Lawrence & Memorial Corporation and Subsidiaries

Consolidated Financial Statements
September 30, 2011 and 2010

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Report of Independent Auditors

To the Board of Directors of
Lawrence & Memorial Corporation

In our opinion, based on our audits and the report of other auditors, the accompanying consolidated balance sheets and the related consolidated statements of operations, changes in net assets, and cash flows present fairly, in all material respects, the financial position of Lawrence & Memorial Corporation (the "Corporation") and subsidiaries at September 30, 2011 and 2010 and the results of their operations, of their changes in net assets, and of their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of Visiting Nurses Association ("VNA") of Southeastern Connecticut, Inc., a wholly-owned subsidiary, whose statements as of September 30, 2011 and 2010 reflect total net assets constituting 6.0% and 5.5%, respectively, and total net revenues constituting 4.1% and 3.6%, respectively, of the related consolidated totals. Those statements have been audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to data included for VNA of Southeastern Connecticut, Inc., is based solely on the reports of the other auditors. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The consolidating information, on pages 25 through 30, is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position and results of operations of the individual organizations. Accordingly, we do not express an opinion on the financial position, results of operations, and changes in net assets, of the individual organizations. However, the consolidating information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and, in our opinion, based on our audits and the report of other auditors, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

PricewaterhouseCoopers LLP

December 16, 2011

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Lawrence & Memorial Corporation and Subsidiaries
Consolidated Balance Sheets
September 30, 2011 and 2010

	2011	2010
Assets		
Current assets		
Cash and cash equivalents	$ 44,580,932	$ 41,222,090
Investments	156,173,381	155,780,987
Patient accounts receivable, net of allowance for doubtful accounts of $7,901,271 and $7,673,848, respectively	32,212,263	32,328,543
Other receivables	4,594,541	6,025,606
Inventories	4,552,611	3,796,086
Due from affiliates	-	1,928
Prepaid expenses and other current assets	2,322,555	1,931,561
Debt service fund	1,109,892	1,248,032
Total current assets	245,546,175	242,334,833
Assets limited as to use		
Cash	179,900	179,215
Construction fund	8,427,695	-
Investments held in trust	11,241,951	11,986,573
Endowment investments	22,056,116	21,666,014
Funds held in trust by others	5,607,933	5,876,049
Contributions receivable	887,468	1,110,916
Fund held in escrow by agreement with State of Connecticut Health and Educational Facilities Authority and trustees	2,247,370	7,156,167
Total assets limited as to use	50,648,433	47,974,934
Deferred financing costs and other assets, net	1,938,833	1,330,365
Property, plant and equipment, net	134,658,395	112,579,230
	$ 432,791,836	$ 404,219,362
Liabilities and Net Assets		
Current liabilities		
Accounts payable	$ 24,115,376	$ 21,876,869
Accrued vacation and sick pay	11,705,811	11,220,455
Salaries, wages, payroll taxes and amounts withheld from employees	3,577,694	5,036,999
Due to affiliates	98,310	-
Due to third party payors	8,013,088	8,839,110
Other current liabilities	65,242	156,861
Current portion of long-term debt	3,202,481	2,906,408
Total current liabilities	50,778,002	50,036,702
Accrued pension and other postretirement benefits	43,423,221	52,135,334
Other liabilities	14,213,720	12,279,482
Long-term debt less current portion	82,249,920	62,148,146
Total liabilities	190,664,863	176,599,664
Net assets		
Unrestricted	217,665,390	202,218,901
Temporarily restricted	18,924,725	19,723,472
Permanently restricted	5,536,858	5,677,325
Total net assets	242,126,973	227,619,698
	$ 432,791,836	$ 404,219,362

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

Lawrence & Memorial Corporation and Subsidiaries
Consolidated Statements of Operations
Years Ended September 30, 2011 and 2010

	2011	2010
Unrestricted revenues, gains and other support		
Net revenues from services to patients	$ 346,642,222	$ 326,063,574
Other operating revenues	17,511,017	19,082,821
Net assets released from restriction used for operations	926,208	891,515
Total unrestricted revenues, gains and other support	365,079,447	346,037,910
Expenses		
Salaries and wages	172,671,132	156,922,676
Employee benefits	45,553,162	43,343,606
Supplies	47,120,092	44,707,786
Purchased services	24,514,687	22,229,769
Other	31,411,435	31,015,798
Interest	2,248,313	2,373,694
Depreciation and amortization	17,704,358	17,160,934
Bad debts	14,608,057	17,229,746
Total expenses	355,831,236	334,984,009
Income from operations	9,248,211	11,053,901
Nonoperating gains/(losses)		
Unrestricted investment income	171,387	175,335
Income/(loss) from investments	8,510,159	3,332,139
Loss on refinancing of debt	(2,026,984)	-
Total nonoperating gains/(losses)	6,654,562	3,507,474
Excess of revenues over expenses	15,902,773	14,561,375
Net unrealized (losses)/gains on investments	(6,670,014)	8,133,243
Transfer to/from affiliate	-	694,257
Net assets released from restrictions used for purchase of property, plant and equipment	176,082	181,470
Pension - related changes other than periodic pension costs	5,839,963	(7,611,564)
Increase/(decrease) in unrestricted net assets	$ 15,248,804	$ 15,958,781

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

Lawrence & Memorial Corporation and Subsidiaries
Consolidated Statements of Changes in Net Assets
Years Ended September 30, 2011 and 2010

	2011	2010
Unrestricted net assets		
Excess of revenues over expenses	$ 15,902,773	$ 14,082,800
Net unrealized (losses)/gains on investments	(6,670,014)	8,133,243
Transfer to/from affiliate	-	694,257
Transfer between donor classification	(867,139)	(1,064,824)
Net assets released from restrictions used for purchase of property, plant and equipment	176,082	660,045
Pension - related changes other than periodic pension costs	5,839,963	(7,611,564)
Increase in unrestricted net assets	14,381,665	14,893,957
Beginning of year unrestricted net assets	203,283,725	187,324,944
End of year unrestricted net assets, as reclassified	$ 217,665,390	$ 202,218,901
Temporarily restricted net assets		
Income from investments	$ 321,776	$ 268,083
Net assets released from restrictions	(1,102,290)	(1,072,985)
Transfer between donor classification	867,139	1,064,824
Contributions received	618,571	530,003
Change in value of irrevocable trusts	(286,646)	159,705
Net realized and unrealized (losses)/gains on investments	(152,473)	1,014,887
(Decrease)/increase in temporarily restricted net assets	266,077	1,964,517
Beginning of year temporarily restricted net assets	18,658,648	17,758,955
End of year temporarily restricted net assets	$ 18,924,725	$ 19,723,472
Permanently restricted net assets		
Change in value of funds held in trust by others	$ (140,467)	$ 105,212
(Decrease)/increase in permanently restricted net assets	(140,467)	105,212
Beginning of year permanently restricted net assets	5,677,325	5,572,113
End of year permanently restricted net assets	$ 5,536,858	$ 5,677,325

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

Lawrence & Memorial Corporation and Subsidiaries
Consolidated Statements of Cash Flows
Years Ended September 30, 2011 and 2010

	2011	2010
Cash flows from operating activities		
Change in net assets	$ 14,507,275	$ 16,963,686
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	17,704,358	17,160,934
Net unrealized and realized losses/(gains) on investments	7,717,656	(8,864,739)
Provision for bad debts	14,608,057	17,229,746
(Increase)/decrease in funds held in trust by others	268,116	(264,481)
Decrease/(increase) in contributions receivable	223,448	216,197
Restricted contributions and investment income	(940,347)	(798,086)
Changes in other operating accounts		
Patient accounts receivable, net	(14,491,777)	(18,112,620)
Other receivables, net	1,431,065	517,804
Inventories	(756,525)	(289,973)
Prepaid expenses and other current assets	(390,994)	606,440
Deferred financing costs and other assets	(608,468)	87,927
Accounts payable	2,356,149	5,125,506
Accrued vacation and sick pay	485,356	579,004
Salaries, wages, payroll taxes and amounts withheld from employees	(1,459,305)	852,666
Due to affiliates	98,310	(718,757)
Due from affiliates	1,928	22,572
Due to third party payors	(826,022)	(383,626)
Pension, postretirement and other liabilities	(6,869,494)	8,970,087
Net cash provided by operating activities	33,058,786	38,900,287
Cash flows from investing activities		
Purchase of property, plant and equipment, net	(39,901,165)	(20,085,147)
Purchases of investments	(107,504,126)	(151,368,583)
Sales of investments	91,320,215	145,197,517
Decrease/(increase) in debt service fund	138,140	47,062
Decrease in funds held in escrow	4,908,797	3,443
Net cash used in investing activities	(51,038,139)	(26,205,708)
Cash flows from financing activities		
Restricted contributions	940,347	798,086
Contributions restricted for purchasing equipment	-	-
Principal payments of long term debt	(3,005,100)	(2,320,524)
Proceeds of long term debt	23,402,948	-
Net cash used in financing activities	21,338,195	(1,522,438)
Net increase in cash and cash equivalents	3,358,842	11,172,141
Cash and cash equivalents		
Beginning of year	41,222,090	30,049,949
End of year	$ 44,580,932	$ 41,222,090
Supplemental disclosure of non cash activities		
Construction in process included in accounts payable	$ 1,644,565	$ 1,526,923
Contributed securities	$ 940,347	$ 798,086

