



SILVER HILL HOSPITAL, INC.

Financial Statements

February 28, 2011

(With Independent Auditors' Report Thereon)

SILVER HILL HOSPITAL, INC.

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KPMG LLP
345 Park Avenue
New York, NY 10154-0102

Independent Auditors' Report

The Board of Directors
Silver Hill Hospital, Inc.:

We have audited the accompanying statement of financial position of Silver Hill Hospital, Inc. (the Hospital) as of February 28, 2011, and the related statements of operations, changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 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 Hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Silver Hill Hospital, Inc. as of February 28, 2011, and the results of its operations, changes in its net assets, and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

KPMG LLP

August 17, 2011

SILVER HILL HOSPITAL, INC.

Statement of Financial Position

February 28, 2011

Assets

Current assets:

Cash and cash equivalents	\$ 2,553,698
Investments (note 3)	9,708,200
Patient accounts receivable, net of allowance for doubtful accounts of \$733,775 (note 5)	2,347,022
Prepaid expenses	489,261
Pledges receivable	107,421
Other current assets	114,400
Assets limited as to use – current liabilities (note 3)	1,157,113
Total current assets	<u>16,477,115</u>
Assets limited as to use (note 3):	
Temporarily and permanently restricted donations	1,197,193
Line of credit – liquid reserve requirement	1,100,000
Total assets limited as to use	<u>2,297,193</u>
Other assets, net	90,178
Property and equipment, net (note 4)	<u>19,117,005</u>
Total assets	<u>\$ 37,981,491</u>

Liabilities and Net Assets

Current liabilities:

Accounts payable and accrued expenses	\$ 1,255,281
Deposits due to patients and third parties	497,162
Accrued salaries, taxes, and other compensation	959,300
Other current liabilities	804,936
Total current liabilities	<u>3,516,679</u>
Line of credit (note 6)	6,327,680
Other liabilities	117,811
Total liabilities	<u>9,962,170</u>
Net assets:	
Unrestricted	26,822,128
Temporarily restricted (note 11)	984,193
Permanently restricted (note 11)	213,000
Total net assets	<u>28,019,321</u>
Commitments and contingencies (notes 7 and 8)	
Total liabilities and net assets	<u>\$ 37,981,491</u>

See accompanying notes to financial statements.

SILVER HILL HOSPITAL, INC.

Statement of Operations

Year ended February 28, 2011

Unrestricted revenues, gains, and other support:	
Net patient service revenue (note 2)	\$ 30,301,949
Contributions	786,665
Other revenue	220,675
Net assets released from restriction for use in operations	234,037
Total unrestricted revenues, gains, and other support	<u>31,543,326</u>
Operating expenses (note 10):	
Salaries and related costs	14,827,345
Employee benefits (note 9)	3,591,508
Supplies and services	8,097,416
Depreciation and amortization	1,207,933
Provision for bad debts	587,384
Development expense	510,919
Interest expense	443,185
Loss on the disposal of property and equipment	37,044
Total operating expenses	<u>29,302,734</u>
Income from operations	<u>2,240,592</u>
Nonoperating gains (losses):	
Investment income	367,917
Realized gains on investments	127,194
Provision for uncollectible pledges	(2,500)
Other gains, net	9,141
Total nonoperating gains (losses), net	<u>501,752</u>
Excess of unrestricted revenues, gains, and other support and nonoperating gains (losses) over expenses	2,742,344
Other changes in unrestricted net assets:	
Change in net unrealized gains on other than trading securities	824,958
Net assets released from restriction for use in capital projects	268,965
Increase in unrestricted net assets	<u>\$ 3,836,267</u>

See accompanying notes to financial statements.

SILVER HILL HOSPITAL, INC.

