

# Gaylord Farm Association, Inc.

Independent Auditors' Report,  
Consolidated Financial Statements and  
Supplemental Information

As of and for the Years Ended  
September 30, 2011 and 2010

**Gaylord Farm Association, Inc.**  
**Independent Auditors' Report, Consolidated Financial Statements**  
**and Supplemental Information**  
**As of and for the Years Ended September 30, 2011 and 2010**

Table of Contents

	<u>Page</u>
Independent Auditors' Report.....	1
Consolidated Financial Statements:	
Consolidated Balance Sheets.....	2
Consolidated Statements of Operations and Changes in Net Assets and Shareholder's Equity .....	3
Consolidated Statements of Cash Flows .....	5
Notes to the Consolidated Financial Statements .....	6
Supplemental Information:	
Consolidating Balance Sheet - 2011.....	30
Consolidating Balance Sheet - 2010.....	31
Consolidating Statement of Operations - 2011.....	32
Consolidating Statement of Operations - 2010.....	33

Independent Auditors' Report

To the Board of Directors of  
Gaylord Farm Association, Inc.:

We have audited the accompanying consolidated balance sheets of Gaylord Farm Association, Inc. (the Association) as of September 30, 2011 and 2010, and the related consolidated statements of operations and changes in net assets and shareholder's equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the financial statements of Gaylord Risk Solutions, Ltd., a wholly-owned subsidiary, whose statements reflect total assets of \$5,354,067 and \$5,477,101 as of September 30, 2011 and 2010, total liabilities of \$3,550,951 and \$3,291,837 as of September 30, 2011 and 2010, and total revenues of (\$135,312) and \$575,000 and net (loss) income of (\$121,844) and \$328,315 for the years then ended, respectively. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Gaylord Risk Solutions, Ltd., is based solely on the report of the other auditors.

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 of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Gaylord Farm Association, Inc. as of September 30, 2011 and 2010, and the results of its consolidated operations and its consolidated cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The consolidating information listed within the Table of Contents is presented for purposes 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 it is not a required part of the consolidated financial statements. Accordingly, we do not express an opinion on the financial position, results of operations and cash flows of the individual companies. The consolidating information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

*Saslow Luftkin & Buggy, LLP*

January 27, 2012  
Avon, Connecticut

**Gaylord Farm Association, Inc.**  
**Consolidated Balance Sheets**  
**September 30, 2011 and 2010**

	<b>2011</b>	<b>2010</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 884,695	\$ 2,376,012
Patient accounts receivable (less allowance for doubtful accounts of \$503,000 in 2011 and \$540,000 in 2010)	10,001,815	9,115,849
Assets whose use is limited:		
Assets held under bond indenture agreement	179,780	171,783
Pledges receivable	386,657	495,086
Other current assets	1,944,851	1,725,017
Total current assets	13,397,798	13,883,747
Assets whose use is limited:		
Pledges receivable	310,105	689,220
Board-designated investments	13,693,257	16,458,755
Donor restricted investments	5,529,789	5,500,469
Beneficial interest in trusts held by others	9,748,956	10,168,420
	29,282,107	32,816,864
Property, plant and equipment, net	41,937,586	44,202,592
Investments held for captive insurance liabilities	3,517,224	3,909,996
Reinsurance recoverable relating to captive insurance liabilities	678,921	757,650
Other assets (Note 7)	1,086,089	1,181,912
	\$ 89,899,725	\$ 96,752,761
<b>Liabilities, Net Assets and Shareholder's Equity</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 4,853,991	\$ 5,100,337
Accrued payroll and related taxes	3,819,490	3,375,454
Line of credit	450,000	1,025,000
Estimated amounts due to third-party payers	246,805	246,805
Current portion of accrued pension obligation	2,743,352	2,086,158
Current portion of long-term debt and capital lease obligations	1,487,242	1,453,373
Total current liabilities	13,600,880	13,287,127
Long-term debt and capital lease obligations, less current portion	19,570,309	21,086,278
Accrued pension obligation	14,699,268	13,002,959
Captive insurance loss and other reserves	2,827,083	3,049,299
Interest rate swap liability	4,155,222	3,647,029
Total liabilities	54,852,762	54,072,692
Net assets and shareholder's equity:		
Unrestricted net assets	16,757,868	23,044,098
Temporarily restricted net assets	1,207,234	1,781,818
Permanently restricted net assets	15,278,745	15,668,889
Shareholder's equity	1,803,116	2,185,264
Total net assets and shareholder's equity	35,046,963	42,680,069
	\$ 89,899,725	\$ 96,752,761

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

**Gaylord Farm Association, Inc.**  
**Consolidated Statements of Operations and**  
**Changes in Net Assets and Shareholder's Equity**  
**For the Years Ended September 30, 2011 and 2010**

	<b>2011</b>	<b>2010</b>
Revenues:		
Net patient service revenue	\$ <b>67,064,747</b>	\$ 67,801,584
Contributions and bequests	<b>913,165</b>	872,470
Ceded premium	<b>(332,500)</b>	(364,465)
Other operating revenue	<b>637,668</b>	677,534
Net assets released from restrictions used for operations	<b>145,235</b>	181,824
Total revenues	<b>68,428,315</b>	69,168,947
Expenses:		
Salaries and related expenses	<b>46,823,491</b>	45,433,743
Other operating expenses	<b>5,992,459</b>	5,392,045
Professional fees and contract services	<b>6,587,269</b>	6,624,882
Supplies	<b>5,062,760</b>	5,781,010
Depreciation and amortization	<b>3,890,429</b>	3,857,884
Occupancy costs	<b>1,871,403</b>	1,843,607
Provision for bad debts	<b>344,715</b>	802,494
Interest	<b>919,764</b>	965,660
Losses and loss adjustment (recoveries) expenses	<b>(141,200)</b>	157,126
Total expenses	<b>71,351,090</b>	70,858,451
Loss from operations	<b>(2,922,775)</b>	(1,689,504)
Other gains (losses):		
Dividend and interest income	<b>586,562</b>	573,473
Net realized gains on investments	<b>140,830</b>	37,303
Loss on equity investments	<b>(5,304)</b>	(92,815)
Change in fair value of interest rate swap agreement	<b>(508,193)</b>	(1,014,191)
Loss on lease abandonment	<b>-</b>	(147,543)
Total other gains (losses)	<b>213,895</b>	(643,773)
Excess of revenues over (under) expenses	<b>\$ (2,708,880)</b>	\$ (2,333,277)

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

**Gaylord Farm Association, Inc.**  
**Consolidated Statements of Operations and**  
**Changes in Net Assets and Shareholder's Equity (continued)**  
**For the Years Ended September 30, 2011 and 2010**

	<b>2011</b>	<b>2010</b>
Unrestricted net assets:		
Excess of revenues over (under) expenses	\$ (2,708,880)	\$ (2,333,277)
Net unrealized (losses) gains on investments	(1,132,499)	1,508,283
Pension related changes other than net periodic pension cost	(3,183,532)	(795,655)
Net loss (income) of GRS	121,844	(328,315)
Net assets released from restrictions used for purchases of property, plant and equipment	616,837	685,137
Change in unrestricted net assets	(6,286,230)	(1,263,827)
Temporarily restricted net assets:		
Restricted pledges and contributions	187,488	500,053
Net assets released from restrictions	(762,072)	(866,961)
Change in temporarily restricted net assets	(574,584)	(366,908)
Permanently restricted net assets:		
Restricted contributions and bequests	29,320	514,253
Change in beneficial interest in trusts held by others	(419,464)	224,514
Change in permanently restricted net assets	(390,144)	738,767
Shareholder's equity:		
Net (loss) income of GRS	(121,844)	328,315
Net unrealized (losses) gains on investments of GRS	(260,304)	59,976
Change in shareholder's equity	(382,148)	388,291
Change in net assets and shareholder's equity	(7,633,106)	(503,677)
Net assets and shareholder's equity, beginning of year	42,680,069	43,183,746
Net assets and shareholder's equity, end of year	\$ 35,046,963	\$ 42,680,069

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

**Gaylord Farm Association, Inc.**  
**Consolidated Statements of Cash Flows**  
**For the Years Ended September 30, 2011 and 2010**

	<u>2011</u>	<u>2010</u>
Operating activities:		
Change in net assets and shareholder's equity	\$ (7,633,106)	\$ (503,677)
Adjustments to reconcile change in net assets and shareholder's equity to net cash provided by operating activities:		
Depreciation and amortization	3,890,429	3,857,884
Pension related changes other than net periodic pension cost	3,183,532	795,655
Change in fair value of interest rate swap	508,193	1,014,191
Net realized and unrealized losses (gains) on investments	991,669	(1,545,586)
Loss from equity investments	5,304	92,815
Change in beneficial interest in trusts held by others	419,464	(224,514)
Restricted contributions and bequests received	(216,808)	(1,014,306)
Changes in operating assets and liabilities:		
Patient accounts receivable	(885,966)	577,875
Other current assets	(219,834)	(145,630)
Pledges receivable	487,544	599,029
Investments held for captive insurance liabilities	392,772	(785,962)
Reinsurance recoverable relating to captive insurance	78,729	(59,515)
Other assets	121,120	42,001
Accounts payable and accrued expenses	(246,346)	(279,832)
Accrued payroll and related taxes	444,036	89,855
Accrued pension obligation	(830,029)	(600,878)
Captive insurance loss and other reserves	(222,216)	43,336
Net cash provided by operating activities	<u>268,487</u>	<u>1,952,741</u>
Investing activities:		
Assets held under bond indenture agreement	(7,997)	(6,541)
Investments in joint ventures	(30,601)	(231,955)
Purchases of property, plant and equipment	(1,625,423)	(1,647,912)
Sales and purchases of investments, net	1,744,509	768,017
Net cash provided by (used in) investing activities	<u>80,488</u>	<u>(1,118,391)</u>
Financing activities:		
Principal payments on long-term debt	(640,000)	(615,000)
Net payments on lines of credit	(575,000)	(600,000)
Principal payments on capital lease obligations	(842,100)	(508,680)
Restricted contributions and bequests received	216,808	1,014,306
Net cash used in financing activities	<u>(1,840,292)</u>	<u>(709,374)</u>
Change in cash and cash equivalents	(1,491,317)	124,976
Cash and cash equivalents, beginning of year	<u>2,376,012</u>	<u>2,251,036</u>
Cash and cash equivalents, end of year	<u>\$ 884,695</u>	<u>\$ 2,376,012</u>

