Audited Financial Statements and Other Financial Information

The William W. Backus Hospital
Years Ended September 30, 2009 and 2008
With Report of Independent Auditors

The William W. Backus Hospital

Audited Financial Statements
and Other Financial Information

Years Ended September 30, 2009 and 2008

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Report of Independent Auditors

The Board of Trustees
The William W. Backus Hospital

We have audited the accompanying balance sheets of The William W. Backus Hospital (the Hospital) as of September 30, 2009 and 2008, and the related statements of operations, changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Hospital's internal control over financial reporting. Our audits included 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 Hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit also 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 provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The William W. Backus Hospital as of September 30, 2009 and 2008, and the results of its operations, changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

December 1, 2009

The William W. Backus Hospital

Balance Sheets

	September 30 2009	September 30 2008
Assets		
Current assets:		
Cash and cash equivalents	**$ 57,570,735**	$ 46,717,416
Assets whose use is limited – required for current liabilities	**7,240,812**	6,648,187
Accounts receivable, less allowance for uncollectible accounts (2009 – $20,629,000; 2008 – $15,610,000)	**36,111,295**	33,683,248
Due from affiliates	**3,901,924**	3,388,030
Inventories of supplies	**3,252,641**	1,923,318
Prepaid expenses and other	**925,340**	1,779,906
Total current assets	**109,002,747**	94,140,105
Assets whose use is limited:		
Board-designated investments	**44,500,233**	43,002,912
Held by trustee	**22,743,662**	18,156,456
Total assets whose use is limited	**67,243,895**	61,159,368
Less assets whose use is limited – required for current liabilities	**7,240,812**	6,648,187
	60,003,083	54,511,181
Interest in Foundation	**41,147,474**	39,032,937
Property, plant, and equipment, net	**98,131,132**	95,130,673
Deferred financing costs	**2,025,397**	2,118,397
Other assets	**1,801,751**	3,788,338
Total assets	**$ 312,111,584**	$ 288,721,631

	September 30	
	2009	**2008**
Liabilities and net assets		
Current liabilities:		
Accounts payable – trade	**$ 10,508,835**	$ 9,994,419
Salaries and wages, payroll taxes, and taxes withheld from payroll	**8,205,022**	6,787,976
Other accrued liabilities	**6,325,794**	5,843,160
Due to third-party reimbursement agencies	**1,831,013**	1,270,638
Interest payable	**864,418**	880,518
Current portion of long-term debt	**1,825,000**	1,755,000
Total current liabilities	**29,560,082**	26,531,711
Other liabilities:		
Long-term debt – State of Connecticut Health and Educational Facilities Authority Revenue Bonds, less current portion	**63,931,536**	65,808,169
Employee related obligations	**84,442,697**	39,209,762
Self-insured professional liability	**10,580,762**	11,939,205
Due to third-party reimbursement agencies	**10,307,215**	3,892,438
Other	**667,654**	534,191
	169,929,864	121,383,765
Net assets:		
Unrestricted	**102,312,376**	132,409,920
Temporarily restricted	**3,447,432**	2,475,427
Permanently restricted	**6,861,830**	5,920,808
Total net assets	**112,621,638**	140,806,155
Total liabilities and net assets	**$ 312,111,584**	$ 288,721,631

See accompanying notes.

The William W. Backus Hospital

Statements of Operations

	Year Ended September 30 2009	2008
Operating revenues:		
Net patient service revenue	**$ 259,652,271**	$ 242,131,827
Other operating revenues	**4,213,341**	4,727,859
	263,865,612	246,859,686
Operating expenses:		
Salaries, wages, and professional fees	**112,184,033**	102,256,348
Payroll taxes and other fringe benefits	**27,425,902**	23,695,796
Supplies, insurance, and other	**74,547,698**	78,669,671
Provision for uncollectible accounts	**16,898,318**	14,162,003
Depreciation and amortization	**16,939,369**	16,453,137
Interest	**3,091,298**	3,003,005
	251,086,618	238,239,960
Operating income	**12,778,994**	8,619,726
Nonoperating gains and (losses):		
Income (loss) from investments	**2,799,208**	(4,802,633)
Change in value of swap		(843,514)
Other	**(366,280)**	201,183
Change in equity interest in net assets of Foundation	**(3,735,563)**	(167,456)
Excess of revenues over expenses	**$ 11,476,359**	$ 3,007,306

See accompanying notes.