Statement of Changes in Net Assets

Year ended February 28, 2011

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Net assets at February 28, 2010	\$ 22,985,861	111,408	213,000	23,310,269
Excess of unrestricted revenues, gains, and other support and nonoperating gains (losses) over expenses	2,742,344	—	—	2,742,344
Restricted contributions	—	197,397	—	197,397
Special event revenue – gala for scholarships, net of direct donor benefit of 416,303	—	1,173,642	—	1,173,642
Investment income, net of realized gains (losses)	—	4,748	—	4,748
Change in net unrealized gains on other than trading securities	824,958	—	—	824,958
Net assets released from restriction for use in operations	—	(234,037)	—	(234,037)
Net assets released from restriction for use in capital projects	268,965	(268,965)	—	—
Change in net assets	<u>3,836,267</u>	<u>872,785</u>	<u>—</u>	<u>4,709,052</u>
Net assets at February 28, 2011	<u>\$ 26,822,128</u>	<u>984,193</u>	<u>213,000</u>	<u>28,019,321</u>

See accompanying notes to financial statements.

SILVER HILL HOSPITAL, INC.

Statement of Cash Flows

Year ended February 28, 2011

Cash flows from operating activities:	
Change in net assets	\$ 4,709,052
Adjustments to reconcile the change in net assets to net cash provided by operating activities:	
Depreciation and amortization	1,207,933
Provision for bad debts	587,384
Loss on disposal of assets	37,044
Provision for uncollectible pledges	2,500
Contributions restricted for capital projects	(186,000)
Net unrealized gains on other than trading securities	(824,958)
Realized gains on investments	(127,194)
Changes in assets and liabilities:	
Patient accounts receivable	(143,138)
Prepaid expenses	(18,962)
Pledges receivable	28,652
Other current assets	296,232
Other assets	1,415
Accounts payable and accrued expenses	(42,946)
Deposits due to patients and third parties	(158,178)
Accrued salaries, taxes, and other compensation	79,968
Other current liabilities	96,468
Other liabilities	29,597
Net cash provided by operating activities	<u>5,574,869</u>
Cash flows from investing activities:	
Purchases of property and equipment	(246,026)
Expenditures for Hospital campus renovations	(3,410,004)
Purchases of investments	(2,001,510)
Proceeds from sale of investments	2,478,083
Change in assets limited as to use	(2,854,307)
Net cash used in investing activities	<u>(6,033,764)</u>
Cash flows from financing activities:	
Contributions restricted for capital projects	186,000
Repayment of line of credit	(2,000,000)
Deferred financing costs	(29,523)
Net cash used in financing activities	<u>(1,843,523)</u>
Decrease in cash and cash equivalents	(2,302,418)
Cash and cash equivalents, beginning of year	<u>4,856,116</u>
Cash and cash equivalents, end of year	<u>\$ 2,553,698</u>
Supplemental disclosures of cash flow information:	
Cash paid during the year for interest, including capitalized interest	\$ 548,562
Increase in accounts payable and accrued expense for Hospital campus renovation expenditures	547,252

See accompanying notes to financial statements.

SILVER HILL HOSPITAL, INC.

Notes to Financial Statements

February 28, 2011

(1) Nature of Activities and Significant Accounting Policies

Nature of Activities

Silver Hill Hospital, Inc. (the Hospital) is a not-for-profit private psychiatric hospital, which provides medical attention to patients with psychiatric or substance abuse diagnosis through inpatient and outpatient programs. Silver Hill was incorporated in the State of Connecticut in 1934.

A summary of the Hospital's significant accounting policies is as follows:

(a) *Basis of Accounting*

The Hospital's financial statements have been prepared on the accrual basis of accounting.

(b) *Cash and Cash Equivalents*

The Hospital considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

(c) *Concentration of Credit Risk*

Financial instruments that potentially subject the Hospital to concentrations of credit risk consist principally of temporary cash investments. A portion of temporary cash investments may exceed federally insured levels from time to time.