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

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 1 - General**

**Organization** - Gaylord Farm Association, Inc. (the Association) is a not-for-profit corporation, which is a supporting corporation for Gaylord Hospital, Inc. (Gaylord), Gaylord Research Institute, Inc. (GRI), The Gaylord Foundation, Inc. (TGF), Farm Properties, Inc. (FP), Gaylord Farm Rehabilitation Center (GFRC) and Gaylord Risk Solutions, Ltd. (GRS).

Gaylord operates a chronic disease hospital that specializes in the care and treatment of people with medically complex conditions and rehabilitation including brain and spinal cord injury, pulmonary illness, stroke, neurological and orthopedic conditions. In addition, Gaylord runs outpatient clinics to provide physical therapy, occupational therapy, speech therapy and physiatry services as well as sleep disorder centers.

GRI, TGF and FP are dormant corporations with no activity and GFRC is the supporting corporation for the Traurig House, which is a component of the Association's traumatic brain injury care and treatment department.

GRS was incorporated on December 12, 2007 and operates subject to the provisions of the Companies Law of the Cayman Islands. GRS was granted an Unrestricted Class "B" Insurer's license on December 28, 2007, which it holds subject to the provisions of the Insurance Law of the Cayman Islands. GRS is a wholly owned subsidiary of the Association.

**Note 2 - Summary of Significant Accounting Policies**

**Basis of Presentation** - The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP), as promulgated by the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC). The consolidated financial statements include the accounts of the Association and its wholly-owned subsidiaries. All significant inter-company balances and transactions have been eliminated in consolidation.

**Use of Estimates** - The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and related footnotes. Actual results could differ from those estimates. Significant accounts that are impacted by such estimates and assumptions are the allowance for doubtful accounts, allowances for third-party payer discounts and settlements, accrued pension liabilities, malpractice loss reserves and the reserves for workers' compensation insurance.

**Cash and Cash Equivalents** - Cash and cash equivalents include highly liquid investments with maturities of three months or less when purchased. In general, the Federal Deposit Insurance Corporation (FDIC) insures cash balances up to \$250,000 per depositor, per bank. The FDIC also provides separate unlimited coverage for deposit accounts that meet the definition of non-interest bearing accounts. Unlimited coverage on non-interest bearing accounts extends until December 31, 2012. It is the Association's policy to monitor the financial strength of the banks that hold its deposits on an ongoing basis. During the normal course of business, the Association maintains cash balances in excess of the FDIC insurance limit.



**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 2 - Summary of Significant Accounting Policies (continued)**

**Property, Plant and Equipment** - Property, plant and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable assets and is computed using the straight-line method. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the consolidated financial statements. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Maintenance and repairs are charged to expense as incurred.

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

**Investments** - Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the consolidated balance sheets. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in the excess of revenues over (under) expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from the excess of revenues over (under) expenses unless the investments are trading securities. Unrealized losses that have been deemed to be other than temporarily impaired are included within excess of revenues over (under) expenses.

**Other Than Temporary Impairments on Investments** - The Association accounts for other than temporary impairments in accordance with FASB ASC 320-10 "*Investments - Debt and Equity Securities*" and continually reviews its securities for impairment conditions, which could indicate that an other than temporary decline in market value has occurred. In conducting this review, numerous factors are considered, which include specific information pertaining to an individual company or a particular industry, general market conditions that reflect prospects for the economy as a whole, and the ability and intent to hold securities until recovery. The carrying value of investments is reduced to its estimated realizable value if a decline in fair value is considered to be other than temporary. There were no impairments recorded in 2011 or 2010.

**Equity Investments** - The Association has a fifty percent ownership interest in North Haven Fitness & Wellness, LLC (Fitness & Wellness). In addition, the Association has a fifty percent ownership in Gaylord Sleep HealthCenters of Connecticut, LLC (GSHC). The Association accounts for its investment interest in these entities using the equity method of accounting. As such, the Association adjusts its investments by its share of the investees net income (loss).

**Deferred Financing Costs** - Deferred financing costs have been recorded as an asset and are being amortized using the effective interest method over the term of the related financing agreement.

**Temporarily and Permanently Restricted Net Assets** - Temporarily restricted net assets are those whose use by the Association has been limited by donors to a specific time frame or purpose and are included in investments. Temporarily restricted net assets are available primarily for health care services, including cancer and pediatric programs and capital replacement.

Permanently restricted net assets consist of funds held in trust by others and the Association's permanently restricted endowments, which are included in donor restricted investments. Permanently restricted endowments are investments to be held in perpetuity, the income from which is expendable to support health care services. The income from funds held in trust by others is expendable to support health care services.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 2 - Summary of Significant Accounting Policies (continued)**

**Donor Restricted Gifts** - Unconditional promises to give cash and other assets to the Association 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. 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 as unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

**Excess of Revenues Over (Under) Expenses** - The consolidated statements of operations and changes in net assets includes excess of revenues over (under) expenses. Changes in unrestricted net assets, which are excluded from excess of revenues over (under) expenses, consistent with industry practice, include unrealized gains and losses on investments other than trading securities, assets released from restrictions for purchase of property, plant and equipment and certain changes in the pension liability.

**Income Taxes** - The Association is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and is exempt from federal and state income taxes on related income pursuant to Section 501(a) of the Code. GRS is a not-for-profit captive insurance company organized under the laws of the Cayman Islands.

The Association accounts for uncertain tax positions with provisions of FASB ASC 740, "Income Taxes" which provide a framework for how companies should recognize, measure, present and disclose uncertain tax positions in their consolidated financial statements. The Association may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The Association does not have any uncertain tax positions as of September 30, 2011 and 2010. As of September 30, 2011 and 2010, the Association did not record any penalties or interest associated with uncertain tax positions. The Association's prior three tax years are open and subject to examination by the Internal Revenue Service.

**Goodwill** - The Association recorded the excess of the purchase price of a New Haven based sleep center over the fair value of the assets acquired as goodwill. On an annual basis, management reviews the goodwill for impairment by considering the estimated fair value of the business acquired as compared to the net assets of the business. An impairment adjustment of \$18,219 was recognized for fiscal years 2011 and 2010.

**Assets Whose Use is Limited** - Assets which have limited use include assets deposited with a trustee for debt service, pledges, assets set aside by the Board of Directors for future capital improvements and the Association's beneficial interest in funds held in trust held by others.

**Interest Rate Swap Agreement** - The Association uses an interest rate swap agreement to modify its variable interest rate debt to a fixed interest rate, thereby reducing the Association's exposure to interest rate market fluctuations. The interest rate swap agreement involves the exchange of amounts based on a fixed interest rate for amounts based on variable rates over the life of the agreement without the exchange of the notional amount upon which payments are based. The differential of amounts paid and received during the year is charged to interest expense and the amounts payable or receivable from the counter-party is included as an adjustment to accrued interest.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 2 - Summary of Significant Accounting Policies (continued)**

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

**Charity Care** - The Association provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Association does not pursue collection of amounts determined to qualify as charity care, the charges related to charity care services are offset within net patient service revenue. Charity care of \$53,299 and \$67,246, as measured at the Association's respective established rates, was provided in fiscal years 2011 and 2010, respectively.

**Estimated Malpractice Costs** - The Association maintains malpractice insurance coverage under claims made policies through GRS in 2011 and 2010. A provision for estimated medical malpractice claims includes estimates of the ultimate costs for claims incurred but not reported and is included within accounts payable and accrued expenses on the Association's consolidated balance sheets.

**Workers Compensation Costs** - The Association is self-insured for workers' compensation. Estimated self-insurance liabilities are included within accrued payroll and related taxes and are \$1,092,336 and \$1,046,597 as of September 30, 2011 and 2010, respectively, and include estimates for claim obligations related to claims through September 30, 2011 and 2010.

**Unpaid Losses and Loss Adjustment Expenses** - The reserve for unpaid losses and loss adjustment expenses and the related reinsurance recoverable includes case basis estimates of reported losses, plus supplemental amounts calculated based upon loss projections utilizing actuarial studies, Gaylord's own historical data and industry data. In establishing this reserve and the related reinsurance recoverable, GRS utilizes the findings of an independent consulting actuary. Management believes that its aggregate reserve for unpaid losses and loss adjustment expenses and the related reinsurance recoverable at year-end represents its best estimate, based on the available data, of the amount necessary to cover the ultimate cost of losses; however, because of the nature of the insured risks and limited historical experience, actual loss experience may not conform to the assumptions used in determining the estimated amounts for such asset and liability at the consolidated balance sheet date. Accordingly, the ultimate asset and liability could be significantly in excess of or less than the amount indicated in these consolidated financial statements. As adjustments to these estimates become necessary, such adjustments are reflected in current operations.