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

1. Significant Accounting Policies and Organization

Organization

Lawrence & Memorial Corporation (the “Corporation”) is a not-for-profit organization incorporated under the Nonstock Corporation Act of the State of Connecticut. The Corporation is organized exclusively for public welfare, charitable, scientific, literary and education purposes, including the furtherance of the welfare, programs and activities of Lawrence & Memorial Hospital (the “Hospital”), a nonprofit organization incorporated under the General Statutes of the State of Connecticut.

The following entities are subsidiaries of the Corporation: Lawrence & Memorial Hospital (“L&M”), L& M Physician Association Inc., L&M Systems, Inc., VNA of Southeastern Connecticut, L&M Healthcare, and L&M Indemnity Ltd. The VNA of Southeastern Connecticut Inc. is consolidated using financial statement balances at June 30, 2011 and 2010.

L&M Healthcare has an affiliation agreement effective January 31, 1999 (the “Agreement”) with the Hospice of Southeastern Connecticut, Inc. (the “Hospice”). The Agreement gives L&M Healthcare a membership of the Hospice with one other not-for-profit healthcare organization. L&M Healthcare does not have an equity investment in the Hospice because the affiliation agreement does not require L&M Healthcare to provide capital to the Hospice and L&M Healthcare is not entitled to any of the net assets of the Hospice should the relationship terminate or the Hospice dissolve. The Corporation and its subsidiaries have never given capital to the Hospice and the Hospice has never made capital distributions to the Corporation or its subsidiaries.

L & M Physician Association, Inc. ("LMPA") was formed exclusively for the charitable purpose of benefiting, supporting, and furthering the charitable activities of Lawrence & Memorial Hospital by engaging physicians to provide physician services to the Hospital, organizations affiliated with the Hospital and communities they serve for purpose of practicing medicine and health care services.

Principles of Consolidation

The consolidated financial statements include the accounts of the Corporation and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying footnotes. Actual results could differ from those estimates and there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The Corporation’s significant estimates include the collectability of patient accounts receivable, useful lives of fixed assets, settlements due to third party payors, estimated reserves for self-insurance liabilities, and benefit plan assumptions.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the Corporation has been limited by donors to a specific time frame or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Corporation and its subsidiaries in perpetuity or in funds held in trust by others whose purpose is for the funds to be maintained in perpetuity.

Donor Restricted Gifts
Unconditional promises to give cash and other assets are reported at fair value at the date the promise 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 to unrestricted net assets and reported in the statement of operations as net assets released from restrictions. Donor restricted contributions whose restrictions are met within the same year as received are recorded as unrestricted contributions in the accompanying consolidated statement of operations.

Cash and Cash Equivalents
The Corporation and its subsidiaries consider all highly liquid investments with original maturities of three months or less at the date of purchase to be cash equivalents.

Investments
Investments in equity and debt securities are recorded at fair value in the balance sheet. Fair value is generally determined based on quoted market prices. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in the excess of revenues over expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are included in the change in net assets. Under accounting principles generally accepted in the United States of America, an “other than temporary impairment” is recognized if the Corporation does not expect the fair value of a security to recover above cost or amortized cost. Once an “other than temporary impairment” charge has been recorded, a new cost basis is established.

The Corporation continues to review its securities for appropriate valuation on an ongoing basis. The Corporation determined that none of their investments were impaired as of September 30, 2011 or 2010.

Realized and unrealized gains and losses on donor restricted endowment funds are included in temporarily restricted net assets under State law which allows the Board to appropriate as much of the net appreciation of investments as is prudent considering the Corporation’s long and short-term needs, present and anticipated financial requirements, expected total return on its investments, price level trends, and general economic conditions.

Investments in limited liability companies are accounted for using the equity method in instances where the limited partner’s interest is more than minor (3-5%).

Fair Value Measurements
Fair value guidance establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Observable inputs reflect market data obtained from sources independent of the reporting entity and unobservable inputs reflect the entities own assumptions about how market participants would value an asset or liability based on the best information available. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The guidance describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value.

The following describes the hierarchy of inputs used to measure fair value and the primary valuation methodologies used by the Corporation for financial instruments measured at fair value on a recurring basis. The three levels of inputs are as follows:

- Level 1 – Quoted prices in active markets for identical assets.

- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets in active markets, quoted prices in markets that are not active, or can be corroborated by observable market data for substantially the same term of the assets.

- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets.

Assets Held in Trust by Others
The Hospital has been named sole or participating beneficiary in several perpetual and charitable remainder trusts. Under the terms of these trusts, the Hospital has the irrevocable right to receive the income earned on the trust assets in perpetuity from the perpetual trusts and to receive the remainder of the trust assets for the charitable remainder trusts. For perpetual trusts, the estimated present value of the future payments to the Hospital is recorded at the fair value of the assets held in the trust. The charitable remainder trusts are recorded at the present value of the estimated future distributions expected to be received over the expected term of the trust agreement. The Hospital uses appropriate credit adjusted rates to discount amounts.

Assets Limited as to Use
Assets limited as to use include assets set aside by the Board of Directors to fund the deductible portion of malpractice insurance coverage (maintained in an irrevocable trust), contribution receivables and for the established purpose of providing for future improvement, expansion and replacement of plant and equipment. In addition, funds held in trust by others, unexpended bond proceeds for construction purposes, and assets held by trustees under indenture agreements relating to financing activities with the State of Connecticut Health and Education Facilities Authority ("CHEFA") are also included therein.

Property, Plant and Equipment
Property, plant and equipment are recorded at cost, or if received as a donation, at the fair value on the date received. The Corporation provides for depreciation of property, plant and equipment using the straight-line method in amounts sufficient to amortize the cost of its assets over their estimated useful lives. American Hospital Association lives are generally used and provide for a 2-25 year life for land improvements, 5-50 year life for buildings and a 2-25 year life for equipment. Lease improvements are amortized over the life of the lease.

Nonoperating Gains and Losses
Activities other than in connection with providing health care services are considered to be nonoperating.

Excess of Revenues over Expenses
The consolidated statement of operations includes excess of revenues over expenses. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice, include unrealized gains and losses on investments, permanent transfers of assets to and from affiliates for other than goods and services, contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets), and pension-related charges other than periodic pension costs and other postretirement benefits liabilities.

Fair Value of Financial Instruments
Investments and other assets and liabilities are carried at amounts that approximate fair value based on current market conditions. The fair value of long term debt is estimated based on the quoted market prices for the same or similar issues or on current rates offered to the Corporation and its Subsidiaries for debt of the same remaining maturities.

Benefit Plans
The Hospital has a defined benefit plan and a defined contribution plan. The VNA also has a defined contribution plan (see Note 8).

Medical Malpractice Self-Insurance
The Hospital purchases claims made professional and general liability insurance to cover medical malpractice claims. The Hospital has adopted the policy of self-insuring the deductible portion of its malpractice insurance coverage up to certain per claim and aggregate limits. The Hospital has established an irrevocable trust for the purpose of setting aside assets which can only be used for the payment of malpractice losses, related expenses, and the cost of administering the trust. Management accrues its best estimate of losses as incidents which give rise to potential losses occur. The Corporation has created an offshore captive insurance company, L&M Indemnity Ltd. to administer all medical malpractice and general liability coverage. L&M Indemnity Ltd. was created on September 28, 2011, however it will not process claims until fiscal year 2012.