The William W. Backus Hospital

Statements of Changes in Net Assets

	Total	Unrestricted	Temporarily Restricted	Permanently Restricted
Net assets, October 1, 2007	$ 163,733,063	$ 154,458,390	$ 2,945,255	$ 6,329,418
Excess of revenues over expenses	3,007,306	3,007,306		
Investment income	2,550		2,550	
Change in pension funding and postretirement obligation	(14,558,507)	(14,558,507)		
Change in equity interest in net unrealized losses of Foundation	(10,497,269)	(10,497,269)		
Change in equity interest in net assets of Foundation	(880,988)		(472,378)	(408,610)
Decrease in net assets	(22,926,908)	(22,048,470)	(469,828)	(408,610)
Net assets, September 30, 2008	140,806,155	132,409,920	2,475,427	5,920,808
Excess of revenues over expenses	**11,476,359**	**11,476,359**		
Investment income	**1,350**		**1,350**	
Effect of early measurement date elimination	**(1,762,428)**	**(1,762,428)**		
Change in pension funding and postretirement obligation	**(43,749,898)**	**(43,749,898)**		
Changes in equity interest in net unrealized gains of Foundation	**3,938,423**	**3,938,423**		
Change in equity interest in net assets of Foundation	**1,911,677**		**970,655**	**941,022**
(Decrease) increase in net assets	**(28,184,517)**	**(30,097,544)**	**972,005**	**941,022**
Net assets, September 30, 2009	**$ 112,621,638**	**$ 102,312,376**	**$ 3,447,432**	**$ 6,861,830**

See accompanying notes.

The William W. Backus Hospital

Statements of Cash Flows

	Year Ended September 30	
	2009	**2008**
Operating activities		
Decrease in net assets	**$ (28,184,517)**	$ (22,926,908)
Adjustments to reconcile decrease in net assets to net cash provided by operating activities:		
Depreciation and amortization	**16,939,369**	16,453,137
Provision for uncollectible accounts	**16,898,318**	14,162,003
Effect of early measurement date elimination	**1,762,428**	
Change in pension funding and postretirement obligation	**43,749,898**	14,558,507
(Purchase) proceeds from sale of investments – board designated, net	**(1,497,321)**	1,409,265
Change in equity interest in net assets of Foundation	**(2,114,537)**	13,542,282
Changes in operating assets and liabilities *(Note 15)*	**(12,446,239)**	(17,206,997)
Net cash provided by operating activities	**35,107,399**	19,991,289
Investing activities		
Purchase of investments – held in trust, net	**(4,587,206)**	(1,279,461)
Net additions to property, plant, and equipment	**(18,720,156)**	(15,818,207)
Decrease (increase) in other assets	**859,915**	(504,083)
Net cash used in investing activities	**(22,447,447)**	(17,601,751)
Financing activities		
Principal payments on long-term debt	**(1,755,000)**	(815,000)
Change in deferred financing costs and amortization of bond premium	**(51,633)**	(127,164)
Net cash used in financing activities	**(1,806,633)**	(942,164)
Net increase in cash and cash equivalents	**10,853,319**	1,447,374
Cash and cash equivalents at beginning of year	**46,717,416**	45,270,042
Cash and cash equivalents at end of year	**$ 57,570,735**	$ 46,717,416

See accompanying notes.

1. Significant Accounting Policies

Organization

The William W. Backus Hospital (the Hospital), a voluntary association incorporated under the General Statutes of the State of Connecticut, is a wholly-owned subsidiary of Backus Corporation (the sole member). The Board of Directors of Backus Corporation elects a Board of Trustees that has control of the operations of the Hospital. Refer to Note 7 for further discussion of related party transactions.

The financial statements include the operations of Backus Medical Center Condominium Association, Inc. (the Association). All intercompany transactions have been eliminated in consolidation.

Use of Estimates

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

Regulatory Matters

The Hospital is required to file annual operating information with the State of Connecticut Office of Health Care Access (OHCA).

Cash Equivalents

The Hospital considers all highly liquid time deposits, commercial paper, and money market mutual funds purchased with a maturity at date of acquisition of three months or less to be cash equivalents.

1. Significant Accounting Policies (continued)

Assets Whose Use Is Limited

The Board of Trustees has designated certain unrestricted funds, including principal and income, for construction and other purposes. The President and Chief Executive Officer of the Hospital may, after consultation with the Chairman, Vice Chairman, or the Board of Trustees, use board-designated funds, if required, to meet short-term operating cash requirements of the Hospital. Assets whose use is limited also include assets obtained through a financing arrangement with the State of Connecticut Health and Educational Facilities Authority (the Authority), as more fully explained in Note 6. The portion of those amounts required for funding current liabilities is included in current assets. The carrying amounts reported in the balance sheets are stated at fair value.

Investments

Marketable securities are classified as trading securities. Investments in debt and equity securities with readily determinable fair values are reported at fair value based on quoted market prices. Investment income or loss (including realized gains and losses on investments, interest and dividends) and the change in the net unrealized gains and losses are included in the excess of revenues over expenses unless the income or loss is restricted by the donor.

Inventories

Inventories are stated at the lower of cost (first-in, first-out method), or market.

Property, Plant, and Equipment

Property, plant, and equipment are stated on the basis of cost. The Hospital provides for depreciation using the straight-line method in amounts sufficient to depreciate the cost of its assets over their estimated useful lives.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the Hospital 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 Hospital in perpetuity.

1. Significant Accounting Policies (continued)

Nonoperating Gains and Losses

Activities other than those in connection with providing health care services are considered to be nonoperating. Nonoperating gains and losses primarily consist of income on invested funds, and changes in the equity interest in net assets of Backus Foundation, Inc. (the Foundation).

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 as unrestricted net assets and reported in the statements of operations and changes in net assets as net assets released from restrictions, which is included in other operating revenue. Donor-restricted contributions whose restrictions are met within the same year as received are classified as unrestricted contributions in the accompanying financial statements.