**Recognition of Premium Revenues** - Premiums written are earned on a pro-rata basis over the related policy period. The portion of premiums that will be earned in the future is deferred and reported as unearned premiums.

**Reinsurance** - In the normal course of business, GRS seeks to reduce its loss exposure by reinsuring certain levels of risk with reinsurers. Reinsurance is accounted for in accordance with FASB ASC 944-20, "Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts". Premiums ceded are expensed over the term of their related policies.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 2 - Summary of Significant Accounting Policies (continued)**

**Legislation** - The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services and Medicare and Medicaid fraud and abuse. Government activity continues with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Association is in compliance with fraud and abuse as well as other applicable government laws and regulations. While no known regulatory inquiries are pending, compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

**New Accounting Pronouncements** - In January 2010, the FASB issued guidance that clarifies and requires new disclosures about fair value measurements. The clarifications and requirement to disclose the amounts and reasons for significant transfers between Level 1 and Level 2, as well as significant transfers in and out of Level 3 of the fair value hierarchy, is effective for interim and annual reporting periods beginning after December 15, 2009. The new guidance also requires that purchases, sales, issuances, and settlements be presented gross in the Level 3 reconciliation and that requirement is effective for fiscal years beginning after December 15, 2010 and for interim periods within those years, with early adoption permitted. Since this new guidance only amends the disclosure requirements, it did not impact the Association's financial position, results of operations or cash flows.

In August 2010, the FASB issued Accounting Standards Updated (ASU) No. 2010-23, "*Health Care Entities (Topic 954): Measuring Charity Care for Disclosure*". ASU No. 2010-23 is intended to reduce the diversity in practice regarding the measurement basis used in the disclosure of charity care. ASU No. 2010-23 requires that cost be used as the measurement basis for charity care disclosure purposes and that cost be identified as the direct or indirect cost of providing the charity care, and requires disclosure of the method used to identify or determine such costs. The adoption of this new guidance is effective for the Association beginning October 1, 2011.

In August 2010, the FASB issued ASU No. 2010-24, "*Health Care Entities (Topic 954) Presentation of Insurance Claims and Related Insurance Recoveries*". ASU No. 2010-24 is intended to address current diversity in practice to the accounting by healthcare entities for medical malpractice claims and similar liabilities and their related anticipated insurance recoveries. Most healthcare entities have netted anticipated insurance recoveries against the related accrued liability, although some entities have presented the anticipated insurance recovery and related liability on a gross basis. The existing guidance does not permit offsetting of conditional or unconditional liabilities with anticipated insurance recoveries from third parties. This update clarifies that a healthcare entity should not net insurance recoveries against related claim liability. Additionally, the amount of the claim liability should be determined without consideration of insurance recoveries. The adoption of this new guidance is effective for the Association beginning October 1, 2011.

In July 2011, the FASB issued ASU No. 2011-07, "*Health Care Entities (Topic 954), Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*", which requires a healthcare entity to change the presentation of their statement of operations by reclassifying the provision for bad debts associated with patient service revenue from an operating expense to a deduction from patient service revenue (net of contractual allowances and discounts). Additionally, enhanced disclosures about an entity's policies for recognizing revenue, assessing bad debts, as well as qualitative and quantitative information about changes in the allowance for doubtful accounts are required. The adoption of ASU 2011-07 is effective for the Association beginning October 1, 2012.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 2 - Summary of Significant Accounting Policies (continued)**

*Subsequent Events* - Subsequent events have been evaluated through January 27, 2012, the date through which procedures were performed to prepare the consolidated financial statements for issuance. Management believes there are no subsequent events having a material impact on the consolidated financial statements.

**Note 3 - Net Patient Service Revenue**

The Association has agreements with third-party payers that provide for payments to the Association at amounts different from its established rates. Contractual payment rates are subject to final determination by reimbursement agencies under each program. A summary of the payment arrangements with major third-party payers follows:

*Medicare* - Inpatient and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient payments are made based on a per discharge amount under the LTCH-DRG inpatient payment system. Outpatient payments are made based on a per encounter amount under the APC outpatient payment system. The Association is reimbursed under the prospective payment system and files annual cost reports, which are subject to audit. The Association's Medicare cost reports have been audited by the Medicare fiscal intermediary through 2003.

*Medicaid* - Inpatient services rendered to Medicaid program beneficiaries are reimbursed at prospective rates per day of hospitalization. These rates are not subject to retroactive adjustment. Outpatient services are reimbursed based on a fee schedule or percent of charges based on the services provided.

*Blue Cross* - Services rendered to Blue Cross beneficiaries are reimbursed on a per diem basis based on contracted rates.

The Association has also entered into payment agreements with certain other commercial insurance carriers and health maintenance organizations. The basis for payment to the Association under these agreements includes prompt payment provisions and discounts from established charges.

Net patient service revenue for the years ended September 30, 2011 and 2010 is as follows:

	<u>2011</u>	<u>2010</u>
Gross patient service revenue	\$ 195,812,053	\$ 191,451,300
Contractual allowances and adjustments	<u>(128,747,306)</u>	<u>(123,649,716)</u>
Net revenue from services to patients	<u>\$ 67,064,747</u>	<u>\$ 67,801,584</u>

Revenue from the Medicare and Medicaid programs accounted for approximately 40% and 9%, respectively, of the Association's net patient revenue for 2011 and 48% and 7% respectively, for 2010. Revenue from Blue Cross accounted for approximately 19% in both 2011 and 2010. No other payer accounted for more than 10% of revenue in 2011 and 2010. Net patient service revenues are based upon complex payment systems and include estimates of amounts yet to be collected. As a result, there is at least a reasonable possibility that recorded estimates will change in the near term. Any changes to estimates are recorded within current year operations.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 3 - Net Patient Service Revenue (continued)**

The Association grants credit without collateral to its patients, most of whom are insured under third-party payer agreements. The following summarizes payers that account for more than 10 percent of patient accounts receivable as of September 30, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Medicare	<b>46%</b>	45%
Medicaid	<b>11%</b>	13%
Blue Cross	<b>14%</b>	17%

Monthly, management reviews accounts receivable for uncollectible amounts and records an allowance for doubtful accounts based on specifically identified accounts, as well as an amount for expected bad debt based on historical losses.

**Note 4 - Investments**

Board-designated and restricted investments are invested as follows as of September 30, 2011 and 2010:

	<u>2011</u>		<u>2010</u>	
	<u>Cost</u>	<u>Market Value</u>	<u>Cost</u>	<u>Market Value</u>
Cash and money market	\$ 318,590	\$ 318,590	\$ 181,621	\$ 181,621
Alternative investment funds	2,519,488	2,047,429	2,208,709	1,765,125
Equity securities	5,116,350	5,164,432	2,048,327	2,381,487
Mutual funds - fixed income	5,840,852	5,786,021	6,249,330	6,468,723
Mutual funds - equity	5,657,540	5,906,574	10,368,512	11,162,268
<b>Total</b>	<b>\$ 19,452,820</b>	<b>\$ 19,223,046</b>	<b>\$ 21,056,499</b>	<b>\$ 21,959,224</b>

Investment balances that have been restricted by donors as of September 30, 2011 and 2010 are \$5,529,789 and \$5,500,469, respectively. The Board of Directors of the Association has restricted all other investments.

Current assets that are held under a bond indenture agreement, are deposited with a trustee for debt service funds. Such amounts are invested in United States treasury notes. In addition, investments held for funding of captive insurance liabilities of \$3,517,224 and \$3,909,996 as of September 30, 2011 and 2010, respectively, are invested in bonds and fixed income mutual funds.

The Hospital also has a beneficial interest in trusts held by others of \$9,748,956 and \$10,168,420 as of September 30, 2011 and 2010, respectively. These funds are managed by the trustees of each fund and are invested primarily in cash equivalents, fixed income and equity securities.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 4 - Investments (continued)**

The following table shows the investments' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, as of September 30, 2011 and 2010:

2011	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Equity securities	\$ 641,790	\$ (141,811)	\$ 105,990	\$ (18,418)	\$ 747,780	\$ (160,229)
Alternative investment funds	-	-	1,543,651	(430,058)	1,543,651	(430,058)
Mutual funds	3,788,645	(140,895)	5,542,242	(884,964)	9,330,887	(1,025,859)
Total	<u>\$ 4,430,435</u>	<u>\$ (282,706)</u>	<u>\$ 7,191,883</u>	<u>\$ (1,333,440)</u>	<u>\$ 11,622,318</u>	<u>\$ (1,616,146)</u>

  

2010	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Equity securities	\$ 545,273	\$ (46,997)	\$ 78,244	\$ (7,811)	\$ 623,517	\$ (54,808)
Alternative investment funds	-	-	1,765,125	(443,584)	1,765,125	(443,584)
Mutual funds	-	-	2,459,293	(131,741)	2,459,293	(131,741)
Total	<u>\$ 545,273</u>	<u>\$ (46,997)</u>	<u>\$ 4,302,662</u>	<u>\$ (583,136)</u>	<u>\$ 4,847,935</u>	<u>\$ (630,133)</u>

In 2011 and 2010, none of the investments that were in an unrealized loss position were considered to be other than temporarily impaired.

