primarily of the Company's Plaza Tower project, which is estimated to require additional costs to complete of \$9,124 as of September 30, 2013, in which funds are expected to come from the Company's existing working capital, cash flow from operations, and liquidation of investments.

Depreciation and amortization expense for the years ended September 30, 2013 and 2012, amounted to \$27,482 and \$21,462, respectively.

7. DEBT

A summary of long-term debt as of September 30, 2013 and 2012, is as follows:

	2013	2012
Long-term debt:		
Health Facility Revenue Bonds — Series 2012	\$ 148,000	\$ -
Health Facility Revenue Bonds — Series 2011	40,200	40,750
Health Facility Revenue Bonds — Series 2009	105,080	260,255
Unamortized bond discount — Series 2011	(424)	(446)
Unamortized bond premium — Series 2009	89	133
Less current portion	<u>(7,940)</u>	<u>(7,725)</u>
Total long-term debt	<u>\$ 285,005</u>	<u>\$ 292,967</u>

Series 2012 Health Facility Revenue Bonds — On December 31, 2012, the Hospital, InterHealth, and IHMC (collectively, the "Obligated Group") replaced its Series 2009 B and Series 2009 C City of Whittier Health Facility Revenue Bonds (aggregate of \$148,000 principal amount) with private placement bonds with varying term periods. The Series 2012 City of Whittier Health Facility Bonds ("Series 2012 Bonds") consists of three series: Series 2012 A with a notional amount of \$48,000 with a five-year term, Series 2012 B with a notional amount of \$50,000 with a six-year term, and Series 2012 C with a notional amount of \$50,000 with a seven-year term. The Series 2012 Bonds are held by three large financial institutions and bear interest at approximately 65% to 68% of one-month London InterBank Offered Rate (LIBOR), plus 80 to 81 basis points.

Series 2011 Health Facility Revenue Bonds — On March 31, 2011, Obligated Group jointly issued \$41,305 aggregate principal amount of City of Whittier Health Facility Revenue fixed-rate bonds ("Series 2011 Bonds") at a discount of \$477. The proceeds of these bonds were used to finance certain facilities for the benefit of the Hospital and pay certain costs of issuance of the Series 2011 Bonds.

The Series 2011 Bonds bear fixed-interest rates ranging from 4% to 6.25% and have maturities beginning in 2012 and ending in 2036.

Series 2009 Health Facility Revenue Bonds — On May 14, 2009, the Obligated Group jointly issued \$222,000 aggregate principal amount of City of Whittier Health Facility Revenue variable rate bonds, Series 2009 A, Series 2009 B, and Series 2009 C bonds (the “Variable Rate Bonds”), at par. Concurrently, the Obligated Group jointly issued \$58,000 aggregate principal amount of City of Whittier Health Facility Revenue fixed-rate bonds, Series D (the “Fixed Rate Bonds”) at a premium of \$329. The Fixed Rate Bonds, together with the Variable Rate Bonds, are referred to as the “Series 2009 Bonds.” The proceeds of these bonds were used to (1) finance certain facilities for the benefit of the Hospital, (2) advance refund the Series 2007 City of Whittier Health Facility Revenue Bonds (“Series 2007 Bonds”), (3) fund a reserve fund for the Series 2009 D Bonds, and (4) pay certain costs of issuance of the Series 2009 Bonds. The Series 2007 Bonds were originally issued with a principal balance of \$292,000 at par on January 31, 2007.

The Variable Rate Bonds bear interest at a weekly interest rate determined by the remarketing agents. During the year ended September 30, 2013, the weekly interest rate ranged from 0.03% to 0.21% and its weighted average was 0.13%. During the year ended September 30, 2012, the weekly interest rate ranged from 0.02% to 0.25% and its weighted average was 0.11%. If certain conditions are met, the Company may elect to convert the weekly interest rate period to either a daily or a long-term period. The Variable Rate Bonds have sinking fund requirements beginning in 2017 and ending in 2036. The Fixed Rate Bonds bear fixed interest rates ranging from 4% to 5% and have maturities beginning in 2012 and ending in 2017.

The payment of principal and interest on the Variable Rate Bonds was secured by a \$225,065 standby letter of credit (“Letter of Credit Facility”) issued by a syndicated bank group. The interest rate on any draws against the Letter of Credit Facility was based on either the prime rate, federal funds rate, or one-month London InterBank Offered Rate (LIBOR) at the option of the Company. The Company paid an annual commitment fee of 0.85%, which was based on its current A+ Standard & Poor’s (S&P) rating.

Upon issuance of the Series 2012 Bonds, the Letter of Credit Facility was amended and the standby letter of credit amount was reduced to \$75,022 to reflect the redemption of the Series 2009 B and Series 2009 C bonds. Under the revised agreement, the Company must pay an annual commitment fee of 0.65%, which was based on its current A+ S&P rating. There were no draws against the Letter of Credit Facility in fiscal year 2013 and 2012.

Scheduled principal repayments on long-term debt as of September 30, 2013, are as follows:

Years Ending September 30	Principal Repayment
2014	\$ 7,940
2015	8,465
2016	8,870
2017	9,320
2018	9,830
Thereafter	<u>248,855</u>
Total principal repayments	<u>\$ 293,280</u>

Short-term loan borrowing — The Company also has a Line of Credit with one of its investment custodians, which is secured by the investment held. The Line of Credit total is based on the current market value of the eligible investments (amount is currently \$45,000). The interest rate on any draws against the Line of Credit is based on one-month LIBOR. In September 2013, the Company borrowed \$30,500 against the Line of Credit with an interest rate of 1.43%. The \$30,500 was repaid in October 2013.

