Garrett County Memorial Hospital and Subsidiary

Consolidated Audited Financial Statements

June 30, 2014 and 2013

DIXON HUGHES GOODMAN LLP
Certified Public Accountants and Advisors

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Independent Auditors' Report

The Board of Governors
Garrett County Memorial Hospital
Oakland, Maryland

We have audited the accompanying financial statements of Garrett County Memorial Hospital and subsidiary (collectively, the Company), which comprise the consolidated balance sheet as of June 30, 2014, and the related consolidated statements of operations and other changes in unrestricted net assets, changes in net assets and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free of material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Garrett County Memorial Hospital and subsidiary as of June 30, 2014, and the consolidated results of their operations, changes in net assets and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Prior Period Financial Statements

The financial statements as of June 30, 2013 were audited by Cohen, Rutherford + Knight, P.C. certain of whose shareholders joined Dixon Hughes Goodman LLP as of June 1, 2014 and whose report dated October 16, 2013, expressed an unmodified opinion on those statements.

Supplementary Schedules

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information is presented for purposes of additional analysis rather than to present the financial position, results of operations, and cash flows of the individual companies and is not a required part of the consolidated financial statements. Such 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. The consolidating 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 information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report October 23, 2014 on our consideration of the Company's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Company's internal control over financial reporting and compliance.

Dixon Hughes Goodman LLP

October 23, 2014
Tysons, Virginia

Garrett County Memorial Hospital and Subsidiary
Consolidated Balance Sheets

	June 30 2014	June 30 2013
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 8,143,571	$ 7,359,186
Short-term investments -- *Note B*	18,911,273	15,910,000
Patient accounts receivable, net of allowance for doubtful accounts of $2,386,815 and $3,395,041 at June 30, 2014 and 2013, respectively -- *Note K*	5,177,670	5,702,475
Other amounts receivable	326,473	393,050
Assets whose use is limited by donors and others -- *Note B*	112,582	58,584
Inventories	990,630	1,074,724
Prepaid expenses	465,465	407,768
TOTAL CURRENT ASSETS	34,127,664	30,905,787
NONCURRENT ASSETS		
Property and equipment, net -- *Note D*	20,739,582	20,299,943
Insurance recoverable -- *Note J*	588,715	551,665
Long-term investments -- *Note B*	4,955,150	4,187,796
Investment in affiliates -- *Note C*	185,950	121,387
Assets whose use is limited by donors and others, less current portion -- *Note B*	457,585	304,480
Assets whose use is limited by board of governors -- *Note B*	698,073	698,073
Deferred financing costs, net	22,633	23,986
TOTAL NONCURRENT ASSETS	27,647,688	26,187,330
TOTAL ASSETS	$ 61,775,352	$ 57,093,117

(Continued)

Garrett County Memorial Hospital and Subsidiary
Consolidated Balance Sheets – Continued

	June 30	
	2014	**2013**
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	$ 973,451	$ 796,171
Accrued salaries and wages	1,960,742	2,096,945
Advances from third parties	466,983	559,883
Current portion of long-term debt -- *Note E*	165,867	156,113
Other current liabilities -- *Note J*	440,218	300,387
TOTAL CURRENT LIABILITIES	4,007,261	3,909,499
Long-term debt, less current portion -- *Note E*	3,400,857	3,564,483
Pension obligation -- *Note G*	10,149,757	10,065,522
Other long-term liabilities -- *Note J*	1,445,031	1,407,981
TOTAL LIABILITIES	19,002,906	18,947,485
NET ASSETS		
Unrestricted	42,282,088	37,849,653
Temporarily restricted -- *Note F*	454,247	260,393
Permanently restricted -- *Note M*	36,111	35,586
TOTAL NET ASSETS	42,772,446	38,145,632
TOTAL LIABILITIES AND NET ASSETS	$ 61,775,352	$ 57,093,117

See the accompanying notes to the consolidated financial statements.

Garrett County Memorial Hospital and Subsidiary
Consolidated Statements of Operations and Other Changes in Unrestricted Net Assets

	Year Ended June 30	
	2014	**2013**
REVENUE		
Net patient service revenue -- *Note K*		
Patient service revenue (net of contractual allowances and discounts)	$ 42,742,778	$ 42,041,077
Less: provision for uncollectible accounts	(1,575,843)	(2,587,532)
	41,166,935	39,453,545
Other revenue	2,183,038	984,738
Net assets released from restriction for use in operations -- *Note F*	35,203	10,551
TOTAL REVENUE	43,385,176	40,448,834
EXPENSES -- *Note L*		
Salaries and wages	16,943,308	16,605,162
Employee benefits -- *Note G*	6,433,065	6,590,045
Supplies	6,675,000	6,257,675
Utilities	704,650	650,356
Purchased services	5,442,102	5,321,650
Depreciation and amortization -- *Note D*	2,687,542	2,621,454
Interest -- *Note E*	150,180	154,034
Other expenses	988,117	962,288
TOTAL OPERATING EXPENSES	40,023,964	39,162,664
GAIN FROM OPERATIONS	3,361,212	1,286,170
OTHER INCOME		
Investment income -- *Note B*	750,271	506,970
Equity in income of affiliates -- *Note C*	29,563	94,084
Other	97,897	153,885
TOTAL OTHER INCOME	877,731	754,939
EXCESS OF REVENUE OVER EXPENSES	4,238,943	2,041,109
Net assets released from restriction for the purchase of property and equipment -- *Note F*	259,183	231,377
Pension-related changes other than net periodic pension cost -- *Note G*	(65,691)	996,394
INCREASE IN UNRESTRICTED NET ASSETS	$ 4,432,435	$ 3,268,880

See the accompanying notes to the consolidated financial statements.

Garrett County Memorial Hospital and Subsidiary
Consolidated Statements of Changes in Net Assets

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Assets
BALANCE AT JUNE 30, 2012	$ 34,580,773	$ 442,210	$ 35,086	$ 35,058,069
Excess revenue over expenses	2,041,109	0	0	2,041,109
Net assets released from restriction for the purchase of property and equipment -- *Note F*	231,377	(231,377)	0	0
Pension-related changes other than net periodic pension cost -- *Note G*	996,394	0	0	996,394
Contributions	0	60,111	500	60,611
Net assets released from restriction for use in operations -- *Note F*	0	(10,551)	0	(10,551)
INCREASE (DECREASE) IN NET ASSETS	3,268,880	(181,817)	500	3,087,563
BALANCE AT JUNE 30, 2013	37,849,653	260,393	35,586	38,145,632
Excess revenue over expenses	4,238,943	0	0	4,238,943
Net assets released from restriction for the purchase of property and equipment -- *Note F*	259,183	(259,183)	0	0
Pension-related changes other than net periodic pension cost -- *Note G*	(65,691)	0	0	(65,691)
Contributions	0	488,240	525	488,765
Net assets released from restriction for use in operations -- *Note F*	0	(35,203)	0	(35,203)
INCREASE IN NET ASSETS	4,432,435	193,854	525	4,626,814
BALANCE AT JUNE 30, 2014	$ 42,282,088	$ 454,247	$ 36,111	$ 42,772,446

See the accompanying notes to the consolidated financial statements.