Investment income is comprised of the following for the years ended September 30, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Income:		
Dividend and interest income	\$ 586,562	\$ 573,473
Net realized gains on investments	<u>140,830</u>	<u>37,303</u>
Total investment return	<u>\$ 727,392</u>	<u>\$ 610,776</u>
Other changes in unrestricted net assets:		
Unrealized (losses) gains on other than trading securities	<u>\$ (1,132,499)</u>	<u>\$ 1,508,283</u>

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 4 - Investments (continued)**

*Investments in Joint Ventures* - The Association has a fifty percent ownership interest in Fitness & Wellness and effective in fiscal 2010, a fifty percent ownership interest in GSHC. The Association accounts for its investment interest in these entities using the equity method of accounting.

The Association's share of Fitness & Wellness's net loss for the years ended September 30, 2011 and 2010 was \$118,629 and \$107,264, respectively. In addition, the Association made a capital contribution to Fitness & Wellness of \$30,601 and \$156,955 during the fiscal years ending September 30, 2011 and 2010, respectively. The carrying amount of the Fitness & Wellness investment was \$486,566 and \$574,594 as of September 30, 2011 and 2010, respectively and is included in other assets.

The Association's share of GSHC's net gain for the year ended September 30, 2011 and 2010 was \$113,325 and \$14,449, respectively. The Association has a receivable of \$102,213 due from GSHC for a capital distribution, which is included within other current assets on the accompanying consolidated balance sheets. In addition, the Association made a capital contribution to GSHC of \$75,000 during the fiscal year ending September 30, 2010. The carrying amount of the GSHC investment was \$100,562 and \$89,449 as of September 30, 2011 and 2010, respectively and is included in other assets.

**Note 5 - Fair Value Measurements**

FASB ASC 820-10, "*Fair Value Measurements and Disclosures*", provides a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under FASB ASC 820-10 are described as follows:

*Level 1* - Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Association has the ability to access.

*Level 2* - Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has specified (contractual) terms, the Level 2 input must be observable for substantially the full term of the asset or liability.

*Level 3* - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

The Association's valuation methodologies used to measure financial assets and liabilities at fair value are outlined below. Where applicable, the Association uses quoted prices in active markets for identical assets and liabilities to determine fair value (Level 1 inputs). This pricing methodology applies to cash and cash equivalents, equities, money market funds and mutual funds.



**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 5 - Fair Value Measurements (continued)**

If quoted prices in active markets for identical assets and liabilities are not available, then quoted prices for similar assets and liabilities, quoted prices for identical assets or liabilities in inactive markets or inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly, will be used to determine fair value (Level 2 inputs). Securities typically priced using Level 2 inputs include government securities, corporate bonds and certificates of deposit.

Assets and liabilities that are valued using significant unobservable inputs, such as extrapolated data, proprietary models, or indicative quotes that cannot be corroborated with market data are classified in Level 3 within the fair value hierarchy. The Association's beneficial interest in trusts are classified within the Level 3 classification. The value of the Association's assets is based on total fund values and the Association's corresponding beneficiary percentage.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Association believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table presents the financial instruments carried at fair value as of September 30, 2011 by the valuation hierarchy:

<u>2011</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Assets:				
Cash and cash equivalents	\$ 884,695	\$ -	\$ -	\$ 884,695
Investments:				
Cash and money market funds	318,590	-	-	318,590
Alternative investment funds	-	2,047,429	-	2,047,429
Equity securities	5,164,432	-	-	5,164,432
Mutual funds - fixed income	5,786,021	-	-	5,786,021
Mutual funds - equity	5,906,574	-	-	5,906,574
Total	<u>17,175,617</u>	<u>2,047,429</u>	-	<u>19,223,046</u>
Investments held for captive insurance liabilities:				
Mutual funds - fixed income	47,232	896,974	-	944,206
Mutual funds - equity	269,369	-	-	269,369
Fixed income securities	-	2,303,649	-	2,303,649
Total	<u>316,601</u>	<u>3,200,623</u>	-	<u>3,517,224</u>
Funds held under bond agreements	179,780	-	-	179,780
Beneficial interest in trusts	-	-	9,748,956	9,748,956
Total	<u>\$ 18,556,693</u>	<u>\$ 5,248,052</u>	<u>\$ 9,748,956</u>	<u>\$ 33,553,701</u>
Liabilities:				
Interest rate swap liability	\$ -	\$ 4,155,222	\$ -	\$ 4,155,222
Total	<u>\$ -</u>	<u>\$ 4,155,222</u>	<u>\$ -</u>	<u>\$ 4,155,222</u>

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 5 - Fair Value Measurements (continued)**

The following table presents the financial instruments carried at fair value as of September 30, 2010 by the valuation hierarchy:

<u>2010</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Assets:				
Cash and cash equivalents	\$ 2,376,012	\$ -	\$ -	\$ 2,376,012
Investments:				
Cash and money market funds	181,621	-	-	181,621
Alternative investment funds	-	1,765,125	-	1,765,125
Equity securities	2,381,487	-	-	2,381,487
Mutual funds - fixed income	6,468,723	-	-	6,468,723
Mutual funds - equity	11,162,268	-	-	11,162,268
Total	<u>20,194,099</u>	<u>1,765,125</u>	<u>-</u>	<u>21,959,224</u>
Investments held for captive insurance liabilities:				
Mutual funds - fixed income	1,684,799	175,510	-	1,860,309
Mutual funds - equity	-	307,038	-	307,038
Fixed income securities	-	1,742,649	-	1,742,649
Total	<u>1,684,799</u>	<u>2,225,197</u>	<u>-</u>	<u>3,909,996</u>
Funds held under bond agreements	171,783	-	-	171,783
Beneficial interest in trusts	-	-	10,168,420	10,168,420
Total	<u>\$ 22,741,894</u>	<u>\$ 1,765,125</u>	<u>\$ 10,168,420</u>	<u>\$ 34,675,439</u>
Liabilities:				
Interest rate swap liability	<u>\$ -</u>	<u>\$ 3,647,029</u>	<u>\$ -</u>	<u>\$ 3,647,029</u>
Total	<u>\$ -</u>	<u>\$ 3,647,029</u>	<u>\$ -</u>	<u>\$ 3,647,029</u>

As of September 30, 2011 and 2010, the Association's other financial instruments included accounts receivable, pledges receivable, accounts payable and accrued expenses, line of credit, estimated third-party payer settlements, captive insurance reserves, long-term debt and capital lease obligations. The carrying amounts reported in the consolidated balance sheets for these financial instruments approximate their fair value.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 5 - Fair Value Measurements (continued)**

The following are the changes within the beneficial interest in trusts for the years ended September 30, 2011 and 2010, which are classified as Level 3 within the fair value hierarchy:

	<b>2011</b>
Balance as of October 1, 2010	\$ 10,168,420
Net change in market value	48,072
Distributions	(467,536)
Balance as of September 30, 2011	\$ 9,748,956
	<b>2010</b>
Balance as of October 1, 2009	\$ 9,943,906
Net change in market value	595,433
Distributions	(370,919)
Balance as of September 30, 2010	\$ 10,168,420

**Note 6 - Property, Plant and Equipment**

Property, plant and equipment consist of the following as of September 30, 2011 and 2010:

	<b>2011</b>	<b>2010</b>
Land and improvements	\$ 3,567,551	\$ 3,617,551
Buildings and improvements	57,358,538	57,319,835
Fixed and moveable equipment	32,234,859	31,241,896
	93,160,948	92,179,282
Less: accumulated depreciation and amortization	(51,406,912)	(47,976,690)
	41,754,036	44,202,592
Construction in progress	183,550	-
Total	\$ 41,937,586	\$ 44,202,592

Depreciation expense for the years ended September 30, 2011 and 2010 amounted to \$3,455,220 and \$3,405,282, respectively. Amortization expense for equipment under capital lease obligations was \$416,990 and \$428,820 as of September 30, 2011 and 2010, respectively.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 7 - Other Assets**

Other assets as of September 30, 2011 and 2010 are as follows:

	<b>2011</b>	<b>2010</b>
Investment in Fitness & Wellness	\$ 486,566	\$ 574,594
Investment in GSHC	100,562	89,449
Deferred financing costs	352,214	376,020
Goodwill	104,021	122,240
Deposits	42,726	19,609
Total	<b>\$ 1,086,089</b>	<b>\$ 1,181,912</b>

**Note 8 - Long-term Debt, Lines of Credit and Lease Arrangements**

**Lines of Credit** - The Association also had available a \$5,000,000 line of credit agreement, which was available for payment of costs associated with the construction of the 36-bed inpatient pavilion. On January 30, 2009, the Association converted this line of credit to a line of credit note in the amount of \$1,625,000. As of September 30, 2011 and 2010, the Association had \$450,000 and \$1,025,000, respectively, outstanding on this line of credit note. Borrowings on the line of credit note are payable in annual installments with the final payment due on July 3, 2012. At the Association's option, the line of credit note bears interest at the bank's prime rate, as defined, plus 150 basis points or LIBOR plus 175 basis points.