Income Taxes
The Corporation and its subsidiaries are not-for-profit organizations and are exempt from federal income taxes on related income under Section 501(c)(3) of the Internal Revenue Code, except for L&M Systems. L&M Systems provides for taxes based on current taxable income and the future tax consequences of temporary differences between financial and income tax reporting. Such amounts are not material to the consolidated financial statements. LMPA became tax exempt under Section 501(c)(3) of the Internal Revenue Code on October 13, 2009.

Inventories
Inventory consists of supplies, both medical and general pharmaceuticals and food products needed to sustain daily operation of patient care. Inventories are carried at the lower of cost or market under the first-in-first-out (FIFO) method.

Impairment of Long-Lived Assets
Long-lived assets to be held and used are reviewed for impairment whenever circumstances indicate that the carrying amount of an asset may not be recoverable. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value less cost to dispose.

Accrued Vacation and Sick Pay
Accrued vacation is recorded as a liability as time is earned. As the time is used, the time is relieved from the liability. Accrued sick time is recorded as a percent for employees who have a balance greater than or equal to 800 hours. The payout is only upon termination of employment.

Subsequent Events

The Corporation has performed an evaluation of subsequent events through December 16, 2011, which is the date the financial statements were issued.

2. Revenues from Services to Patients and Charity Care

The following summarizes net revenues from services to patients:

	2011	2010
Gross charges from services to patients	$ 699,985,953	$ 663,899,138
Less: Charity care	6,383,831	5,279,619
Charges from services to patients, net of charity care	693,602,122	658,619,519
Deductions		
Allowances	348,886,832	334,462,279
State of Connecticut uncompensated care system (receipts)	(1,926,932)	(1,906,334)
Total deductions	346,959,900	332,555,945
Net revenues from services to patients	$ 346,642,222	$ 326,063,574

Patient accounts receivable and revenues are recorded when patient services are performed. Amounts received from most payors are different from established billing rates of the Corporation, and these differences are accounted for as allowances. The Corporation receives cash from the State of Connecticut Uncompensated Care Pool. The Corporation records this as an increase to their net revenues from services to patients.

Net patient service revenue is reported at the estimated net realizable amounts from patients, third party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Adjustments related to prior year settlements increased the Hospital’s revenues by approximately $3,852,000 and $16,000 in 2011 and 2010, respectively.

During 2011 and 2010, approximately 32% and 33%, respectively, of net patient service revenue was received under the Medicare program, and 12% and 10%, respectively, under the state Medicaid program. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. Changes in the Medicare and Medicaid programs and reductions of funding levels could have an adverse impact on the Hospital.

The Hospital accepts all patients regardless of their ability to pay. A patient is classified as a charity patient by reference to the established policies of the Hospital. Essentially, these policies define charity services as those services for which no payment is anticipated. In assessing a patient's inability to pay, the Hospital utilizes the generally recognized federal poverty income guidelines, but also includes certain cases where incurred charges are significant when compared to income. These charges are not included in net patient service revenues for financial reporting purposes.

3. Investments

Investments included in current assets consist of the following:

	2011	2010
Pooled endowment funds		
Cash and cash equivalents	$ 761,635	$ 635,077
Bonds	4,086,658	3,851,439
Mutual funds	10,672,092	986,991
Hedge funds	4,903,092	4,468,891
Marketable equities	1,632,639	11,723,616
Total pooled endowment funds	22,056,116	21,666,014
Investments held in trust by others		
Cash and cash equivalents	140,077	168,922
Bonds	2,814,055	1,949,338
Marketable equities	2,389,834	3,580,952
Other investments	263,967	176,837
Total investments held in trust by others	5,607,933	5,876,049
Other investments		
Cash and cash equivalents	11,416,712	10,528,349
Bonds	42,790,328	45,270,709
Mutual funds	2,508,041	1,014,889
Hedge funds	46,329,357	43,314,198
Equity investments	13,319	13,681
Marketable equities	53,115,624	55,639,161
Total other investments	156,173,381	155,780,987
	$ 183,837,430	$ 183,323,050

The Corporation's financial instrument categorization is based upon the lowest level of input that is significant to the fair value measurement within the valuation hierarchy. The following table presents the financial instruments carried at fair value using the by the fair value guidance valuation hierarchy defined above:

	2011			
	Level 1	Level 2	Level 3	Total Fair Value
Pooled endowment funds				
Cash and cash equivalents	$ 761,635	$ -	$ -	$ 761,635
Bonds	4,086,658	-	-	4,086,658
Mutual funds	10,672,092	-	-	10,672,092
Hedge funds	-	-	4,903,092	4,903,092
Marketable equities	1,632,639	-	-	1,632,639
Total pooled endowment funds	17,153,024	-	4,903,092	22,056,116
Held in trust by others				
Cash and cash equivalents	-	-	140,077	140,077
Bonds	-	-	2,814,055	2,814,055
Other assets	-	-	263,967	263,967
Marketable equities	-	-	2,389,834	2,389,834
Total held in trust by others	-	-	5,607,933	5,607,933
Other investments				
Cash and cash equivalents	11,416,712	-	-	11,416,712
Bonds	42,790,328	-	-	42,790,328
Mutual funds	2,508,041	-	-	2,508,041
Hedge funds	-	-	46,329,357	46,329,357
Marketable equities	53,115,624	-	-	53,115,624
Total other investments	109,830,705	-	46,329,357	156,160,062
	$ 126,983,729	$ -	$ 56,840,382	$ 183,824,111

	2010			
	Level 1	Level 2	Level 3	Total Fair Value
Pooled endowment funds				
Cash and cash equivalents	$ 635,077	$ -	$ -	$ 635,077
Bonds	1,253,172	2,598,267	-	3,851,439
Mutual funds	986,991	-	-	986,991
Hedge funds	-	-	4,468,891	4,468,891
Marketable equities	7,819,113	3,904,503	-	11,723,616
Total pooled endowment funds	10,694,353	6,502,770	4,468,891	21,666,014
Held in trust by others				
Cash and cash equivalents	-	-	168,922	168,922
Bonds	-	-	1,949,338	1,949,338
Other assets	-	-	3,580,952	3,580,952
Marketable equities	-	-	176,837	176,837
Total held in trust by others	-	-	5,876,049	5,876,049
Other investments				
Cash and cash equivalents	10,528,349	-	-	10,528,349
Bonds	15,249,556	30,021,153	-	45,270,709
Mutual funds	1,014,889	-	-	1,014,889
Hedge funds	-	-	43,314,996	43,314,996
Marketable equities	27,559,945	28,079,216	-	55,639,161
Total other investments	54,352,739	58,100,369	43,314,996	155,768,104
	$ 65,047,092	$ 64,603,139	$ 53,659,936	$ 183,310,167

Fair value for Level 1 is based upon quoted prices in active markets that the Corporation has the ability to access at the measurement date. Market price data is generally obtained from exchange or dealer markets. The Corporation does not adjust the quoted price for such assets.
Fair value for Level 2 is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Inputs are obtained from various sources including market participants, dealers and brokers.

Fair value for Level 3 is based on valuation techniques that use significant inputs that are unobservable as they trade infrequently or not at all and reflect assumptions based on the best information available in the circumstances.

Investments included in Level 3 primarily consist of the Corporations ownership in alternative investments (principally limited partnership interests in hedge funds). The value of these alternative investments represents the ownership interest in the net asset value (“NAV”) of the respective partnership. The fair values of the securities held by limited partnerships that do not have readily determinable fair values are determined by the general partner and are based on appraisals, or other estimates that require varying degrees of judgment. If no public market exists for the investment securities, the fair value is determined by the general partner taking into consideration, among other things, the cost of the securities, prices of recent significant placements of securities of the same issuer, and subsequent developments concerning the companies to which the securities relate. Also included in Level 3 investments are charitable remainder trusts held by third parties which are recorded at the present value of the future distributions expected to be received over the term of the agreement and investments in for-profit companies.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Corporation 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 estimate of fair value at the reporting date.