General and Professional Liability Self-Insurance

The Hospital has adopted the policy of self-insuring the deductible portion of its general and professional liability insurance coverage. The deductible limits are $1,000,000 per claim and $4,000,000 annually for 2009 and for 2008. Management accrues its best estimate of ultimate losses for both reported claims and claims incurred but not reported.

Excess of Revenues Over Expenses

The statements of operations and changes in net assets include excess of revenues over expenses. Changes in unrestricted net assets which are excluded from the excess of revenues over expenses (the performance indicator), consistent with industry practice, include changes in equity interest in net unrealized gains of Foundation, change in equity interest in net assets of Foundation, the change in pension funding and postretirement obligation changes in the fair value of the interest rate swap, and the effect of early measurement date elimination.

1. Significant Accounting Policies (continued)

Interest in Foundation

The interest in Foundation represents the Hospital's interest in the net assets of the Foundation. This investment is accounted for in accordance with the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 958-20, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others*.

Income Taxes

The Hospital 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 income taxes on related income pursuant to Section 501(a) of the Code. The Association is a taxable entity; however, any taxes are immaterial to the financial statements of the Hospital taken as a whole.

ASC 740-10, *Uncertain Tax Positions*, prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, and disclosure requirements for uncertain tax positions. Management has evaluated the implications of ASC 740-10 and determined that its impact on the financial statements is not significant.

Adoption of New Authoritative Pronouncements

In June 2009, FASB issued FASB ASC 105, *Generally Accepted Accounting Principles* (ASC 105), which establishes the FASB Accounting Standards Codification as the sole source of authoritative generally accepted accounting principles. Pursuant to the provisions of ASC 105, the Hospital has updated references to GAAP in its financial statements for the year ended September 30, 2009. The adoption of ASC 105 did not impact the Hospital's financial position or results of operations.

Effective 2009, the Hospital adopted ASC 820-10, *Fair Value*, which defines fair value, establishes a framework for measuring fair value in accordance with GAAP, and expands disclosure about fair value measurements.

In 2009, the Hospital adopted ASC 825-10, *Fair Value Option*, which permits companies to choose to measure certain financial instruments and other items at fair value that are not currently required to be measured at fair value. The Hospital did not elect fair value accounting for any asset or liability not currently required to be measured at fair value.

1. Significant Accounting Policies (continued)

In June 2009, the Hospital adopted the provisions of ASC 855-10, *Subsequent Events*, which establishes standards of accounting for disclosure of events or transactions that occur after the balance sheet date, but before the financial statements are issued or available to be issued. ASC 855-10 is effective on a prospective basis for financial periods ended after June 15, 2009. The Hospital evaluated the impact of subsequent events through December 1, 2009, representing the date at which the financial statements were available to be issued. The adoption of ASC 855-10 in 2009 did not impact the Hospital's financial position or results of operations. Management evaluated subsequent events through December 1, 2009, the date the financial statements were available to be issued.

2. Revenues from Services to Patients and Charity Care

Net patient service revenue for the years ended September 30, 2009 and 2008 consists of the following:

	Year Ended September 30	
	2009	**2008**
Gross patient service revenue	**$ 560,641,054**	$ 512,314,357
Deductions:		
Allowances	**(294,073,379)**	(263,580,702)
Charity care (at charges)	**(6,915,404)**	(6,601,828)
	(300,988,783)	(270,182,530)
	$ 259,652,271	$ 242,131,827

Patient accounts receivable and revenues are recorded when patient services are performed. Differences between amounts received from most third-party payors and the established billing rates of the Hospital are accounted for as allowances.

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. Changes in estimates increased net patient service revenue by approximately $671,000 and $3,600 in 2009 and 2008, respectively.

2. Revenues from Services to Patients and Charity Care (continued)

Revenues from the Medicare and Medicaid programs accounted for approximately 28% and 7%, respectively, of the Hospital's net patient service revenue for the year ended September 30, 2009 and 30% and 6% for the year ended September 30, 2008. 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 such regulatory inquiries are outstanding, 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 the reduction of funding levels could have an adverse impact on the Hospital.

3. Charity Care

The Hospital provides services without charge, or at amounts less than its established rates, to patients who meet the criteria of its charity care policy. Because the Hospital does not pursue collection of amounts determined to be charity care, such services are not reported as net revenue. The Hospital's charity care policy utilizes the generally recognized poverty income levels for the state. For patients who do not apply or do not qualify, the uncollected amounts are recognized as bad debt expense.

Together, charity care and bad debt expense represent uncompensated care. The following summarizes uncompensated care:

	At Charge	Estimated Cost
Charity care	**$ 6,915,404**	**$ 3,042,778**
Bad debt	**16,898,318**	**7,435,260**
Total uncompensated care, September 30, 2009	**$ 23,813,722**	**$ 10,478,038**
Charity care	$ 6,601,828	$ 3,016,131
Bad debt	14,162,003	6,470,095
Total uncompensated care, September 30, 2008	$ 20,763,831	$ 9,486,226

Estimated cost is based on the ratio of cost to charges, as determined by Hospital-specific data.