(d) *Patient Accounts Receivable*

The collection of receivables from third-party payors and patients is the Hospital's primary source of cash for operations and is critical to its operating performance. The primary collection risks relate to uninsured patient accounts and patient accounts for which the primary insurance payor has paid, but patient responsibility amounts (deductibles and copayments) remain outstanding. Patient receivables, where a third-party payor is responsible for paying the amount, are carried at a net amount determined by the original charge for the service provided, less an estimate made for contractual adjustments to third-party payors. Patient receivables due directly from the patients are carried at the original charge for the service provided less amounts covered by third-party payors and less an estimated allowance for uncollectible receivables. Management estimates this allowance based on the aging of its accounts receivable and its historical collection experience for each payor type. Recoveries of receivables previously written off are recorded as a reduction of the provision for uncollectible accounts when received. The past-due status of receivables is determined on a case-by-case basis depending on the responsible payor. Interest is generally not charged on past-due accounts.

(e) *Pledges Receivable*

Pledges, less an allowance for uncollectible amounts (if warranted), are recorded as pledges receivable in the year made.

SILVER HILL HOSPITAL, INC.

Notes to Financial Statements

February 28, 2011

(f) *Assets Limited as to Use*

Assets limited as to use include assets set aside for current liabilities, including the Hospital 401(k) contribution to employees and deposits due to patients and third parties, assets restricted based on donors' intents, and liquid assets restricted by the line-of-credit agreement.

(g) *Investments*

The Hospital accounts for its investments in accordance with current accounting standards for not-for-profit organizations. Under these standards, investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair values in the statement of financial position. Realized and unrealized gains (losses) on investments, interest, and dividends are included in the change in unrestricted net assets in the accompanying statement of changes in net assets, unless donor or law restricted the use of the income or loss. Investments are available for current operations and therefore are classified as current in the accompanying statement of financial position.

Financial Accounting Standards Board (FASB) Accounting standards Codification (ASC) 820, *Fair Value Measurements*, establishes a formal hierarchy and framework for measuring fair value, and expanded disclosure about fair value measurements and the reliability of valuation impacts. The guidance requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1 – Quoted prices in active markets for identical assets or liabilities. All of the Hospital's investments were Level 1 assets;

Level 2 – Observable inputs other than Level 1 prices such as quoted prices for similar instruments; 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; and

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 include those whose value is determined using pricing models, discounted cash flows methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Investment securities, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the value of investment securities will occur in the near term.

SILVER HILL HOSPITAL, INC.

Notes to Financial Statements

February 28, 2011

(h) Property and Equipment

Property and equipment are recorded at cost and depreciated over the estimated useful life of each class of depreciable assets, using the straight-line method. Interest costs incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Estimated useful lives of capital assets are as follows:

	<u>Years</u>
Land improvements	20 years
Buildings	25 years
Vehicles	5 years
Equipment	3 – 7 years

(i) Deferred Financing Costs

Deferred financing costs are amortized to interest expense, on a straight-line basis, over the term of the related debt.

(j) Deposits Due to Patients

Amounts received from patients as a deposit for services to be performed are recorded as an amount owed to the patient. The deposit amount that is received is either returned or recognized as income based on the patient's account status after completion of services.

(k) Net Assets

The net assets of the Hospital and changes therein are classified and reported as follows:

Unrestricted Net Assets – unrestricted net assets are those whose use is not restricted by donors, even though their use may be limited in other respects, such as by contract, board designation, or under debt agreements.

Temporarily and Permanently Restricted Net Assets – temporarily restricted net assets are those whose use by the Hospital has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained in perpetuity.

(l) Excess of Unrestricted Revenues, Gains, other Support and Nonoperating Gains (Losses) over Expenses

The statement of operations includes the excess of unrestricted revenues, gains, other support, and nonoperating gains (losses) over expenses. Changes in unrestricted net assets that are excluded from excess of unrestricted revenues, gains, other support and nonoperating gains (losses) over expenses, consistent with industry practice, include changes in net unrealized gains on other than trading securities and assets released from restriction for capital projects.

SILVER HILL HOSPITAL, INC.

Notes to Financial Statements

February 28, 2011

(m) Net Patient Service Revenue

The Hospital has agreements with third-party payors, which provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

(n) Charity Care

The Hospital provides care to patients who meet certain criteria established under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not pursue collection of accounts determined to qualify as charity care, they are not reported as revenue. The amount of charity care provided to patients under the Hospital's policy during the year ended February 28, 2011 was approximately \$529,400.