The following table is a roll forward of the amounts by investment type for financial instruments classified by the Corporation within Level 3 of the fair value hierarchy defined above:

	Beginning October 1, 2010	Investment Income	Realized Gains	Unrealized Losses	Investment Fees	Net Purchases	Ending September 30, 2011
Investment pool							
Hedge funds	$ 47,783,887	$ 325,584	$ 343,439	$ (192,120)	$ (116,775)	$ 3,088,434	$ 51,232,449
Funds held in trust	5,876,049	-	-	(268,116)	-	-	5,607,933
Total	$ 53,659,936	$ 325,584	$ 343,439	$ (460,236)	$ (116,775)	$ 3,088,434	$ 56,840,382

	Beginning October 1, 2009	Investment Income	Realized Gains	Unrealized Gains	Investment Fees	Net Purchases	Ending September 30, 2010
Investment pool							
Hedge funds	$ 24,801,331	$ 193,449	$ 138,022	$ 2,007,761	$ (75,692)	$ 20,719,016	$ 47,783,887
Funds held in trust	5,611,568	-	-	264,481	-	-	5,876,049
Total	$ 30,412,899	$ 193,449	$ 138,022	$ 2,272,242	$ (75,692)	$ 20,719,016	$ 53,659,936

There were no significant transfers of assets between levels for the year ended September 30, 2011. A summary of the pooled endowment investment return is presented below:

	2011	2010
Investment income	$ 486,586	$ 442,274
Realized and unrealized gains/(losses)	405,538	1,527,335
Management fees and other costs	(41,119)	(46,136)
Total return on pooled endowment investments	$ 851,005	$ 1,923,473

Following is additional information related to funds whose fair value is not readily determinable as of September 30, 2011.

	Strategy	Fair Value	# of Investments	Remaining Life	$ Amount of Unfunded Commitments	Timing to Draw Down Commitments	Redemption Terms	Redemption Restrictions	Restrictions in Place at Year End
Equity securities	Global developed and emerging market equity	$ 10,021,080	1	N/A	-	No remaining commitments	Monthly with 10 day's notice		None
Absolute return	Long/short and long-biased equity and credit hedge funds	14,633,040	1	N/A	-	No remaining commitments	Annual with 90 day's notice	lock up provision of 12 months from the purchase date	None
Directional hedge	Long/short and long-biased equity and credit hedge funds	21,209,816	1	N/A	-	No remaining commitments	Quarterly with 60 day's notice	lock up provision of 25 months from the purchase date	None
Commodities	Commodity index	5,288,513	1	N/A	-	No remaining commitments	Monthly with 5 day's notice		None
Private Equity	Private equity	80,000	1	N/A	-	Illiquid long term 5 years	None	None	None
		$ 51,232,449							

4. Endowments

The Corporation's endowments consist of donor restricted endowment funds for a variety of purposes. The net assets associated with endowment funds including funds designated by the Board of Directors to function as endowments are classified and reported based on the existence or absence of donor imposed restrictions.

The Corporation understands net asset classification guidance to require that donor restricted endowment gifts be maintained in perpetuity. Consistent with net asset classification guidance, the Corporation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure. The Corporation considers the following factors in making a determination to appropriate or accumulate endowment funds:

- The duration and preservation of the fund
- The purposes of the Corporation and donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the Corporation
- The investment policies of the Corporation

Changes in endowment net assets for the year ended September 30:

	2011			
	Unrestricted	**Temporarily Restricted**	**Permanently Restricted**	**Total**
Endowment net assets, beginning of year	$ 5,470,122	$12,134,604	$ 2,866,683	$20,471,409
Investment return				
Investment income	130,164	114,203	-	244,367
Net realized and unrealized gain (loss)	914,699	(286,646)	-	628,053
Total investment return	1,044,863	(172,443)	-	872,420
Income distribution	-	(173,182)	-	(173,182)
Endowment net assets, end of year	$ 6,514,985	$11,788,979	$ 2,866,683	$21,170,647

	2010			
	Unrestricted	**Temporarily Restricted**	**Permanently Restricted**	**Total**
Endowment net assets, beginning of year	$ 4,930,901	$11,222,301	$ 2,866,683	$19,019,885
Investment return				
Investment income	125,722	55,426	-	181,148
Net realized and unrealized gain (loss)	413,499	1,014,887	-	1,428,386
Total investment return	539,221	1,070,313	-	1,609,534
Income distribution		(158,010)	-	(158,010)
Endowment net assets, end of year	$ 5,470,122	$12,134,604	$ 2,866,683	$20,471,409

Endowment funds classified as permanently and temporarily restricted net assets:

The portion of perpetual endowment funds retained permanently either by explicit donor stipulation or by net asset classification guidance is summarized as follows:

	2011	**2010**
Temporarily restricted net assets		
Unspent income and appreciation on permanently restricted endowments for purchase of equipment and healthcare services	$ 12,053,786	$ 12,541,912
Total endowment funds classified as temporarily restricted net assets	$ 12,053,786	$ 12,541,912
Permanently restricted net assets		
Corpus of permanently restricted contributions for purchase of equipment and healthcare services	$ 2,866,683	$ 2,866,683
Total endowment funds classified as permanently restricted net assets	$ 2,866,683	$ 2,866,683

Endowment Funds with Deficits
From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the value of the initial and subsequent donor gift amounts (deficit). When donor endowment deficits exist they are classified as a reduction of unrestricted net assets. The Corporation analyzed the endowments and notes there are no deficits as of September 30, 2011 and 2010.

Endowment Investment Return Objectives and Risk Parameters
The Corporation has adopted endowment investment and spending policies that attempt to provide predictable stream of funding to programs supported by the endowment while seeking to maintain the permanent nature of endowment funds. Under this policy, the return objective for the endowment assets measured over a full market cycle shall be to maximize the return against a blended index, based on the endowment's target asset allocation applied to the appropriate individual benchmarks.

Strategies Employed for Achieving Endowment Investment Objectives
To achieve its long-term rate of return objectives, the Corporation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized gains) and current yield (interest and dividends). The Corporation targets a diversified asset allocation to achieve its long-term objectives within prudent Corporation risk constraints.

Endowment Spending Allocation and Relationship of Spending Policy to Investment Objectives
Spending is guided by several factors most important is the value of the portfolio. Generally, the Board will approve a spending policy limiting annual expenditures for grants and operating expenses up to 4.5% of the value of the Funds' assets based on a 12 quarter rolling average for the endowment, Kitchings and operating funds. The Corporation will designate the spending amount on an as-needed basis for the special account.

Investment managers are given ample notice of the required withdrawal schedule. Appropriate liquidity is maintained to fund these withdrawals without impairing the investment process.

5. Temporary and Permanently Restricted Net Assets

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

	2011	2010
Temporarily restricted net assets		
Funds held in trust by others	$ 2,959,565	$ 3,086,274
Contributions receivable	887,467	1,110,916
Free beds and plant replacement and expansion	12,053,786	12,541,912
Specific purpose reserves	3,023,907	2,984,370
	$ 18,924,725	$ 19,723,472

Permanently restricted net assets at September 30, 2011 and 2010 are restricted to:

	2011	2010
Permanently restricted net assets		
Funds held in trust by others	$ 2,670,175	$ 2,810,642
Donor restricted endowment funds	2,866,683	2,866,683
	$ 5,536,858	$ 5,677,325

6. Property, Plant and Equipment

Property, plant and equipment consists of the following:

	2011	2010
Land and land improvements	$ 17,953,282	$ 6,073,611
Buildings	115,186,586	110,416,648
Equipment	205,006,378	181,640,842
	338,146,246	298,131,101
Less: Accumulated depreciation	(213,597,308)	(195,187,155)
	124,548,938	102,943,946
Construction in progress (estimated cost to complete at September 30, 2011 is $14,873,263 (unaudited))	10,109,457	9,635,284
	$ 134,658,395	$ 112,579,230

7. Long-Term Debt

	2011	2010
CHEFA Series F Revenue Bonds		
Various rate bonds, due 2012 to 2026	$ 39,135,000	$ -
5.0% Term Bonds, due 2027 to 2031	8,705,000	-
5.0% Term Bonds, due 2032 to 2036	11,100,000	-
CHEFA Series D revenue bonds		
5.0% Term bonds, due 2009 to 2013	-	8,750,000
5.0% Term bonds, due 2014 to 2022	-	33,870,000
CHEFA Series E revenue bonds		
Variable rate bonds, due 2023-2034	22,990,000	22,990,000
VNA mortgage note		
Variable rate, due 2001 to 2011	225,988	265,903
VNA Interest rate swap agreement	-	39,028
Capital lease obligation	405,373	377,538
Total long-term debt outstanding	82,561,361	66,292,469
Less: Amounts classified as current	3,202,481	2,906,408
Less: Bond discount	-	1,237,915
Add: Bond Premium	2,891,040	-
Total long-term portion of long-term debt	$ 82,249,920	$ 62,148,146

On September 15, 2011 CHEFA issued $58,940,000 of Series F Bonds (the "Series F Bonds") on behalf of the Hospital and the Corporation (collectively referred to as the "Obligated Group" under the Series F Bond agreements). The Series F Bonds are structured with a term bond due July 1, 2036, with annual sinking fund payments due each July 1st commencing July 1, 2012. Interest on the Series F Bonds is payable semiannually on the first business day of January 1 and July 1 beginning January 1, 2012.