4. Investments

Investment income and gains (losses) are comprised of the following for the years ended September 30, 2009 and 2008:

	Year Ended September 30 2009	2008
Realized and unrealized gains (losses) on investments	**$ 1,621,546**	$ (5,689,835)
Interest and dividend income	**1,331,067**	1,352,412
Other investment income (loss)	**14,767**	(222,664)
Investment fees	**(168,172)**	(242,546)
	$ 2,799,208	$ (4,802,633)

The market value of assets whose use is limited at September 30 is set forth in the following table:

	2009	2008
Board designated:		
Cash and cash equivalents	**$ 16,508,452**	$ 16,123,886
Common stocks	**13,153,726**	11,361,170
Government bonds	**9,679,063**	12,538,088
Corporate bonds	**5,158,992**	2,979,768
	$ 44,500,233	$ 43,002,912
Held by trustee:		
Mutual funds	**$ 17,496,461**	$ 9,613,200
Cash and cash equivalents	**4,804,214**	8,096,731
Government bonds	**442,987**	446,525
	$ 22,743,662	$ 18,156,456

In 2009, the Hospital adopted ASC 958-205, *Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act and Enhanced Disclosures for All Endowment Funds,* which, among other things, provides guidance on the net asset classification of donor-restricted endowment funds subject to the Uniform Prudent Management of Institutional Funds Act (UPMIFA), as well as requiring additional disclosures about endowment funds.

4. Investments (continued)

The Board of Trustees of the Hospital has interpreted UPMIFA as requiring the preservation of the fair value of the original gift at the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result, the Hospital classifies as permanently restricted net assets (a) the original value of the gifts donated to the permanent endowment, (b) the original value of the 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 primary objective of the endowment fund is to provide long-term support for the Hospital's capital and operating programs. The Hospital's investment goals are to maximize total return (capital appreciation, dividends and interest) while also protecting the Hospital's inflation-adjusted value over time. The Hospital's assets are diversified across multiple asset classes (e.g., common stocks, bonds and cash) to achieve an optimal balance between risk and return and between current income and capital appreciation. The investment program is structured to offer reasonably high probability of generating a real return of 5% per year over a period of five to ten years to protect the real inflation-adjusted value of assets and to meet the spending requirements. The Investment Committee reviews investment policies annually to determine if changes need to be made due to changing market conditions or other factors.

Management evaluates endowment spending in light of capital replacement and expansion plans. The spending policy does not apply a prescribed rate of spending in a given year, but does consider expenditures based on need and current market conditions as well as long-term investment goals.

4. Investments (continued)

Endowment assets are donor-restricted gifts which are meant to provide a permanent source of income to the Hospital and are included in permanently restricted net assets. The activity for the year ended September 30, 2009 is as follows:

	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets at beginning of year		$ 3,871,631	$ 3,871,631
Investment return:			
Investment income		85,680	85,680
Net appreciation (realized and unrealized)		49,535	49,535
Earnings reclassified	$ 135,215	(135,215)	
Total investment return	135,215	3,871,631	4,006,846
Contributions		970,000	970,000
Endowment net assets at end of year	$ 135,215	$ 4,841,631	$ 4,976,846

5. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available for the following purposes at September 30:

	2009	2008
Capital projects	**$ 1,548,434**	$ 933,829
Preventive care	**763,501**	778,537
Health care services	**414,281**	340,180
Other	**358,416**	66,956
Laboratory	**184,552**	181,410
Extraordinary nursing care	**97,635**	96,765
Nursing education	**70,948**	68,085
Free beds	**9,665**	9,665
	$ 3,447,432	$ 2,475,427

5. Temporarily and Permanently Restricted Net Assets (continued)

Permanently restricted net assets at September 30 are restricted to the following:

	2009	2008
Income to be used:		
For general uses and purposes	**$ 6,018,245**	$ 5,077,223
To provide free beds	**527,060**	527,060
For laboratory	**258,182**	258,182
To provide extraordinary nursing care	**48,203**	48,203
For nursing education	**10,140**	10,140
	$ 6,861,830	$ 5,920,808

6. Long-term Debt

A summary of long-term debt at September 30 is as follows:

	2009	2008
Tax-exempt Hospital Revenue Bonds:		
Series E, serial maturities ($1,630,000) from 2010 to 2012, with interest rates ranging from 4.60% to 4.80%, term maturities ($7,515,000) from 2017 to 2022 at an interest rate of 5.00%	**$ 9,145,000**	$ 9,640,000
Series F, serial maturities ($7,300,000) from 2010 to 2018, with interest rates of 4.00% to 4.25%, term maturities ($22,125,000) from 2023 to 2035 with interest rates of 5.00% to 5.25%	**29,425,000**	30,100,000
Series G, serial maturities ($18,960,000) from 2010 to 2026, with interest rates of 3.25% to 5.00%, term maturities ($7,420,000) in 2035 at an interest rate of 5%	**26,380,000**	26,965,000
	64,950,000	66,705,000
Add net unamortized bond premium	**806,536**	858,169
Less current portion	**(1,825,000)**	(1,755,000)
Long-term debt	**$ 63,931,536**	$ 65,808,169

6. Long-Term Debt (continued)

The Master Indenture, as amended and supplemented by Supplemental Master Indenture No. 4, provides for, among other things, a pledge of the gross receipts, as defined, of the Hospital, restriction on the incurrence of certain indebtedness of the Hospital, and covenants regarding the Hospital's debt service coverage ratios, sale and lease of assets, and other covenants similar in financings of this type. The bonds are secured by the real property of the Hospital, including all buildings and equipment. Pursuant to the loan agreements, the Hospital is obligated to provide amounts which will be sufficient to enable the Authority to pay the principal and interest on the Series E, Series F and Series G bonds.