Interest Rate Swaps — In connection with the issuance of the Series 2007 Bonds and in an effort to reduce its interest costs, the Hospital entered into three separate interest rate swap agreements having a total notional amount of \$222,000. Under the terms of the agreements, the Hospital agreed to pay to the counterparty a fixed rate of interest on the notional amount in exchange for receiving a payment from the counterparty based on a floating rate tied to the one-month LIBOR. The swap agreements effectively reduced or increased the Hospital's interest costs by swapping the variable interest rate on the Series 2007 Bonds to a fixed rate.

On March 11, 2009, the agreement with the counterparty was amended in advance of the issuance of the Series 2009 Bonds and in advance refunding of the Series 2007 Bonds. Under the amended agreement, the counterparty released its rights under a surety bond and, in exchange, the interest rates on the three swaps increased by 3.5 basis points and the Company was required to immediately post cash collateral. The amount of the collateral is based on (1) the daily valuation of the swaps, (2) the Company's S&P rating, and (3) the excess valuation over predetermined dollar thresholds. In 2009, the Company maintained an A+ S&P rating, which established a \$15,000 collateral threshold per swap. On December 31, 2012, the Company novated its swap program by adding another counterparty and the collateral threshold was raised from \$15,000 to \$30,000. As a result, the cash collateral was returned to the Company and there was no collateral balance as of September 30, 2013. The posted collateral balance as of September 30, 2012, was \$39,050. The interest rates paid on the Series 2009 A, Series 2009 B, and Series 2009 C swaps were 3.132%, 3.120%, and 3.202%, respectively, for the years ended September 30, 2013 and 2012.

The swap agreements terminate on the same date that the related bonds were scheduled to mature. As of September 30, 2013 and 2012, the swaps were recorded as a liability of \$35,919 and \$53,054, respectively. The change in value of the swaps totaling \$(17,135) and \$3,497 in the years ended September 30, 2013 and 2012, respectively, is recorded in the consolidated statements of operations as change in fair value of interest rate swaps, in addition to interest expense related to the swaps. As of September 30, 2013 and 2012, management has not designated the swaps as a hedge in accordance with ASC 815.

8. TEMPORARILY AND PERMANENTLY RESTRICTED NET ASSETS

Temporarily restricted net assets as of September 30, 2013 and 2012, are available for the following purposes or periods:

	2013	2012
Contributions received and restricted for patient care	\$ 2,548	\$ 2,854
Contributions restricted for construction projects	1,464	1,713
Contributions restricted for specific programs	<u>256</u>	<u>1,013</u>
Total temporarily restricted net assets	<u>\$ 4,268</u>	<u>\$ 5,580</u>

There were no time-restricted contributions during the fiscal years 2013 and 2012. Net assets released from restrictions in the accompanying consolidated statements of operations represent purpose-restricted contributions utilized for their restricted purpose during the years ended September 30, 2013 and 2012, and are summarized as follows:

	2013	2012
Program	\$ 866	\$ 954
Capital	<u>1,993</u>	<u>46</u>
Total assets released from temporarily restricted net assets	<u>\$2,859</u>	<u>\$1,000</u>

Permanently restricted net assets as of September 30, 2013 and 2012, in the amount of \$971 are held in perpetuity, the income from which is expended to support the Company's resident Chaplain office.

9. PENSION PLAN

The Company has a defined benefit pension plan (the "Plan") covering substantially all employees. It is subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA). Under the terms of the Plan, participants are eligible for monthly benefit payments upon reaching age 65, as defined in the Plan document. Vesting occurs after completion of five years of cumulative service. Participants are eligible for reduced benefits upon early retirement under certain circumstances. Monthly benefit payments are determined by application of a benefit formula to a participant's annual wages for all years of eligibility in the Plan before retirement. Under the terms of the Plan, participants are not required or permitted to make contributions to the Plan.

The Company's policy is to fund its pension cost in accordance with the provisions of ERISA. Contributions are intended to provide not only for benefits attributed to service to date, but also for those expected to be earned in the future.

Net periodic benefit cost for the years ended September 30, 2013 and 2012, includes the following components:

	2013	2012
Service cost	\$ 12,240	\$ 10,102
Interest cost	8,233	8,554
Expected return on Plan assets	(8,928)	(8,501)
Amortization of prior-service cost	(21)	
Recognized actuarial loss	<u>6,739</u>	<u>5,154</u>
Net periodic benefit cost	<u>\$ 18,263</u>	<u>\$ 15,309</u>

A summary of the components of net pension cost as of the date of the latest actuarial valuation as of September 30, 2013 and 2012, is as follows:

	2013	2012
Changes in benefit obligation:		
Benefit obligation — beginning of year	\$ 198,965	\$ 162,043
Service cost	12,240	10,102
Interest cost	8,233	8,554
Amendments		(201)
Benefits paid	(10,894)	(10,620)
Actuarial (gain) loss	<u>(32,764)</u>	<u>29,087</u>
Benefit obligation — end of year	<u>175,780</u>	<u>198,965</u>
Changes in Plan assets:		
Fair value of Plan assets — beginning of year	123,319	110,707
Actual return on Plan assets	8,081	13,712
Employer contributions	8,510	9,520
Benefits paid	<u>(10,894)</u>	<u>(10,620)</u>
Fair value of Plan assets — end of year	<u>129,016</u>	<u>123,319</u>
Funded status	<u>(46,764)</u>	<u>(75,646)</u>
Pension liability	<u>\$ (46,764)</u>	<u>\$ (75,646)</u>
Amounts recognized in the consolidated balance sheets consist of — pension liability	<u>\$ (46,764)</u>	<u>\$ (75,646)</u>
	2013	2012
Amounts recognized in the change in unrestricted net assets consist of:		
Prior-service cost	\$ 180	\$ 201
Net actuarial loss	<u>(45,906)</u>	<u>(84,563)</u>
Accumulated change from pension in unrestricted net assets	(45,726)	(84,362)
Cumulative employer contributions (less than) in excess of net periodic benefit cost	<u>(1,038)</u>	<u>8,716</u>
Obligation recognized	<u>\$ (46,764)</u>	<u>\$ (75,646)</u>

The amount expected to be recognized as a component of net periodic benefit cost over the next fiscal year includes the following:

Net loss	<u>\$ 2,979</u>
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The accumulated benefit obligation for the Plan was \$159,705 and \$179,754 as of September 30, 2013 and 2012, respectively.

