

Gaylord Farm Association, Inc.

Independent Auditors' Report,
Consolidated Financial Statements and
Supplemental Information

As of and for the Years Ended
September 30, 2010 and 2009



Saslow Lufkin & Buggy, LLP
Certified Public Accountants and Consultants

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and Supplemental Information
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Independent Auditors' Report

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

We have audited the accompanying consolidated balance sheets of Gaylord Farm Association, Inc. (the Association) as of September 30, 2010 and 2009, and the related consolidated statements of operations and changes in net assets and shareholder's equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the financial statements of Gaylord Risk Solutions, Ltd., a wholly-owned subsidiary, whose statements reflect total assets of \$5,477,101 and \$4,838,777 as of September 30, 2010 and 2009, and total revenues of \$575,000 and \$717,500 and net income of \$328,315 and \$393,051 for the years then ended, respectively. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Gaylord Risk Solutions, Ltd., is based solely on the report of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Gaylord Farm Association, Inc. as of September 30, 2010 and 2009, and the results of its consolidated operations and its consolidated cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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

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Gaylord Farm Association, Inc.
Consolidated Balance Sheets
September 30, 2010 and 2009

	2010	2009
Assets		
Current assets:		
Cash and cash equivalents	\$ 2,376,012	\$ 2,251,036
Patient accounts receivable (less allowance for doubtful accounts of \$540,000 in 2010 and \$1,191,000 in 2009)	9,115,849	9,693,724
Assets whose use is limited:		
Assets held under bond indenture agreement	171,783	165,242
Pledges receivable	495,086	580,943
Other current assets	1,725,017	1,579,387
Total current assets	13,883,747	14,270,332
Assets whose use is limited:		
Pledges receivable	689,220	1,202,392
Board-designated investments	16,458,755	16,195,439
Donor restricted investments	5,500,469	4,986,216
Beneficial interest in trusts held by others	10,168,420	9,943,906
	32,816,864	32,327,953
Property, plant and equipment, net	44,202,592	46,412,564
Investments held for captive insurance liabilities	3,909,996	3,124,034
Reinsurance recoverable relating to captive insurance liabilities	757,650	698,135
Other assets (Note 7)	1,181,912	1,084,773
	\$ 96,752,761	\$ 97,917,791
Liabilities, Net Assets and Shareholder's Equity		
Current liabilities:		
Accounts payable and accrued expenses	\$ 5,100,337	\$ 5,380,169
Accrued payroll and related taxes	3,375,453	3,285,598
Line of credit	1,025,000	1,625,000
Estimated amounts due to third-party payers	246,806	246,806
Current portion of accrued pension obligation	2,086,158	1,244,534
Current portion of long-term debt and capital lease obligations	1,453,373	1,399,430
Total current liabilities	13,287,127	13,181,537
Long-term debt and capital lease obligations, less current portion	21,086,278	22,263,901
Accrued pension obligation	13,002,959	13,649,806
Captive insurance reserves	3,049,299	3,005,963
Interest rate swap liability	3,647,029	2,632,838
Total liabilities	54,072,692	54,734,045
Net assets and shareholder's equity:		
Unrestricted net assets	23,044,098	24,307,925
Temporarily restricted net assets	1,781,818	2,148,726
Permanently restricted net assets	15,668,889	14,930,122
Shareholder's equity	2,185,264	1,796,973
Total net assets and shareholder's equity	42,680,069	43,183,746
	\$ 96,752,761	\$ 97,917,791

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

Gaylord Farm Association, Inc.
Consolidated Statements of Operations and
Changes in Net Assets and Shareholder's Equity
For the Years Ended September 30, 2010 and 2009

	2010	2009
Revenues:		
Net patient service revenue	\$ 67,801,584	\$ 66,829,960
Contributions and bequests	872,470	695,886
Ceded premium	(364,465)	(389,199)
Other operating revenue	677,534	635,021
Net assets released from restrictions used for operations	181,824	225,494
Total revenues	69,168,947	67,997,162
Expenses:		
Salaries and related expenses	45,433,743	46,610,184
Other operating expenses	5,392,045	5,008,972
Professional fees and contract services	6,624,882	5,308,794
Supplies	5,781,010	4,975,353
Depreciation and amortization	3,857,884	3,709,051
Occupancy costs	1,843,607	2,203,004
Provision for bad debts	802,494	616,185
Interest	965,660	914,053
Losses and loss adjustment expenses	157,126	252,379
Total expenses	70,858,451	69,597,975
Loss from operations	(1,689,504)	(1,600,813)
Other (losses) gains:		
Dividend and interest income	573,473	648,145
Net realized gains (losses) on investments	37,303	(1,255,984)
Loss on equity investments	(92,815)	(223,957)
Change in fair value of interest rate swap agreement	(1,014,191)	(1,496,063)
Loss on lease abandonment	(147,543)	(92,035)
Total other (losses) gains	(643,773)	(2,419,894)
Excess of revenues over (under) expenses	\$ (2,333,277)	\$ (4,020,707)

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

Gaylord Farm Association, Inc.
Consolidated Statements of Operations and
Changes in Net Assets and Shareholder's Equity (continued)
For the Years Ended September 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Unrestricted net assets:		
Excess of revenues over (under) expenses	\$ (2,333,277)	\$ (4,020,707)
Net unrealized gains on investments	1,508,283	766,643
Pension related changes other than net periodic pension cost	(795,655)	(8,671,657)
Net income of GRS	(328,315)	(393,051)
Net assets released from restrictions used for purchases of property, plant and equipment	685,137	1,259,334
Change in unrestricted net assets	<u>(1,263,827)</u>	<u>(11,059,438)</u>
Temporarily restricted net assets:		
Restricted pledges and contributions	500,053	719,682
Net assets released from restrictions	(866,961)	(1,484,828)
Change in temporarily restricted net assets	<u>(366,908)</u>	<u>(765,146)</u>
Permanently restricted net assets:		
Restricted contributions and bequests	514,253	48,013
Change in beneficial interest in trusts held by others	224,514	(282,398)
Change in permanently restricted net assets	<u>738,767</u>	<u>(234,385)</u>
Shareholder's equity:		
Net income of GRS	328,315	393,051
Net unrealized gains on investments of GRS	59,976	119,682
Change in shareholder's equity	<u>388,291</u>	<u>512,733</u>
Change in net assets and shareholder's equity	(503,677)	(11,546,236)
Net assets and shareholder's equity, beginning of year	<u>43,183,746</u>	<u>54,729,982</u>
Net assets and shareholder's equity, end of year	<u>\$ 42,680,069</u>	<u>\$ 43,183,746</u>

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

Gaylord Farm Association, Inc.
Consolidated Statements of Cash Flows
For the Years Ended September 30, 2010 and 2009