Series E bonds maturing on or after July 1, 2008 are subject to redemption prior to maturity. Series F bonds maturing after July 1, 2018 are subject to optional redemption prior to maturity. Series G bonds maturing on or before July 1, 2015 are not subject to optional redemption prior to maturity; however, those maturing after July 1, 2015 are subject to optional redemption prior to maturity.

Future minimum principal payments during each of the next five fiscal years, and in the aggregate, are as follows:

2010	$ 1,825,000
2011	1,895,000
2012	1,965,000
2013	2,045,000
2014	2,120,000
Aggregate thereafter	55,100,000
	64,950,000
Less current portion	1,825,000
Add net unamortized bond premium	806,536
	$ 63,931,536

The Hospital paid interest of $3,158,024 and $2,706,703 in 2009 and 2008, respectively. Interest incurred in 2009 and 2008 was $3,091,298 and $3,003,005, respectively.

In June 2008 the Hospital remarketed its Series F bonds, converting them from a variable auction rate to a fixed rate. As a result, the swap associated with the original bond issue, which was intended to effectively fix the interest rate paid on the bonds, was terminated. The change in the value of the swap presented in the statement of operations at September 30, 2008 of $(843,514) reflects the change in the fair value of the swap plus the reclassification of prior deferrals.

7. Related Party Transactions

Amounts due from affiliates at September 30, 2009 and 2008 includes advances to Backus Properties of approximately $1,720,000 and $1,883,000 for building improvements and property acquisitions during 2009 and 2008, respectively. Amounts due from the Foundation include monies in support of charity care and Hospital programs of approximately $43,000 and $93,000 for 2009 and 2008, respectively. In addition, the Hospital processes payroll and disbursements for several of its affiliated entities for which it is reimbursed. Reimbursements due to the Hospital at September 30, 2009 and 2008 were approximately $668,000 and $760,000, respectively.

The Hospital has unconditionally guaranteed full and prompt payment and performance of all liabilities of an affiliate organization to the lessor for a term of twenty years. The maximum potential amount of future payments includes lease payments for the first ten years of $2,095,890. Payments over the remaining term of the lease are based on a future interest rate that is not yet determinable. There are no recourse provisions available to the Hospital upon breach of contract by the affiliate.

Subsequent to year end, Backus Foundation Inc. and Backus Properties Inc. (Properties) will cease to exist as separate entities and all assets, liabilities, equity and operations will merge into the Hospital. The merger of the Foundation will not impact net assets as it is currently accounted for under ASC 958-20 as described in Note 1. The merger of Properties will result in an increase in unrestricted net assets of approximately $1,400,000.

8. Retirement Benefit Plans

The Hospital maintains a noncontributory defined benefit pension plan covering substantially all of its employees. The Hospital also provides noncontributory postretirement health care benefits to eligible retirees and eligible spouses of retirees who retired prior to January 1, 1994. Subsequent to 1993, covered retirees contribute a percentage of the costs based on years of service. In addition, the Hospital sponsors a nonqualified pension benefit program. Included in long-term liabilities at September 30, 2009 and 2008 is approximately $3,600,000 and $850,000, respectively, related to the future obligation for the nonqualified benefits.

Effective January 1, 2010, the Hospital will amend its defined benefit pension plan to close the plan to new participants and to freeze accruals for the existing participants. Management anticipates that the change in the pension plan will result in a reduction of the unfunded liability of approximately $35 million. It is the Hospital’s intention to establish a defined contribution plan concurrent with the amendment of the defined benefit plan.

8. Retirement Benefit Plans (continued)

Effective October 1, 2008, the Hospital adopted ASC 715-20, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, which requires elimination of the early measurement date of the plans.

Included in unrestricted net assets at September 30 are the following amounts that have not yet been recognized in net periodic benefit cost:

	Pension Benefits		Postretirement Benefits	
	2009	**2008**	**2009**	**2008**
	(In thousands)			
Unrecognized actuarial (loss) gain	**$ (67,240)**	$ (26,335)	**$ 1,249**	$ 2,223
Unrecognized prior service cost	**(15)**	(19)		
Unrecognized transition obligation			**(1,213)**	(1,617)
	$ (67,255)	$ (26,354)	**$ 36**	$ 606

The prior service cost, actuarial (loss) gain and transition obligation included in unrestricted net assets and expected to be recognized in net periodic benefit cost during the year ending September 30, 2010 are $3,323, $5,129,108 and $323,491, respectively.