(o) Donor-Restricted Gifts

Unconditional promises to give cash and other assets to the Hospital are reported at fair value at the date the promise is received. The Hospital has incorporated a formal development program to solicit charitable contributions, therefore unconditional promises to give are classified as unrestricted revenues, gains and other support in the accompanying statement of operations. Conditional promises to give and indication 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 statement of operations and changes in net assets as net assets released from restrictions. In the absence of donor specifications that income and gains on donated funds are restricted, such donated funds are reported as income and gains within the accompanying statement of operations.

(p) Income Taxes

The Hospital is qualified as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code (the Code), and as such, no provision for income taxes has been recorded. The Internal Revenue Service informed the Hospital by a letter dated June 23, 1997 that the Hospital's operations are designed in accordance with such section of the Code. There are certain transactions that could be deemed "Unrelated Business Income" and would result in a tax liability. Management reviews transactions to estimate potential tax liabilities using a threshold of more likely than not. It is management's estimation that there are no material tax liabilities that need to be recorded.

SILVER HILL HOSPITAL, INC.

Notes to Financial Statements

February 28, 2011

(q) *Use of Estimates*

The preparation of financial statements in accordance 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 disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The use of estimates and assumptions in the preparation of the accompanying financial statements is primarily related to the Hospital's determination of the net patient accounts receivable and settlements with third-party payors. Due to uncertainties inherent in the estimation and assumption process, actual results could differ from those estimates and such differences could be material. For the year ended February 28, 2011, a change in estimate related to the allowance for doubtful accounts increased the Hospital's net income by \$523,000.

(r) *Healthcare Reform Legislation*

The Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010 (collectively, the Health Reform Law), which was signed into law on March 23, 2010, will change how health care services are covered, delivered, and reimbursed through expanded coverage of uninsured individuals, reduced growth in Medicare program spending, and the establishment of programs in which reimbursement is tied to quality and integration. In addition, the Health Reform Law reforms certain aspects of health insurance, expands existing efforts to tie Medicare and Medicaid payments to performance and quality, and contains provisions intended to strengthen fraud and abuse enforcement. Because of the many variables involved with the Health Reform Law, we are unable to predict the net effect on the Hospital of the expected increases in insured individuals using its facilities, the reductions in Medicare spending and funding, and numerous other provisions in the law that may affect the Hospital.

(s) *Recent Accounting Pronouncements*

In August 2010, the FASB issued Accounting Standards Update (ASU) No. 2010-23, *Health Care Entities (Topic 954): Measuring Charity Care for Disclosure*. ASU No. 2010-23 is intended to reduce diversity in practice regarding the measurement basis used in the disclosure of charity care. ASU No. 2010-23 requires cost be used as a measurement basis for charity care disclosure purposes and that cost be identified as the direct or indirect cost of providing charity care, and requires disclosure of the method used to identify or determine such costs. The ASU is effective for the Hospital on March 1, 2011. The Hospital is currently evaluating the impact on its disclosures from the adoption of this pronouncement.

In August 2010, the FASB issued ASU No. 2010-24, *Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries*. ASU No. 2010-24 is intended to address current diversity in practice to the accounting by healthcare entities for medical malpractice claims and similar liabilities and their related anticipated insurance recoveries. Most healthcare entities have netted anticipated insurance recoveries against the related accrued liability, although some entities

SILVER HILL HOSPITAL, INC.

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February 28, 2011

have presented the anticipated insurance recovery and related liability on a gross basis. The existing guidance does not permit offsetting of conditional or unconditional liabilities with anticipated insurance recoveries from third parties. This update clarifies that a healthcare entity should not net insurance recoveries against the related claim liability. Additionally, the amount of the claim liability should be determined without consideration of insurance recoveries. The ASU is effective for the Hospital on March 1, 2011. The Hospital is currently evaluating the impact on its disclosures from the adoption of this pronouncement.