	2010	2009
Operating activities:		
Change in net assets and shareholder's equity	\$ (503,677)	\$ (11,546,236)
Adjustments to reconcile change in net assets and shareholder's equity to net cash provided by (used in) operating activities:		
Depreciation and amortization	3,857,884	3,709,051
Pension related changes other than net periodic pension cost	795,655	8,671,657
Change in fair value of interest rate swap	1,014,191	1,496,063
Net realized and unrealized (gains) losses on investments	(1,545,586)	489,341
Loss from equity investments	92,815	223,957
Change in beneficial interest in trusts held by others	(224,514)	282,398
Restricted contributions and bequests received	(1,014,306)	(767,695)
Changes in operating assets and liabilities:		
Patient accounts receivable	577,875	(447,819)
Other current assets	(145,630)	(442,068)
Pledges receivable	599,029	49,126
Investments held for captive insurance liabilities	(785,962)	(357,004)
Reinsurance recoverable relating to captive insurance	(59,515)	(82,039)
Other assets	42,001	33,150
Accounts payable and accrued expenses	(279,832)	(1,827,710)
Accrued payroll and related taxes	89,855	(281,144)
Accrued pension obligation	(600,878)	(38,936)
Captive insurance liabilities	43,336	332,147
Net cash provided by (used in) operating activities	1,952,741	(503,761)
Investing activities:		
Assets held under bond indenture agreement	(6,541)	28,620
Investments in joint ventures	(231,955)	(62,296)
Purchases of property, plant and equipment	(1,647,912)	(3,168,260)
Sales and purchases of investments, net	768,017	892,754
Net cash used in investing activities	(1,118,391)	(2,309,182)
Financing activities:		
Principal payments on long-term debt	(615,000)	(990,000)
Net payments on lines of credit	(600,000)	(1,375,000)
Proceeds from borrowings on term note	-	3,000,000
Principal payments on capital lease obligations	(508,680)	(302,038)
Restricted contributions and bequests received	1,014,306	767,695
Net cash (used in) provided by financing activities	(709,374)	1,100,657
Change in cash and cash equivalents	124,976	(1,712,286)
Cash and cash equivalents, beginning of year	2,251,036	3,963,322
Cash and cash equivalents, end of year	\$ 2,376,012	\$ 2,251,036

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

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 1 - General

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

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

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

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

Note 2 - Summary of Significant Accounting Policies

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

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

Cash and Cash Equivalents - The Association considers all highly liquid investments with original maturities of three months or less at date of purchase to be cash equivalents. At times, the Association maintains cash balances that are in excess of the \$250,000 Federal Depository Insurance Corporation (FDIC) insured limits. In addition, FDIC coverage for balances in non-interest bearing transaction deposit accounts is unlimited if the bank elects to participate. The Association maintains its cash at Bank of America and EFG - Bahamas, and it is the Association's policy to monitor the banks' financial strength on an ongoing basis.

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 2 - Summary of Significant Accounting Policies (continued)

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

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

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

Other Than Temporary Impairments on Investments - The Association accounts for other than temporary impairments in accordance with FASB ASC 320-10 and continually reviews its securities for impairment conditions, which could indicate that an other than temporary decline in market value has occurred. In conducting this review, numerous factors are considered, which include specific information pertaining to an individual company or a particular industry, general market conditions that reflect prospects for the economy as a whole, and the ability and intent to hold securities until recovery. The carrying value of investments is reduced to its estimated realizable value if a decline in fair value is considered to be other than temporary. There were no impairments recorded in 2010 or 2009.

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

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

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

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 2 - Summary of Significant Accounting Policies (continued)

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

Donor Restricted Gifts - Unconditional promises to give cash and other assets to the Association are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

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

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

The Association accounts for uncertain tax positions with provisions of FASB ASC 740, "Income Taxes" which provide a new framework for how companies should recognize, measure, present and disclose uncertain tax positions in their consolidated financial statements. With these changes, the Association may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The Association does not have any uncertain tax positions as of September 30, 2010 and 2009. As of September 30, 2010 and 2009, the Association did not record any penalties or interest associated with uncertain tax positions.

Goodwill - The Association recorded the excess of the purchase price of a New Haven based sleep center over the fair value of the assets acquired as goodwill. On an annual basis, management reviews the goodwill for impairment by considering the estimated fair value of the business acquired as compared to the net assets of the business. An impairment adjustment of \$18,219 was recognized for fiscal years 2010 and 2009.

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

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 2 - Summary of Significant Accounting Policies (continued)

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

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

Charity Care - The Association provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Association does not pursue collection of amounts determined to qualify as charity care, the charges related to charity care services are offset within net patient service revenue. Charity care of \$67,246 and \$107,276, as measured at the Association's respective established rates, was provided in fiscal years 2010 and 2009, respectively.

Estimated Malpractice Costs - The Association maintains malpractice insurance coverage under claims made policies through GRS in 2010 and 2009. A provision for estimated medical malpractice claims includes estimates of the ultimate costs for claims incurred but not reported and is included within accounts payable and accrued expenses on the Association's consolidated balance sheets.

Workers Compensation Costs - The Association is self-insured for workers' compensation. Estimated self-insurance liabilities are included within accrued payroll and related taxes and are \$1,046,597 and \$1,013,836 as of September 30, 2010 and 2009, respectively, and include estimates for claim obligations related to claims through September 30, 2010 and 2009.

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

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

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 2 - Summary of Significant Accounting Policies (continued)

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

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

New Accounting Pronouncements - In September 2009, the FASB released ASU 2009-12, which includes guidance on fair value measurements and disclosures relating to investments that calculate net asset value (NAV) per share (or its equivalent). The guidance permits, as a practical expedient, an entity holding investments in certain entities that calculate NAV per share or its equivalent for which the fair value is not readily determinable, to measure the fair value of such investments on the basis of that NAV per share, or its equivalent, without adjustment. The guidance also requires disclosure of the attributes of investments within the scope of the guidance by major category of investment. Such disclosures include the nature of any restrictions on an investor's ability to redeem its investments at the measurement date, any unfunded commitments and the investment strategies of the investee. The guidance is effective for interim and annual periods ending after December 15, 2009. The Association has adopted this guidance effect with the issuance of its September 30, 2010 consolidated financial statements.

In January 2010, the FASB issued FASB ASU 2010-06, which clarifies certain existing fair value measurement disclosure requirements of FASB ASC 820-10 and also requires additional fair value measurement disclosures. The new disclosures relate to transfers in and out of Level 1 and 2 investments, and disclosures about inputs and valuation techniques. The disclosures regarding transfers in and out of Level 1 and 2 investments, and clarifications to existing disclosures are effective for interim and annual periods beginning after December 15, 2009. The disclosures of Level 3 investment rollforward of activity on a gross basis are effective for fiscal years beginning after December 15, 2010. The Association is currently evaluating the impact of these disclosures on its consolidated financial statements.

