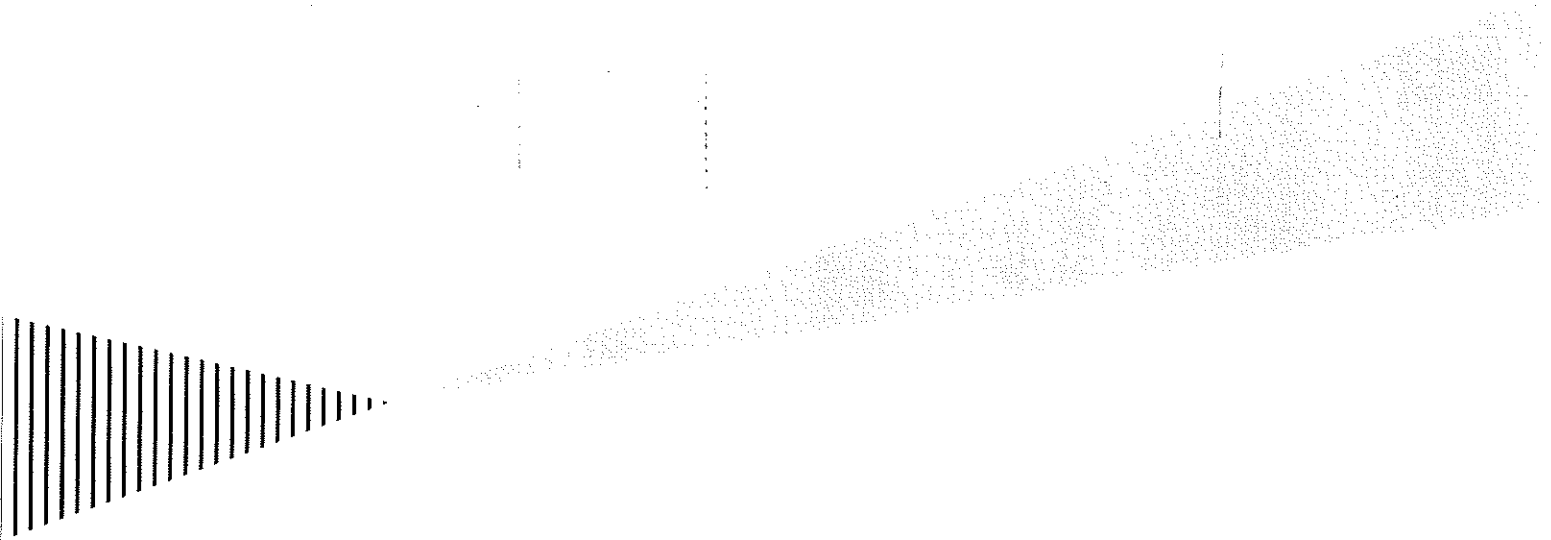


FINANCIAL STATEMENTS

The New Milford Hospital, Incorporated
Years Ended September 30, 2014 and 2013
With Report of Independent Auditors

Ernst & Young LLP



Building a better
working world

The New Milford Hospital, Incorporated

Financial Statements

Years Ended September 30, 2014 and 2013

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Report of Independent Auditors

The Board of Directors
Western Connecticut Health Network, Inc.

We have audited the accompanying financial statements of The New Milford Hospital, Incorporated (the Hospital), which comprise the balance sheets as of September 30, 2014 and 2013, and the related statements of operations and changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements.

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



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The New Milford Hospital, Incorporated at September 30, 2014 and 2013, and the results of its operations and changes in net assets and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

February 27, 2015

The New Milford Hospital, Incorporated

Balance Sheets

	September 30	
	2014	2013
Assets		
Current assets:		
Cash and cash equivalents	\$ 1,731,840	\$ 2,221,385
Accounts receivable, less allowance for uncollectible accounts of approximately \$1,482,000 in 2014 and \$1,893,000 in 2013	6,782,651	7,314,799
Inventories	1,588,724	1,521,171
Prepaid expenses and other	411,351	371,475
Total current assets	<u>10,514,566</u>	<u>11,428,830</u>
Other assets	4,789,007	4,652,903
Interest in Western Connecticut Health Network Foundation, Inc.	10,840,989	11,319,493
Property, plant, and equipment:		
Land and land improvements	1,484,368	1,461,567
Buildings and building improvements	49,609,366	47,784,373
Equipment and other	46,131,727	43,953,291
Construction-in-progress (estimated cost to complete at September 30, 2014: \$6,703,000)	12,765,062	4,537,992
	<u>109,990,523</u>	<u>97,737,223</u>
Less accumulated depreciation	69,346,293	63,868,519
	<u>40,644,230</u>	<u>33,868,704</u>
Total assets	<u>\$ 66,788,792</u>	<u>\$ 61,269,930</u>