Garrett County Memorial Hospital and Subsidiary
Consolidated Statements of Cash Flows

	Year Ended June 30 2014	Year Ended June 30 2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Increase in net assets	$ 4,626,814	$ 3,087,563
Adjustments to reconcile increase in net assets to net cash and cash equivalents provided by operating activities:		
Net unrealized gain	(385,481)	(211,675)
Restricted contributions	(488,240)	(60,111)
Depreciation	2,686,189	2,620,100
Amortization of deferred financing costs	1,353	1,354
Provision for uncollectible accounts	1,575,843	2,587,532
Equity in income of affiliates	(29,563)	(94,084)
Loss (gain) on disposal of equipment	23,326	(9,431)
Decrease (increase) in:		
Patient accounts receivable	(1,051,038)	(2,285,771)
Supplies	84,094	(104,687)
Prepaid expenses	(57,697)	77,389
Insurance recoverable	(37,050)	7,474
Other amounts receivable	66,577	230,113
Increase (decrease) in:		
Accounts payable	177,280	(98,887)
Accrued salaries and wages	(136,203)	(38,485)
Advances from third parties	(92,900)	91,800
Pension obligation	84,235	(506,318)
Other current liabilities	176,881	(781,731)
NET CASH AND CASH EQUIVALENTS PROVIDED BY OPERATING ACTIVITIES	7,224,420	4,512,145

(Continued)

Garrett County Memorial Hospital and Subsidiary
Consolidated Statements of Cash Flows – Continued

	Year Ended June 30 2014	Year Ended June 30 2013
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	$ (3,143,949)	$ (1,659,140)
Net purchase of trading securities	(3,590,249)	(2,113,297)
Distribution from (to) affiliate	(35,000)	100,000
NET CASH AND CASH EQUIVALENTS USED IN INVESTING ACTIVITIES	(6,769,198)	(3,672,437)
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayments of long-term debt	(159,077)	(159,667)
Proceeds from restricted contributions	488,240	60,111
NET CASH AND CASH EQUIVALENTS PROVIDED BY (USED IN) FINANCING ACTIVITIES	329,163	(99,556)
NET INCREASE IN CASH AND CASH EQUIVALENTS	784,385	740,152
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	7,359,186	6,619,034
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 8,143,571	$ 7,359,186
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for interest	$ 150,487	$ 154,107
Equipment under capital lease	$ 5,205	$ 139,007

See the accompanying notes to the consolidated financial statements.

Note A – Organization and Summary of Significant Accounting Principles

Organization

Garrett County Memorial Hospital (the Hospital) is an instrumentality of Garrett County, Maryland. The Hospital was organized for charitable purposes and is exempt from income taxes as an instrumentality of Garrett County. In 2003, the Hospital formed and became the sole member of Professional Emergency Physician Services, LLC, (PEPS) which is a for-profit limited liability company. The purpose of PEPS is to provide professional emergency services solely to the Hospital. In addition, the Hospital owns 100% of the outstanding shares of Garrett Community Health Services (GCHS), which is a for-profit corporation. GCHS had no activity for the years ended June 30, 2014 and 2013.

Principles of Consolidation

The consolidated financial statements include the accounts of Garrett County Memorial Hospital, Professional Emergency Physician Services, LLC, and Garrett Community Health Services, (collectively referred to as the Company). All significant intercompany accounts and transactions have been eliminated in consolidation.

Basis of Presentation

The consolidated financial statements are prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Contributions, including unconditional promises to give, with no donor-imposed restrictions are recognized in the period received as increases in unrestricted net assets. Contributions with donor-imposed restrictions are reported as increases in temporarily or permanently restricted net assets. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets.

Income and realized net gains (losses) on investments are reported as follows:

- Increases (decreases) in permanently restricted net assets if the terms of the gift or the Hospital's interpretation of relevant state law require that they be added to the principal of a permanent net asset;

- Increases (decreases) in temporarily restricted net assets if the terms of the gift impose restrictions on the use of the income;

- Increases (decreases) in unrestricted net assets in all other cases.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, after contractual adjustments. Patient accounts receivable include charges for amounts due from Medicare, Maryland Medical Assistance (Medicaid), Blue Cross, commercial insurers, and self-pay patients (*see Note K*). Contractual adjustments represent the differences between amounts billed as patient service revenue and amounts contracted with third party payers, and are accrued on an estimated basis in the period in which the related services are rendered and adjusted in future periods as final settlements are determined. Rates charged are based primarily on rates established by the State of Maryland Health Services Cost Review Commission (HSCRC); accordingly, revenue reflects actual charges to patients based on rates in effect during the period in which the services are rendered (*see Note I*).

The Company grants credit without collateral to its patients, most of whom are local residents insured under third-party payer agreements (*see Note K*). Accounts receivable are reported at their net realizable value from third-party payers, patients, residents and others for services rendered. Allowances are provided for third-party payers based on estimated reimbursement rates. Allowances are also provided for bad debts based on an estimate of uncollectible accounts. Write-off of uncollectible accounts is determined on a case-by-case basis after a review of the circumstances surrounding individual patient accounts.

Allowance for Doubtful Accounts

The provision for doubtful accounts is based upon management's judgmental assessment of historical and expected net collections considering business and general economic conditions in its service area, trends in healthcare coverage, and other collection indicators. On a relatively continuous basis, management assesses the adequacy of the allowance for doubtful accounts based upon its review of accounts receivable payer category, payer agreement rate changes and other factors. The results of these assessments are used to make modifications to the provision for bad debts and to establish an appropriate allowance for doubtful accounts.

For self-pay patients, the provision is based on an analysis of past experience related to collection rates of self-pay balances. The Company follows established guidelines for placing certain past-due patient balances with external collection agencies.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Charity Care

The Hospital 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 Hospital does not pursue collection of amounts determined to qualify as charity care, such amounts are not reported as net patient service revenue.

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy. Under current accounting standards, the Hospital is required to report the cost of providing charity care. The cost of charity care provided by the Hospital totaled $2,512,558 and $2,404,444 for the years ended June 30, 2014 and 2013, respectively. Rates charged by the Hospital for regulated services are determined based on an assessment of direct and indirect cost calculated pursuant to the methodology established by the HSCRC (*see Note I*), and therefore the cost of charity services noted above for the Hospital are equivalent to its established rates for those services.

For any charity services rendered by the Company other than the regulated services of the Hospital, the cost of charity care is calculated by applying the estimated total cost-to-charge ratio for the non-Hospital services to the total amount of charges for services provided to patients benefitting from the charity care policies of the Company's non-Hospital affiliates.

The HSCRC established an uncompensated care fund whereby all hospitals are required to contribute 0.75% of revenues to this fund to help provide for the cost associated with uncompensated care for certain Maryland hospitals above the State average. In December 2008, the Commission modified this mechanism to finance uncompensated care statewide. The policy implemented 100% pooling and all Maryland hospitals have the same percentage of uncompensated care in rates. High uncompensated care hospitals receive funds and low uncompensated care hospitals pay into the fund. The Hospital had net receipts of $1,024,026 and $1,027,901 for 2014 and 2013, respectively, related to its participation in the uncompensated care fund mechanism.

Advertising Expense

The Company expenses advertising costs as they are incurred.

Cash and Cash Equivalents

Cash and cash equivalents include investments in certain highly liquid debt instruments with maturities of three months or less when purchased. The Company has cash holdings in commercial banks that routinely exceed the Federal Deposit Insurance Corporation maximum insurance limit of $250,000.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Inventories

Inventories consist primarily of drugs and medical supplies and are carried at the lower of cost (first-in, first-out) or market.