**Long-term Obligations** - The Association had a \$3,000,000 line of credit agreement, which was renewable on an annual basis. On January 30, 2009, the Association converted this line of credit into a term loan promissory note whereby the \$3,000,000 is payable in equal monthly installments of \$50,000 with a final payment on January 31, 2014. At the Association's option, the term loan promissory note bears interest at the bank's prime rate, as defined, or LIBOR plus 100 basis points. As of September 30, 2011 and 2010, the Association had \$1,400,000 and \$2,000,000, respectively, outstanding on this term loan.

In April 2007, the Association, in conjunction with the State of Connecticut Health and Educational Facilities Authority (CHEFA), issued \$21,530,000 of Gaylord Hospital Series B variable rate demand revenue bonds (the Series B Bonds). The bond proceeds were used to refinance the amounts outstanding on the CHEFA Series A revenue bonds and for the construction of a 36-bed addition.

The Series B Bonds bear interest at a variable rate as determined by a re-marketing agent (approximately 0.3% as of September 30, 2011 and 2010), which is adjusted weekly, and matures on July 1, 2037. For as long as the bonds are variable rate, the bond holders have the option to tender their bonds for repayment. The Association has a letter of credit from Bank of America, N.A., which is available to support its obligations under the Series B Bonds during this period. The letter of credit expires on July 3, 2012, subject to extension or earlier termination upon the occurrence of certain events set forth in the letter of credit agreement. At that time, the letter of credit can be renewed, at the bank's discretion, the Association can convert the bonds to a fixed rate or repurchase the bonds outstanding on that date at their par value. Tenders made by bond holders will be remarketed or, if necessary, paid by the drawdowns on the letter of credit. Any tender drawings made under the letter of credit are to be repaid by the Association on the expiration date of the letter of credit. As of September 30, 2011 and 2010, the Association had \$19,135,000 and \$19,775,000, respectively, outstanding on the Series B Bonds.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 8 - Long-term Debt, Lines of Credit and Lease Arrangements (continued)**

The Series B loan and letter of credit agreements include certain financial covenants including a minimum debt service coverage ratio of 1.25 to 1, a liquidity to debt ratio of 30%, and other restrictions, including limitations on future indebtedness and liens. The Association was in compliance with all covenants for 2011 and 2010.

**Lease Abandonment Obligations** - During 2010, the Association recorded a loss on abandonment of a long-term rental property in the amount of \$147,543. The lease was previously accounted for as an operating lease and the Association was no longer utilizing the rental property and is unable to sublease the property. Consequently, the Association's liability represents the present value of future minimum lease payments under this lease of \$78,857 as of September 30, 2011. The lease expires in January 2013.

During 2009, the Association recorded a loss on abandonment of a long-term rental property in the amount of \$92,035. The lease was previously accounted for as an operating lease and the Association was no longer utilizing the rental property and is unable to sublease the property. Consequently, the Association's liability represents the present value of future minimum lease payments under this lease of \$27,650 as of September 30, 2011. The lease expires in December 2013.

**Letter of Credit** - As a result of being self-funded for its workers' compensation program, the Association is required by the State of Connecticut Workers' Compensation Commission to hold a letter of credit in the aggregate amount of \$650,000 as of September 30, 2011 and 2010. As of September 30, 2011 and 2010, there was no outstanding balances on the letter of credit.

**Capital Lease Obligations** - The Association leases certain equipment and software under capital lease obligations, expiring through December 2019. Future payments, including interest are as follows:

2012	\$	162,674
2013		162,674
2014		45,096
2015		21,580
2016		21,580
Thereafter		68,337
Less: interest		(65,897)
Total	\$	416,044

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 8 - Long-term Debt, Lines of Credit and Lease Arrangements (continued)**

A summary of long-term debt and capital lease obligations as of September 30, 2011 and 2010 are as follows:

	<b>2011</b>	<b>2010</b>
Long-term debt obligation	<b>\$ 19,135,000</b>	\$ 19,775,000
Term loan promissory note	<b>1,400,000</b>	2,000,000
Capital lease obligations	<b>416,044</b>	545,613
Lease abandonment obligation	<b>106,507</b>	219,038
	<b>21,057,551</b>	22,539,651
Less: current portion	<b>(1,487,242)</b>	(1,453,373)
Total	<b>\$ 19,570,309</b>	\$ 21,086,278

Scheduled principal repayments on the long-term debt and capital lease obligations as of September 30, 2011 are as follows:

2012	\$ 1,487,242
2013	1,464,924
2014	972,905
2015	775,165
2016	806,367
Thereafter	15,550,948
Total	\$ 21,057,551

**Operating Leases** - The Association leases various equipment and space under operating leases expiring at various dates and month-to-month agreements. Some of these leases contain renewal options. Rent expense under such operating leases and agreements was \$490,304 and \$746,945, in 2011 and 2010, respectively. The following is a schedule of future minimum payments under non-cancellable operating leases as of September 30, 2011:

2012	\$ 381,520
2013	388,490
2014	388,490
2015	394,034
2016	354,571
Thereafter	583,070
Total	\$ 2,490,175

In addition, the Association leases land under a long-term lease agreement through 2106 to a third-party. Rental income is based on a percentage of the gross income earned by the lessee. Total rental income from this property was \$182,096 and \$224,058 for 2011 and 2010, respectively and is included in other operating revenue in the accompanying consolidated statements of operations and changes in net assets.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 9 - Derivatives**

The Association uses derivative instruments, specifically an interest rate swap, to manage its exposure to changes in the interest rate on its CHEFA debt. The use of derivative instruments exposes the Association to additional risks related to the derivative instrument, including market risk, credit risk and termination risk as described below, and the Association has defined risk management practices to mitigate these risks, as appropriate.

Market risk represents the potential adverse effect on the fair value and cash flow of a derivative instrument due to changes in interest rates or rate spreads. Market risk is managed through ongoing monitoring of interest rate exposure based on set parameters regarding the type and degree of market risk that the Association will accept. Credit risk is the risk that the counterparty on a derivative instrument may be unable to perform its obligation during the term of the contract. When the fair value of a derivative contract is positive, the counterparty owes the Association, which creates credit risk. Credit risk is managed by setting stringent requirements for qualified counterparties at the date of execution of a derivative transaction and requiring counterparties to post collateral in the event of a credit rating downgrade or if the fair value of the derivative contract exceeds a negotiated threshold.

Termination risk represents the risk that the Association may be required to make a significant payment to the counterparty, if the derivative contract is terminated early. Termination risk is assessed at onset by performing a statistical analysis of the potential for a significant termination payment under various scenarios designed to encompass expected interest rate changes over the life of the proposed contract. The test measures the ability to make a termination payment without a significant impairment to the Association's ability to meet its debts or liquidity covenants.

On August 1, 2007, the Association entered into an interest rate swap agreement with an initial notional amount of \$21,530,000 to reduce the exposure to fluctuations in interest rates related to its CHEFA debt. The swap agreement, which expires in June 2027, requires that the Association make monthly payments to the counter-party, Bank of America, N.A., based upon a fixed interest rate of 4.28% and in return receives monthly payments from Bank of America, N.A. based on the Bond Index Association Municipal Swap Rate Index rate (0.16% and 0.27% as of September 30, 2011 and 2010, respectively). The notional amount is scheduled to decrease as principal is paid on the CHEFA debt. Net amounts paid under the swap is recorded as additional interest expense. Based on information received from the counter-party, the swap agreement had an unfavorable fair value of \$4,155,222 and \$3,647,029 as of September 30, 2011 and 2010, respectively.

Management has not designated the swap agreement as a hedging instrument. The change in fair value of the interest rate swap of \$508,193 and \$1,014,191 for the years ended September 30, 2011 and 2010, respectively, is recorded in the consolidated statements of operations and changes in net assets as a component of non-operating income.

**Note 10 - Net Assets**

Temporarily restricted net assets are available for the following purposes as of September 30, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Health care services:		
Patient special needs	\$ 11,506	\$ 16,926
Other restricted purposes	498,966	580,586
Capital campaign	<u>696,762</u>	<u>1,184,306</u>
Total	<u>\$ 1,207,234</u>	<u>\$ 1,781,818</u>

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 10 - Net Assets (continued)**

The assets in the above table restricted for health care services are included within cash and cash equivalents on the accompanying consolidated balance sheets.

Permanently restricted net assets are restricted to the following purposes as of September 30, 2011 and 2010:

	<b>2011</b>	<b>2010</b>
Investments to be held in perpetuity, the income of which is expendable to support patient special needs and other services	<b>\$ 5,529,789</b>	\$ 5,500,469
Beneficial interest in trusts held by others, the income of which is expendable to support other health care services	<b>9,748,956</b>	10,168,420
Total	<b><u>\$ 15,278,745</u></b>	<b><u>\$ 15,668,889</u></b>

The Association's endowment consists of multiple funds established for a variety of purposes. The endowment includes both donor-restricted endowment fund and funds designated by the Board of Directors to function as endowments. As required by GAAP, net assets associated with endowment funds, included funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor restrictions.

The Association has interpreted the relevant laws as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Association during its annual budgeting process.

The Association considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the fund; (2) the purposes of the Association and the donor-restricted endowment fund; (3) general economic conditions; (4) the possible effect of inflation and deflation; (5) the expected total return from income and the appreciation of investments; (6) other resources of the Association; and (7) the investment policies of the Association.