Weighted-average assumptions used to determine benefit obligations as of September 30, 2013 and 2012, are as follows:

	2013	2012
Discount rate	5.30 %	4.35 %
Rate of compensation increase	3.00	3.00

Weighted-average assumptions used to determine net periodic benefit cost for the years ended September 30, 2013 and 2012, are as follows:

	2013	2012
Discount rate	4.35 %	5.35 %
Expected long-term rate of return on assets	7.50	7.50
Rate of compensation increase	3.00	4.00

To develop the expected long-term rate of return on assets assumption, the Company 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.

The primary asset classifications utilized to achieve both appreciation and diversification are domestic large-cap equity, domestic mid-cap equity, domestic small-cap equity, domestic medium-cap equity, international equity, domestic investment-grade fixed income, high-yield fixed income, and inflation-indexed fixed income. The investment policy reflects the expected allocation between these different asset classes in order to best achieve the objectives of the Plan. Investments are rebalanced, as appropriate, to maintain the desired asset allocation.

Asset allocations by asset category as of September 30, 2013 and 2012, are as follows:

Asset Category	2013	2012
Equity securities	44.2 %	35.3 %
Debt securities	43.5	52.6
Real estate	3.3	3.2
Other	<u>9.0</u>	<u>8.9</u>
Total	<u>100.0 %</u>	<u>100.0 %</u>

The investment policy has been established to provide a total investment return that will, over time, maintain purchasing power parity for the Plan's variable benefits and keep the Company's Plan funding at a reasonable level. The primary asset classes utilized to attain these objectives are equity securities, debt securities, real estate, and all other with target allocations of 44%, 42%, 4%, and 10%, respectively.

The fair value hierarchy of investments held by the Plan by level as of September 30, 2013 and 2012, is as follows:

As of September 30, 2013	Level 1	Level 2	Total
Cash and cash equivalents	<u>\$ 3,115</u>	<u>\$ -</u>	<u>\$ 3,115</u>
Fixed-income securities:			
U.S. government and agency		17,211	17,211
Corporate debt instruments		19,505	19,505
State and municipal		<u>3,433</u>	<u>3,433</u>
Total fixed-income securities	<u>-</u>	<u>40,149</u>	<u>40,149</u>
Common stock:			
Consumer discretionary	3,754		3,754
Consumer staples	1,732		1,732
Energy	988		988
Financials	4,033		4,033
Health care	1,678		1,678
Industrials	3,566		3,566
Information technology	4,704		4,704
Materials	1,742		1,742
Real estate	4,364		4,364
Telecommunications	219		219
Utilities	<u>228</u>		<u>228</u>
Total common stock	<u>27,008</u>	<u>-</u>	<u>27,008</u>
Mutual funds:			
Balanced funds	16,922		16,922
Bond funds	14,593		14,593
Equity funds	<u>27,229</u>		<u>27,229</u>
Total mutual funds	<u>58,744</u>	<u>-</u>	<u>58,744</u>
Total	<u>\$ 88,867</u>	<u>\$ 40,149</u>	<u>\$ 129,016</u>

As of September 30, 2012	Level 1	Level 2	Total
Cash and cash equivalents	<u>\$ 10,751</u>	<u>\$ -</u>	<u>\$ 10,751</u>
Fixed-income securities:			
U.S. government and agency		21,097	21,097
Corporate debt instruments		20,292	20,292
Foreign obligations		1,310	1,310
State and municipal		<u>3,524</u>	<u>3,524</u>
Total fixed-income securities	<u>-</u>	<u>46,223</u>	<u>46,223</u>
Common stock:			
Consumer discretionary	2,390		2,390
Consumer staples	733		733
Energy	2,159		2,159
Financials	3,137		3,137
Health care	1,832		1,832
Industrials	922		922
Information technology	3,639		3,639
Materials	913		913
Real estate	4,283		4,283
Utilities	<u>101</u>		<u>101</u>
Total common stock	<u>20,109</u>	<u>-</u>	<u>20,109</u>
Mutual funds:			
Balanced funds	14,173		14,173
Bond funds	8,374		8,374
Equity funds	<u>23,689</u>		<u>23,689</u>
Total mutual funds	<u>46,236</u>	<u>-</u>	<u>46,236</u>
Total	<u>\$ 77,096</u>	<u>\$ 46,223</u>	<u>\$ 123,319</u>

There were no significant transfers between Level 1 and Level 2 during the year ended September 30, 2013, and there were no Level 3 securities held by the Plan during the years ended September 30, 2013 or 2012.

The Plan's policy is to classify investments with quoted prices from active markets for identical assets as Level 1. During the year ended September 30, 2013, management identified \$10,634 of U.S. government securities in the Plan's portfolio as of September 30, 2012, that trade over the counter which had previously been classified as Level 1 and should have been classified as Level 2. Accordingly, the amount has been reclassified from Level 1 to Level 2 to correct the error. Plan management identified this discrepancy through the process of adopting ASU No. 2011-04.

The Company expects to contribute \$9,336 to the Plan for the fiscal year ending September 30, 2014. Benefit payments, which reflect expected future service, as appropriate, as of September 30, 2013, are expected to be paid as follows:

**Years Ending
September 30**

2014	\$ 10,019
2015	9,155
2016	9,792
2017	10,139
2018	11,009
2019–2023	<u>67,638</u>
Total	<u>\$ 117,752</u>

10. COMMITMENTS AND CONTINGENCIES

Insurance Programs — The Company partially insures or self-insures against malpractice and general liability claims, workers’ compensation claims, and certain employee group health and dental benefits. Under the malpractice and general liability program, effective January 1, 2009, the Company is self-insured for up to \$500 consolidated indemnity and expense per occurrence with maximum annual coverage of \$24,000 per occurrence annual aggregate. With regard to workers’ compensation claims, the Company has reinsurance coverage for individual claim expenses in excess of \$1,000 per occurrence with maximum annual coverage of \$50,000 per occurrence. Self-insurance reserves as of September 30, 2013 and 2012, are as follows: malpractice and general liability claims of \$9,556 and \$7,821, workers’ compensation claims of \$13,564 and \$14,481, employee health insurance claims of \$3,073 and \$3,209, and employee dental benefits claims of \$663 and \$569, respectively.