Donor-Restricted Funds

Donor-restricted funds are used to differentiate resources, the use of which are limited by the donor, from resources on which the donor places no restriction or which arise as a result of the operation of the Hospital for its stated purposes. Restricted funds for care of needy patients and other temporarily restricted net assets are reflected in operating revenue to the extent restrictions have been met; net assets restricted for property and equipment are reclassified to the unrestricted net assets balance when those assets are acquired.

Assets Whose Use is Limited

Assets limited as to use primarily consist of cash, certificates of deposit, pledges receivable and investments. Assets limited as to use include donor restricted assets, funds held by trustee, and assets designated by the board of governors for future capital improvements, over which the board retains control and may, at its discretion, subsequently use for other purposes.

Property and Equipment

Property and equipment are stated at cost, except for donated items which are recorded at fair value at the date of donation. Depreciation is provided on a straight-line basis over the estimated useful lives of the assets. Equipment under capital lease obligations is amortized on a straight-line basis over the shorter period of the lease terms or the estimated useful lives of the equipment. Such amortization is included in depreciation in the accompanying 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.

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 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.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Deferred Financing Costs

Costs related to issuance of debt are deferred and amortized using the straight-line method, which approximates the interest method.

Investments

Investments are exposed to certain risks such as interest rate, credit and overall market volatility. Due to the level of risk associated with certain investment securities, changes in the value of investment securities could occur in the near term, and these changes could materially differ from the amounts reported in the accompanying consolidated financial statements. Investments and assets whose use is limited, which are invested in marketable securities, are reported at their fair value, based on quoted market prices provided by the asset managers. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in the excess of revenues over expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from the excess of revenues over expenses unless the investments are trading securities (*see Note B*).

Investments in Affiliates

The Hospital maintains certain investments in unconsolidated entities. These investments are accounted for using the equity method (*see Note C*).

Excess of Revenue over Expenses

The accompanying consolidated statements of operations include excess of revenue over expenses. Changes in unrestricted net assets which are excluded from excess of revenue over expenses, consistent with industry practice, include unrealized gains and losses on other than trading securities, pension-related changes other than net periodic pension cost, any permanent transfers of assets to and from affiliates for other than goods or services and contributions of long lived assets (including assets required using contributions which by donor restriction were to be used for the purpose of acquiring such assets).

Meaningful Use Incentive

Under the provisions of the American Recovery and Reinvestment Act of 2009, incentive payments are available to certain healthcare providers that can demonstrate "meaningful use" of certified electronic health records technology. The Hospital recognized these incentive payments when it is reasonably assured that they will successfully demonstrate compliance with meaningful use criteria. During 2014, the Hospital recognized approximately $1,517,000 of these incentive payments in other operating revenue in the accompanying consolidated financial statements.

Note A – Organization and Summary of Significant Accounting Principles – Continued

Estimated Malpractice Costs

The costs of professional and general liability insurance include estimates for both reported claims and claims incurred but not reported, based on the evaluation of pending claims and past experience (*see Note J*).

Use of Estimates

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

Income Taxes

The Hospital and PEPS have been recognized by the Internal Revenue Service (IRS) as tax exempt under Section 115 as an instrumentality of a political subdivision of the State of Maryland. GCHS is organized as a for-profit entity and therefore is subject to federal and state income taxes.

The state in which the Hospital operates also provides general exemption from state income taxation for organizations that are exempt from federal income taxation. However, the Hospital is subject to both federal and state income taxation at corporate tax rates on its unrelated business income. Exemption from other state taxes, such as real and personal property taxes, is separately determined.

The Hospital had no unrecognized tax benefits or such amounts were immaterial during the periods presented. For tax periods with respect to which no unrelated business income was recognized, no tax return was required. Tax periods for which no return is filed remain open for examination indefinitely. No tax returns were filed for the Hospital during 2014 and 2013.

Management has also considered the impact of unrelated business activities and has concluded that the Hospital is not subject to unrelated business tax or any other taxes that could be imposed by the Internal Revenue Code or state taxing authorities. As such no provision is made for income taxes and no asset or liability has been recognized for deferred taxes.

Subsequent Events

Management has evaluated activities subsequent to June 30, 2014, and determined that, as of October 23, 2014 there are no reportable subsequent events.

Note B – Investments and Assets Whose Use is Limited

Investments and assets limited as to use consist of the following:

	Investments	Assets whose use is limited by donors	Assets whose use is limited by the Board of Governors	Total
At June 30, 2014:				
Cash and cash equivalents	$ 259,796	$ 6,914	$ 0	$ 266,710
Certificates of deposit	18,911,273	0	698,073	19,609,346
Government securities	70,224	17,868	0	88,092
Corporate bonds	602,341	0	0	602,341
Mutual funds	3,185,066	69,136	0	3,254,202
Common stock	837,723	39,326	0	877,049
Pledges receivable, net	0	436,923	0	436,923
	23,866,423	570,167	698,073	25,134,663
Less short-term portion	18,911,273	112,582	0	19,023,855
	$ 4,955,150	$ 457,585	$ 698,073	$ 6,110,808

	Investments	Assets whose use is limited by donors	Assets whose use is limited by the Board of Governors	Total
At June 30, 2013:				
Cash and cash equivalents	$ 291,614	$ 18,086	$ 0	$ 309,700
Certificates of deposit	15,910,000	0	698,073	16,608,073
Government securities	85,585	1,015	0	86,600
Corporate bonds	459,965	15,173	0	475,138
Preferred stock	38,830	1,262	0	40,092
Mutual funds	2,679,773	86,694	0	2,766,467
Common stock	632,029	21,520	0	653,549
Pledges receivable, net	0	219,314	0	219,314
	20,097,796	363,064	698,073	21,158,933
Less short-term portion	15,910,000	58,584	0	15,968,584
	$ 4,187,796	$ 304,480	$ 698,073	$ 5,190,349

Assets whose use is limited include investments and pledges receivable. Board designated funds consist of certificates of deposit at June 30, 2014 and 2013.

Note B – Investments and Assets Whose Use is Limited – Continued

Pledges receivable are recorded net of an allowance for uncollectible pledges of $27,968 and $11,753 at June 30, 2014 and 2013, respectively. Pledges are recorded at their net present value and are due as follows at June 30, 2014:

2015	$	117,455
2016		91,515
2017		84,471
2018		60,604
2019		42,696
After 2019		77,605
		474,346
Present value discount		(9,455)
Allowance for uncollectible pledges		(27,968)
	$	436,923

The investment return on the Company's investments and assets limited as to use consists of the following for the years ended June 30:

		2014		2013
Interest and dividends	$	182,025	$	182,086
Net realized gains		182,765		113,209
Net unrealized gains		385,481		211,675
	$	750,271	$	506,970

Current accounting standards define fair value as 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, and establish a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date, as follows:

Level 1: Quoted prices in active markets for identical assets or liabilities.

Level 2: Observable input other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Note B – Investments and Assets Whose Use is Limited – Continued

The following discussion describes the valuation methodologies used for financial assets measured at fair value. The techniques utilized in estimating the fair values are affected by the assumptions used, including discount rates, and estimates of the amount and timing of future cash flows. Care should be exercised in deriving conclusions about the Company's business, its value, or financial position based on the fair value information of financial assets presented below.