**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 10 - Net Assets (continued)**

Changes in net assets for endowments and temporary restricted funds for the year ended September 30, 2011 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance at October 1, 2010	\$ 16,458,755	\$ 597,512	\$ 5,500,469	\$ 22,556,736
Investment return:				
Investment income	586,562	-	-	586,562
Net change in market value	(1,321,431)	-	-	(1,321,431)
Contributions	-	187,488	29,320	216,808
Expenditures	(2,030,629)	(274,528)	-	(2,305,157)
Balance at September 30, 2011	<u>\$ 13,693,257</u>	<u>\$ 510,472</u>	<u>\$ 5,529,789</u>	<u>\$ 19,733,518</u>

Changes in net assets for endowments and temporary restricted funds for the year ended September 30, 2010 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance at October 1, 2009	\$ 16,195,439	\$ 365,661	\$ 4,986,216	\$ 21,547,316
Investment return:				
Investment income	573,473	-	-	573,473
Net change in market value	1,856,279	-	-	1,856,279
Contributions	-	500,053	514,253	1,014,306
Expenditures	(2,166,436)	(268,202)	-	(2,434,638)
Balance at September 30, 2010	<u>\$ 16,458,755</u>	<u>\$ 597,512</u>	<u>\$ 5,500,469</u>	<u>\$ 22,556,736</u>

**Funds with Deficiencies** - From time to time the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or relevant law requires the Association to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature are reported in unrestricted net assets. As of September 30, 2011 and 2010, there were no funds that were below the level required by donor or law.

**Return Objectives and Risk Parameters** - The Association's investment and spending policies for endowment assets attempts to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of the S&P 500 index while assuming a moderate level of investment risk.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 10 - Net Assets (continued)**

*Strategies Employed for Achieving Objectives* - To satisfy its long-term rate-of-return objectives, the Association relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Board targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

*Spending Policy* - During its annual budgeting process, the Association appropriates donor restricted endowment funds for expenditure in accordance with donor purpose and time restrictions. During the year ended September 30, 2011 and 2010, the Board appropriated \$2,030,629 and \$2,166,436, respectively of funds for expenditure from its board restricted endowment funds. The board restricted endowment funds are being held for long-term growth and to maintain capital reserves for the Association.

**Note 11 - Pension Plans**

The Association has a noncontributory, defined benefit plan (the Plan). The benefits are based on years of service and an average of the five consecutive calendar years of highest compensation during the last ten years of employment. The Association makes contributions in amounts sufficient to fund the Plan as required by ERISA. The Plan was frozen effective October 31, 2004.

The following summarizes significant disclosures relating to the Plan as of September 30, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
<b>Change in benefit obligations:</b>		
Benefit obligations at beginning of year	\$ 34,102,808	\$ 32,562,858
Interest cost	1,712,734	1,720,670
Service cost	250,000	210,000
Actuarial loss	2,410,259	1,486,630
Expected administrative expenses	(250,000)	(210,000)
Benefits and plan expenses paid	<u>(2,058,129)</u>	<u>(1,667,350)</u>
Benefit obligations at end of year	<u>\$ 36,167,672</u>	<u>\$ 34,102,808</u>
<b>Change in plan assets:</b>		
Fair value of plan assets at beginning of year	\$ 19,013,691	\$ 17,668,518
Actual return on plan assets	418,501	1,985,069
Employer contributions	1,669,458	1,244,534
Benefits and plan expenses paid	(2,058,129)	(1,667,350)
Administrative expenses	<u>(318,469)</u>	<u>(217,080)</u>
Fair value of plan assets at end of year	<u>\$ 18,725,052</u>	<u>\$ 19,013,691</u>
<b>Accrued pension liability:</b>		
Unfunded status	<u>\$ (17,442,620)</u>	<u>\$ (15,089,117)</u>

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 11 - Pension Plans (continued)**

	<u>2011</u>	<u>2010</u>
<b>Net periodic benefit cost:</b>		
Interest cost	\$ 1,712,734	\$ 1,720,670
Service cost	250,000	210,000
Actuarial loss recognized	302,929	192,673
Expected return on plan assets	<u>(1,426,234)</u>	<u>(1,479,687)</u>
Net periodic benefit cost	<u>\$ 839,429</u>	<u>\$ 643,656</u>

Benefits expected to be paid over the next five years and the five years thereafter are as follows:

2012	\$ 2,834,325
2013	\$ 2,179,839
2014	\$ 2,930,510
2015	\$ 2,223,729
2016	\$ 2,817,466
Years 2017-2021	\$ 13,623,531

Amounts recorded in unrestricted net assets as of September 30, 2011 and 2010, not yet amortized as components of net periodic benefit cost are as follows:

	<u>2011</u>	<u>2010</u>
Unamortized actuarial loss	<u>\$ 18,168,312</u>	<u>\$ 14,984,780</u>

The amortization of the above items expected to be recognized in net periodic benefit income for the year ended September 30, 2012 is \$446,966.

The following summarizes the key weighted-average actuarial assumptions used in determining the Plan's benefit obligation and net benefit income:

	<u>2011</u>	<u>2010</u>
<b>Benefit obligations</b>		
Discount rate	4.75%	5.25%
<b>Net periodic benefit cost</b>		
Discount rate	5.25%	5.50%
Expected long-term return on plan assets	6.80%	6.80%

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 11 - Pension Plans (continued)**

The fair values of the Association's Plan assets, by asset category are as follows, for the year ending September 30, 2011 and 2010:

<u>2011</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Money market securities	\$ 634,938	\$ -	\$ -	\$ 634,938
Mutual funds - fixed income	8,943,175	-	-	8,943,175
Mutual funds - equities	3,982,364	-	-	3,982,364
Equity securities	4,586,904	-	-	4,586,904
Other	-	-	577,671	577,671
	<u>                    </u>	<u>                    </u>	<u>                    </u>	<u>                    </u>
Total	<u>\$ 18,147,381</u>	<u>\$ -</u>	<u>\$ 577,671</u>	<u>\$ 18,725,052</u>
	<u>                    </u>	<u>                    </u>	<u>                    </u>	<u>                    </u>
<u>2010</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Money market securities	\$ 596,818	\$ -	\$ -	\$ 596,818
Mutual funds - fixed income	7,971,893	-	-	7,971,893
Mutual funds - equities	4,713,643	-	-	4,713,643
Equity securities	5,070,215	-	-	5,070,215
Other	-	-	661,122	661,122
	<u>                    </u>	<u>                    </u>	<u>                    </u>	<u>                    </u>
Total	<u>\$ 18,352,569</u>	<u>\$ -</u>	<u>\$ 661,122</u>	<u>\$ 19,013,691</u>
	<u>                    </u>	<u>                    </u>	<u>                    </u>	<u>                    </u>

The level 3 investments decreased \$83,451 and increased \$95,958 during 2011 and 2010, respectively, due to changes in market values.

The Association's investment policy is to minimize risk by balancing investments between equity securities and fixed income debt securities, utilizing a weighted average approach with a minimum split of 60% equity securities and 40% fixed income debt securities and a maximum split of 80% equity securities and 20% fixed income debt securities. The expected return on plan assets assumption was determined based on a review of the Plan's asset mix, capital market assumptions, and a review of the actual return on plan assets over the past ten years.

The Association has a defined contribution benefit plan, which became effective January 1, 2005. Substantially all full time employees are eligible to participate in the defined contribution plan. The Association made contributions to this plan totaling \$971,397 and \$650,537 in 2011 and 2010, respectively. Employees become vested in the Association's contributions in three to five years. The portion of the employees contributions unvested upon termination are forfeited and used to reduce future contributions made by the Association on a dollar-for-dollar basis.

The Association also has established a 403(b) plan. Participants may elect to contribute a specific percentage of their compensation in pre-tax deferrals subject to established Internal Revenue Code limitations. Currently, the Association does not contribute to this plan.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 11 - Pension Plans (continued)**

The Association also has a supplemental retirement plan agreement with a senior executive. The obligation related to this agreement is approximately \$1,067,000 and \$828,000 as of September 30, 2011 and 2010, respectively, and is recorded within accounts payable and accrued expenses within the accompanying consolidated balance sheets.

**Note 12 - Functional Expenses**

The Association provides health care services to residents within its geographic location. Expenses related to providing these services for the years ended September 30, 2011 and 2010 is as follows:

	<b>2011</b>	<b>2010</b>
Health care services	\$ <b>54,890,641</b>	\$ 55,228,965
General and administrative	<b>15,821,689</b>	15,004,397
Fundraising	<b>638,760</b>	625,089
Total	<b>\$ 71,351,090</b>	\$ 70,858,451

**Note 13 - Captive Insurance Activities**

Effective January 1, 2008, GRS provided commercial and general liability coverage on a claims made basis to the Association. The coverage limits for the Association were \$1,000,000 per claim with an annual aggregate of \$4,000,000, plus \$100,000 each incident in the event the aggregate is fully eroded. There is no aggregate limit for the commercial general liability.

Effective January 1, 2008, GRS provided an umbrella liability claims-made policy with a limit of \$10,000,000 each claim and in the aggregate. GRS has fully reinsured this coverage with a highly rated commercial reinsurance carrier.

Effective January 1, 2008, GRS assumed through a loss portfolio transfer the outstanding loss obligations produced by CHCP, which covered incidents of healthcare professional liability and commercial general liability occurring at the Association from April 1, 2003 through December 31, 2007. The amount of the loss portfolio transfer was \$1,482,688.

During the year ended September 30, 2011, GRS issued a return premium in the amount of \$675,000 to the Association. This return premium remains unpaid at September 30, 2011 and is reflected within due from affiliates on the accompanying consolidating balance sheet of the Hospital and is eliminated in consolidation.