(2) Net Patient Service Revenue

The Hospital has agreements with third-party payors, which provide for reimbursement to the Hospital at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Hospital's billings at list price and the amounts reimbursed by Medicare, Blue Cross, and certain other third-party payors, and any differences between estimated third-party reimbursement settlements for prior years and subsequent final settlements. Contractual adjustments under third-party reimbursement programs are accrued on an estimated basis in the period the related services are rendered and are adjusted in future periods as final settlements are determined. A summary of the basis of reimbursement with major third-party payors is as follows:

(a) *Medicare*

The Hospital is paid for inpatient services rendered to Medicare program beneficiaries under the Inpatient Psychiatric Facility Prospective Payment System, which was implemented in 2005. During the initial three-year phase-in period, Medicare reimbursement to the Hospital was based on a combination of prospective payments and the cost-based TEFRA system, with a final settlement determined after submission of annual reimbursement reports by the Hospital and audits by the Medicare fiscal intermediary. For the year ended February 28, 2011, revenue from the Medicare program accounted for approximately 4% of the Hospital's net patient service revenue.

Laws and regulations governing the Medicare programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change in the near term. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare programs. Third-party payor settlements for 2011 were not significant to the financial statements.

(b) *Managed Care Organizations*

The Hospital has also entered into reimbursement agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment under these agreements includes contractual allowances from established charges and prospectively determined per diem rates.

SILVER HILL HOSPITAL, INC.

Notes to Financial Statements

February 28, 2011

(3) Assets Limited as to Use and Investments

Assets limited as to use and investments consisted of the following as of February 28, 2011:

Assets limited as to use:

Current liabilities:

Cash and cash equivalents	\$ 1,157,113
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Donor restricted assets:

Cash and cash equivalents	959,707
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Certificate of deposit	237,486
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	<u>1,197,193</u>
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Line of credit – liquid reserve requirement:

Cash and cash equivalents	500,000
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Mutual funds	600,000
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	<u>1,100,000</u>
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Total assets limited as to use	3,454,306
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Less current portion	<u>(1,157,113)</u>
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Assets limited as to use, net of current portion	<u>2,297,193</u>
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Investments:

Mutual funds	9,564,050
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Certificate of deposit	94,088
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Corporate bonds	50,062
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	<u>\$ 9,708,200</u>
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Total assets limited as to use and investments	<u>\$ 13,162,506</u>
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The current liabilities balance of \$1,157,113 includes the Hospital 401(k) contribution to employees of \$650,951 and deposits due to patients and third parties of \$497,162.

SILVER HILL HOSPITAL, INC.

Notes to Financial Statements

February 28, 2011

The cost and market values of all investments, including those categorized as assets limited as to use, are summarized as follows as of February 28, 2011:

	Cost	Unrealized gains	Fair value
Investments :			
Mutual funds:			
Fixed income – domestic	\$ 5,585,571	93,324	5,678,895
Domestic	2,745,481	838,349	3,583,830
International	749,690	151,635	901,325
	9,080,742	1,083,308	10,164,050
Corporate bonds	48,881	1,181	50,062
Certificates of deposit	331,486	88	331,574
	\$ 9,461,109	1,084,577	10,545,686

At February 28, 2011, the Hospital has estimated the fair value of its investments based on Level 1 inputs.

(4) Property and Equipment

At February 28, 2011, property and equipment consist of:

Land and land improvements	\$ 1,942,373
Buildings	24,257,130
Vehicles	301,241
Equipment	5,165,235
Construction in progress	2,896,561
	34,562,540
Less accumulated depreciation	(15,445,535)
	\$ 19,117,005

Construction in progress mainly comprises renovation expenditures for Scavetta House and the Martin Center, as of February 28, 2011. The estimated cost to complete these projects is approximately \$3,500,000, as of February 28, 2011.