In March 2010, the Association adopted FASB ASU 2010-11, which expands the disclosure requirements for derivative instruments and hedging activities to include an explanation of the entity's reason for using derivative instruments, the risks involved, and how these instruments and related hedge items affect an entity's financial position, financial performance, and cash flow. To meet these objectives, FASB ASU 2010-11 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about the fair values of derivative instruments and their gains and losses, and disclosures about credit-risk-related contingent features in derivative agreements. The enhanced disclosures about derivative instruments and hedging activities are included in Note 9.

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 2 - Summary of Significant Accounting Policies (continued)

In December 2008, the FASB issued additional authoritative guidance regarding an employer's disclosures about postretirement benefit plan assets, currently included in FASB ASC 715 (formerly FASB Staff Position FAS 132(R)-1, *Employers' Disclosures about Postretirement Benefit Plan Assets*). This guidance requires disclosure about the major classes of postretirement benefit plan assets, including a description of the inputs and valuation techniques used to measure those assets and the designation of such assets by level; how investment allocation decisions are made; the effect of fair value measurements using significant unobservable inputs on changes in plan assets for the period; and significant concentrations of risk within plan assets. See Note 11 for these additional disclosures for the year ended September 30, 2010. The adoption of this guidance did not have a significant impact on the Association's consolidated financial statements for the year ended September 30, 2010.

In August 2010, the FASB issued ASU 2010-23, which is intended to reduce the diversity in practice regarding the measurement basis used in the disclosure of charity care. ASU 2010-23 requires that cost be used as the measurement basis for charity care disclosure purposes and that cost be identified as the direct and indirect costs of providing the charity care, and requires disclosure of the method used to identify or determine such costs. This ASU is effective for the Association on October 1, 2011. The Association is currently evaluating the impact on its disclosures from the adoption of this pronouncement.

In August 2010, the FASB issued ASU No. 2010-24, which clarifies that a health care entity may not net insurance recoveries against related claim liabilities. In addition, the amount of the claim liability must be determined without consideration of insurance recoveries. This ASU is effective for the Association on October 1, 2011. The Association is currently evaluating the impact on its consolidated financial position and results of operations from the adoption of this pronouncement.

Subsequent Events - Subsequent events have been evaluated through December 7, 2010, the date through which procedures were performed to prepare the consolidated financial statements for issuance.

Note 3 - Net Patient Service Revenue

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

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

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

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

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 3 - Net Patient Service Revenue (continued)

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

Net patient service revenue for the years ended September 30, 2010 and 2009 is as follows:

	<u>2010</u>	<u>2009</u>
Gross patient service revenue	\$ 191,451,300	\$ 185,349,209
Contractual allowances and adjustments	<u>(123,649,716)</u>	<u>(118,519,249)</u>
Net revenue from services to patients	<u>\$ 67,801,584</u>	<u>\$ 66,829,960</u>

Revenue from the Medicare and Medicaid programs accounted for approximately 48% and 7%, respectively, of the Association's net patient revenue for 2010 and 42% and 19% respectively, for 2009. Revenue from Blue Cross accounted for approximately 19% and 17% in 2010 and 2009, respectively. No other payer accounted for more than 10% of revenue in 2010 and 2009. Net patient service revenues are based upon complex payment systems and include estimates of amounts yet to be collected. As a result, there is at least a reasonable possibility that recorded estimates will change in the near term. Any changes to estimates are recorded within current year operations.

The Association grants credit without collateral to its patients, most of whom are insured under third-party payer agreements. The following summarizes payers that account for more than 10 percent of patient accounts receivable as of September 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Medicare	45%	39%
Medicaid	13%	14%
Blue Cross	17%	16%

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

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 4 - Investments

Board-designated and restricted investments are invested as follows as of September 30, 2010 and 2009:

	2010		2009	
	Cost	Market Value	Cost	Market Value
Cash and money market	\$ 181,621	\$ 181,621	\$ 700,603	\$ 700,603
Other funds	2,208,709	1,765,125	2,375,164	2,055,128
Equity securities	2,048,327	2,381,487	3,102,554	3,454,664
Mutual funds - fixed income	6,249,330	6,468,723	6,997,225	6,587,354
Mutual funds - equity	10,330,729	11,162,268	8,905,559	8,383,906
	\$ 21,018,716	\$ 21,959,224	\$ 22,081,105	\$ 21,181,655

Investment balances that have been restricted by donors as of September 30, 2010 and 2009 are \$5,500,469 and \$4,986,216, respectively. The Board of Directors of the Association has restricted all other investments. On January 30, 2009, the Association entered into an agreement with Bank of America to pledge one of the Association's board restricted investment accounts, which had a fair market value of \$5,486,923 as of September 30, 2009. The pledge agreement was executed in conjunction with certain line of credit agreements, which were entered into on January 30, 2009 and are further discussed in Note 8. In accordance with the pledge agreement, the collateral has been released in 2010 as the Association has met the terms of the release agreements.

Current assets that are held under a bond indenture agreement, are deposited with a trustee for debt service funds. Such amounts are invested in United States treasury notes. In addition, investments held for funding of captive insurance liabilities of \$3,909,996 and \$3,124,034 as of September 30, 2010 and 2009, respectively, are invested in bonds and fixed income mutual funds.

The following table shows the investments' gross unrealized losses (which have been adjusted for the other than temporary impairment adjustments) and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, as of September 30, 2010 and 2009:

	2010				2009	
	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Equity securities	\$ 545,273	\$ (46,997)	\$ 78,244	\$ (7,811)	\$ 623,517	\$ (54,808)
Other funds	-	-	1,765,125	(443,584)	1,765,125	(443,584)
Mutual funds	-	-	2,459,293	(131,741)	2,459,293	(131,741)
	\$ 545,273	\$ (46,997)	\$ 4,302,662	\$ (583,136)	\$ 4,847,935	\$ (630,133)

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 4 - Investments (continued)

2009	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Equity securities	\$ 103,884	\$ (5,528)	\$ 507,367	\$ (81,010)	\$ 611,251	\$ (86,538)
Other funds	-	-	2,055,128	(333,863)	2,055,128	(333,863)
Mutual funds	4,023,151	(440,442)	9,427,987	(756,742)	13,451,138	(1,197,184)
	<u>\$ 4,127,035</u>	<u>\$ (445,970)</u>	<u>\$ 11,990,482</u>	<u>\$ (1,171,615)</u>	<u>\$ 16,117,517</u>	<u>\$ (1,617,585)</u>

In 2010 and 2009, none of the investments that were in an unrealized loss position were considered to be other than temporarily impaired.