A reconciliation of direct to net premiums on a written and earned basis is summarized as follows for year ended September 30, 2011 and 2010:

	<b>Premium Written</b>		<b>Premium Earned</b>	
	<b>2011</b>	<b>2010</b>	<b>2011</b>	<b>2010</b>
Direct premiums	\$ <b>201,875</b>	\$ 993,750	\$ <b>197,188</b>	\$ 939,465
Ceded premiums	<b>(325,000)</b>	(340,000)	<b>(332,500)</b>	(364,465)
Total	<b>\$ (123,125)</b>	\$ 653,750	<b>\$ (135,312)</b>	\$ 575,000

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 13 - Captive Insurance Activities (continued)**

The liability for unpaid losses and loss adjustment expenses is included within captive insurance loss and other reserves on the accompanying consolidated balance sheets. Activity in the liability for unpaid losses and loss adjustment expenses is summarized as follows for the year ended September 30, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Balance at beginning of the year	\$ 2,615,549	\$ 2,626,498
Less: reinsurance recoverables	<u>(757,650)</u>	<u>(698,135)</u>
Net balance beginning of the year	1,857,899	1,928,363
Incurred related to:		
Current year	333,402	717,430
Prior years	<u>(474,602)</u>	<u>(560,304)</u>
Total incurred	<u>(141,200)</u>	157,126
Paid related to:		
Current year	-	(1,039)
Prior years	<u>(6,974)</u>	<u>(226,551)</u>
Total paid	<u>(6,974)</u>	<u>(227,590)</u>
Net balance at end of year	1,709,725	1,857,899
Plus: reinsurance recoverables	<u>678,921</u>	<u>757,650</u>
Balance at the end of the year	<u>\$ 2,388,646</u>	<u>\$ 2,615,549</u>

As a result of changes in estimates of insured events in prior years, the provision for losses and loss adjustment expenses decreased by \$474,602 and \$560,304 in 2011 and 2010, respectively.

The above liability for loss and loss adjustment expenses have been determined using a 4% discount rate. The ultimate settlement of losses may vary significantly from the reserves recorded. In particular, ultimate settlements on medical malpractice claims depend, among other things, on the resolution of litigation, the outcome of which is difficult to predict. Also, since the reserves have been discounted, there is the possibility that the timing of loss payments and income earned on invested assets will be significantly different than anticipated.

Included on the accompanying consolidated balance sheets is a reinsurance recoverable of \$678,921 and \$757,650 as of September 30, 2011 and 2010, respectively, which is due from one reinsurer. GRS continually evaluates the reinsurer's financial condition. There can be no assurance that reinsurance will continue to be available to GRS to the same extent, and at the same cost, as it has in the past. GRS may choose in the future to reevaluate the use of reinsurance to increase or decrease the amounts of risk it cedes to reinsurers.

**Gaylord Farm Association, Inc.**  
**Notes to the Consolidated Financial Statements**  
**For the Years Ended September 30, 2011 and 2010**

**Note 14 - Commitments and Contingencies**

The Association is involved in various legal actions arising in the normal course of activities. Although the ultimate outcome is not determinable at this time, management, after taking into consideration advice of legal counsel, believes that the resolution of these pending matters will not have a material adverse effect, individually or in the aggregate, upon the Association's financial condition.

ASC 410-20 "Accounting for Asset Retirement Obligations" addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets such as facilities containing asbestos, when the amount of the liability can be reasonably estimated. No Asset Retirement Obligation (ARO) has been established as of September 30, 2011 and 2010, as no plans to renovate or sell any facility, or area within, with significant asbestos have been identified and therefore no settlement date has been determined. Management will continue to evaluate its exposure to asbestos removal and establish an ARO for the fair value of the associated costs once sufficient information has been obtained and a settlement date has been determined. Management does not believe that the liability is material to the overall consolidated financial results of the Association.

**Note 15 - Risks and Uncertainties**

Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the consolidated statements of financial position.

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

**Note 16 - Pledges Receivable**

Pledges receivable represent unconditional promises to give for the 36-bed addition. The following pledges are due to the Association as of September 30, 2011:

Due within one year	\$	386,657
Due in one to five years		387,523
		774,180
Less: allowance for uncollectible pledges		(77,418)
Total	\$	696,762

**Note 17 - Supplemental Cash Flow Disclosures**

The Association paid interest in the amount of \$919,764 and \$966,853 for the years ended September 30, 2011 and 2010, respectively. In addition, the Association acquired equipment by incurring capital lease obligations of \$151,500 during the year ended September 30, 2010.

**Gaylord Farm Association, Inc.**  
**Consolidating Balance Sheet**  
**September 30, 2011**

	<u>Gaylord Hospital, Inc.</u>	<u>Gaylord Risk Solutions, Ltd.</u>	<u>Gaylord Farm Rehabilitation Center</u>	<u>Gaylord Research Institute, Inc.</u>	<u>Eliminations</u>	<u>Gaylord Farm Association, Inc.</u>
<b>Assets</b>						
Current assets:						
Cash and cash equivalents	\$ 487,626	\$ 397,069	\$ -	\$ -	\$ -	\$ 884,695
Patient accounts receivable (less allowance of \$503,000)	10,001,815	-	-	-	-	10,001,815
Assets whose use is limited:						
Assets held under bond indenture agreement	179,780	-	-	-	-	179,780
Pledges receivable	386,657	-	-	-	-	386,657
Due from affiliates	2,543,065	-	-	1,972	(2,545,037)	-
Other current assets	1,183,998	760,853	-	-	-	1,944,851
Total current assets	<u>14,782,941</u>	<u>1,157,922</u>	<u>-</u>	<u>1,972</u>	<u>(2,545,037)</u>	<u>13,397,798</u>
Assets whose use is limited:						
Pledges receivable	310,105	-	-	-	-	310,105
Board-designated investments	13,693,257	-	-	-	-	13,693,257
Donor restricted investments	5,529,789	-	-	-	-	5,529,789
Beneficial interest in trusts held by others	9,748,956	-	-	-	-	9,748,956
	<u>29,282,107</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>29,282,107</u>
Property, plant and equipment, net	41,937,586	-	-	-	-	41,937,586
Investments held for captive insurance liabilities	-	3,517,224	-	-	-	3,517,224
Reinsurance recoverable relating to captive insurance liabilities	-	678,921	-	-	-	678,921
Other assets	1,086,089	-	-	-	-	1,086,089
Total assets	<u>\$ 87,088,723</u>	<u>\$ 5,354,067</u>	<u>\$ -</u>	<u>\$ 1,972</u>	<u>\$ (2,545,037)</u>	<u>\$ 89,899,725</u>
<b>Liabilities, Net Assets and Shareholder's Equity</b>						
Current liabilities:						
Accounts payable and accrued expenses	\$ 4,805,123	\$ 48,868	\$ -	\$ -	\$ -	\$ 4,853,991
Accrued payroll and related taxes	3,819,490	-	-	-	-	3,819,490
Line of credit	450,000	-	-	-	-	450,000
Due to affiliates	-	675,000	1,870,037	-	(2,545,037)	-
Estimated amounts due to third-party payers	246,805	-	-	-	-	246,805
Current portion of accrued pension obligation	2,743,352	-	-	-	-	2,743,352
Current portion of long-term debt and capital lease obligations	1,487,242	-	-	-	-	1,487,242
Total current liabilities	<u>13,552,012</u>	<u>723,868</u>	<u>1,870,037</u>	<u>-</u>	<u>(2,545,037)</u>	<u>13,600,880</u>
Long-term debt and capital lease obligations, less current portion	19,570,309	-	-	-	-	19,570,309
Accrued pension obligation	14,699,268	-	-	-	-	14,699,268
Captive insurance loss and other reserves	-	2,827,083	-	-	-	2,827,083
Interest rate swap liability	4,155,222	-	-	-	-	4,155,222
Total liabilities	<u>51,976,811</u>	<u>3,550,951</u>	<u>1,870,037</u>	<u>-</u>	<u>(2,545,037)</u>	<u>54,852,762</u>
Net assets and shareholder's equity:						
Unrestricted	18,625,933	-	(1,870,037)	1,972	-	16,757,868
Temporarily restricted	1,207,234	-	-	-	-	1,207,234
Permanently restricted	15,278,745	-	-	-	-	15,278,745
Shareholder's equity	-	1,803,116	-	-	-	1,803,116
Total net assets and shareholder's equity	<u>35,111,912</u>	<u>1,803,116</u>	<u>(1,870,037)</u>	<u>1,972</u>	<u>-</u>	<u>35,046,963</u>
Total liabilities, net assets and shareholder's equity	<u>\$ 87,088,723</u>	<u>\$ 5,354,067</u>	<u>\$ -</u>	<u>\$ 1,972</u>	<u>\$ (2,545,037)</u>	<u>\$ 89,899,725</u>

See accompanying Independent Auditors' Report.