The proceeds of the Series F Bonds were used to refund the outstanding Authority Revenue Bonds, Lawrence & Memorial Hospital Issue, Series D (the "Series D Bonds") and are being used to fund all or a portion of the following capital projects: (i) replacement of a linear accelerator on the main campus of the Hospital; (ii) capital improvements for infrastructure renovation and improvement on the main campus, including heating, ventilation, and air conditioning project; (iii) replacement of a catheterization lab and equipment on the main campus; (iv) acquisition of approximately 100 acres of land in Waterford, Connecticut for development of a new cancer center; and (v) acquisition and installation of Magnetic Resonance Imaging and CT equipment at the Crossroads facility.

On June 24, 2004 CHEFA issued $22,990,000 of Series E Bonds (the "Series E Bonds") on behalf of the Hospital and the Corporation (collectively referred to as the "Obligated Group" under the Series E Bond agreements). The Series E Bonds are structured with a term bond due July 1, 2034, with annual sinking fund payments due each July 1st commencing July 1, 2003. Interest on the Series E Bonds accrues at the weekly rate and is payable on the first business day of each month commencing July 1, 2004.

The proceeds of the Series E Bonds were used to finance the acquisition, construction, capital improvements, renovation, and/or equipping of the expansion of the Hospital's Pequot Health Center, including a new 37,000 square foot building addition to house an ambulatory surgery unit, MRI services, and mobile medical technologies. The proceeds were also used to fund the debt service reserve fund and costs related to the issuance and interest related to the Series E Bonds. Under the terms of the trust indenture for the Series E Bonds, the Obligated Group is required to meet certain financial covenants including a debt service coverage ratio and days cash on hand ratio. Members of the Obligated Group are jointly and severally obligated to provide amounts sufficient to enable the Authority to pay principal and interest on the Series E bonds. The bonds and bond proceeds have been allocated to the Hospital and as such, the Hospital will make future debt service payments as required under the terms of the bonds.

The bonds may be retired at an earlier date pursuant to terms of the master indenture. Payment of the bonds is collateralized by a pledge of the gross receipts (as defined) and certain real property of the Hospital and Corporation.

Effective January 16, 2008, the Hospital refinanced its CHEFA Series E bonds with JPMorgan Chase Bank, N.A. This reoffering does not update information contained in the original official statement but provides a new letter of credit, which expires in January 2013.

The Series E Bonds are considered variable rate demand bonds and are remarketed on a weekly basis. If the bonds are unable to be remarketed, the letter of credit could be utilized to purchase the bonds. The Obligated Group would then be subject to the payment terms of the letter of credit, which are equal quarterly installments beginning in the first quarter that is at least 367 days after the initial draw down on the letter of credit. The Series E Bonds have been successfully remarketed and there have been no draws on the letter of credit.

In accordance with the long-term loan agreement with CHEFA, certain trusteed funds are required to be maintained. These funds provide for debt service and other related payments. The income derived from these funds is required to be reinvested in the trusteed funds and is not available for current operating purposes.

The agreements will remain in force until principal and interest on the bonds and any other costs of the Authority with respect to the project have been fully paid or provided for. Annual payments due under the loan agreements include interest on the outstanding bonds.

The fair value of the Series E Bonds, using discounted cash flow analyses, approximates carrying value. The fair value of the Series D Bonds is approximately $0 million and $64.5 million at September 30, 2011 and 2010, respectively.

The VNA has a $1.0 million ten year variable rate mortgage note bearing interest at one percent above the LIBOR rate (1.181% and 2.19% at June 30, 2011 and 2010, respectively). The VNA maintains an interest rate swap agreement for this debt at a rate of 8.35%. The loan is based on a 20 year amortization period. The balance of the loan is $225,988 and $265,903 at June 30, 2011 and 2010, respectively. The remaining principal balance is due September 2011. The note is collateralized by a first mortgage on the property, buildings and building improvements located in Waterford, Connecticut.

Principal repayments, excluding the capital lease, are as follows:

Year	Annual Principal Repayment
2012	$ 2,885,000
2013	2,625,000
2014	2,725,000
2015	2,835,000
2016 and thereafter	70,860,000
	$ 81,930,000

Cash interest payments of $2,215,476 and $2,350,752 were made in fiscal year 2011 and 2010, respectively. No interest was capitalized during 2011 and 2010.

8. Pension and Other Postretirement Benefits

The Hospital has a defined benefit plan covering all employees who elected to stay in the plan. The plan is frozen to new participants as of June 30, 1999. The benefits are based on years of service and the employee’s compensation during the last five years of employment. Assets of the plan include mutual funds, marketable equity securities, corporate and government bonds, notes, and hedge funds.

The Hospital provides health care and life insurance benefits to its retired employees who meet certain eligibility requirements. The Hospital’s policy is to fund the cost of postretirement benefits other than pensions as incurred. This plan was frozen to include only those employees who retired prior to May 1, 1994.

The following table sets forth the Hospital's plans' funded status and amounts recognized in the consolidated statement of financial position for fiscal year 2011 and 2010 as of September 30 (measurement date of September 30):

	Pension Benefits		Other Postretirement Benefits	
	2011	**2010**	**2011**	**2010**
Change in benefit obligation				
Benefit obligation at beginning of year	$ 131,200,922	$ 117,330,146	$ 1,277,520	$ 1,290,578
Service cost	1,941,270	1,927,395	-	-
Interest cost	6,505,871	6,646,772	59,018	70,433
Employee contributions	163,401	180,479	-	-
Benefits paid	(5,255,985)	(5,267,983)	(120,183)	(130,095)
Actuarial (gain)/loss	(7,891,942)	10,384,113	(49,354)	46,604
Benefit obligation at end of year	$ 126,663,537	$ 131,200,922	$ 1,167,001	$ 1,277,520
Change in plan assets				
Fair value of plan assets at beginning of year	$ 81,387,819	$ 76,344,572	$ -	$ -
Actual return on plan assets	2,092,350	7,130,751	-	-
Employee contributions	163,401	180,479	-	-
Employer contributions	7,100,000	3,000,000	120,183	130,095
Benefits paid	(5,255,985)	(5,267,983)	(120,183)	(130,095)
Fair value of plan assets at end of year	$ 85,487,585	$ 81,387,819	$ -	$ -
Funded status of the plan	$ (41,175,952)	$ (49,813,103)	$ (1,167,001)	$ (1,277,520)
Unrecognized net loss (gain) from past experience different from that assumed and effects of changes in assumptions	31,903,948	37,618,950	(526,034)	(531,764)
Unrecognized prior service cost	471,588	596,549	-	-
Accrued benefit costs recognized in the statement of operation	$ (8,800,416)	$ (11,597,604)	$ (1,693,035)	$ (1,809,284)
Components of net periodic benefit costs				
Service cost	$ 1,941,270	$ 1,927,395	$ -	$ -
Interest cost	6,505,871	6,646,772	59,018	70,433
Expected return on plan assets	(6,850,835)	(6,350,382)	-	-
Amortization of net loss/(gain)	2,581,545	1,867,224	(55,084)	(61,546)
Net amortization and deferral	124,961	124,956	-	-
Benefit cost	$ 4,302,812	$ 4,215,965	$ 3,934	$ 8,887

The weighted average assumptions used to determine the net benefit cost at the beginning of the year are as follows:

	2011	**2010**
Discount rate	5.07 %	5.80 %
Average rate of compensation increases	4.25 %	4.25 %
Expected return on assets	8.50 %	8.50 %

The weighted average assumptions used to determine the benefit obligation at the end of the year are as follows:

	2011	**2010**
Discount rate	5.34 %	5.07 %
Average rate of compensation increases	3.50 %	4.25 %

The Plan's asset allocations as of September 30, 2011 and 2010 are as follows:

Asset Category	**2011**	**2010**
Cash	5%	2%
Bonds	30%	24%
Hedge Funds	31%	30%
Marketable Equities	34%	44%
Total	100%	100%

The expected rate of return on plan assets is calculated based on past experience.