At September 30, 2008, the unfunded status of the pension plan is included in long-term liabilities in the amount of $30,206,752. The unfunded status of the postretirement benefits is $5,045,761, with $479,175 included in short-term liabilities, and the remainder of $4,566,586 included in long-term liabilities. At September 30, 2009, the unfunded status of the pension plan is included in long-term liabilities in the amount of $71,685,446. The unfunded status of the postretirement benefits is $4,968,915, with $462,097 included in short-term liabilities, and the remainder of $4,506,818 included in long-term liabilities.

8. Retirement Benefit Plans (continued)

The following table sets forth the funded status of the plans as of the measurement date of September 30 in 2009 and June 30 in 2008 for each plan and amounts recognized in the Hospital's balance sheets at September 30. In 2008, contributions made subsequent to the measurement date, but prior to September 30, reduced the accrued benefit liability.

	Pension Benefits		Postretirement Benefits	
	2009	**2008**	**2009**	**2008**
	(In thousands)			
Change in projected benefit obligation				
Benefit obligation at beginning of year	**$ (133,189)**	$ (124,809)	**$ (5,156)**	$ (5,524)
Service cost	**(4,484)**	(4,620)	**(22)**	(30)
Interest cost	**(9,002)**	(7,986)	**(338)**	(334)
Change in assumptions	**(38,217)**	5,256	**(558)**	134
Actuarial (loss) gain	**(2,156)**	(4,249)	**382**	199
Effect of early measurement date elimination	**11,740**		**295**	
Benefits paid	**3,477**	3,219	**428**	399
Benefit obligation at end of year	**$ (171,831)**	$ (133,189)	**$ (4,969)**	$ (5,156)
Change in plan assets				
Fair value of plan assets at beginning of year	**$ 100,957**	$ 102,625		
Actual return on plan assets	**2,662**	(7,224)		
Effect of early measurement date elimination	**(8,097)**			
Contributions	**8,100**	8,775	**$ 428**	$ 399
Benefits paid	**(3,477)**	(3,219)	**(428)**	(399)
Fair value of plan assets at end of year	**$ 100,145**	$ 100,957	**$**	$
Reconciliation of underfunded status				
Underfunded status	**$ (71,686)**	$ (32,232)	**$ (4,969)**	$ (5,156)
Contribution subsequent to measurement date		2,025		111
Accrued benefit liability recognized in the balance sheets	**$ (71,686)**	$ (30,207)	**$ (4,969)**	$ (5,045)
Components of net periodic benefit cost				
Service cost	**$ 4,484**	$ 4,620	**$ 22**	$ 30
Interest cost	**9,002**	7,986	**338**	334
Expected return on plan assets	**(7,605)**	(8,417)		
Net amortization and deferral	**1,129**	3	**(541)**	(260)
Net periodic benefit cost	**$ 7,010**	$ 4,192	**$ (181)**	$ 104

8. Retirement Benefit Plans (continued)

	Pension Benefits		Postretirement Benefits	
	2009	**2008**	**2009**	**2008**
	(In thousands)			
Assumptions**:**				
Weighted-average assumptions used to determine benefit obligations:				
Discount rate	**5.60%**	6.50%	**5.60%**	6.50%
Rate of compensation increase	**5.00**	5.00		
Weighted-average assumptions used to determine net periodic benefit cost:				
Discount rate	**7.25**	6.25	**7.25**	6.25
Expected long-term rate of return on plan assets	**8.00**	8.00		
Rate of compensation increase	**5.00**	5.00		

The expected long-term rate of return on plan assets was determined by the expected return on each asset class based on a model that considers historical and expected future performance.

The accumulated benefit obligation at September 30, 2009 and 2008 was $137,279,286 and $107,697,366, respectively.

The asset allocations for the retirement plan at the end of 2009 and 2008 and the target allocation by asset category are as follows:

	Target Allocation		Percentage of Plan Assets	
Asset Category	**Minimum**	**Maximum**	**2009**	**2008**
US Equity Large Cap	35%	45%	**27%**	34%
US Equity Small Cap		10	**4**	5
International Equity	17	27	**17**	19
Core Fixed Income	25	35	**52**	42
Real estate		6		
Total			**100%**	100%

8. Retirement Benefit Plans (continued)

Information about the expected cash flows for both plans is as follows:

	Pension Benefits	Postretirement Benefits
Expected employer contributions for 2010	$ 8,100,000	$ 462,097
Estimated future benefit payments:		
2010	4,462,917	462,097
2011	4,982,416	464,756
2012	5,495,548	472,761
2013	6,025,576	481,792
2014	6,719,521	481,673
2015-2019	46,736,124	2,066,165

Assumed healthcare cost trend rates for 2009 are as follows:	
Health care trend rate assumed for next year	8.50%
Rate to which the cost rate trend rate is assumed to decline (the ultimate trend rate)	5.00%
Year that the rate reaches the ultimate trend rate	2014

A one-percentage-point change in assumed health care cost trend rates would have the following effects on the postretirement benefit plan:

	One-Percentage-Point Increase	One-Percentage-Point Decrease
	(In thousands)	
Effect on total of service and interest cost components	$ 2	$ (2)
Effect on postretirement benefit obligation	$ 26	$ (22)

9. Property, Plant, and Equipment

Property, plant, and equipment at September 30 consist of the following:

	2009	2008
Land and land improvements	**$ 2,408,486**	$ 2,373,312
Buildings and leasehold improvements	**109,893,844**	102,370,729
Equipment	**95,975,645**	86,262,740
Construction in process (2009 estimated cost to complete $6,900,000)	**4,251,661**	4,429,799
Less accumulated depreciation	**(114,398,504)**	(100,305,907)
	$ 98,131,132	$ 95,130,673

Included in construction in progress at September 30, 2009 are $1,280,000 of internally developed software costs. The Hospital wrote off approximately $1,426,000 of fully depreciated assets in 2009.