	September 30	
	2014	2013
Liabilities and net assets		
Current liabilities:		
Accounts payable	\$ 3,506,647	\$ 2,545,429
Payroll-related accruals	2,394,662	2,391,153
Due to third-party payors	2,776,797	1,973,652
Current portion of due to related parties	4,086,934	6,514,591
Other accrued expenses	283,335	358,515
Total current liabilities	<u>13,048,375</u>	<u>13,783,340</u>
Accrued pension liabilities and other	18,529,628	13,282,674
Due to related parties, less current portion	1,082,488	2,476,284
Total liabilities	<u>32,660,491</u>	<u>29,542,298</u>
Net assets:		
Unrestricted	26,205,321	23,332,942
Temporarily restricted	3,596,815	4,125,215
Permanently restricted	4,326,165	4,269,475
Total net assets	<u>34,128,301</u>	<u>31,727,632</u>
Total liabilities and net assets	<u>\$ 66,788,792</u>	<u>\$ 61,269,930</u>

See accompanying notes.

The New Milford Hospital, Incorporated

Statements of Operations and Changes in Net Assets

	Year Ended September 30	
	2014	2013
Unrestricted revenues:		
Net patient service revenue	\$ 63,850,140	\$ 72,281,954
Provision for uncollectible accounts	2,043,381	2,859,657
Net patient service revenue less provision for uncollectible accounts	61,806,759	69,422,297
Net assets released from restriction	18,850	130,298
Other operating revenue	987,944	744,102
	<u>62,813,553</u>	<u>70,296,697</u>
Expenses:		
Salaries, benefits, and fees	37,998,243	44,019,423
Supplies and other	19,129,407	20,871,060
Insurance	2,092,747	2,065,741
Depreciation and amortization	5,477,484	5,443,180
Interest	128,030	263,572
	<u>64,825,911</u>	<u>72,662,976</u>
Loss from operations	(2,012,358)	(2,366,279)
Nonoperating (loss) income:		
Change in equity interest in unrestricted net assets of the Western Connecticut Health Network Foundation, Inc.	(6,796)	282,759
	<u>(6,796)</u>	<u>282,759</u>
Deficiency of revenues over expenses	(2,019,154)	(2,083,520)

Continued on next page.

The New Milford Hospital, Incorporated

Statements of Operations and Changes in Net Assets (continued)

	Year Ended September 30	
	2014	2013
Unrestricted net assets:		
Deficiency of revenues over expenses (continued)	\$ (2,019,154)	\$ (2,083,520)
Change in equity interest of the Western Connecticut Health Network Foundation, Inc.	-	2,642,044
Net assets released from restrictions for property, plant, and equipment	1,484,197	1,107,256
Change in pension funding obligation	(7,005,612)	11,821,833
Transfer from Western Connecticut Health Network Foundation, Inc.	-	4,010,000
Transfer from (to) Western Connecticut Health Network, Inc.	10,412,948	(6,652,044)
Increase in unrestricted net assets	<u>2,872,379</u>	<u>10,845,569</u>
Temporarily restricted net assets:		
Net assets released from restriction	(18,850)	(130,298)
Net assets released from restrictions for property, plant, and equipment	(1,484,197)	(1,107,256)
Change in equity interest of the Western Connecticut Health Network Foundation, Inc.	(528,400)	4,125,215
Transfer from Western Connecticut Health Network Foundation, Inc.	1,503,047	1,237,554
Transfer to Western Connecticut Health Network, Inc.	-	(3,923,984)
(Decrease) increase in temporarily restricted net assets	<u>(528,400)</u>	<u>201,231</u>
Permanently restricted net assets:		
Change in equity interest of the Western Connecticut Health Network Foundation, Inc.	56,690	4,269,475
Transfer to Western Connecticut Health Network, Inc.	-	(4,134,546)
Increase in permanently restricted net assets	<u>56,690</u>	<u>134,929</u>
Increase in net assets	<u>2,400,669</u>	<u>11,181,729</u>
Net assets at beginning of year	<u>31,727,632</u>	<u>20,545,903</u>
Net assets at end of year	<u>\$ 34,128,301</u>	<u>\$ 31,727,632</u>

See accompanying notes.