Fair value estimates are made at a specific point in time, based on available market information and judgments about the financial asset, including estimates of the timing, amount of expected future cash flows, and the credit standing of the issuer. In some cases, the fair value estimates cannot be substantiated by comparison to independent markets. In addition, the disclosed fair value may not be realized in the immediate settlement of the financial asset. Furthermore, the disclosed fair values do not reflect any premium or discount that could result from offering for sale at one time an entire holding of a particular financial asset. Potential taxes and other expenses that would be incurred in an actual sale or settlement are not reflected in the amounts disclosed.

Fair values of the Company's government securities and corporate bonds are based on prices provided by its investment managers, who use a variety of pricing sources to determine market valuations. Each designate specific pricing services or indexes for each sector of the market based upon the provider's experience. The Company's government securities and corporate bonds portfolio is highly liquid, which allows for a high percentage of the portfolio to be priced through pricing services. Fair values of the Company's certificate of deposits are based on cost plus accrued interest, which in the opinion of management approximates fair value. Fair values of marketable equity securities (mutual funds and stock) have been determined by the Company from observable market quotations, when available. Private placement securities and other equity securities where a public quotation is not available are valued by using broker quotes.

Note B – Investments and Assets Whose Use is Limited – Continued

The following table presents the Company's fair value hierarchy for assets measured at fair value on a recurring basis as of June 30, 2014:

	Level 1	Level 2	Total
Cash and cash equivalents	$ 266,710	$ 0	$ 266,710
Certificates of deposit	19,609,346		19,609,346
Government securities			
Maturity 1 - 10 years	0	54,458	54,458
Maturity > 10 years	0	33,634	33,634
Corporate bonds			
Maturity 1 - 10 years	0	449,104	449,104
Maturity > 10 years	0	153,237	153,237
Mutual funds			
Bank Loan	140,895	0	140,895
Foreign Large Blend	332,142	0	332,142
Intermediate-Term Bond	444,876	0	444,876
Large Blend	393,430	0	393,430
Large Growth	175,986	0	175,986
Large Value	299,366	0	299,366
Mid-Cap Value	166,620	0	166,620
Mid-Cap Growth	119,144	0	119,144
Short-Term Bond	209,338	0	209,338
Other	972,405	0	972,405
Stocks			
Basic Materials	190,872	0	190,872
Healthcare	117,192	0	117,192
Services	181,171	0	181,171
Technology	126,579	0	126,579
Other	261,235	0	261,235
	$ 24,007,307	$ 690,433	$ 24,697,740

Note B – Investments and Assets Whose Use is Limited – Continued

The following table presents the Company's fair value hierarchy for assets measured at fair value on a recurring basis as of June 30, 2013:

	Level 1	Level 2	Total
Cash and cash equivalents	$ 309,700	$ 0	$ 309,700
Certificates of deposit	16,608,073	0	16,608,073
Government securities			
Maturity 1 - 10 years	0	27,950	27,950
Maturity > 10 years	0	58,650	58,650
Corporate bonds			
Maturity 1 - 10 years	0	293,641	293,641
Maturity > 10 years	0	181,497	181,497
Mutual funds			
Bank Loan	94,239	0	94,239
Diversified Emerging Markets	123,954	0	123,954
Emerging Markets Bond	69,623	0	69,623
Foreign Large Blend	369,586	0	369,586
High Yield Bond	85,909	0	85,909
Intermediate-Term Bond	406,653	0	406,653
Large Blend	355,227	0	355,227
Large Growth	155,036	0	155,036
Large Value	221,404	0	221,404
Mid-Cap Value	102,389	0	102,389
Mid-Cap Growth	85,588	0	85,588
Short-Term Bond	102,775	0	102,775
Small Growth	76,070	0	76,070
Technology	70,376	0	70,376
World Bond	56,981	0	56,981
Other	390,657	0	390,657
Stocks			
Basic Materials	103,653	0	103,653
Conglomerates	37,980	0	37,980
Consumer Goods	42,743	0	42,743
Financial	52,121	0	52,121
Healthcare	97,692	0	97,692
Industrial Goods	32,127	0	32,127
Preferred Stock	40,092	0	40,092
Services	167,070	0	167,070
Technology	97,435	0	97,435
Utilities	22,728	0	22,728
	$ 20,377,881	$ 561,738	$ 20,939,619

There were no transfers between levels during 2014 and 2013.

Note C – Investments in Affiliates

The Hospital maintains investments in joint ventures at June 30 as follows:

Joint Venture	Type of organization	Business purpose	Percentage ownership 2014	Percentage ownership 2013
Garrett Rehabilitation Services (GRS)	For-profit	Medical, rehabilitative and therapy services	0%	50%
Oakland MRI Center, LLC (OMRI)	For-profit	MRI and Dexa scan services	50%	50%
Freestate Healthcare Insurance Company, Ltd. (Freestate)	For-profit	Malpractice and professional liability insurance	20%	20%
Western Maryland Medical Supply, LLC (WMMS)	For-profit	Durable medical equipment services	33.3%	33.3%

GRS was a joint venture in which the Hospital and Select Medical of Maryland, Inc. invested equally. In 2014, GRS was dissolved. GRS provided physical therapy, speech pathology, occupational therapy and general rehabilitation services in an outpatient clinical setting. GRS also provided inpatient rehabilitation services for the Hospital. Such services to the Hospital approximated $138,504 in 2014 and $351,291 in 2013.

In April 2004, the Hospital formed OMRI with Premier Imaging, LLC. The purpose of this joint venture is to provide MRI and Dexa Scan services to the local and surrounding communities. The Hospital made an initial capital contribution of $162,000 in 2005. OMRI began operations in January 2006.

In December 2004, the Hospital joined Freestate along with seven other community hospitals from Maryland. Freestate is a Cayman Islands corporation formed for the purpose of providing insurance coverage to its members, their affiliates and their respective employees (*see Note J*). The Hospital contributed $15,000 of equity to Freestate during 2005.

In April 2009, the Hospital joined Western Maryland Medical Supply, LLC (WMMS). WMMS provides durable medical equipment to the local and surrounding communities. The Hospital initially contributed $201,403 in 2009.