Revenue Recovery Audit — The Company is subject to audit through the use of Revenue Recovery Audit Contractors (RACs) under the Medicare Modernization Act of 2003. The resolution of the outstanding RAC audits is not expected to have a material adverse effect on the Company’s consolidated balance sheets, the results of its operations, or cash flows.

Litigation — From time to time, the Company is subject to claims arising in the ordinary course of business. In the opinion of management, the ultimate resolution to these legal proceedings will not have a material adverse effect on the consolidated balance sheets of the Company, the results of its operations, or cash flows.

Guarantees — In accordance with the requirements of California Health and Safety Code Section 1375.4(b)(1)(B), in December 2005, InterHealth and BHP signed a guaranty agreement (the “Guaranty”). Under the terms of the Guaranty, InterHealth has unconditionally guaranteed all liabilities of BHP not to exceed \$30,000. InterHealth made an equity transfer of \$30,000 to BHP in 2013.

In conjunction with the Bright Acquisition, BHP entered into a professional service agreement (“Service Agreement”), effective February 1, 2008, and as amended on November 1, 2008, and August 1, 2009, with a California professional corporation composed of individual physicians providing medical and health care services at the former BMA clinics. The Service Agreement includes a payment guarantee provision, whereby PIH guarantees all obligations to the California professional corporation on behalf of BHP not to exceed \$15,000. The Guaranty remains in effect for the life of the Service Agreement, which has an initial term of 10 years and remains in effect until BHP ceases to be a ‘risk bearing entity.’

Operating Leases — The Company leases certain buildings and equipment under noncancelable operating leases. Rent expense relating to operating leases was \$3,512 and \$2,612 for the years ended September 30, 2013 and 2012, respectively. Future minimum lease payments required under operating leases as of September 30, 2013, are summarized in the following table:

Years Ending September 30	
2014	\$ 1,763
2015	1,292
2016	1,038
2017	972
2018	978
Thereafter	<u>3,126</u>
	<u>\$ 9,169</u>

11. INCOME TAXES

InterHealth and its eight affiliates are nonprofit corporations as described in Section 501(c)(3) of the Internal Revenue Code (the “Code”) and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code and from state income taxes under similar provisions of the California Revenue and Taxation Code. Accordingly, no provision for income taxes has been recorded in the accompanying consolidated financial statements.

GAAP requires management to evaluate tax positions taken by the Company and recognize a tax liability (or asset) if the Company has taken an uncertain position that more likely than not would not be sustained upon examination by the Internal Revenue Service or State of California Franchise Tax Board. Management has analyzed the tax positions taken by the Company and has concluded that as of September 30, 2013, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the consolidated financial statements. The Company is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. The Company believes it is no longer subject to income tax examinations for years prior to 2010 for federal purposes and 2009 for California purposes.

12. CONCENTRATION OF CREDIT RISK

The Hospital and BHP grant credit without collateral to their patients, most of whom are local residents and are insured under third-party payor agreements. The mix of gross patient accounts receivable from patients and third-party payors as of September 30, 2013 and 2012, was as follows:

	2013	2012
Medicare	26 %	25 %
Medi-Cal	10	9
HMO	32	34
PPO	17	16
Other third party and self-payors	<u>15</u>	<u>16</u>
	<u>100 %</u>	<u>100 %</u>

13. FAIR VALUE OF FINANCIAL INSTRUMENTS

Due to the short-term nature of cash and cash equivalents and other financial instruments, such as receivables, payables and short-term loan borrowing, their fair value approximates their carrying value. The fair values of investments, assets limited as to use, and investments in mutual funds and other investments are based on quoted market prices, if available, or estimated using quoted market prices for similar securities on the last business day of the fiscal year.

The fair values of long-term debts are estimated based on the current rates offered for debts of similar issues and same remaining maturities (Level 2). As of September 30, 2013 and 2012, the fair value of the Series 2009 Bonds was \$105,080 and \$260,255, respectively. As of September 30, 2013 and 2012, the fair value of the Series 2011 Bonds was \$40,200 and \$40,750, respectively. As of September 30, 2013, the fair value of the Series 2012 Bonds was \$148,000.

14. FUNCTIONAL EXPENSES

The Company provides general health care services to residents within its geographical location. Expenses related to providing these services for the years ended September 30, 2013 and 2012, are as follows:

	2013	2012
Health care services	\$ 519,096	\$ 491,439
Management and general	77,426	59,847
Fund raising	993	847
	<u>\$ 597,515</u>	<u>\$ 552,133</u>

15. HOSPITAL FEE PROGRAM

In January 2010, the State of California enacted legislation that provides for supplemental Medi-Cal payments to certain hospitals funded by a quality assurance fee paid by participating hospitals, as well as matching federal funds (the "Hospital Fee Program"). In September 2010, this legislation was amended at the request of Centers for Medicare and Medicaid Services (CMS). In October 2010, CMS substantially approved the program and the state of California began its implementation. The supplemental payments encompass fee-for-service payments directly from the California Department of Health Care Services, as well as payments routed through managed care plans.