In 2004, the Hospital began leasing space to be used for patient services. The initial lease term is for a period of ten years, with two five-year renewal options available at the discretion of the Hospital. Rent expense for the years ended September 30, 2009 and 2008 was $705,436 and $667,384, respectively.

The Hospital leases various types of equipment with annual payments ranging from $103 to $119,064. Expenses as a result of these leases were approximately $478,000 and $928,000 for the years ended September 30, 2009 and 2008, respectively.

The Hospital also leases various properties from a related party. Rent expense for those leases totaled approximately $644,000 and $610,000 for the years ended September 30, 2009 and 2008, respectively. As described in Note 7, the related party will be merged with the Hospital for years beginning in 2010. As a result, no lease payments to that related party are included in the future minimum payments listed below. However, leases between the related party and unrelated lessors are included.

9. Property, Plant, and Equipment (continued)

Future minimum lease payments under the above leases during each of the next five years were as follows:

2010	$ 1,233,982
2011	1,042,391
2012	775,265
2013	748,603
2014	145,161
Aggregate thereafter	1,102,588
	$ 5,047,990

10. Concentrations of Credit Risk

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of accounts receivable, net of contractual allowances, from patients and third-party payors at September 30 is as follows:

	2009	**%**	**2008**	**%**
Medicare	**$ 14,223,122**	**25%**	$ 12,265,855	25%
Medicaid	**4,685,984**	**8**	3,166,368	6
Anthem Blue Cross/Blue Shield	**7,989,343**	**14**	8,128,274	16
Health Maintenance Organizations	**9,452,755**	**17**	7,671,571	16
Commercial	**2,776,338**	**5**	3,140,618	6
Self pay	**13,430,756**	**24**	11,688,493	24
Other state agencies	**4,182,234**	**7**	3,231,784	7
	56,740,532	**100%**	49,292,963	100%
Less allowance for uncollectible accounts	**20,629,237**		15,609,715	
	$ 36,111,295		$ 33,683,248	

11. Contingencies

There have been malpractice claims that fall within the Hospital's partially self-insured program (see Note 1) which have been asserted against the Hospital. In addition, there are known incidents that have occurred through September 30, 2009 that may result in the assertion of claims. Hospital management, in conjunction with its consulting actuaries, has accrued its best estimate of these contingent losses.

11. Contingencies (continued)

The Hospital is a party to various lawsuits incidental to its business. Management believes that the lawsuits will not have a material adverse effect on the Hospital's financial position or results of operations.

12. Other Operating Revenues

Other operating revenues consist of the following:

	Year Ended September 30	
	2009	**2008**
Cafeteria sales	**$ 1,049,650**	$ 989,415
Grants	**642,728**	630,810
Rental income	**568,148**	482,704
Interest	**476,907**	1,505,928
Condominium income	**440,047**	306,803
Miscellaneous	**424,282**	326,336
Child care	**336,700**	350,051
Purchase discounts	**274,879**	135,812
	$ 4,213,341	$ 4,727,859

13. Functional Expenses

The Hospital provides inpatient medical and surgical, outpatient, psychiatric and emergency care services to residents of eastern Connecticut. Expenses related to providing these services are as follows:

	Year Ended September 30	
	2009	**2008**
Health care services	**$ 188,561,536**	$ 180,224,412
General and administrative	**62,525,082**	58,015,548
	$ 251,086,618	$ 238,239,960

Costs for interest and insurance are included in general and administrative expenses. Malpractice insurance is included in health care services.

14. Fair Value of Financial Instruments

On October 1, 2008, the Hospital adopted ASC 820-10, *Fair Value*, which defines fair value, establishes a framework for measuring fair value in accordance with U.S. GAAP, and expands disclosure about fair value measurements.

Fair value, as defined in ASC 820-10, is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. To increase consistency and comparability, ASC 820-10 established a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels. Level one inputs are quoted market prices in active markets that are accessible at the measurement date. Level two inputs are observable, but not quoted in active markets. Level three inputs are unobservable and are used when little or no market data is available.

Financial assets as of September 30, 2009 are classified in the table below:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	$ 57,570,735			$ 57,570,735
Assets whose use is limited	67,243,895			67,243,895

The carrying amount of certain of the Hospital's financial instruments, including cash and cash equivalents, approximate fair value due to the relatively short maturities of such instruments. Fair values of investments are based on quoted market prices and are recorded on the balance sheets as such. Fair value of the long-term debt is estimated using discounted cash flow analysis which is based on the AAA insured bond rate at fiscal year end. The fair value of long-term debt is $68,087,973 and $65,336,934 at September 30, 2009 and 2008, respectively.