Expected benefits to be paid under the Hospital's plans are as follows:

Fiscal Years Beginning October 1	**Expected Benefits**
2011	$ 6,227,427
2012	6,509,958
2013	6,910,790
2014	7,155,303
2015	7,572,842
Expected Aggregate for 5 fiscal years beginning 2016	42,922,899

Annual contributions are determined by the Hospital based upon calculations prepared by the plan's actuary. Expected contributions to the Pension and Retiree Health Plan for 2011 are approximately:

Pension	$ 6,509,958
Retiree Health	125,125

The weighted-average annual assumed rate of increase in the per capita cost of covered benefits (i.e., health care cost trend rate) for participants is assumed to be 9% in 2012 reducing to 5.0% by the year 2016 and remaining at that level thereafter. This health care cost trend rate assumption has a significant effect on the amounts reported. To illustrate, a one percentage point increase in the assumed health care cost trend rate would increase the accumulated postretirement benefit obligation and service cost plus interest cost by approximately $80,000 and $94,000, respectively, at September 30, 2011 and 2010. A one percentage point decrease in the assumed health care cost trend rate would decrease the accumulated postretirement benefit obligation and service cost plus interest cost by approximately $73,000 and $86,000, respectively, at September 30, 2011 and 2010.

Plan Assets
The defined benefit plan assets are valued utilizing the same fair value hierarchy as the Hospital's investments as described in Note 1.

The following table summarizes the fair values of investments by major type held by the staff pension plan at September 30, 2011:

	Level 1	Level 2	Level 3	2011
Investments, at fair value				
Cash	$ 3,847,979	$ -	$ -	3,847,979
Bonds	25,779,769	-	-	25,779,769
Hedge Funds	-	-	26,524,387	26,524,387
Marketable Equities	26,050,106	3,285,344	-	29,335,450
Total investments, at fair value	$ 55,677,854	$ 3,285,344	$ 26,524,387	$ 85,487,585

The following table summarizes the fair values of investments by major type held by the staff pension health plan at September 30, 2010:

	Level 1	Level 2	Level 3	2010
Investments, at fair value				
Cash	$ 1,873,724	$ -	$ -	$ 1,873,724
Bonds	-	19,609,144	-	19,609,144
Hedge Funds	-	-	24,333,144	24,333,144
Marketable Equities	14,103,283	21,468,524	-	35,571,807
Total investments, at fair value	$ 15,977,007	$ 41,077,668	$ 24,333,144	$ 81,387,819

There are no transfers between levels comparing last to this year for assets that are in the portfolio.

The table below represents the change in fair value measurements for Level 3 investments held by the staff pension plans' years ended September 30, 2011 and 2010, respectively:

	2011	2010
Beginning balance	$ 24,333,144	$ 19,719,016
Realized and unrealized gain, net	249,105	1,629,862
Purchases (sales), net	1,942,138	2,984,266
Ending balance	$ 26,524,387	$ 24,333,144

The investment objective for the pension and post retirement plans seeks a positive long-term total return after inflation to meet the Hospital's current and future plan obligations.

Asset allocations for both plans combine tested theory and informed market judgment to balance investment risks with the need for high returns.

The Hospital's 401(k) plan covers eligible employees who elected to participate in the plan. Eligible employees may contribute a percentage of their salary to the plan. The Hospital matches 100% of the first 4% of gross pay deferred by employees for those employees who do not participate in the defined benefit plan. Plan contributions charged to operations were approximately $3,677,000 and $3,628,000 for 2011 and 2010, respectively.

The VNA has a defined contribution pension plan which covers substantially all of its employees who have met specified age and length of service requirements. Contributions to the plan are based on 5% of eligible salaries and totaled approximately $432,537 and $433,118 for the years ended June 30, 2011 and 2010, respectively.

9. Medical Malpractice Self-Insurance

There have been malpractice claims that fall within the Hospital's self-insured program which have been asserted against the Hospital. In addition, there are known incidents that have occurred through September 30, 2010 that may result in the assertion of claims. The Hospital has engaged independent actuaries to estimate the ultimate cost of the settlement of such claims. Accrued malpractice losses have been discounted at 4% for 2011 and 5% for 2010. The Hospital maintains a trust to fund these liabilities on a long-term basis. The Corporation has adopted an offshore captive to administer all medical malpractice and general liability coverage in the coming year.

10. Functional Expenses

The Corporation and its subsidiaries provide general health care services to residents within its geographic location including pediatric care, cardiac catheterization, and outpatient surgery. Expenses by function are as follows:

	2011	2010
Health care services	$ 271,059,762	$ 256,962,275
General and administrative	84,771,474	78,021,734
	$ 355,831,236	$ 334,984,009

11. Contingencies

The Corporation and its subsidiaries are parties to various lawsuits incidental to their business. Management believes that the lawsuits will not have a material adverse effect on their financial position, results of operations, changes in net assets or cash flows.

Lawrence & Memorial Corporation and Subsidiaries
Consolidating Balance Sheet
September 30, 2011

	Lawrence & Memorial Hospital	Lawrence & Memorial Corporation	Eliminating Entries	Obligated Group	L&M Systems, Inc.	LMPA	L&M Indemity	VNA of Southeastern Connecticut, Inc.	Eliminating Entries	Consolidated
Assets										
Current assets										
Cash and cash equivalents	$ 41,797,328	$ 814,528	$ -	$ 42,611,856	$ 399	$ 56,951	$ 120,000	$ 1,791,726	$ -	$ 44,580,932
Investments	105,904,042	44,333,741	-	150,237,783	-	-	-	5,935,598	-	156,173,381
Accounts receivable	30,483,331	-	-	30,483,331	-	589,495	-	1,139,437	-	32,212,263
Other receivables	3,998,458	-	-	3,998,458	559,288	36,795	-	-	-	4,594,541
Inventories	4,528,017	-	-	4,528,017	-	24,594	-	-	-	4,552,611
Due from affiliates	578,161	861,458	(578,161)	861,458	1,087,749	3,754	-	-	(1,952,961)	-
Prepaid expenses and other current assets	1,739,804	-	-	1,739,804	-	283,749	-	299,002	-	2,322,555
Debt service fund	1,109,892	-	-	1,109,892	-	-	-	-	-	1,109,892
Total current assets	190,139,033	46,009,727	(578,161)	235,570,599	1,647,436	995,338	120,000	9,165,763	(1,952,961)	245,546,175
Assets limited as to use										
Cash	179,900	-	-	179,900	-	-	-	-	-	179,900
Construction funds	8,427,695	-	-	8,427,695	-	-	-	-	-	8,427,695
Investments held in trust	11,241,951	-	-	11,241,951	-	-	-	-	-	11,241,951
Endowment investments	14,398,888	2,598,927	-	16,997,815	-	-	-	5,058,301	-	22,056,116
Investment in subsidiaries	-	3,182,689	-	3,182,689	-	-	-	-	(3,182,689)	-
Funds held in Trust by others	5,607,933	-	-	5,607,933	-	-	-	-	-	5,607,933
Contributions receivable	20,328	867,140	-	887,468	-	-	-	-	-	887,468
Funds held in escrow by agreement with	-	-	-	-	-	-	-	-	-	-
Statement of Connecticut Health and	-	-	-	-	-	-	-	-	-	-
Debt service reserve fund										
Educational Facilities Authority and trustees	2,247,370	-	-	2,247,370	-	-	-	-	-	2,247,370
Total assets limited as to use	42,124,065	6,648,756	-	48,772,821	-	-	-	5,058,301	(3,182,689)	50,648,433
Other assets										
Deferred financing costs and other assets, net	1,938,833	-	-	1,938,833	-	-	-	-	-	1,938,833
Property, plant and equipment										
Land improvements	6,506,216	11,116,791	-	17,623,007	-	-	-	330,275	-	17,953,282
Buildings/leasehold improvements	111,446,370	148,821	-	111,595,191	-	1,396,975	-	2,194,420	-	115,186,586
Equipment/furniture	203,329,727	21,774	-	203,351,501	-	745,052	-	909,825	-	205,006,378
Accumulated depreciation	(210,414,909)	(74,691)	-	(210,489,600)	-	(1,631,229)	-	(1,476,479)	-	(213,597,308)
Construction in progress	10,109,457	-	-	10,109,457	-	-	-	-	-	10,109,457
Property, plant and equipment, net	120,976,861	11,212,695	-	132,189,556	-	510,798	-	1,958,041	-	134,658,395
	$ 355,178,792	$ 63,871,178	$ (578,161)	$ 418,471,809	$ 1,647,436	$ 1,506,136	$ 120,000	$ 16,182,105	$ (5,135,650)	$ 432,791,836