To date, there have been three segments (or "rounds") of the Hospital Fee Program. The first round covered the 21-month service period from April 1, 2009, through December 31, 2010. The second round covered the six-month service period from January 1, 2011, through June 30, 2011, and the latest, third round, covers the 30-month period from July 1, 2011, through December 31, 2013. Each round of legislation is subject to CMS review and approval. Recognition in the consolidated financial statements of each round of the program is determined upon respective CMS program approval thereof. To date, CMS has approved all portions of the first and second rounds of legislation, as well as a major portion of the third round of legislation.

Supplemental payments related to the Hospital Fee Program in the amounts of \$20,784 and \$28,623 were recorded in net patient service revenue for the fiscal years ended September 30, 2013 and 2012, respectively. Program expenses in the amounts of \$17,584 and \$28,315 were recorded in expenses — Hospital Fee Program in the consolidated statements of operations for the years ended September 30, 2013 and 2012, respectively.

The California Hospital Association created a private program, the California Health Foundation and Trust (CHFT), established for several purposes, one of which is aggregating and distributing financial resources to support charitable activities at various hospitals and health systems in California. Under a pledge agreement between the Company and CHFT, the Company expensed \$0 and \$58 in the fiscal years ended September 30, 2013 and 2012, respectively, into a grant fund established by CHFT. These expenses are included in expenses — Hospital Fee Program in the consolidated statements of operations.

As of September 30, 2011, the Hospital had received \$10,012 and paid \$6,304 in supplemental payments and fees, respectively, related to the Hospital Fee Program, for the period from January 1, 2011, through June 30, 2011, which included \$28 paid by the Hospital into the grant fund established by CHFT. As of September 30, 2011, these supplemental payments received and supplemental fees paid were included in other current liability — Hospital Fee Program and other current assets — Hospital Fee Program, respectively, in the consolidated balance sheets, pending final approval from CMS of this part of the program. This approval was received in December 2011 and the deferred amounts were recognized in the consolidated statement of operations in the fiscal year ended September 30, 2012.

As of September 30, 2012, CMS granted approval for a major portion of the third round of the Hospital Fee Program and the Hospital accrued \$17,285 in related net patient service revenues and \$21,980 in related expenses for the fiscal year ended September 30, 2012. The amounts accrued represent estimated amounts due and payable for the service period from July 1, 2011, through September 30, 2012, and includes \$4,016 of expenses related to the managed care portion of the Hospital Fee Program, which are probable and estimable as of September 30, 2012. As of September 30, 2012, the accrued revenues and accrued expenses were included in other current assets — Hospital Fee Program and other current liability — Hospital Fee Program, respectively, in the consolidated balance sheets.

As of September 30, 2013, the Hospital had received \$23,735 and paid \$27,254 in supplemental payments and fees, respectively, related to the third round 30-month Hospital Fee Program. For the fiscal year ended September 30, 2013, the Hospital recognized \$20,784 in related net patient service revenues and \$17,584 in related expenses, representing estimated amounts due and payable for the service period from October 1, 2012, through September 30, 2013. As of September 30, 2013, the accrued revenues and accrued expenses were included in other current assets — Hospital Fee Program and other current liability — Hospital Fee Program, respectively, in the consolidated balance sheets.

In September 2012, the Hospital received \$1,662 from CHFT relating to the third round of the Hospital Fee Program, of which \$831 was included in other operating revenue in the consolidated statement of operations and \$831 was included in other current liability — Hospital Fee Program in the consolidated balance sheets as of September 30, 2012. For the fiscal year ended September 30, 2013, \$664 was recorded in other operating revenue and the remaining \$166 was included in other current liability — Hospital Fee Program in the consolidated balance sheets as of September 30, 2013.

16. AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009 (ARRA)

Under certain provisions of the ARRA, federal incentive payments are available to hospitals, physicians, and certain other professionals (“Providers”) when they adopt certified electronic health record (EHR) technology or become “meaningful users” of EHR technology in ways that demonstrate improved quality, safety, and effectiveness of care. Providers can become eligible for annual Medicare incentive payments by demonstrating meaningful use of EHR technology in each period over four annual periods matching the federal fiscal years between 2011 and 2015. Medicaid Providers can receive their initial incentive payment by adopting, implementing, or upgrading (AIU) certified EHR technology, but must demonstrate meaningful use of EHR technology in subsequent years in order to qualify for additional payments. Hospitals may be eligible for both Medicare and Medicaid EHR incentive payments;

however, physicians and other professionals may be eligible for either Medicare or Medicaid incentive payments, but not both. Medicaid EHR incentive payments to Providers are 100% federally funded and administered by the states; however, the states are not required to offer EHR incentive payments to Providers. The CMS established calendar year 2011 as the first year states could offer EHR incentive payments.

During the fiscal years preceding September 30, 2011, and during the fiscal year ended September 30, 2011, the Company acquired certified EHR technology for the Hospital and BHP and for the CMS-approved state Medicaid (“Medi-Cal”) plans for California (the only state in which the Hospital operates). Accordingly, the Hospital is entitled to receive Medicaid (Medi-Cal) incentive payments for the adoption of certified EHR technology for the Hospital in California and received CMS approval once it has satisfied the statutory and regulatory AIU requirements. The Hospital filed its attestation for “meaningful use” for the Hospital in October 2012 and 2011. As a result of this filing, the Hospital and BHP received \$2,972 and \$3,383 in the fiscal years ended September 30, 2013 and 2012, respectively, which is included in other operating revenue in the consolidated statements of operations. These incentive payment revenues partially offset significantly higher expenses the Hospital and BHP incurred in the several fiscal years preceding fiscal 2011, and including the fiscal year 2011 related to the Hospital’s and BHP’s overall EHR implementation program.

Also, if the Hospital satisfies specified meaningful use criteria in future periods, the Hospital may become entitled to additional Medicaid incentive payments, as well as Medicare incentive payments if this reimbursement program continues to remain in place.