Investment income is comprised of the following for the years ended September 30, 2010 and 2009:

	2010	2009
Income:		
Net realized gains (losses) on investments	\$ 37,303	\$ (1,255,984)
Dividend and interest income	573,473	648,145
	<u>\$ 610,776</u>	<u>\$ (607,839)</u>
Total investment return		
Other changes in unrestricted net assets:		
Unrealized gains on other than trading securities	<u>\$ 1,508,283</u>	<u>\$ 766,643</u>

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

The Association's share of Fitness & Wellness's net loss for the years ended September 30, 2010 and 2009 was \$107,264 and \$223,957, respectively. In addition, the Association made a capital contribution to Fitness & Wellness of \$156,955 and \$62,296 during the fiscal years ending September 30, 2010, and 2009, respectively. The carrying amount of the Fitness & Wellness investment was \$574,594 and \$524,903 as of September 30, 2010 and 2009, respectively and is included in other assets.

The Association's share of GSHC's net gain for the year ended September 30, 2010 was \$14,449. In addition, the Association made a capital contribution to GSHC of \$75,000 during the fiscal year ending September 30, 2010. The carrying amount of the GSHC investment was \$89,449 as of September 30, 2010 and is included in other assets.

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 5 - Fair Value Measurements

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

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

Level 2 - Inputs to the valuation methodology include:

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

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

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

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

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

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

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

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

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 5 - Fair Value Measurements (continued)

The following table presents the financial instruments carried at fair value as of September 30, 2010 and 2009 by the valuation hierarchy:

2010	Level 1	Level 2	Level 3	Total
Assets:				
Cash and cash equivalents	\$ 2,376,012	\$ -	\$ -	\$ 2,376,012
Investments:				
Cash and money market	181,621	-	-	181,621
Other funds	-	1,765,125	-	1,765,125
Equity securities	2,381,487	-	-	2,381,487
Mutual funds - fixed income	6,468,723	-	-	6,468,723
Mutual funds - equity	11,162,268	-	-	11,162,268
Total investments	<u>20,194,099</u>	<u>1,765,125</u>	<u>-</u>	<u>21,959,224</u>
Funds held under bond agreements	171,783	-	-	171,783
Beneficial interest in trusts	-	-	10,168,420	10,168,420
	<u>\$ 22,741,894</u>	<u>\$ 1,765,125</u>	<u>\$ 10,168,420</u>	<u>\$ 34,675,439</u>
Liabilities:				
Interest rate swap liability	\$ -	\$ 3,647,029	\$ -	\$ 3,647,029
	<u>\$ -</u>	<u>\$ 3,647,029</u>	<u>\$ -</u>	<u>\$ 3,647,029</u>
2009				
Assets:				
Cash and cash equivalents	\$ 2,251,036	\$ -	\$ -	\$ 2,251,036
Investments:				
Cash and money market	700,603	-	-	700,603
Other funds	-	2,055,128	-	2,055,128
Equity securities	3,454,664	-	-	3,454,664
Mutual funds - fixed income	6,587,354	-	-	6,587,354
Mutual funds - equity	8,383,906	-	-	8,383,906
Total investments	<u>19,126,527</u>	<u>2,055,128</u>	<u>-</u>	<u>21,181,655</u>
Funds held under bond agreements	165,242	-	-	165,242
Beneficial interest in trusts	-	-	9,943,906	9,943,906
	<u>\$ 21,542,805</u>	<u>\$ 2,055,128</u>	<u>\$ 9,943,906</u>	<u>\$ 33,541,839</u>
Liabilities:				
Interest rate swap liability	\$ -	\$ 2,632,838	\$ -	\$ 2,632,838
	<u>\$ -</u>	<u>\$ 2,632,838</u>	<u>\$ -</u>	<u>\$ 2,632,838</u>

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 5 - Fair Value Measurements (continued)

As of September 30, 2010 and 2009, the Association's other financial instruments included accounts receivable, pledges receivable, accounts payable and accrued expenses, line of credit, estimated third-party payer settlements, captive insurance reserves, long-term debt and capital lease obligations. The carrying amounts reported in the consolidated balance sheets for these financial instruments approximate their fair value.

A rollforward of the beneficial interest in trusts, which are classified as Level 3 within the fair value hierarchy, are as follows.

	2010
Balance as of October 1, 2009	\$ 9,943,906
Net change in market value	595,433
Distributions	(370,919)
Balance as of September 30, 2010	\$ 10,168,420
	2009
Balance as of October 1, 2008	\$ 10,226,304
Net change in market value	129,535
Distributions	(411,933)
Balance as of September 30, 2009	\$ 9,943,906

Note 6 - Property, Plant and Equipment

Property, plant and equipment consist of the following as of September 30, 2010 and 2009:

	2010	2009
Land and improvements	\$ 3,617,551	\$ 3,667,551
Buildings and improvements	57,319,835	56,858,114
Fixed and moveable equipment	31,241,896	30,423,786
	92,179,282	90,949,451
Less: accumulated depreciation and amortization	(47,976,690)	(44,565,847)
	44,202,592	46,383,604
Construction in progress	-	28,960
	\$ 44,202,592	\$ 46,412,564

Depreciation expense for the years ended September 30, 2010 and 2009 amounted to \$3,405,282 and \$3,335,398, respectively. Amortization expense for equipment under capital lease obligations was \$428,820 and \$355,435 as of September 30, 2010 and 2009, respectively.

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
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Note 7 - Other Assets

Other assets as of September 30, 2010 and 2009 are as follows:

	2010	2009
Investment in Fitness & Wellness	\$ 574,594	\$ 524,903
Investment in GSHC	89,449	-
Deferred finance costs, net of accumulated amortization of \$35,935 and \$12,153, respectively	376,020	399,802
Goodwill	122,240	140,459
Deposits	19,609	19,609
	\$ 1,181,912	\$ 1,084,773

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

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

Long-term Obligations - The Association had a \$3,000,000 line of credit agreement, which was renewable on an annual basis. At the Association's option, the line of credit bore interest at the bank's prime rate, as defined, or LIBOR plus 75 basis points. On January 30, 2009, the Association converted this line of credit into a term loan promissory note whereby the \$3,000,000 is payable in equal monthly installments of \$50,000 with a balloon payment of \$1,250,000 on January 31, 2012. At the Association's option, the term loan promissory note bears interest at the bank's prime rate, as defined, or LIBOR plus 100 basis points.