Note C – Investments in Affiliates – Continued

The Hospital's investment balance and income in earnings of these joint ventures as of June 30 are as follows:

	Investment balance		Equity (loss) in earnings	
	2014	2013	2014	2013
GRS	$ 0	$ (9,242)	$ (70,758)	$ (30,282)
OMRI	239,853	193,069	91,784	149,598
Freestate	20,542	20,543	0	50
WMMS	(74,445)	(82,983)	8,537	(25,282)
	$ 185,950	$ 121,387	$ 29,563	$ 94,084

Summary combined financial information (unaudited) for these joint ventures as of and for the year ended June 30 was as follows:

	2014	2013
Current assets	$ 43,171,869	$ 24,012,140
Noncurrent assets	2,224,103	18,883,463
TOTAL ASSETS	45,395,972	42,895,603
Current liabilities	1,106,449	1,569,307
Noncurrent liabilities	43,587,023	40,603,153
Net worth	702,500	723,143
TOTAL LIABILITIES AND NET WORTH	$ 45,395,972	$ 42,895,603
Total operating revenue	$ 8,264,511	$ 6,807,342
Total operating expense	7,583,163	6,451,805
NET INCOME	$ 681,348	$ 355,537

Note D – Property and Equipment

Property and equipment and their related estimated useful lives as of June 30 are summarized as follows:

	Estimated useful life	2014	2013
Land improvements	10 - 40 years	$ 775,233	$ 745,443
Buildings and improvements	15 - 40 years	28,338,866	27,953,386
Fixed equipment	5 - 20 years	5,131,805	4,776,396
Movable equipment	3 - 20 years	16,539,182	16,105,903
Equipment under capital lease	lease term	144,211	574,406
		50,929,297	50,155,534
Less accumulated depreciation		32,907,155	31,727,999
		18,022,142	18,427,535
Land		1,162,039	1,162,039
Construction in progress		1,555,401	710,369
		$ 20,739,582	$ 20,299,943

Depreciation expense for the years ended June 30, 2014 and 2013 was $2,686,189 and $2,620,100, respectively. Accumulated amortization of capital leases was $44,679 and $451,557 in June 30, 2014 and 2013, respectively.

In August 2014, the Hospital signed a construction management contract for approximately $16 million of which $1.9 million was signed in June 2014 for various renovations and an additional wing to the Hospital. Construction is expected to be completed by July 2017.

Note E – Long-Term Debt

Long-term debt as of June 30 consists of the following:

	2013	2012
USDA bonds	$ 2,588,149	$ 2,657,867
Series 2004 bonds	874,492	939,116
Capital lease obligation	104,083	123,613
	3,566,724	3,720,596
Less current portion	165,867	156,113
	$ 3,400,857	$ 3,564,483

United States Department of Agriculture (USDA) Bonds

In June 2007, Garrett County issued the Garrett County Memorial Hospital Refunding Bonds, Series 2007 (Series 2007 Bonds), for the purpose of providing funding for the Hospital's Emergency Room/Same Day Surgery/Admissions construction and renovation project. The Series 2007 Bonds represent a supplemental loan agreement between the Hospital and Garrett County Maryland for amounts that are equal to the loan principal of the Garrett County Series 2007 Bonds. The funds were provided to Garrett County from the USDA. Funding from the bonds was also used to refinance other outstanding indebtedness.

The Series 2007 Bonds bear interest at an average rate of approximately 4.125%. Bond principal and interest payments are made in monthly installments to a trustee to meet the payment schedule stipulated in the loan agreement. The bonds mature June 28, 2037.

Series 2004 Bonds

In November 2004, Garrett County issued County Commissioners of Garret County Hospital Refunding Bonds, Series 2004 (Series 2004 Bonds) for the purpose of refunding a portion of other outstanding indebtedness. The Series 2004 Bonds represent a supplemental loan agreement between the Hospital and Garrett County for amounts that are equal to the loan principal of the County's Series 2004 Bonds.

The Series 2004 Bonds incur interest at a rate of 4.12% per annum. Bond principal and interest payments are made in semiannual installments to a trustee to meet the payment schedule stipulated in the loan agreement. The loan matures on November 19, 2024.

Note E – Long-Term Debt – Continued

Capital Leases

The Hospital periodically enters into various leases for equipment that meet the criteria for capitalization under current accounting standards.

Aggregate maturities of all long-term debt as of June 30, 2014 are as follows:

2015	$	165,867
2016		172,482
2017		179,363
2018		170,739
2019		161,684
After 2019		2,716,589
	$	3,566,724

The Company is subject to certain restrictive covenants defined in various agreements with lenders. In the opinion of management, the Company was in compliance with all applicable restrictive covenants as of June 30, 2014 and 2013.

Note F – Temporarily Restricted Net Assets

Temporarily restricted net assets of $454,247 and $260,393 at June 30, 2014 and 2013, respectively, are restricted primarily for property replacement, expansion, and health care clinical services.

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors as follows during the years ended June 30:

	2014	2013
Health care clinical services	$ 35,203	$ 10,551
Plant replacement and expansion	259,183	231,377
	$ 294,386	$ 241,928

Note G – Pension Plan

The Hospital has a noncontributory defined benefit pension plan (the Plan) covering all employees of the Hospital who work at least twenty hours per week. Benefits are based on the participants' credited service and average monthly earnings. The Hospital's funding policy is to contribute an amount annually that is equal to the normal cost plus interest on the unfunded accrued liability. The Internal Revenue Service classifies the Plan as a government plan, and the Plan, as such, is exempt from the requirements of the Employee Retirement Income Security Act of 1974. The Hospital uses a June 30 measurement date for the Plan. The Hospital intends to contribute $1,250,000 for fiscal year 2015. The assumption change in the table below represents change in the discount rate and rate of compensation increase for 2014 and 2013

The following table sets forth the changes in the benefit obligation at June 30:

	2014	2013
Projected benefit obligation at beginning of year	$ 30,780,349	$ 29,011,730
Service cost	1,004,186	1,144,387
Interest	1,482,410	1,378,797
Assumption change	2,215,485	(256,990)
Actuarial loss	(133,444)	339,979
Benefits paid	(1,025,018)	(837,554)
Projected benefit obligation at end of year	$ 34,323,968	$ 30,780,349

The following table sets forth the changes in the Plan assets at June 30:

	2014	2013
Fair value of Plan assets as beginning of year	$ 20,714,827	$ 18,439,890
Actual return on Plan assets	3,254,178	2,014,329
Employer contribution	1,230,224	1,098,162
Benefits paid	(1,025,018)	(837,554)
Fair value of Plan assets as end of year	$ 24,174,211	$ 20,714,827
Funded status	$ (10,149,757)	$ (10,065,522)
Net loss included in unrestricted net assets	$ 8,486,610	$ 8,420,919
Accumulated benefit obligation	$ 29,302,297	$ 26,726,235

The components of the net periodic benefit cost consist of the following at June 30:

	2014	2013
Service cost	$ 1,004,186	$ 1,144,387
Interest cost	1,482,410	1,378,797
Expected return on assets held in the plan	(1,662,445)	(1,485,561)
Amortization of net loss	424,617	550,615
	$ 1,248,768	$ 1,588,238

Note G – Pension Plan – Continued

The assumptions used in the accounting for the benefit obligation are as follows at June 30:

	2014	2013
Discount rate	4.39%	4.89%
Rate of compensation increase	3.89%	3.83%

The weighted average assumptions used in the accounting for the net periodic benefit cost are as follows for the years ended June 30:

	2014	2013
Discount rate	4.39%	4.89%
Rate of compensation increase	3.89%	3.83%
Expected long-term return on plan assets	8.00%	8.00%

The Hospital's weighted average asset allocations for Plan assets are as follows at June 30:

	2014	2013
Equity securities	56%	58%
Fixed maturity securities	42%	36%
Other	2%	6%
Total plan assets	100%	100%

Plan assets are invested in accordance with the investment policy statement objectives in an attempt to maximize return with reasonable and prudent levels of risk. This structure includes various asset classes, investment management styles, asset allocation and acceptable ranges that, in total, are expected to produce a sufficient level of overall diversification and total investment return. The Hospital periodically reviews performance to test progress toward attainment of longer-term targets, compare results to appropriate indices and peer groups, and assess overall investment risk levels. The target weighted-average asset allocation of pension investments is 55% equity securities, 40% debt securities and 5% other. Fixed maturity securities primarily include corporate bonds. Equity securities primarily include investments in large-cap and mid-cap companies and common stock which are valued by observable market quotations.