17. SUBSEQUENT EVENTS

The Company has evaluated subsequent events through January 22, 2014, the date the consolidated financial statements were available to be issued. The following subsequent events were noted:

Acquisition of DRMC — On October 1, 2013, the Company became the sole corporate member of DRMC through a member substitution agreement. DRMC is a sole corporate member of Downey Regional Medical Center Hospital, Inc., a 199-bed acute care hospital; Downey Regional Medical Center Insurance Services, Inc.; Downey Regional Medical Center Properties, Inc.; and Memorial Trust Foundation of Downey Regional Medical Center. The Company renamed DRMC “PIH Health Hospital — Downey” and all current DRMC board members resigned as of September 30, 2013, with an effective date of October 1, 2013, to coincide with the close of the transaction. The Company restructured the PIH Health Hospital — Downey board of directors and immediately began to integrate DRMC into its operating structure. By acquiring DRMC, the Company will expand its primary service area and seek to better serve the health care needs of southeastern Los Angeles County, San Gabriel Valley, and northern Orange County.

As part of the transaction, the Company acquired all the identifiable tangible assets, assumed all the liabilities, and acquired certain intangible assets of DRMC, which may include customer lists, in-place lease agreements, and other intangible assets. There was no cash consideration exchanged between the Company and the previous sole corporate member of DRMC; however, the Company had previously entered into the Assistance Loan with DRMC (see Note 5), which was converted to an intercompany receivable from DRMC upon the closing of the transaction. The Company is still in the process of assessing the fair value of assets acquired and liabilities assumed at the date of acquisition, and the enterprise value of DRMC, as well the fair values of any intangible assets acquired. The Company expects to complete this assessment during the year ended September 30, 2014, and will adjust the provisional amounts that were recorded as of October 1, 2013, to reflect the revised values when additional information becomes known.

Transaction costs incurred as of September 30, 2013, totaled \$1,362 and relate primarily to legal and consulting services, which are included in other expenses in the consolidated statements of operations. The Company incurred additional transaction costs of \$185 subsequent to September 30, 2013. Summarized provisional consolidated balance sheet information for DRMC at October 1, 2013, is shown below:

Consolidated Balance Sheets (in thousands)

Cash and cash equivalents	\$ 1,627	Accounts payable and accrued expenses	\$ 37,962
Restricted cash	2,452	Hospital fee program payable	16,619
Patient accounts receivable - net	18,534	PIH loan payable	23,636
Hospital fee program receivable	13,356	Debt	61,400
Other assets	12,984	Liabilities subject to compromise	12,713
Property and equipment - net	<u>68,517</u>		
Total assets acquired, at estimated fair value	<u>\$117,470</u>	Total liabilities assumed, at estimated fair value	<u>152,330</u>
		Excess of liabilities assumed over assets acquired	<u>\$ 34,860</u>

The supplemental pro forma revenue, earnings, and changes in net assets for the years ended September 30, 2013 and 2012, are as follows (unaudited):

Pro Forma Consolidated Operating Revenue, Excess of Revenues over Expenses, and Changes in Net Assets (in thousands)

	2013	2012
Total operating revenue	\$ 777,654	\$ 754,571
Excess of revenues over expenses *	(9,382)	27,554
Changes in unrestricted net assets	139,864	53,575
Changes in temporarily restricted net assets	(1,312)	1,437
Changes in permanently restricted net assets	0	0

* Performance indicator is the excess of revenues and gains over expenses and losses.

The pro forma information outlined above sets forth the results of operations as if the transaction had been completed as of October 1, 2012.

Loan Agreement — On October 1, 2013, PIH entered into a \$100,000 term loan agreement with a financial institution to provide additional capital for the acquisition and integration of DRMC. The agreement term is for the period ending October 1, 2015, and is subject to certain financial and nonfinancial covenants. The interest rate, as defined in the agreement, is a rate per year equal to the sum of the LIBOR daily floating rate plus 0.45%. With a portion of the proceeds of this loan, PIH retired \$49,685 of DRMC's outstanding long-term debt on October 1, 2013.

* * * * *

SUPPLEMENTARY CONSOLIDATING INFORMATION

INTERHEALTH CORP. AND AFFILIATES

SCHEDULE 1

CONSOLIDATING SCHEDULE — BALANCE SHEET INFORMATION AS OF SEPTEMBER 30, 2013 (In thousands)

	InterHealth Corp.	IHC Management Corp.	Presbyterian Intercommunity Hospital, Inc.*	Obligated Group Total	PIH Foundation	Bright Health Physicians	Med Site — Hacienda Heights	PIH Community Pharmacy	PIH Insurance Company	PIH Healthcare Solutions	Eliminations	Total
ASSETS												
CURRENT ASSETS:												
Cash and cash equivalents	\$ -	\$23,270	\$ 459	\$ 23,729	\$ 189	\$ 161	\$ -	\$ -	\$ 696	\$-	\$ -	\$ 24,775
Investments — short term		1,921	6	1,927					439			2,366
Patient accounts receivable — net			58,815	58,815		6,784						65,599
Inventory			4,061	4,061		433		643				5,137
Other receivables	86		6,322	6,408	2	292	53	101	100			6,956
Prepaid expenses and other assets	134		6,509	6,643	354	546	2		2,858		(1,011)	9,392
Other current assets — Hospital Fee Program			7,598	7,598								7,598
Total current assets	220	25,191	83,770	109,181	545	8,216	55	744	4,093	-	(1,011)	121,823
INVESTMENTS IN MUTUAL FUNDS AND OTHER INVESTMENTS		3,207	19,570	22,777	2,367				9,465			34,609
INVESTMENTS — Assets limited as to use			364,149	364,149								364,149
PROPERTY, PLANT, AND EQUIPMENT — Net	101,876		394,711	496,587	9	17,285	4	104				513,989
INTERCOMPANY RECEIVABLES			142,481	142,481	1,674						(144,155)	-
DEFERRED FINANCING COSTS — Net			2,561	2,561								2,561
GOODWILL — Net			595	595		10,950						11,545
INVESTMENT IN AFFILIATES			1,002	1,002		13					(1,015)	-
OTHER ASSETS	26		1,326	1,352	156	1						1,509
OTHER ASSETS — Downey			23,636	23,636								23,636
TOTAL	<u>\$102,122</u>	<u>\$28,398</u>	<u>\$1,033,801</u>	<u>\$1,164,321</u>	<u>\$4,751</u>	<u>\$36,465</u>	<u>\$ 59</u>	<u>\$ 848</u>	<u>\$13,558</u>	<u>\$-</u>	<u>\$(146,181)</u>	<u>\$1,073,821</u>

See Notes to Consolidating Schedules.