The New Milford Hospital, Incorporated

Statements of Cash Flows

	Year Ended September 30	
	2014	2013
Operating activities		
Increase in net assets	\$ 2,400,669	\$ 11,181,729
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	5,477,484	5,443,180
Change in equity interest of the Western Connecticut Health Network Foundation, Inc.	478,504	(11,319,493)
Transfer from Western Connecticut Health Network Foundation, Inc.	(1,503,047)	(5,247,554)
Transfer (from) to Western Connecticut Health Network, Inc.	(10,412,948)	14,710,574
Change in pension funding obligation	7,005,612	(11,821,833)
Provision for uncollectible accounts	2,043,381	2,859,657
Changes in operating assets and liabilities <i>(see Note 8)</i>	(1,820,732)	(4,287,764)
Net cash provided by operating activities	<u>3,668,923</u>	<u>1,518,496</u>
Investing activities		
Additions to property, plant, and equipment, net	(12,253,010)	(6,871,209)
Change in due to related parties	6,591,495	117,651
Net cash used in investing activities	<u>(5,661,515)</u>	<u>(6,753,558)</u>
Financing activities		
Payments of long-term debt and capital lease obligations	—	(1,508,855)
Transfer from Western Connecticut Health Network Foundation, Inc.	1,503,047	5,247,554
Transfer to Western Connecticut Health Network, Inc.	—	(2,563,268)
Net cash provided by financing activities	<u>1,503,047</u>	<u>1,175,431</u>
Net decrease in cash and cash equivalents	<u>(489,545)</u>	<u>(4,059,631)</u>
Cash and cash equivalents at beginning of year	<u>2,221,385</u>	<u>6,281,016</u>
Cash and cash equivalents at end of year	<u>\$ 1,731,840</u>	<u>\$ 2,221,385</u>

See accompanying notes.

The New Milford Hospital, Incorporated

Notes to Financial Statements

September 30, 2014

1. Summary of Significant Accounting Policies

Organization and Basis of Presentation

The New Milford Hospital, Incorporated (the Hospital) is a voluntary, not-for-profit, non-stock corporation incorporated under the General Statutes of the State of Connecticut. The Hospital is a member of Western Connecticut Health Network, Inc. (WCHN). This affiliation allows the Hospital to retain separate licenses and operate autonomously, while promoting collaboration and efficiencies to provide innovative and accessible quality health care for residents of western Connecticut and adjacent eastern New York. As of October 1, 2014, the Hospital has received regulatory approval to operate under the license of Danbury Hospital, also a member of WCHN (refer to Note 11).

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and related footnotes. There is at least a reasonable possibility that certain estimates will change by material amounts in the near term. Actual results could differ from those estimates.

Regulatory Matters

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

Cash and Cash Equivalents

Cash and cash equivalents consist of cash and short-term investments with a maturity of three months or less at date of purchase other than amounts held in the investment portfolio and assets limited as to use. Cash and cash equivalents are maintained with domestic financial institutions with deposits that exceed federally insured limits. It is the Hospital's policy to monitor the financial strength of these institutions.

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Patient Accounts Receivable

Patient accounts receivable result from the health care services provided by the Hospital. Additions to the allowance for uncollectible accounts result from the provision for uncollectible accounts. Accounts written off as uncollectible are deducted from the allowance for uncollectible accounts.

The Hospital's estimation of the allowance for uncollectible accounts is based primarily upon the type and age of the patient accounts receivable and the effectiveness of the Hospital's collection efforts. The Hospital's policy is to reserve a portion of all self-pay receivables, including amounts due from the uninsured and amounts related to co-payments and deductibles, as these charges are recorded. On a monthly basis, the Hospital reviews its accounts receivable balances and various analytics to support the basis for its estimates. These efforts primarily consist of reviewing the following:

- Historical write-off and collection experience using a hindsight or look-back approach
- Revenue and volume trends by payor, particularly the self-pay components
- Changes in the aging and payor mix of accounts receivable, including increased focus on accounts due from the uninsured and accounts that represent co-payments and deductibles due from patients
- Cash collections as a percentage of net patient revenue less the provision for uncollectible accounts; and
- Trending of days revenue in accounts receivable

The Hospital regularly performs hindsight procedures to evaluate historical write-off and collection experience throughout the year to assist in determining the reasonableness of its process for estimating the allowance for uncollectible accounts.

The amount of the allowance for uncollectible accounts is based upon management's assessment of historical and expected net collections, business and economic conditions, trends in Medicare and Medicaid health care coverage, and other collection indicators. See Note 2 for additional information relative to third-party payor programs.

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

The Hospital's primary concentration of credit risk is patient accounts receivable, which consists of amounts owed by various governmental agencies, insurance companies, and private patients. The Hospital manages the receivables by regularly reviewing its patient accounts and contracts, and by providing appropriate allowances for uncollectible amounts. Significant concentrations of gross patient accounts receivable include 41% and 6%, and 37% and 5%, for Medicare and Medicaid, respectively, at September 30, 2014 and 2013, respectively.