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

The Series B Bonds bear interest at a variable rate as determined by a re-marketing agent (approximately 0.3% as of September 30, 2010 and 2009), which is adjusted weekly, and matures on July 1, 2037. For as long as the bonds are variable rate, the bond holders have the option to tender their bonds for repayment. The Association has a letter of credit from Bank of America, N.A., which is available to support its obligations under the Series B Bonds during this period. The letter of credit expires on July 3, 2012, subject to extension or earlier termination upon the occurrence of certain events set forth in the letter of credit agreement. At that time, the letter of credit can be renewed, at the bank's discretion, the Association can convert the bonds to a fixed rate or repurchase the bonds outstanding on that date at their par value. Tenders made by bond holders will be remarketed or, if necessary, paid by the drawdowns on the letter of credit. Any tender drawings made under the letter of credit are to be repaid by the Association on the expiration date of the letter of credit.

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

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

The Series B loan and letter of credit agreements include certain financial covenants including a minimum debt service coverage ratio of 1.25 to 1, a liquidity to debt ratio of 30%, and other restrictions, including limitations on future indebtedness and liens. The Association was in compliance with all covenants for 2010. The Association was not in compliance with the CHEFA debt service coverage ratio covenant for 2009 and had received a waiver.

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

During 2009, the Association recorded a loss on abandonment of a long-term rental property in the amount of \$92,035. The lease was previously accounted for as an operating lease and the Association was no longer utilizing the rental property and is unable to sublease the property. Consequently, the Association's liability represents the present value of future minimum lease payments under this lease of \$71,495 as of September 30, 2010. The lease expires in December 2013.

Letter of Credit - As a result of being self-funded for its workers' compensation program, the Association is required by the State of Connecticut Workers' Compensation Commission to hold a letter of credit in the aggregate amount of \$650,000 and \$550,000 as of September 30, 2010 and 2009, respectively. As of September 30, 2010 and 2009, there was no outstanding balances on the letter of credit.

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

2011	\$	177,257
2012		162,674
2013		162,674
2014		33,337
2015		21,580
Thereafter		89,916
Less: interest		(101,825)
		\$ 545,613

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

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

A summary of long-term debt and capital lease obligations as of September 30, 2010 and 2009 are as follows:

	<u>2010</u>	<u>2009</u>
Long-term debt obligation	\$ 19,775,000	\$ 20,390,000
Term loan promissory note	2,000,000	2,600,000
Capital lease obligations	545,613	581,296
Lease abandonment obligation	219,038	92,035
	<u>22,539,651</u>	<u>23,663,331</u>
Less: current portion	<u>(1,453,373)</u>	<u>(1,399,430)</u>
	<u>\$ 21,086,278</u>	<u>\$ 22,263,901</u>

Scheduled principal repayments on the long-term debt and capital lease obligations are as follows:

2011	\$ 1,453,373
2012	2,305,394
2013	887,191
2014	761,276
2015	745,165
Thereafter	<u>16,387,252</u>
	<u>\$ 22,539,651</u>

Operating Leases - The Association leases various equipment and space under operating leases expiring at various dates and month-to-month agreements. Some of these leases contain renewal options. Rent expense under such operating leases and agreements was \$746,945 and \$946,586, in 2010 and 2009, respectively. The following is a schedule of future minimum payments under non-cancellable operating leases as of September 30, 2010:

2011	\$ 434,045
2012	436,369
2013	400,920
2014	379,397
2015	384,941
Thereafter	<u>919,980</u>
	<u>\$ 2,955,654</u>

In addition, the Association leases land under a long-term lease agreement through 2106 to a third-party. Rental income is based on a percentage of the gross income earned by the lessee. Total rental income from this property was \$224,058 and \$233,583 for 2010 and 2009, respectively and is included in other operating revenue in the accompanying consolidated statements of operations and changes in net assets.

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 9 - Derivatives

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

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

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

On August 1, 2007, the Association entered into an interest rate swap agreement with an initial notional amount of \$21,530,000 to reduce the exposure to fluctuations in interest rates related to its CHEFA debt. The swap agreement, which expires in June 2027, requires that the Association make monthly payments to the counter-party, Bank of America, N.A., based upon a fixed interest rate of 4.28% and in return receives monthly payments from Bank of America, N.A. based on the Bond Index Association Municipal Swap Rate Index rate (0.27% and 0.24% as of September 30, 2010 and 2009, respectively). The notional amount is scheduled to decrease as principal is paid on the CHEFA debt. Net amounts paid under the swap is recorded as additional interest expense. Based on information received from the counter-party, the swap agreement had an unfavorable fair value of \$3,647,029 and \$2,632,838 as of September 30, 2010 and 2009, respectively.

Management has not designated the swap agreement as a hedging instrument. The change in fair value of the interest rate swap of \$1,014,191 and \$1,496,063 for the years ended September 30, 2010 and 2009, respectively, is recorded in the consolidated statements of operations and changes in net assets as a component of non-operating income.

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
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Note 10 - Net Assets

Temporarily restricted net assets are available for the following purposes as of September 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Health care services:		
Patient special needs	\$ 16,926	\$ 22,735
Other restricted purposes	580,586	342,926
Capital campaign	<u>1,184,306</u>	<u>1,783,065</u>
	<u>\$ 1,781,818</u>	<u>\$ 2,148,726</u>

Permanently restricted net assets are restricted to the following purposes as of September 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Investments to be held in perpetuity, the income of which is expendable to support patient special needs and other services	\$ 5,500,469	\$ 4,986,216
Beneficial interest in trusts held by others, the income of which is expendable to support other health care services	<u>10,168,420</u>	<u>9,943,906</u>
	<u>\$ 15,668,889</u>	<u>\$ 14,930,122</u>

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

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

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

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 10 - Net Assets (continued)

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

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

Changes in net assets for endowments and temporary restricted funds for the year ended September 30, 2009 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance at October 1, 2008	\$ 17,625,547	\$ 565,008	\$ 4,938,203	\$ 23,128,758
Investment return:				
Investment income	580,495	-	-	580,495
Net change in market value	(635,603)	-	-	(635,603)
Contributions	-	76,575	48,013	124,588
Expenditures	(1,375,000)	(275,922)	-	(1,650,922)
Balance at September 30, 2009	<u>\$ 16,195,439</u>	<u>\$ 365,661</u>	<u>\$ 4,986,216</u>	<u>\$ 21,547,316</u>

Funds with Deficiencies - From time to time the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or relevant law requires the Association to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature are reported in unrestricted net assets. As of September 30, 2010 and 2009, there were no funds that were below the level required by donor or law.

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

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 10 - Net Assets (continued)

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

Spending Policy - During its annual budgeting process, the Association appropriates donor restricted endowment funds for expenditure in accordance with donor purpose and time restrictions. During the year ended September 30, 2010 and 2009, the Board appropriated \$2,166,436 and \$1,375,000, respectively of funds for expenditure from its board restricted endowment funds. The board restricted endowment funds are being held for long-term growth and to maintain capital reserves for the Association.