15. Cash Flows

Changes in operating assets and liabilities at September 30 include the following:

	2009	2008
Increase in assets:		
Accounts receivable	**$ (19,326,365)**	$ (17,003,287)
Due from affiliates	**(513,894)**	(1,144,405)
Inventories of supplies, prepaid expenses, and other	**(474,757)**	(25,215)
Increase (decrease) in liabilities:		
Due to third-party reimbursement agencies	**6,975,152**	2,676,010
Accounts payable	**514,416**	(3,105,471)
Employee related obligations	**(279,391)**	(3,431,132)
Interest payable and other accrued liabilities	**466,534**	(15,500)
Salaries and wages, payroll taxes, and taxes withheld from payroll	**1,417,046**	1,264,820
Self-insured professional liability	**(1,358,443)**	3,297,056
Other liabilities	**133,463**	280,127
Changes in operating assets and liabilities	**$ (12,446,239)**	$ (17,206,997)

Other Financial Information

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Report of Independent Auditors on
Other Financial Information

Board of Trustees
The William W. Backus Hospital

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The consolidating information is presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information has been subjected to the auditing procedures applied in our audits of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Ernst & Young LLP

December 1, 2009

The William W. Backus Hospital

Consolidating Balance Sheet

September 30, 2009

	The William W. Backus Hospital	Backus Medical Center Condominium Association, Inc.	Eliminations	Consolidated
Assets				
Current assets:				
Cash and cash equivalents	$ 57,570,735			$ 57,570,735
Assets whose use is limited – required for current liabilities	7,240,812			7,240,812
Accounts receivable, less allowance for uncollectible accounts	36,111,295			36,111,295
Due from affiliates	3,901,924			3,901,924
Inventories of supplies	3,252,641			3,252,641
Prepaid expenses and other	905,576	$ 19,764		925,340
Total current assets	108,982,983	19,764		109,002,747
Assets whose use is limited:				
Board-designated investments	44,500,233			44,500,233
Held by trustee	22,743,662			22,743,662
Total assets whose use is limited	67,243,895			67,243,895
Less assets whose use is limited – required for current liabilities	7,240,812			7,240,812
	60,003,083			60,003,083
Interest in Foundation	41,147,474			41,147,474
Property, plant, and equipment, net	98,131,132			98,131,132
Deferred financing costs	2,025,397			2,025,397
Other assets	1,801,751			1,801,751
Total assets	$ 312,091,820	$ 19,764		$ 312,111,584

The William W. Backus Hospital

Consolidating Balance Sheet (continued)

September 30, 2009

	The William W. Backus Hospital	Backus Medical Center Condominium Association, Inc.	Eliminations	Consolidated
Liabilities and net assets				
Current liabilities:				
Accounts payable – trade	$ 10,508,835			$ 10,508,835
Salaries and wages, payroll taxes, and taxes withheld from payroll	8,205,022			8,205,022
Other accrued liabilities	6,324,099	$ 1,695		6,325,794
Due to third-party reimbursement agencies	1,831,013			1,831,013
Interest payable	864,418			864,418
Current portion of long-term debt	1,825,000			1,825,000
Total current liabilities	29,558,387	1,695		29,560,082
Other liabilities:				
Long-term debt, less current portion	63,931,536			63,931,536
Employee related obligations	84,442,697			84,442,697
Self-insured professional liability	10,580,762			10,580,762
Due to third-party reimbursement agencies	10,307,215			10,307,215
Other	667,654			667,654
	169,929,864			169,929,864
Net assets:				
Unrestricted	102,294,307	18,069		102,312,376
Temporarily restricted	3,447,432			3,447,432
Permanently restricted	6,861,830			6,861,830
Total net assets	112,603,569	18,069		112,621,638
Total liabilities and net assets	$ 312,091,820	$ 19,764		$ 312,111,584

The William W. Backus Hospital

Consolidating Statement of Operations

Year Ended September 30, 2009

	The William W. Backus Hospital	Backus Medical Center Condominium Association, Inc.	Eliminations	Consolidated
Operating revenues:				
Net patient service revenue	$ 259,652,271			$ 259,652,271
Other operating revenues	3,773,294	$ 482,183	$ (42,136)	4,213,341
	263,425,565	482,183	(42,136)	263,865,612
Operating expenses:				
Salaries, wages, and professional fees	112,184,033			112,184,033
Payroll taxes and other fringe benefits	27,425,902			27,425,902
Supplies, insurance, and other	74,107,651	482,183	(42,136)	74,547,698
Provision for uncollectible accounts	16,898,318			16,898,318
Depreciation and amortization	16,939,369			16,939,369
Interest	3,091,298			3,091,298
	250,646,571	482,183	(42,136)	251,086,618
Operating income	12,778,994			12,778,994
Nonoperating gains and (losses):				
Income from investments	2,799,208			2,799,208
Other	(366,280)			(366,280)
Change in equity interest in net assets of Foundation	(3,735,563)			(3,735,563)
Excess of revenues over expenses	$ 11,476,359			$ 11,476,359