The following benefit payments, which reflect expended future service, as appropriate, are expected to be paid:

2015	$ 1,192,000
2016	1,283,000
2017	1,408,000
2018	1,581,000
2019	1,741,000
2020-2025	13,864,000
	$ 21,069,000

Note G – Pension Plan – Continued

The fair values of the Hospital's Plan assets as of June 30, 2014 by asset category are as follows:

	Level 1	Level 2	Total
Cash and Cash Equivalents			
Cash	$ 402,662	$ 0	$ 402,662
Money market funds	400,000	0	400,000
Fixed Income			
Corporate Bonds			
Maturity 1 to 10 years	0	4,066,938	4,066,938
Maturity > 10 years	0	601,452	601,452
Municipal Bonds			
Maturity 1 to 10 years	0	1,266,055	1,266,055
Maturity > 10 years	0	209,166	209,166
Mutual Funds			
Bank Loan	553,105	0	553,105
World Bond	326,852	0	326,852
Inflation-Protected Bond	85,290	0	85,290
Intermediate Government	147,870	0	147,870
High Yield Bond	545,812	0	545,812
Intermediate-Term Bond	394,935	0	394,935
Equity Securities			
Mutual Funds			
Diversified Emerging Markets	166,870	0	166,870
Foreign Large Blend	439,171	0	439,171
Foreign Small/Mid Growth	165,906	0	165,906
Large Blend	548,930	0	548,930
Large Growth	799,830	0	799,830
Large Value	930,063	0	930,063
Mid-Cap Blend	319,777	0	319,777
Mid-Cap Growth	719,047	0	719,047
Mid-Cap Value	622,110	0	622,110
Natural Resources	111,513	0	118,513
Short-Term Bond	399,780	0	399,780
Small Blend	73,099	0	73,099
Small Growth	302,666	0	302,666
Small Value	213,764	0	213,764
Technology	388,060	0	388,060
Ultrashort Bond	897,799	0	897,799

Note G – Pension Plan – Continued

	Level 1	Level 2	Total
	(continued)		
Common Stocks			
Basic Materials	990,555	0	990,555
Conglomerates	236,190	0	236,190
Consumer Goods	318,241	0	318,241
Financial	441,089	0	441,089
Healthcare	420,645	0	420,645
Industrial Goods	244,545	0	244,545
Preferred Shares	252,420	0	252,420
Services	1,184,464	0	1,184,464
Technology	342,981	0	342,981
Utilities	157,344	0	157,344
Exchange Traded Funds			
Health	179,494	0	179,494
Industrials	147,010	0	147,010
Large Growth	409,185	0	409,185
Large Blend	76,710	0	76,710
Large Value	506,350	0	506,350
Mid-Cap Value	320,963	0	320,963
PowerShares	130,048	0	130,048
Mid-Cap Growth	608,160	0	608,160
Small Value	166,334	0	166,334
SPDR	456,748	0	456,748
Technology	385,780	0	385,780
	$ 17,930,167	$ 6,143,611	$ 24,080,778

Note G – Pension Plan – Continued

The fair values of the Hospital's Plan assets as June 30, 2013 by asset category are as follows:

	Level 1	Level 2	Total
Cash and Cash Equivalents			
Cash	$ 8,625	$ 0	$ 8,625
Money market funds	1,191,248	0	1,191,248
Fixed Income			
Corporate Bonds			
Maturity 1 to 10 years	0	3,143,342	3,143,342
Maturity > 10 years	0	480,339	480,339
Municipal Bonds			
Maturity 1 to 10 years	0	1,264,401	1,264,401
Maturity > 10 years	0	295,265	295,265
Mutual Funds			
Bank Loan	250,274	0	250,274
World Bond	316,821	0	316,821
Inflation-Protected Bond	184,617	0	184,617
Intermediate Government	146,007	0	146,007
High Yield Bond	524,316	0	524,316
Intermediate-Term Bond	388,908	0	388,908
Equity Securities			
Mutual Funds			
Diversified Emerging Markets	279,961	0	279,961
Emerging Market Bond	142,580	0	142,580
Equity Energy	63,460	0	63,460
Foreign Large Blend	236,995	0	236,995
Foreign Large Growth	100,532	0	100,532
Foreign Small/Mid Growth	50,932	0	50,932
Large Blend	468,026	0	468,026
Large Growth	598,464	0	598,464
Large Value	810,039	0	810,039
Mid-Cap Blend	365,777	0	365,777
Mid-Cap Growth	705,390	0	705,390
Mid-Cap Value	333,044	0	333,044
Natural Resources	98,696	0	98,696
Short-Term Bond	100,000	0	100,000
Small Blend	69,277	0	69,277
Small Growth	325,990	0	325,990
Small Value	184,756	0	184,756
Technology	244,578	0	244,578
Ultrashort Bond	196,282	0	196,282

Note G – Pension Plan – Continued

	Level 1	Level 2	Total
	(continued)		
Common Stocks			
Basic Materials	640,081	0	640,081
Conglomerates	189,900	0	189,900
Consumer Goods	276,974	0	276,974
Financial	372,646	0	372,646
Healthcare	401,534	0	401,534
Industrial Goods	269,218	0	269,218
Preferred Shares	249,350	0	249,350
Services	862,302	0	862,302
Technology	339,326	0	339,326
Utilities	125,004	0	125,004
Exchange Traded Funds			
Diversified Emerging Markets	169,400	0	169,400
Health	140,266	0	140,266
Industrials	109,890	0	109,890
Large Growth	400,070	0	400,070
Large Blend	459,422	0	459,422
Large Value	478,370	0	478,370
Mid-Cap Value	261,236	0	261,236
PowerShares	609,880	0	609,880
Mid-Cap Growth	103,912	0	103,912
Small Value	135,800	0	135,800
SPDR	146,375	0	146,375
Technology	316,932	0	316,932
	$ 15,443,483	$ 5,183,347	$ 20,626,830

There were no transfers between levels during 2014 and 2013.

Note H – Certain Significant Risks and Uncertainties

The Hospital provides general acute health care services in Garrett County, Maryland. The Company and other health care providers in Maryland are subject to certain inherent risks, including the following:

- Dependence on revenues derived from reimbursement by the Federal Medicare and state Medicaid programs *(see Note K)*;
- Regulation of hospital rates by the State of Maryland Health Services Cost Review Commission *(see Note I)*;
- Government regulation, government budgetary constraints and proposed legislative and regulatory changes; and
- Lawsuits alleging malpractice and related claims (*see Note J*).

Such inherent risks require the use of certain management estimates in the preparation of the Company's consolidated financial statements and it is reasonably possible that a change in such estimates may occur.

The Medicare and state Medicaid reimbursement programs represent a substantial portion of the Company's revenues and the Company's operations are subject to a variety of other Federal, state and local regulatory requirements. Failure to maintain required regulatory approvals and licenses and/or changes in such regulatory requirements could have a significant adverse effect on the Company. Changes in Federal and state reimbursement funding mechanisms and related government budgetary constraints could have a significant adverse effect on the Company.