Note 11 - Pension Plans

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

The following summarizes significant disclosures relating to the Plan as of September 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Change in benefit obligations:		
Benefit obligations at beginning of year	\$ 32,562,858	\$ 26,397,163
Interest cost	1,720,670	1,794,873
Service cost	210,000	100,000
Actuarial loss	1,486,630	6,812,468
Expected administrative expenses	(210,000)	(100,000)
Benefits and plan expenses paid	<u>(1,667,350)</u>	<u>(2,441,646)</u>
Benefit obligations at end of year	<u>\$ 34,102,808</u>	<u>\$ 32,562,858</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	\$ 17,668,518	\$ 20,135,544
Actual return on plan assets	1,985,069	193,430
Employer contributions	1,244,534	-
Benefits and plan expenses paid	(1,667,350)	(2,441,646)
Administrative expenses	<u>(217,080)</u>	<u>(218,810)</u>
Fair value of plan assets at end of year	<u>\$ 19,013,691</u>	<u>\$ 17,668,518</u>
Accrued pension liability:		
Unfunded status	<u>\$ (15,089,117)</u>	<u>\$ (14,894,340)</u>

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 11 - Pension Plans (continued)

	<u>2010</u>	<u>2009</u>
Net periodic benefit cost (income):		
Interest cost	\$ 1,720,670	\$ 1,794,873
Service cost	210,000	100,000
Actuarial loss recognized	192,673	-
Expected return on plan assets	<u>(1,479,687)</u>	<u>(1,933,809)</u>
Net periodic benefit cost (income)	<u>\$ 643,656</u>	<u>\$ (38,936)</u>

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

2011	\$ 3,503,421
2012	\$ 1,875,614
2013	\$ 2,013,875
2014	\$ 2,724,674
2015	\$ 2,100,850
Years 2016-2020	\$ 13,888,139

Amounts recorded in unrestricted net assets as of September 30, 2010 and 2009, not yet amortized as components of net periodic benefit cost (income) is as follows:

	<u>2010</u>	<u>2009</u>
Unamortized actuarial loss	<u>\$ 14,984,780</u>	<u>\$ 14,189,125</u>

The amortization of the above items expected to be recognized in net periodic benefit income for the year ended September 30, 2010 is \$302,929.

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

	<u>2010</u>	<u>2009</u>
Benefit obligations		
Discount rate	5.25%	5.50%
Net periodic benefit cost		
Discount rate	5.50%	7.10%
Expected long-term return on plan assets	6.80%	7.80%

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 11 - Pension Plans (continued)

The fair values of the Association's Plan assets, by asset category are as follows, for the year ending September 30, 2010 and 2009:

2010	Level 1	Level 2	Level 3	Total
Money market securities	\$ 596,818	\$ -	\$ -	\$ 596,818
Mutual funds - fixed income	7,971,893	-	-	7,971,893
Mutual funds - equities	4,713,643	-	-	4,713,643
Equity securities	5,070,215	-	-	5,070,215
Other	-	-	661,122	661,122
	<u>\$ 18,352,569</u>	<u>\$ -</u>	<u>\$ 661,122</u>	<u>\$ 19,013,691</u>
2009	Level 1	Level 2	Level 3	Total
Money market securities	\$ 427,925	\$ -	\$ -	\$ 427,925
Mutual funds - fixed income	7,370,734	-	-	7,370,734
Mutual funds - equities	4,335,655	-	-	4,335,655
Equity securities	4,969,040	-	-	4,969,040
Other	-	-	565,164	565,164
	<u>\$ 17,103,354</u>	<u>\$ -</u>	<u>\$ 565,164</u>	<u>\$ 17,668,518</u>

The level 3 investments increased \$95,958 during 2010 due to changes in market values.

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

The Association has a defined contribution benefit plan, which became effective January 1, 2005. Substantially all full time employees are eligible to participate in the defined contribution plan. The Association made contributions to this plan totaling \$650,537 and \$329,191 in 2010 and 2009, respectively. Employees become vested in the Association's contributions in three to five years. The portion of the employees contributions unvested upon termination are forfeited and used to reduce future contributions made by the Association on a dollar-for-dollar basis.

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

The Association also has a supplemental retirement plan agreement with a senior executive. The obligation related to this agreement is approximately \$828,000 and \$612,000 as of September 30, 2010 and 2009, respectively, and is recorded within accounts payable and accrued expenses within the accompanying consolidated balance sheets.

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 12 - Functional Expenses

The Association provides health care services to residents within its geographic location. Expenses related to providing these services for the years ended September 30, 2010 and 2009 is as follows:

	<u>2010</u>	<u>2009</u>
Health care services	\$ 55,228,965	\$ 55,026,206
General and administrative	15,004,397	13,995,560
Fundraising	<u>625,089</u>	<u>576,209</u>
	<u>\$ 70,858,451</u>	<u>\$ 69,597,975</u>

Note 13 - Captive Insurance Activities

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

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

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

A reconciliation of direct to net premiums on a written and earned basis is summarized as follows for year ended September 30, 2010 and 2009:

	Premium Written		Premium Earned	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Direct premiums	\$ 993,750	\$ 1,226,164	\$ 939,465	\$ 1,106,699
Ceded premiums	<u>(340,000)</u>	<u>(486,164)</u>	<u>(364,465)</u>	<u>(389,199)</u>
	<u>\$ 653,750</u>	<u>\$ 740,000</u>	<u>\$ 575,000</u>	<u>\$ 717,500</u>

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 13 - Captive Insurance Activities (continued)

The liability for unpaid losses and loss adjustment expenses is included within captive insurance reserves on the accompanying consolidated balance sheets. Activity in the liability for unpaid losses and loss adjustment expenses is summarized as follows for the year ended September 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Balance at beginning of the year	\$ 2,626,498	\$ 2,413,816
Less: reinsurance recoverables	<u>(698,135)</u>	<u>(616,096)</u>
Net balance beginning of the year	1,928,363	1,797,720
Incurred related to:		
Current year	717,430	615,929
Prior years	<u>(560,304)</u>	<u>(363,550)</u>
Total incurred	157,126	252,379
Paid related to:		
Current year	(1,039)	-
Prior years	<u>(226,551)</u>	<u>(121,736)</u>
Total paid	<u>(227,590)</u>	<u>(121,736)</u>
Net balance at end of year	1,857,899	1,928,363
Plus: reinsurance recoverables	<u>757,650</u>	<u>698,135</u>
Balance at the end of the year	<u>\$ 2,615,549</u>	<u>\$ 2,626,498</u>

As a result of changes in estimates of insured events in prior years, the provision for losses and loss adjustment expenses decreased by \$560,304 and \$363,550 in 2010 and 2009, respectively.