(Continued)

INTERHEALTH CORP. AND AFFILIATES

SCHEDULE 1

CONSOLIDATING SCHEDULE — BALANCE SHEET INFORMATION AS OF SEPTEMBER 30, 2013 (In thousands)

	InterHealth Corp.	IHC Management Corp.	Presbyterian Intercommunity Hospital, Inc.*	Obligated Group Total	PIH Foundation	Bright Health Physicians	Med Site — Hacienda Heights	PIH Community Pharmacy	PIH Insurance Company	PIH Healthcare Solutions	Eliminations	Total
LIABILITIES AND NET ASSETS (DEFICIT)												
CURRENT LIABILITIES:												
Accounts payable and accrued expenses	\$ 2,707	\$ 48	\$ 43,470	\$ 46,225	\$ 312	\$10,106	\$ 32	\$ 1	\$ 1,368	\$ 10	\$ (1,011)	\$ 57,043
Estimated third-party payor settlements			1,207	1,207								1,207
Accrued interest			1,362	1,362								1,362
Current portion of long-term debt			7,940	7,940								7,940
Short-term loan borrowing			30,500	30,500								30,500
Other current liability — Hospital Fee Program			3,684	3,684								3,684
Retention — self-insurance programs — current portion			5,775	5,775		540			4,611			10,926
Total current liabilities	2,707	48	93,938	96,693	312	10,646	32	1	5,979	10	(1,011)	112,662
DEFERRED COMPENSATION			15,036	15,036								15,036
INTEREST RATE SWAP			35,919	35,919								35,919
LONG-TERM DEBT — Net of current portion			285,005	285,005								285,005
PENSION LIABILITY			46,764	46,764								46,764
RETENTION — Self-insurance programs — net of current portion			12,252	12,252		2,148			1,530			15,930
INTERCOMPANY PAYABLES	99,174	28,244		127,418		12,893	2,356	1,307		181	(144,155)	-
Total liabilities	101,881	28,292	488,914	619,087	312	25,687	2,388	1,308	7,509	191	(145,166)	511,316
NET (DEFICIT) ASSETS:												
Unrestricted net assets/retained earnings (deficit)	241	106	544,887	545,234	(800)	10,778	(2,329)	(460)	6,049	(191)	(1,015)	557,266
Temporarily restricted				-	4,268							4,268
Permanently restricted				-	971							971
Total net assets (deficit)	241	106	544,887	545,234	4,439	10,778	(2,329)	(460)	6,049	(191)	(1,015)	562,505
TOTAL	\$102,122	\$28,398	\$1,033,801	\$1,164,321	\$4,751	\$36,465	\$ 59	\$ 848	\$13,558	\$-	\$(146,181)	\$1,073,821

See Notes to Consolidating Schedules.

(Concluded)

INTERHEALTH CORP. AND AFFILIATES

SCHEDULE 2

CONSOLIDATING SCHEDULE — STATEMENT OF OPERATIONS INFORMATION FOR THE YEAR ENDED SEPTEMBER 30, 2013 (In thousands)

	InterHealth Corp.	IHC Management Corp.	Presbyterian Intercommunity Hospital, Inc.*	Obligated Group Total	PIH Foundation	Bright Health Physicians	Med Site — Hacienda Heights	PIH Community Pharmacy	PIH Insurance Company	PIH Healthcare Solutions	Eliminations	Total
REVENUES:												
Net patient service revenue	\$ -	\$ -	\$494,503	\$494,503	\$ -	\$ 43,339	\$ 546	\$ -	\$ -	\$ -	\$ -	\$538,388
Provision for bad debts			12,134	12,134		1,727	3					13,864
Net patient service revenue			482,369	482,369		41,612	543					524,524
Capitation revenue						77,405						77,405
Other operating revenue	14,485	482	8,576	23,543	3,244	1,499		4,357	3,510		(14,803)	21,350
Net assets released from restrictions used for operations			781	781		50	35					866
Total revenues	14,485	482	491,726	506,693	3,244	120,566	578	4,357	3,510	-	(14,803)	624,145
EXPENSES:												
Salaries and wages	261		170,319	170,580	491	27,984	401	412				199,868
Purchased services	1,716		46,087	47,803	214	38,756	82	2		1		86,858
Medical supplies and drugs	306		60,362	60,668	17	5,848	59	3,707				70,299
Employee benefits	46		70,650	70,696	93	8,834	72	82				79,777
Professional fees	421		31,305	31,726	95	49,763			362	189		82,135
Depreciation and amortization	4,431		21,483	25,914	1	1,545	1	21				27,482
Other expenses	2,295	482	22,467	25,244	82	(5,549)	43	24	64	1		19,909
Interest — net			5,423	5,423								5,423
Insurance			4,618	4,618		1,709			2,146		(3,326)	5,147
Rent/lease expense	279		5,590	5,869	64	7,792	227	76			(10,995)	3,033
Management services expense			482	482							(482)	-
Hospital Fee Program			17,584	17,584								17,584
Total expenses	9,755	482	456,370	466,607	1,057	136,682	885	4,324	2,572	191	(14,803)	597,515
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	4,730	-	35,356	40,086	2,187	(16,116)	(307)	33	938	(191)	-	26,630

See Notes to Consolidating Schedules.