Lawrence & Memorial Corporation and Subsidiaries
Consolidating Balance Sheet
September 30, 2011

	Lawrence & Memorial Hospital	Lawrence & Memorial Corporation	Eliminating Entries	Obligated Group	L&M Systems, Inc.	LMPA	L&M Indemnity	VNA of Southeastern Connecticut, Inc.	Eliminating Entries	Consolidated
Liabilities and Net Assets										
Current liabilities										
Accounts payable	$ 22,690,113	$ 236,343	$ -	$ 22,926,456	$ -	$ 60,230	$ -	$ 1,128,690	$ -	$ 24,115,376
Accrued vacation and sick pay	11,705,811	-	-	11,705,811	-	-	-	-	-	11,705,811
Salaries, wages, payroll taxes and amounts withheld from employees	3,125,898	-	-	3,125,898	-	451,796	-	-	-	3,577,694
Due to affiliates	1,913,991	-	(578,161)	1,335,830	617,131	98,310	-	-	(1,952,961)	98,310
Due to third party payors	7,838,088	-	-	7,838,088	-	-	-	175,000	-	8,013,088
Other current liabilities			-	-	-	-	-	65,242	-	65,242
Current portion of long-term debt	2,976,493	-		2,976,493	-	-	-	225,988	-	3,202,481
Total current liabilities	50,250,394	236,343	(578,161)	49,908,576	617,131	610,336		1,594,920	(1,952,961)	50,778,002
Accrued pension and other postretirement benefits	43,423,221	-	-	43,423,221	-	-	-	-	-	43,423,221
Other liabilities	14,213,720	-	-	14,213,720	-	-	-	-	-	14,213,720
Long-term debt less current portion	82,249,920	-	-	82,249,920	-	-	-	-	-	82,249,920
Total liabilities	190,137,255	236,343	(578,161)	189,795,437	617,131	610,336	-	1,594,920	(1,952,961)	190,664,863
Net assets										
Unrestricted	141,738,900	62,502,889	-	204,241,789	1,030,305	895,800	120,000	14,560,185	(3,182,689)	217,665,390
Temporarily restricted	17,792,779	1,131,946	-	18,924,725	-	-	-	-	-	18,924,725
Permanently restricted	5,509,858	-	-	5,509,858	-	-	-	27,000	-	5,536,858
Total net assets	165,041,537	63,634,835	-	228,676,372	1,030,305	895,800	120,000	14,587,185	(3,182,689)	242,126,973
	$ 355,178,792	$ 63,871,178	$ (578,161)	$ 418,471,809	$ 1,647,436	$ 1,506,136	$ 120,000	$ 16,182,105	$ (5,135,650)	$ 432,791,836

Lawrence & Memorial Corporation and Subsidiaries
Consolidating Balance Sheet
September 30, 2010

	Lawrence & Memorial Hospital	Lawrence & Memorial Corporation	Eliminating Entries	Obligated Group	L&M Systems, Inc.	LMPA	VNA of Southeastern Connecticut, Inc.	Eliminating Entries	Consolidated
Assets									
Current assets									
Cash and cash equivalents	$ 33,160,240	$ 5,285,792	$ -	$ 38,446,032	$ 8,054	$ 239,297	$ 2,528,707	$ -	$ 41,222,090
Investments	106,795,008	44,866,427	-	151,661,435	-	-	4,119,552	-	155,780,987
Accounts receivable	30,942,261	-	-	30,942,261	-	143,715	1,242,567	-	32,328,543
Other receivables	5,765,211	-	-	5,765,211	224,500	35,895	-	-	6,025,606
Inventories	3,796,086	-	-	3,796,086	-	-	-	-	3,796,086
Due from affiliates	6,243,476	541,500	(6,243,476)	541,500	917,707	-	-	(1,457,279)	1,928
Prepaid expenses and other current assets	1,624,613	-	-	1,624,613	-	-	306,948	-	1,931,561
Debt service fund	1,248,032	-	-	1,248,032	-	-	-	-	1,248,032
Total current assets	189,574,927	50,693,719	(6,243,476)	234,025,170	1,150,261	418,907	8,197,774	(1,457,279)	242,334,833
Assets limited as to use									
Cash	179,215	-	-	179,215	-	-	-	-	179,215
Investments held in trust	11,986,573	-	-	11,986,573	-	-	-	-	11,986,573
Endowment investments	14,741,092	2,744,154	-	17,485,246	-	-	4,180,768	-	21,666,014
Investment in subsidiaries	-	3,182,689	-	3,182,689	-	-	-	(3,182,689)	-
Funds held in Trust by others	5,876,049	-	-	5,876,049	-	-	-	-	5,876,049
Contributions receivable	46,092	1,064,824	-	1,110,916	-	-	-	-	1,110,916
Funds held in escrow by agreement with Statement of Connecticut Health and Educational Facilities Authority and trustees	7,156,167	-	-	7,156,167	-	-	-	-	7,156,167
Total assets limited as to use	39,985,188	6,991,667	-	46,976,855	-	-	4,180,768	(3,182,689)	47,974,934
Other assets									
Deferred financing costs and other assets, net	1,330,365	-	-	1,330,365	-	-	-	-	1,330,365
Property, plant and equipment									
Land improvements	5,212,649	530,687	-	5,743,336	-	-	330,275	-	6,073,611
Buildings/leasehold improvements	107,593,741	148,821	-	107,742,562	-	467,701	2,206,385	-	110,416,648
Equipment/furniture	180,454,333	21,774	-	180,476,107	-	157,952	1,006,783	-	181,640,842
Accumulated depreciation	(193,724,896)	(67,012)	-	(193,791,908)	-	-	(1,395,247)	-	(195,187,155)
Construction in progress	9,635,284	-	-	9,635,284	-	-	-	-	9,635,284
Property, plant and equipment, net	109,171,111	634,270	-	109,805,381	-	625,653	2,148,196	-	112,579,230
	$ 340,061,591	$ 58,319,656	$ (6,243,476)	$ 392,137,771	$ 1,150,261	$ 1,044,560	$ 14,526,738	$ (4,639,968)	$ 404,219,362

Lawrence & Memorial Corporation and Subsidiaries
Consolidating Balance Sheet
September 30, 2010