The above liability for loss and loss adjustment expenses have been determined using a 4% discount rate and have been included within other captive insurance reserves as of September 30, 2010 and 2009. The ultimate settlement of losses may vary significantly from the reserves recorded. In particular, ultimate settlements on medical malpractice claims depend, among other things, on the resolution of litigation, the outcome of which is difficult to predict. Also, since the reserves have been discounted, there is the possibility that the timing of loss payments and income earned on invested assets will be significantly different than anticipated.

Included on the accompanying consolidated balance sheets is a reinsurance recoverable of \$757,650 and \$698,135 as of September 30, 2010 and 2009, respectively, which is due from one reinsurer. GRS continually evaluates the reinsurer's financial condition. There can be no assurance that reinsurance will continue to be available to GRS to the same extent, and at the same cost, as it has in the past. GRS may choose in the future to reevaluate the use of reinsurance to increase or decrease the amounts of risk it cedes to reinsurers.

Gaylord Farm Association, Inc.
Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2010 and 2009

Note 14 - Commitments and Contingencies

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

ASC 410-20 "*Accounting for Asset Retirement Obligations*" addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets such as facilities containing asbestos, when the amount of the liability can be reasonably estimated. No Asset Retirement Obligation (ARO) has been established as of September 30, 2010 and 2009, as no plans to renovate or sell any facility, or area within, with significant asbestos have been identified and therefore no settlement date has been determined. Management will continue to evaluate its exposure to asbestos removal and establish an ARO for the fair value of the associated costs once sufficient information has been obtained and a settlement date has been determined. Management does not believe that the liability is material to the overall consolidated financial results of the Association.

Note 15 - Pledges Receivable

Pledges receivable represent unconditional promises to give for the 36-bed addition. The following pledges are due to the Association as of September 30, 2010:

Due within one year	\$	495,086
Due in one to five years		820,809
		1,315,895
Less: allowance for uncollectible pledges		(131,589)
		\$ 1,184,306

Note 16 - Supplemental Cash Flow Disclosures

The Association paid interest in the amount of \$966,853 and \$1,013,196 for the years ended September 30, 2010 and 2009, respectively. Of the 2009 amount, \$68,469 represents interest that has been capitalized as part of the 36-bed addition. In addition, the Association acquired equipment by incurring capital lease obligations of \$151,500 and \$601,000 during the years ended September 30, 2010 and 2009, respectively.

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

Assets	Gaylord Hospital, Inc.	Gaylord Risk Solutions, Ltd.	Gaylord Farm Rehabilitation Center	Gaylord Research Institute, Inc.	Eliminations	Gaylord Farm Association, Inc.
Current assets:						
Cash and cash equivalents	\$ 2,183,087	\$ 190,844	\$ -	\$ 2,081	\$ -	\$ 2,376,012
Patient accounts receivable (less allowance of \$540,000)	9,115,849	-	-	-	-	9,115,849
Assets whose use is limited:						
Assets held under bond indenture agreement	171,783	-	-	-	-	171,783
Pledges receivable	495,086	-	-	-	-	495,086
Due from affiliates	1,913,342	-	-	-	(1,913,342)	-
Other current assets	1,106,406	618,611	-	-	-	1,725,017
Total current assets	<u>14,985,553</u>	<u>809,455</u>	<u>-</u>	<u>2,081</u>	<u>(1,913,342)</u>	<u>13,883,747</u>
Assets whose use is limited:						
Pledges receivable	689,220	-	-	-	-	689,220
Board-designated investments	16,458,755	-	-	-	-	16,458,755
Donor restricted investments	5,500,469	-	-	-	-	5,500,469
Beneficial interest in trusts held by others	10,168,420	-	-	-	-	10,168,420
	<u>32,816,864</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>32,816,864</u>
Property, plant and equipment, net	44,202,592	-	-	-	-	44,202,592
Investments held for captive insurance liabilities	-	3,909,996	-	-	-	3,909,996
Reinsurance recoverable relating to captive insurance liabilities	-	757,650	-	-	-	757,650
Other assets	1,181,912	-	-	-	-	1,181,912
Total assets	<u>\$ 93,186,921</u>	<u>\$ 5,477,101</u>	<u>\$ -</u>	<u>\$ 2,081</u>	<u>\$ (1,913,342)</u>	<u>\$ 96,752,761</u>
Liabilities, Net Assets and Shareholder's Equity						
Current liabilities:						
Accounts payable and accrued expenses	\$ 5,065,117	\$ 35,220	\$ -	\$ -	\$ -	\$ 5,100,337
Accrued payroll and related taxes	3,375,453	-	-	-	-	3,375,453
Line of credit	1,025,000	-	-	-	-	1,025,000
Due to affiliates	-	207,318	1,706,024	-	(1,913,342)	-
Estimated amounts due to third-party payers	246,806	-	-	-	-	246,806
Current portion of accrued pension obligation	2,086,158	-	-	-	-	2,086,158
Current portion of long-term debt and capital lease obligations	1,453,373	-	-	-	-	1,453,373
Total current liabilities	<u>13,251,907</u>	<u>242,538</u>	<u>1,706,024</u>	<u>-</u>	<u>(1,913,342)</u>	<u>13,287,127</u>
Long-term debt and capital lease obligations, less current portion	21,086,278	-	-	-	-	21,086,278
Accrued pension obligation	13,002,959	-	-	-	-	13,002,959
Captive insurance reserves	-	3,049,299	-	-	-	3,049,299
Interest rate swap liability	3,647,029	-	-	-	-	3,647,029
Total liabilities	<u>50,988,173</u>	<u>3,291,837</u>	<u>1,706,024</u>	<u>-</u>	<u>(1,913,342)</u>	<u>54,072,692</u>
Net assets and shareholder's equity:						
Unrestricted	24,748,041	-	(1,706,024)	2,081	-	23,044,098
Temporarily restricted	1,781,818	-	-	-	-	1,781,818
Permanently restricted	15,668,889	-	-	-	-	15,668,889
Shareholder's equity	-	2,185,264	-	-	-	2,185,264
Total net assets and shareholder's equity	<u>42,198,748</u>	<u>2,185,264</u>	<u>(1,706,024)</u>	<u>2,081</u>	<u>-</u>	<u>42,680,069</u>
Total liabilities, net assets and shareholder's equity	<u>\$ 93,186,921</u>	<u>\$ 5,477,101</u>	<u>\$ -</u>	<u>\$ 2,081</u>	<u>\$ (1,913,342)</u>	<u>\$ 96,752,761</u>

See accompanying Independent Auditors' Report.