The healthcare industry is subject to numerous laws and regulation from federal, state and local governments, and the government has increased enforcement of Medicare and Medicaid anti-fraud and abuse laws, as well as physician self-referral laws (STARK law and regulation). The Company's compliance with these laws and regulations is subject to periodic governmental review, which could result in enforcement actions unknown or unasserted at this time.

As a result of recently enacted and pending federal healthcare reform legislation, substantial changes are anticipated in the healthcare system. Such legislation includes numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement to healthcare providers and the legal obligations of health insurers, providers and employers. These provisions are currently slated to take effect at specified times over the next decade. This federal healthcare reform legislation does not affect the consolidated financial statements for the year ended June 30, 2014.

The Company is subject to certain legal proceedings and claims arising in the ordinary course of business. After consultation with legal counsel, it is management's opinion that the ultimate resolution of these claims will not have a material adverse effect on the Company's financial position or changes in net assets.

Note I – Maryland Health Services Cost Review Commission

The Hospital's rate structure is subject to review and approval by the Maryland Health Services Cost Review Commission (HSCRC). The Hospital has entered into a Total Patient Revenue (TPR) System with the HSCRC. Under TPR, gross patient service revenue is determined prospectively for each rate year ending on June 30. TPR-approved revenue and rates are adjusted annually for the effect of cost of inflation, growth of the population area served by the Hospital and variances between TPR-approved revenue versus the actual revenue charged to patients during the prior rate year. Under TPR, the Hospital has the ability (within limits) to adjust rates to charge patients more or less than the gross patient service revenue approved for each year.

The Hospital's policy is to accrue revenue based on actual charges for services to patients in the year in which the services are performed and billed.

The Commission has jurisdiction over hospital reimbursement in Maryland by agreement with the Centers for Medicare and Medicaid Services (CMS). This agreement is based on a waiver from the Medicare Prospective Payment System reimbursement principles granted under Section 1814(b) of the Social Security Act. On January 10, 2014 Maryland's All-Payer Hospital System Modernization was approved by CMS. This is a five year demonstration where Maryland agreed to permanently shift away from its current statutory waiver, which is based on Medicare payment per inpatient admission, in exchange for the new CMS model based on Medicare per capita total hospital cost growth.

Note J – Insurance

Malpractice Insurance

The Company is involved in litigation arising in the normal course of business. Claims alleging malpractice have been asserted against the Hospital and are currently in various stages of litigation. Additional claims may be asserted against the Company arising from services provided through June 30, 2014. Management believes that no material loss will result from any pending or threatened litigation or from incidents incurred but not reported.

In accordance with current accounting standards, the Company reports gross insurance recoveries separately from the related claims liability for professional liability claims already reported to its insurance carrier. As of June 30, 2014 and 2013, the Hospital recorded insurance recoverable and professional claim liability of $588,715 and $551,665, respectively, as both an asset and a liability in the accompanying consolidated financial statements.

Note J – Insurance – Continued

Malpractice Insurance -- Continued

An estimated liability for incurred but not reported professional liability claims has been recorded in the amount of approximately $694,000 for the years ended June 30, 2014 and 2013. This amount is included in other long-term liabilities in the accompanying consolidated financial statements. Management believes this accrual is adequate to provide for all professional liability claims that have been incurred through June 30, 2014, but not reported to its insurance carrier.

Effective March 1, 2005, the Hospital became a shareholder of the newly formed Freestate Healthcare Insurance Company, Ltd. (Freestate), a captive insurance company formed in the Cayman Islands by eight Maryland hospitals. The Hospital became a shareholder of Freestate when the Hospital's insurance company decided not to continue to write insurance policies for hospitals within the State of Maryland effective March 1, 2005. The Hospital believes that becoming a shareholder of the captive insurance company provides the best long-term solution to providing insurance coverage that is cost effective and predictable. Freestate provides insurance coverage on a claims-made basis to its owners for professional liability claims and comprehensive general liability of $1,000,000 for each and every claim. Freestate has entered into reinsurance and excess policy agreements with independent insurance companies to limit its losses for professional liability and comprehensive general liability claims. The Hospital has $2,000,000 of additional insurance in the aggregate through such reinsurance arrangements. Retrospective premium assessments and credits are calculated based on the aggregate experience of all named insureds under the policy. Each named insured's assessment or credit is based on the percentage of their actual exposure to the actual exposure of all named insureds. In management's opinion, the assets of Freestate are sufficient to meet its obligations as of June 30, 2014. If the financial condition of Freestate were to materially deteriorate in the future, and Freestate was unable to pay its claim obligations, the payment of such claims would be the responsibility of the member hospitals. The estimated cost of claims is actuarially determined based upon past experience and discounted using a discount rate of 3.5% in 2014 and 2013.

PEPS' malpractice insurance is provided by a commercial insurance carrier. The policy provides coverage of $1,000,000 for each event, with a physician aggregate of $3,000,000 and a $5,000,000 policy aggregate.

Health Insurance

The Company is self-insured for employee health claims. Under the self-insurance plan, the Company has accrued a liability of $278,716 and $203,387 for the years ended June 30, 2014 and 2013 for incurred but not reported claims. Management believes that the accruals are adequate to provide for all employee health claims that have been incurred for the years ended June 30, 2014 and 2013.

Note K – Business and Credit Concentrations

The Company provides health care services through its inpatient and outpatient care facilities located in Oakland, Maryland. The Company grants credit to patients, substantially all of whom are local residents. The Company generally does not require collateral or other security in extending credit; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits receivable under their health insurance programs, plans, or policies (e.g., Medicare, Medicaid, Blue Cross, health maintenance organizations (HMOs) and commercial insurance policies).

At June 30, the Company had patient accounts receivable, net of contractual allowances from third-party payers and others, as follows:

	2014	2013
Self-pay and others	$ 2,038,934	$ 1,507,021
Medicare	2,455,270	2,879,117
Commercial insurance and HMOs	913,233	1,341,464
Medicaid	1,380,320	1,922,396
Blue Cross	776,728	1,447,518
	7,564,485	9,097,516
Allowance for doubtful accounts	(2,386,815)	(3,395,041)
	$ 5,177,670	$ 5,702,475

Patient service revenue, by payer class, consisted of the following for the years ended June 30:

	2014	2013
Medicare	46%	45%
Commercial insurance and HMOs	15%	16%
Blue Cross	15%	15%
Medicaid	18%	16%
Self-pay and others	6%	8%
	100%	100%

Note L – Functional Expenses

The Company provides general health care services to residents within its geographic location. Expenses related to providing these services, based on management's estimates of expense allocations, are as follows for the years ended June 30:

	2014	2013
Health care services	$ 32,470,427	$ 32,122,243
General and administrative	7,553,537	7,040,421
	$ 40,023,964	$ 39,162,664

Note M – Endowment

Current accounting standards provide guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA) and additional disclosures about an organization's endowment funds. The State of Maryland has adopted UPMIFA.

The Company's endowment consists of one donor-restricted fund. Net assets associated with the endowment fund are classified and reported based on the existence or absence of donor-imposed restrictions.

The board of governors of the Company has interpreted the Maryland State Prudent Management of Institutional Funds Act (SPMIFA) 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. As a result of this interpretation, the Company classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets (if any) is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by SPMIFA.