**Gaylord Farm Association, Inc.**  
**Consolidating Balance Sheet**  
**September 30, 2010**

	<u>Gaylord Hospital, Inc.</u>	<u>Gaylord Risk Solutions, Ltd.</u>	<u>Gaylord Farm Rehabilitation Center</u>	<u>Gaylord Research Institute, Inc.</u>	<u>Eliminations</u>	<u>Gaylord Farm Association, Inc.</u>
<b>Assets</b>						
Current assets:						
Cash and cash equivalents	\$ 2,183,087	\$ 190,844	\$ -	\$ 2,081	\$ -	\$ 2,376,012
Patient accounts receivable (less allowance of \$540,000)	9,115,849	-	-	-	-	9,115,849
Assets whose use is limited:						
Assets held under bond indenture agreement	171,783	-	-	-	-	171,783
Pledges receivable	495,086	-	-	-	-	495,086
Due from affiliates	1,913,342	-	-	-	(1,913,342)	-
Other current assets	1,106,406	618,611	-	-	-	1,725,017
Total current assets	<u>14,985,553</u>	<u>809,455</u>	<u>-</u>	<u>2,081</u>	<u>(1,913,342)</u>	<u>13,883,747</u>
Assets whose use is limited:						
Pledges receivable	689,220	-	-	-	-	689,220
Board-designated investments	16,458,755	-	-	-	-	16,458,755
Donor restricted investments	5,500,469	-	-	-	-	5,500,469
Beneficial interest in trusts held by others	10,168,420	-	-	-	-	10,168,420
	<u>32,816,864</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>32,816,864</u>
Property, plant and equipment, net	44,202,592	-	-	-	-	44,202,592
Investments held for captive insurance liabilities	-	3,909,996	-	-	-	3,909,996
Reinsurance recoverable relating to captive insurance liabilities	-	757,650	-	-	-	757,650
Other assets	1,181,912	-	-	-	-	1,181,912
Total assets	<u>\$ 93,186,921</u>	<u>\$ 5,477,101</u>	<u>\$ -</u>	<u>\$ 2,081</u>	<u>\$ (1,913,342)</u>	<u>\$ 96,752,761</u>
<b>Liabilities, Net Assets and Shareholder's Equity</b>						
Current liabilities:						
Accounts payable and accrued expenses	\$ 5,065,117	\$ 35,220	\$ -	\$ -	\$ -	\$ 5,100,337
Accrued payroll and related taxes	3,375,454	-	-	-	-	3,375,454
Line of credit	1,025,000	-	-	-	-	1,025,000
Due to affiliates	-	207,318	1,706,024	-	(1,913,342)	-
Estimated amounts due to third-party payers	246,805	-	-	-	-	246,805
Current portion of accrued pension obligation	2,086,158	-	-	-	-	2,086,158
Current portion of long-term debt and capital lease obligations	1,453,373	-	-	-	-	1,453,373
Total current liabilities	<u>13,251,907</u>	<u>242,538</u>	<u>1,706,024</u>	<u>-</u>	<u>(1,913,342)</u>	<u>13,287,127</u>
Long-term debt and capital lease obligations, less current portion	21,086,278	-	-	-	-	21,086,278
Accrued pension obligation	13,002,959	-	-	-	-	13,002,959
Captive insurance reserves	-	3,049,299	-	-	-	3,049,299
Interest rate swap liability	3,647,029	-	-	-	-	3,647,029
Total liabilities	<u>50,988,173</u>	<u>3,291,837</u>	<u>1,706,024</u>	<u>-</u>	<u>(1,913,342)</u>	<u>54,072,692</u>
Net assets and shareholder's equity:						
Unrestricted	24,748,041	-	(1,706,024)	2,081	-	23,044,098
Temporarily restricted	1,781,818	-	-	-	-	1,781,818
Permanently restricted	15,668,889	-	-	-	-	15,668,889
Shareholder's equity	-	2,185,264	-	-	-	2,185,264
Total net assets and shareholder's equity	<u>42,198,748</u>	<u>2,185,264</u>	<u>(1,706,024)</u>	<u>2,081</u>	<u>-</u>	<u>42,680,069</u>
Total liabilities, net assets and shareholder's equity	<u>\$ 93,186,921</u>	<u>\$ 5,477,101</u>	<u>\$ -</u>	<u>\$ 2,081</u>	<u>\$ (1,913,342)</u>	<u>\$ 96,752,761</u>

See accompanying Independent Auditors' Report.

**Gaylord Farm Association, Inc.**  
**Consolidating Statement of Operations**  
**For the Year End September 30, 2011**

	<b>Gaylord Hospital, Inc.</b>	<b>Gaylord Risk Solutions, Ltd.</b>	<b>Gaylord Farm Rehabilitation Center</b>	<b>Gaylord Research Institute, Inc.</b>	<b>Eliminations</b>	<b>Gaylord Farm Association, Inc.</b>
Revenues:						
Net patient service revenue	\$ 66,776,439	\$ -	\$ 288,308	\$ -	\$ -	\$ 67,064,747
Contributions and bequests	913,165	-	-	-	-	913,165
Earned written premium	-	197,188	-	-	(197,188)	-
Ceded premium	-	(332,500)	-	-	-	(332,500)
Other operating revenue	507,069	-	130,599	-	-	637,668
Net assets released from restrictions used for operations	145,235	-	-	-	-	145,235
Total revenues	<u>68,341,908</u>	<u>(135,312)</u>	<u>418,907</u>	<u>-</u>	<u>(197,188)</u>	<u>68,428,315</u>
Expenses:						
Salaries and related expenses	46,226,152	-	597,339	-	-	46,823,491
Other operating expenses	5,951,429	178,205	60,013	-	(197,188)	5,992,459
Professional fees and contract services	6,587,269	-	-	-	-	6,587,269
Supplies	5,062,760	-	-	-	-	5,062,760
Depreciation and amortization	3,825,731	-	64,698	-	-	3,890,429
Occupancy costs	1,871,403	-	-	-	-	1,871,403
Provision for bad debts	344,715	-	-	-	-	344,715
Interest	912,115	-	7,649	-	-	919,764
Loss and loss adjustment expenses	-	(141,200)	-	-	-	(141,200)
Total expenses	<u>70,781,574</u>	<u>37,005</u>	<u>729,699</u>	<u>-</u>	<u>(197,188)</u>	<u>71,351,090</u>
Loss from operations	(2,439,666)	(172,317)	(310,792)	-	-	(2,922,775)
Other gains (losses):						
Dividend and interest income	536,089	50,473	-	-	-	586,562
Net realized gains on investments	140,830	-	-	-	-	140,830
Loss on equity investments	(5,304)	-	-	-	-	(5,304)
Change in fair value of interest rate swap agreement	(508,193)	-	-	-	-	(508,193)
Total other gains	<u>163,422</u>	<u>50,473</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>213,895</u>
Excess of revenues (under) over expenses	<u>\$ (2,276,244)</u>	<u>\$ (121,844)</u>	<u>\$ (310,792)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (2,708,880)</u>

See accompanying Independent Auditors' Report.

**Gaylord Farm Association, Inc.**  
**Consolidating Statement of Operations**  
**For the Year Ended September 30, 2010**

	<b>Gaylord Hospital, Inc.</b>	<b>Gaylord Risk Solutions, Ltd.</b>	<b>Gaylord Farm Rehabilitation Center</b>	<b>Gaylord Research Institute, Inc.</b>	<b>Eliminations</b>	<b>Gaylord Farm Association, Inc.</b>
Revenues:						
Net patient service revenue	\$ 67,358,336	\$ -	\$ 443,248	\$ -	\$ -	\$ 67,801,584
Contributions and bequests	872,470	-	-	-	-	872,470
Earned written premium	-	939,465	-	-	(939,465)	-
Ceded premium	-	(364,465)	-	-	-	(364,465)
Other operating revenue	546,935	-	130,599	-	-	677,534
Net assets released from restrictions used for operations	181,824	-	-	-	-	181,824
<b>Total revenues</b>	<b>68,959,565</b>	<b>575,000</b>	<b>573,847</b>	<b>-</b>	<b>(939,465)</b>	<b>69,168,947</b>
Expenses:						
Salaries and related expenses	44,842,364	-	591,379	-	-	45,433,743
Other operating expenses	6,108,261	159,092	64,157	-	(939,465)	5,392,045
Professional fees and contract services	6,624,882	-	-	-	-	6,624,882
Supplies	5,781,010	-	-	-	-	5,781,010
Depreciation and amortization	3,800,825	-	57,059	-	-	3,857,884
Occupancy costs	1,843,607	-	-	-	-	1,843,607
Provision for bad debts	802,494	-	-	-	-	802,494
Interest	957,629	-	8,031	-	-	965,660
Loss and loss adjustment expenses	-	157,126	-	-	-	157,126
<b>Total expenses</b>	<b>70,761,072</b>	<b>316,218</b>	<b>720,626</b>	<b>-</b>	<b>(939,465)</b>	<b>70,858,451</b>
(Loss) income from operations	(1,801,507)	258,782	(146,779)	-	-	(1,689,504)
Other (losses) gains:						
Dividend and interest income	503,940	69,533	-	-	-	573,473
Net realized gains on investments	37,303	-	-	-	-	37,303
Loss on equity investments	(92,815)	-	-	-	-	(92,815)
Change in fair value of interest rate swap agreement	(1,014,191)	-	-	-	-	(1,014,191)
Loss on lease abandonment	(147,543)	-	-	-	-	(147,543)
<b>Total other (losses) gains</b>	<b>(713,306)</b>	<b>69,533</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(643,773)</b>
Excess of revenues (under) over expenses	<u>\$ (2,514,813)</u>	<u>\$ 328,315</u>	<u>\$ (146,779)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (2,333,277)</u>

See accompanying Independent Auditors' Report.