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Notes to Financial Statements

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(5) Classification of Payor Mix

The Hospital requires advanced payments for services not covered by third-party agreements. The significant concentrations of accounts receivable for services to patients include the following:

As of February 28, 2011:

Medicare	\$	10%
Blue cross		16
Other third-party payors		56
Self-pay		18
	\$	<u>100%</u>

(6) Line of Credit

In 2007, the Hospital entered into a revolving line of credit, with a term of 10 years and a maximum available borrowing of \$10,000,000, which was secured by the land and buildings owned by the Hospital. Interest was charged monthly at a rate of 7.15%. In December 2010, the line-of-credit agreement was modified to include an interest rate of 5.25% and an extension of the term to 10 years. The modified line will revolve for a period of four years, with interest payments due monthly based on the balance outstanding. On December 31, 2014, the line will convert to a permanent commercial mortgage for the remaining six years of the term. Upon conversion, principal and interest payments will be due monthly through December 31, 2020 at which time a balloon payment for any unpaid principal and interest will be due. As of February 28, 2011, \$6,327,680 was outstanding on the line. In 2011, interest incurred on the line was \$530,425, of which \$87,237 was capitalized and included in property and equipment on the statement of financial position. The line-of-credit agreement requires a liquid reserve of \$1,100,000 to be maintained over the term of the loan, which is included in assets limited as to use. As part of the line-of-credit agreement, the Hospital must maintain a compensating balance at the bank of \$500,000.

(7) Lease Obligations

The Hospital has noncancelable operating leases, which expire through April 2015. Future minimum lease payments under these noncancelable operating leases are as follows:

Year ending February 28:		
2012	\$	272,838
2013		270,351
2014		228,079
2015		22,626
2016		658
	\$	<u>794,552</u>

Rental expense for all operating leases totaled approximately \$273,000 in 2011.

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Notes to Financial Statements

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(8) Commitments and Contingencies

Malpractice insurance coverage is provided on a claims-made basis. The claims-made policy, which is subject to renewal on an annual basis, covers only claims made during the term of the policy but not those occurrences for which claims may be made after expiration of the policy. The Hospital intends to renew its coverage on a claims-made basis and has no reason to believe that it may be prevented from renewing such coverage. Additionally, the Hospital believes that there is no significant exposure for claims incurred but not reported. Furthermore, the Hospital is party to routine litigation arising in the ordinary course of business. Although some of the matters are still in a preliminary stage and definite conclusions cannot be made as to those matters, the Hospital is of the opinion that based on information presently available, the lawsuits will not have a materially adverse effect on the financial statements of the Hospital.

The Hospital contracts with Unidine to provide food service to its patients. The contract is cancelable by either party if the other party fails to perform all of its material obligations as outlined in the agreement. The cost is approximately \$23,000 per week.

(9) Retirement Plan

The Hospital has a 401(k) defined contribution plan (401(k) Plan) that covers all full-time employees who have both attained age 21 and completed at least 1,000 hours of service during the first year of employment. The 401(k) plan provides for an employer-based contribution allowing the Hospital to make contributions ranging from 2.5% to 7.5% of each participant's annual compensation, depending on years of vested service. Employees may also make annual contributions up to the amount permitted by law. Expenses related to the 401(k) plan were approximately \$579,000 for the year ended February 28, 2011 and are included with employee benefits within the accompanying statement of operations.

(10) Functional Expenses

The Hospital provides psychiatric and substance abuse healthcare services to residents within its geographic location. Expenses related to providing these services included in the statement of operations are as follows:

Healthcare services	\$	23,391,890
Development		510,919
General and administrative		5,399,925
	\$	<u>29,302,734</u>

SILVER HILL HOSPITAL, INC.

Notes to Financial Statements

February 28, 2011

(11) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available for the following purposes as of February 28, 2011:

Scholarship Fund for Young Adults	\$	959,270
Pain Program		17,060
Employee Assistance Fund		<u>7,863</u>
	\$	<u>984,193</u>

Permanently restricted net assets of \$213,000 at February 28, 2011 consist of donor-restricted funds to be maintained by the Hospital in perpetuity. The income generated from permanently restricted funds is expendable for purposes designated by donors, including adolescent and chemical dependency program services.

(12) Subsequent Events

The Hospital has evaluated subsequent events through the date at which these financial statements were available for distribution on August 17, 2011, and determined there have not been any events that have occurred that would require adjustments to the audited financial statements.