Gaylord Farm Association, Inc.
Consolidating Balance Sheet
September 30, 2009

Assets	Gaylord Hospital, Inc.	Gaylord Risk Solutions, Ltd.	Gaylord Farm Rehabilitation Center	Gaylord Research Institute, Inc.	Eliminations	Gaylord Farm Association, Inc.
Current assets:						
Cash and cash equivalents	\$ 1,853,446	\$ 395,492	\$ -	\$ 2,098	\$ -	\$ 2,251,036
Patient accounts receivable (less allowance of \$1,191,000)	9,693,724	-	-	-	-	9,693,724
Assets whose use is limited:						
Assets held under bond indenture agreement	165,242	-	-	-	-	165,242
Pledges receivable	580,943	-	-	-	-	580,943
Due from affiliates	1,559,245	-	-	-	(1,559,245)	-
Other current assets	958,271	621,116	-	-	-	1,579,387
Total current assets	<u>14,810,871</u>	<u>1,016,608</u>	<u>-</u>	<u>2,098</u>	<u>(1,559,245)</u>	<u>14,270,332</u>
Assets whose use is limited:						
Pledges receivable	1,202,392	-	-	-	-	1,202,392
Board-designated investments	16,195,439	-	-	-	-	16,195,439
Donor restricted investments	4,986,216	-	-	-	-	4,986,216
Beneficial interest in trusts held by others	9,943,906	-	-	-	-	9,943,906
	<u>32,327,953</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>32,327,953</u>
Property, plant and equipment, net	46,412,564	-	-	-	-	46,412,564
Investments held for captive insurance liabilities	-	3,124,034	-	-	-	3,124,034
Reinsurance recoverable relating to captive insurance liabilities	-	698,135	-	-	-	698,135
Other assets	1,084,773	-	-	-	-	1,084,773
Total assets	<u>\$ 94,636,161</u>	<u>\$ 4,838,777</u>	<u>\$ -</u>	<u>\$ 2,098</u>	<u>\$ (1,559,245)</u>	<u>\$ 97,917,791</u>
Liabilities, Net Assets and Shareholder's Equity						
Current liabilities:						
Accounts payable and accrued expenses	\$ 5,344,328	\$ 35,841	\$ -	\$ -	\$ -	\$ 5,380,169
Accrued payroll and related taxes	3,285,598	-	-	-	-	3,285,598
Line of credit	1,625,000	-	-	-	-	1,625,000
Due to affiliates	-	-	1,559,245	-	(1,559,245)	-
Estimated amounts due to third-party payers	246,806	-	-	-	-	246,806
Current portion of accrued pension obligation	1,244,534	-	-	-	-	1,244,534
Current portion of long-term debt and capital lease obligations	1,399,430	-	-	-	-	1,399,430
Total current liabilities	<u>13,145,696</u>	<u>35,841</u>	<u>1,559,245</u>	<u>-</u>	<u>(1,559,245)</u>	<u>13,181,537</u>
Long-term debt and capital lease obligations, less current portion	22,263,901	-	-	-	-	22,263,901
Accrued pension obligation	13,649,806	-	-	-	-	13,649,806
Captive insurance reserves	-	3,005,963	-	-	-	3,005,963
Interest rate swap liability	2,632,838	-	-	-	-	2,632,838
Total liabilities	<u>51,692,241</u>	<u>3,041,804</u>	<u>1,559,245</u>	<u>-</u>	<u>(1,559,245)</u>	<u>54,734,045</u>
Net assets and shareholder's equity:						
Unrestricted	25,865,072	-	(1,559,245)	2,098	-	24,307,925
Temporarily restricted	2,148,726	-	-	-	-	2,148,726
Permanently restricted	14,930,122	-	-	-	-	14,930,122
Shareholder's equity	-	1,796,973	-	-	-	1,796,973
Total net assets and shareholder's equity	<u>42,943,920</u>	<u>1,796,973</u>	<u>(1,559,245)</u>	<u>2,098</u>	<u>-</u>	<u>43,183,746</u>
Total liabilities, net assets and shareholder's equity	<u>\$ 94,636,161</u>	<u>\$ 4,838,777</u>	<u>\$ -</u>	<u>\$ 2,098</u>	<u>\$ (1,559,245)</u>	<u>\$ 97,917,791</u>

See accompanying Independent Auditors' Report.

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

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

See accompanying Independent Auditors' Report.

Gaylord Farm Association, Inc.
Consolidating Statement of Operations
For the Year Ended September 30, 2009

	Gaylord Hospital, Inc.	Gaylord Risk Solutions, Ltd.	Gaylord Farm Rehabilitation Center	Gaylord Research Institute, Inc.	Eliminations	Gaylord Farm Association, Inc.
Revenues:						
Net patient service revenue	\$ 66,535,150	\$ -	\$ 294,810	\$ -	\$ -	\$ 66,829,960
Contributions and bequests	695,886	-	-	-	-	695,886
Earned written premium	-	1,106,699	-	-	(1,106,699)	-
Ceded premium	-	(389,199)	-	-	-	(389,199)
Other operating revenue	500,634	-	134,387	-	-	635,021
Net assets released from restrictions used for operations	225,494	-	-	-	-	225,494
Total revenues	<u>67,957,164</u>	<u>717,500</u>	<u>429,197</u>	<u>-</u>	<u>(1,106,699)</u>	<u>67,997,162</u>
Expenses:						
Salaries and related expenses	46,051,927	-	558,257	-	-	46,610,184
Other operating expenses	5,868,628	139,720	107,323	-	(1,106,699)	5,008,972
Professional fees and contract services	5,308,794	-	-	-	-	5,308,794
Supplies	4,975,353	-	-	-	-	4,975,353
Depreciation and amortization	3,665,561	-	43,490	-	-	3,709,051
Occupancy costs	2,203,004	-	-	-	-	2,203,004
Provision for bad debts	616,185	-	-	-	-	616,185
Interest	904,243	-	9,810	-	-	914,053
Loss and loss adjustment expenses	-	252,379	-	-	-	252,379
Total expenses	<u>69,593,695</u>	<u>392,099</u>	<u>718,880</u>	<u>-</u>	<u>(1,106,699)</u>	<u>69,597,975</u>
(Loss) income from operations	(1,636,531)	325,401	(289,683)	-	-	(1,600,813)
Other (losses) gains:						
Dividend and interest income	580,495	67,650	-	-	-	648,145
Net realized gains on investments	(1,255,984)	-	-	-	-	(1,255,984)
Loss on equity investments	(223,957)	-	-	-	-	(223,957)
Change in fair value of interest rate swap agreement	(1,496,063)	-	-	-	-	(1,496,063)
Loss on lease abandonment	(92,035)	-	-	-	-	(92,035)
Total other (losses) gains	<u>(2,487,544)</u>	<u>67,650</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(2,419,894)</u>
Excess of revenues (under) over expenses	<u>\$ (4,124,075)</u>	<u>\$ 393,051</u>	<u>\$ (289,683)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (4,020,707)</u>

See accompanying Independent Auditors' Report.