(Continued)

INTERHEALTH CORP. AND AFFILIATES

SCHEDULE 2

CONSOLIDATING SCHEDULE — STATEMENT OF OPERATIONS INFORMATION FOR THE YEAR ENDED SEPTEMBER 30, 2013 (In thousands)

	InterHealth Corp.	IHC Management Corp.	Presbyterian Intercommunity Hospital, Inc.*	Obligated Group Total	PIH Foundation	Bright Health Physicians	Med Site — Hacienda Heights	PIH Community Pharmacy	PIH Insurance Company	PIH Healthcare Solutions	Eliminations	Total
OTHER GAINS (LOSSES) — Net:												
Net investment income	\$ -	\$ 116	\$ 9,672	\$ 9,788	\$ 87	\$ -	\$ -	\$ -	\$ 88	\$ -	\$ -	\$ 9,963
Realized (losses) gains on investments — net		(65)	13,753	13,688	29				5			13,722
Change in fair value of interest rate swap and interest expense			10,477	10,477								10,477
Loss on extinguishment of debt — net			(1,416)	(1,416)								(1,416)
Total other gains — net	-	51	32,486	32,537	116	-	-	-	93	-	-	32,746
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES AND OTHER GAINS (LOSSES)	4,730	51	67,842	72,623	2,303	(16,116)	(307)	33	1,031	(191)		59,376
CHANGE IN UNREALIZED LOSSES ON INVESTMENTS — Net		(50)	3,634	3,584	64				363			4,011
PENSION-RELATED CHANGES OTHER THAN NET PERIODIC PENSION COST			38,636	38,636								38,636
NET ASSETS RELEASED FROM RESTRICTIONS USED FOR LONG-LIVED ASSETS			1,993	1,993								1,993
OTHER LOSSES — Net			(157)	(157)		(7)						(164)
TOTAL INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS	\$ 4,730	\$ 1	\$ 111,948	\$ 116,679	\$ 2,367	\$ (16,123)	\$ (307)	\$ 33	\$ 1,394	\$ (191)	-	\$ 103,852

See Notes to Consolidating Schedules.

(Concluded)

INTERHEALTH CORP. AND AFFILIATES

SCHEDULE 3

CONSOLIDATING SCHEDULE — STATEMENT OF CHANGES IN NET ASSETS INFORMATION FOR THE YEAR ENDED SEPTEMBER 30, 2013 (In thousands)

	InterHealth Corp.	IHC Management Corp.	Presbyterian Intercommunity Hospital, Inc.*	Obligated Group Total	PIH Foundation	Bright Health Physicians	Med Site — Hacienda Heights	PIH Community Pharmacy	PIH Insurance Company	PIH Healthcare Solutions	Eliminations	Total
UNRESTRICTED NET ASSETS —												
Increase (decrease) in unrestricted net assets	\$ 4,730	\$ 1	\$111,948	\$116,679	\$ 2,367	\$(16,123)	\$ (307)	\$ 33	\$1,394	\$(191)	\$ -	\$103,852
TEMPORARILY RESTRICTED NET ASSETS:												
Contributions and grants received				-	1,547							1,547
Net assets released from restrictions				-	(2,859)							(2,859)
Change in temporarily restricted net assets	-	-	-	-	(1,312)	-	-	-	-	-	-	(1,312)
CHANGE IN NET ASSETS BEFORE INVESTMENT IN AFFILIATES	4,730	1	111,948	116,679	1,055	(16,123)	(307)	33	1,394	(191)		102,540
INVESTMENT IN AFFILIATES				-		2					(2)	-
CHANGE IN NET ASSETS (DEFICIT) EQUITY TRANSFER	4,730	1	111,948	116,679	1,055	(16,121)	(307)	33	1,394	(191)	(2)	102,540
EQUITY TRANSFER			(30,000)	(30,000)		30,000						-
CHANGE IN NET ASSETS (DEFICIT)	4,730	1	81,948	86,679	1,055	13,879	(307)	33	1,394	(191)	(2)	102,540
NET (DEFICIT) ASSETS — Beginning of year	(4,489)	105	462,939	458,555	3,384	(3,101)	(2,022)	(493)	4,655		(1,013)	459,965
NET (DEFICIT) ASSETS — End of year	\$ 241	\$106	\$544,887	\$545,234	\$ 4,439	\$ 10,778	\$(2,329)	\$(460)	\$6,049	\$(191)	\$(1,015)	\$562,505

See Notes to Consolidating Schedules.

INTERHEALTH CORP. AND AFFILIATES

NOTES TO CONSOLIDATING SCHEDULES AS OF AND FOR THE YEAR ENDED SEPTEMBER 30, 2013

1. BASIS OF PRESENTATION

The accompanying consolidating balance sheet information, statements of operations information, and statements of changes in net assets information (collectively, the “consolidating schedules”) are prepared on the accrual basis of accounting. The preparation of the consolidating schedules 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 consolidating schedules, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

The Company eliminates intercompany transactions, such as investments in affiliates and the related equity and results of operations, and records its investment in affiliates at a cost basis. Net assets released from restrictions are transferred immediately to recipient affiliates.

2. ALLOCATIONS

Assets, liabilities, expenses, and revenues have been allocated to the affiliates based on the number of employees, patients seen, or other relevant benchmarks except as outlined below:

Items Maintained at the Hospital — Line of credit, deferred compensation, and the pension liability are held and maintained by the Hospital and not allocated to the individual affiliates because these items would be maintained by the Hospital regardless of the operations of the affiliates. The net periodic benefit cost of the pension plan is allocated to the affiliates based on the number of employees eligible for the benefit.

Items Maintained within the Obligated Group — Pooled investments, bonds, deferred financing costs, interest rate swap, accrued interest, and interest expense related to such are held at the Hospital, InterHealth, and IHMC which are all members of the Obligated Group and have not been allocated to the affiliates within the Obligated Group due to feasibility.