	Lawrence & Memorial Hospital	Lawrence & Memorial Corporation	Eliminating Entries	Obligated Group	L&M Systems, Inc.	LMPA	VNA of Southeastern Connecticut, Inc.	Eliminating Entries	Consolidated
Liabilities and Net Assets									
Current liabilities									
Accounts payable	$ 19,524,046	$ 85,083	$ -	$ 19,609,129	$ 1,688	$ 925,527	$ 1,340,525	$ -	$ 21,876,869
Accrued vacation and sick pay	11,220,455	-	-	11,220,455	-	-	-	-	11,220,455
Salaries, wages, payroll taxes and amounts withheld from employees	5,023,219	-	-	5,023,219	-	13,780	-	-	5,036,999
Due to affiliates	4,764,147	2,395,108	(6,243,476)	915,779	541,500	-	-	(1,457,279)	-
Due to third party payors	8,559,110	-	-	8,559,110	-	-	280,000	-	8,839,110
Other current liabilities	-	-	-	-	5,969	-	150,892	-	156,861
Current portion of long-term debt	2,866,493	-	-	2,866,493	-	-	39,915	-	2,906,408
Total current liabilities	51,957,470	2,480,191	(6,243,476)	48,194,185	549,157	939,307	1,811,332	(1,457,279)	50,036,702
Accrued pension and other postretirement benefits	52,131,286	-	-	52,131,286	4,048	-	-	-	52,135,334
Other liabilities	12,279,482	-	-	12,279,482	-	-	-	-	12,279,482
Long-term debt less current portion	61,883,130	-	-	61,883,130	-	-	265,016	-	62,148,146
Total liabilities	178,251,368	2,480,191	(6,243,476)	174,488,083	553,205	939,307	2,076,348	(1,457,279)	176,599,664
Net assets									
Unrestricted	137,908,558	54,367,333	-	192,275,891	597,056	105,253	12,423,390	(3,182,689)	202,218,901
Temporarily restricted	18,251,340	1,472,132	-	19,723,472	-	-	-	-	19,723,472
Permanently restricted	5,650,325	-	-	5,650,325	-	-	27,000	-	5,677,325
Total net assets	161,810,223	55,839,465	-	217,649,688	597,056	105,253	12,450,390	(3,182,689)	227,619,698
	$ 340,061,591	$ 58,319,656	$ (6,243,476)	$ 392,137,771	$ 1,150,261	$ 1,044,560	$ 14,526,738	$ (4,639,968)	$ 404,219,362

Lawrence & Memorial Corporation and Subsidiaries
Consolidating Statement of Operations
Year Ended September 30, 2011

	Lawrence & Memorial Hospital	Lawrence & Memorial Corporation	Eliminating Entries	Obligated Group	L&M Systems, Inc.	LMPA	L&M Indemnity	VNA of Southeastern Connecticut, Inc.	Eliminating Entries	Consolidated
Net revenues from services to patients	$ 325,275,690	$ -	$ -	$ 325,275,690	$ -	$ 9,653,134	$ -	$ 11,713,398	$ -	$ 346,642,222
Other operating revenues	11,091,202	4,913,892	-	16,005,094	514,414	1,445,368	-	3,410,342	(3,864,201)	17,511,017
Net assets released from restriction	394,829	531,379	-	926,208	-	-	-	-	-	926,208
	336,761,721	5,445,271	-	342,206,992	514,414	11,098,502		15,123,740	(3,864,201)	365,079,447
Operating expenses										
Salaries and wages	149,953,412	-	-	149,953,412	-	13,088,769	-	10,144,682	(515,730)	172,671,133
Employee benefits	41,985,784	-	-	41,985,784	252,925	2,238,134	-	2,678,647	(1,602,328)	45,553,162
Supplies	45,904,757	531,874	-	46,436,631	50	543,449	-	139,962	-	47,120,092
Purchased services	23,474,674	387,423	-	23,862,097	6,284	1,447,160	-	730,460	(1,531,315)	24,514,686
Other	29,046,249	75,670	-	29,121,919	29	1,806,420	-	698,016	(214,828)	31,411,556
Interest	2,212,181	-	-	2,212,181	-	-	-	36,011	-	2,248,192
Depreciation and amortization	17,199,566	7,680	-	17,207,246	-	270,863	-	226,249	-	17,704,358
Bad debts	14,356,474	-	-	14,356,474	-	176,603	-	74,980	-	14,608,057
	324,133,097	1,002,647	-	325,135,744	259,288	19,571,398	-	14,729,007	(3,864,201)	355,831,236
Income from operations	12,628,624	4,442,624	-	17,071,248	255,126	(8,472,896)		394,733	-	9,248,211
Nonoperating gains										
Unrestricted investment income	171,387	-	-	171,387	-	-	-	-	-	171,387
Income/(loss) from investments	5,993,369	2,233,886	-	8,227,255	-	-	-	282,904	-	8,510,159
Loss on refinancing of debt	(2,026,984)	-	-	(2,026,984)	-	-	-	-	-	(2,026,984)
	4,137,772	2,233,886	-	6,371,658	-	-	-	282,904	-	6,654,562
Excess of revenues over expenses	16,766,396	6,676,510	-	23,442,906	255,126	(8,472,896)	-	677,637	-	15,902,773
Net unrealized (losses)/gains on investments	(6,282,024)	(1,847,148)	-	(8,129,172)	-	-	-	1,459,158	-	(6,670,014)
Transfer to L & M Affiliate	(12,670,075)	3,228,509	-	(9,441,566)	178,123	9,263,443	-		-	-
Net assets released from restrictions used for purchases of property and equipment	176,082	-	-	176,082	-	-	-	-	-	176,082
Pension - related changes other than periodic pension costs	5,839,963	-	-	5,839,963	-	-	-	-	-	5,839,963
Decrease in unrestricted net assets	$ 3,830,342	$ 8,057,871	$ -	$ 11,888,213	$ 433,249	$ 790,547	$ -	$ 2,136,795	$ -	$ 15,248,804

Lawrence & Memorial Corporation and Subsidiaries
Consolidating Statement of Operations
Year Ended September 30, 2010

	Lawrence & Memorial Hospital	Lawrence & Memorial Corporation	Eliminating Entries	Obligated Group	L&M Systems, Inc.	LMPA	VNA of Southeastern Connecticut, Inc.	Eliminating Entries	Consolidated
Net revenues from services to patients	$ 314,168,301	$ -	$ -	314,168,301	$ -	$ -	$ 11,895,273	$ -	$ 326,063,574
Other operating revenues	9,926,307	1,839,886	-	11,766,193	2,526,955	2,513,560	3,103,359	(827,246)	19,082,821
Net assets released from restriction	412,940	478,575	-	891,515	-	-	-	-	891,515
	324,507,548	2,318,461	-	326,826,009	2,526,955	2,513,560	14,998,632	(827,246)	346,037,910
Operating expenses									
Salaries and wages	143,999,074	-	-	143,999,074	914,300	2,523,605	9,714,975	(229,278)	156,922,676
Employee benefits	40,325,006	-	-	40,325,006	346,137	909,151	2,361,280	(597,968)	43,343,606
Supplies	43,164,547	480,820	-	43,645,367	176,929	144,643	740,847	-	44,707,786
Purchased services	21,093,240	115,342	-	21,208,582	396,398	448,152	176,637	-	22,229,769
Other	29,171,055	76,723	-	29,247,778	522,190	587,347	658,483	-	31,015,798
Interest	2,332,245	-	-	2,332,245	4,773	-	36,676	-	2,373,694
Depreciation and amortization	16,728,407	7,680	-	16,736,087	168,695	-	256,152	-	17,160,934
Bad debts	15,052,335	-	-	15,052,335	670,481	1,619,872	125,000	(237,942)	17,229,746
	311,865,909	680,565	-	312,546,474	3,199,903	6,232,770	14,070,050	(1,065,188)	334,984,009
Income from operations	12,641,639	1,637,896	-	14,279,535	(672,948)	(3,719,210)	928,582	237,942	11,053,901
Nonoperating gains									
Unrestricted investment income	175,335	-	-	175,335	-	-	-	-	175,335
(Loss)/income on investments	2,341,396	(15,980,979)	-	(13,639,583)	(297,132)	-	99,780	17,169,074	3,332,139
	2,516,731	(15,980,979)	-	(13,464,248)	(297,132)	-	99,780	17,169,074	3,507,474
Excess of revenues over expenses	15,158,370	(14,343,083)	-	815,287	(970,080)	(3,719,210)	1,028,362	17,407,016	14,561,375
Net unrealized gains/(losses) on investments	5,459,058	1,901,354	-	7,360,412	-	-	772,831	-	8,133,243
Transfer to L & M Affiliate	(4,900,000)	4,900,000	-	-	(642,774)	642,774	-	-	-
Net assets released from restrictions used for purchases of property and equipment	181,470	-	-	181,470	-	-	-	-	181,470
Transfer to/from affiliate	-	-	-	-	694,257	-	-	-	694,257
Forgiveness of debt	-	-	-	-	399,419	3,181,689	-	(3,581,108)	-
Pension - related changes other than periodic pension costs	(7,611,564)	-	-	(7,611,564)	-	-	-	-	(7,611,564)
Decrease in unrestricted net assets	$ 8,287,334	$ (7,541,729)	$ -	$ 745,605	$ (519,178)	$ 105,253	$ 1,801,193	$ 13,825,908	$ 15,958,781