Note N – Endowment - Continued

In accordance with SPMIFA, the Company 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 Company 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 Company
7. The investment policies of the Company

From time to time, the fair value of assets associated with the endowment fund may fall below the level that the donor or SPMIFA required the Company to retain as a fund of perpetual duration. There were no such deficiencies as of June 30, 2014 or 2013.

The Company has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity. Under this policy, as approved by the board of governors, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of the Lehman Intermediate Government/Corporate Bond index while assuming a moderate level of investment risk. The Company expects its endowment funds, over time, to provide an average rate of return of approximately 8% percent annually. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate-of-return objectives, the Company 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 Company targets a diversified asset allocation that places a greater emphasis on highly liquid investments such as money market accounts to achieve its long-term return objectives within prudent risk constraints.

The endowment's net asset composition and the changes therein were as follows:

	2014			2013		
	Unrestricted	Permanently Restricted	Endowment Total	Unrestricted	Permanently Restricted	Endowment Total
Beginning balance	$ 10,965	$ 35,586	$ 46,551	$ 9,721	$ 35,086	$ 44,807
Interest and dividends	1,301	0	1,301	1,244	0	1,244
Contributions	0	525	0	0	500	0
Ending Balance	**$ 12,266**	**$ 36,111**	**$ 47,852**	**$ 10,965**	**$ 35,586**	**$ 46,051**

Garrett County Memorial Hospital
Consolidating Balance Sheet Information
As of June 30, 2014

	Garrett County Memorial Hospital	Professional Emergency Physician Services, LLC	Elimination Entries	Consolidated
ASSETS				
CURRENT ASSETS				
Cash and cash equivalents	$ 7,859,027	$ 284,544	$ 0	$ 8,143,571
Short-term investments	18,911,273	0	0	18,911,273
Patient accounts receivable, net	5,035,383	142,287	0	5,177,670
Other amounts receivable	324,157	2,316	0	326,473
Assets whose use is limited by donors	112,582	0	0	112,582
Inventories	990,156	474	0	990,630
Prepaid expenses	403,665	61,800	0	465,465
Due from affiliates	1,093,074	0	(1,093,074)	0
TOTAL CURRENT ASSETS	34,729,317	491,421	(1,093,074)	34,127,664
NONCURRENT ASSETS				
Property and equipment	20,739,582	0	0	20,739,582
Insurance recoverable	588,715	0	0	588,715
Long-term investments	4,955,150	0	0	4,955,150
Investment in affiliates	185,950	0	0	185,950
Assets whose use is limited by donors, less current portion	457,585	0	0	457,585
Assets whose use is limited by board of governors	698,073	0	0	698,073
Deferred financing costs, net	22,633	0	0	22,633
TOTAL NONCURRENT ASSETS	27,647,688	0	0	27,647,688
TOTAL ASSETS	$ 62,377,005	$ 491,421	$ (1,093,074)	$ 61,775,352

See the accompanying report of independent auditors on other financial information.

Garrett County Memorial Hospital
Consolidating Balance Sheet Information – Continued
As of June 30, 2014

	Garrett County Memorial Hospital	Professional Emergency Physician Services, LLC	Elimination Entries	Consolidated
LIABILITIES AND NET ASSETS				
CURRENT LIABILITIES				
Accounts payable	$ 968,298	$ 5,153	$ 0	$ 973,451
Accrued salaries and wages	1,808,415	152,327	0	1,960,742
Due to affiliates	0	1,093,074	(1,093,074)	0
Advances from third parties	466,983	0	0	466,983
Current portion of long-term debt	165,867	0	0	165,867
Other current liabilities	423,211	17,007	0	440,218
TOTAL CURRENT LIABILITIES	3,832,774	1,267,561	(1,093,074)	4,007,261
Long-term debt, less current portion	3,400,857	0	0	3,400,857
Pension obligation	10,149,757	0	0	10,149,757
Other long-term liabilities	1,282,291	162,740	0	1,445,031
TOTAL LIABILITIES	18,665,679	1,430,301	(1,093,074)	19,002,906
NET ASSETS				
Unrestricted	43,220,968	(938,880)	0	42,282,088
Temporarily restricted	454,247	0	0	454,247
Permanently restricted	36,111	0	0	36,111
TOTAL NET ASSETS	43,711,326	(938,880)	0	42,772,446
TOTAL LIABILITIES AND NET ASSETS	$ 62,377,005	$ 491,421	$ (1,093,074)	$ 61,775,352

See the accompanying report of independent auditors on other financial information.

Garrett County Memorial Hospital
Consolidating Statement of Operations Information
For the Year Ended June 30, 2014

	Garrett County Memorial Hospital	Professional Emergency Physician Services, LLC	Elimination Entries	Consolidated
REVENUE				
Net patient service revenue				
Patient service revenue (net of contractual allowances and discounts)	$ 40,746,006	$ 1,996,772	$ 0	$ 42,742,778
Less: provision for uncollectible accounts	(1,157,703)	(418,140)	0	(1,575,843)
	39,588,303	1,578,632	0	41,166,935
Other revenue	2,356,039	332	(173,333)	2,183,038
Net assets released from restriction for use in operations	35,203	0	0	35,203
TOTAL REVENUE	41,979,545	1,578,964	(173,333)	43,385,176
EXPENSES				
Salaries and wages	15,661,251	1,282,057	0	16,943,308
Employee benefits	6,231,302	201,763	0	6,433,065
Supplies	6,670,835	4,165	0	6,675,000
Utilities	698,714	5,936	0	704,650
Purchased services	5,148,267	293,835	0	5,442,102
Depreciation and amortization	2,687,542	0	0	2,687,542
Interest	150,180	0	0	150,180
Management fees	0	173,333	(173,333)	0
Other expenses	946,314	41,803	0	988,117
TOTAL EXPENSES	38,194,405	2,002,892	(173,333)	40,023,964
GAIN (LOSS) FROM OPERATIONS	3,785,140	(423,928)	0	3,361,212
OTHER INCOME				
Investment income	750,003	268	0	750,271
Equity in earnings of affiliates	29,563	0	0	29,563
Other	97,897	0	0	97,897
TOTAL OTHER INCOME	877,463	268	0	877,731
EXCESS REVENUE OVER EXPENSES (EXPENSES OVER REVENUE)	$ 4,662,603	$ (423,660)	$ 0	$ 4,238,943

See the accompanying report of independent auditors on other financial information.

DIXON HUGHES GOODMAN LLP
Certified Public Accountants and Advisors

Independent Auditors Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed In Accordance with *Government Auditing Standards*

The Board of Governors
Garrett County Memorial Hospital
Oakland, Maryland

We have audited the consolidated financial statements, which comprise the consolidated balance sheet, the related consolidated statements of operations and other changes in unrestricted net assets, changes in net assets and cash flows for the year then ended, and the related notes to the consolidated financial statements, of Garrett County Memorial Hospital and subsidiary (collectively, the Company) as of and for the year ended June 30, 2014, and have issued our report thereon dated October 23, 2014. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Company's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Company's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statement will not be prevented or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. Given these limitations, we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined previously. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Company's consolidated financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purposes of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Company's internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Company's internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

This report is intended solely for the information and use of management, the Board of Governors, management, others within the Company, and the United States Department of Agriculture, and is not intended to be and should not be used by anyone other than these specified parties.

Dixon Hughes Goodman LLP

October 23, 2014
Tysons, Virginia