Fair Value of Financial Instruments

The carrying value of financial instruments classified as current assets and current liabilities as of September 30, 2014 and 2013, approximate fair value based on current market conditions. The fair values of other financial instruments are disclosed in Note 3.

Inventories

Inventories, used in general operations of the Hospital, are stated at average cost.

Property, Plant, and Equipment

Property, plant, and equipment are recorded at cost. The Hospital provides for depreciation of property, plant, and equipment using the straight-line method in amounts sufficient to depreciate the cost of its assets over their estimated useful lives. The remaining useful lives range from 1 to 40 years.

Nonoperating (Loss) Income

Activities other than those in connection with providing healthcare services are considered to be non-operating. Non-operating (loss) income consists of the change in the equity interest in unrestricted net assets of the Western Connecticut Health Network Foundation, Inc.

Deficiency of Revenues Over Expenses

The accompanying statements of operations and changes in net assets include the deficiency of revenues over expenses as the performance indicator. Changes in unrestricted net assets, which are excluded from the deficiency of revenues over expenses, include contributions of long-lived

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

assets, including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets, change in pension funding obligation, transfers to and from related entities, and change in equity interest of the Western Connecticut Health Network Foundation, Inc.

Transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported within loss from operations.

Professional Liability Insurance

Professional liability insurance coverage is provided under claims-made policies. The coverage limits are \$5,000,000 per claim and \$25,000,000 in the aggregate. The excess indemnity coverage is \$40,000,000 per claim and \$40,000,000 in the aggregate. There are known claims and incidents that may result in the assertion of additional claims, as well as claims from unknown incidents that may be asserted arising from services provided to patients. Management estimates and records a liability for incurred but not reported incidents (IBNR). The Hospital has recorded \$590,669 and \$1,065,668 based on a discount rate of 3.5% as of September 30, 2014 and 2013, respectively. The actuarially determined present value of the IBNR is included within accrued pension liabilities and other on the accompanying balance sheets.

Income Taxes

The Hospital is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (IRC) and is exempt from federal income taxes on related income pursuant to Section 501(a) of the IRC. The Hospital is also exempt from state and local taxes.

As of September 30, 2014 and 2013, the Hospital has net operating loss carryforwards from unrelated business activities of approximately \$2,409,000 and \$1,678,000, respectively. These losses generated a potential deferred tax asset of approximately \$964,000 and \$671,000, which is offset by a corresponding valuation allowance of the same amount due to the uncertainty of utilizing the deferred tax asset in future periods.

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the Hospital has been limited by donors to a specific time frame or purpose. Temporarily restricted net assets consist of the Hospital's interest in Western Connecticut Health Network Foundation, Inc. related to contributions restricted for certain health care services. Permanently restricted net assets consist of the Hospital's interest in Western Connecticut Health Network Foundation, Inc. assets held in trusts by others, which are to be maintained in perpetuity.

Interest in the Western Connecticut Health Network Foundation, Inc.

Interest in the Western Connecticut Health Network Foundation, Inc. represents the Hospital's interest in the net assets of the Western Connecticut Health Network Foundation, Inc. and is accounted for in accordance with Accounting Standards Codification 958-20, *Not-for-Profit Entities – Financially Interrelated Entities*.

New Accounting Pronouncement

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The adoption of ASU 2014-09 is required on October 1, 2017, and management is currently evaluating the effect of this guidance on its financial statements.

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

2. Net Patient Service Revenue and Charity Care

The following table summarizes net revenues from services to patients by the Hospital:

	Year Ended September 30	
	2014	2013
Gross patient service revenue	\$ 172,137,054	\$ 184,161,328
Deductions:		
Allowances	107,352,613	110,830,443
Charity care	934,301	1,048,931
	108,286,914	111,879,374
Net patient service revenue	63,850,140	72,281,954
Provision for uncollectible accounts	2,043,381	2,859,657
Net patient service revenue less provision for uncollectible accounts	\$ 61,806,759	\$ 69,422,297

Patient accounts receivable and revenues are recorded when patient services are performed.

During 2014 and 2013, approximately 33% and 8%, and 34% and 6%, respectively, of net patient service revenue was received under the Medicare and Medicaid programs, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare and Medicaid programs. The Hospital believes it is in compliance with all applicable laws and regulations. Changes in the Medicaid and Medicare programs and the reduction in funding levels could have an adverse impact on the Hospital.

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. The difference is accounted for as allowances. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, fee-for-service, discounted charges, and per diem payments. Net patient service revenue is affected by the State of Connecticut Disproportionate Share program and is reported at the estimated net realizable amounts due from patients, third-party payors, and others for services rendered and includes estimated retroactive revenue adjustments due to ongoing and future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

2. Net Patient Service Revenue and Charity Care (continued)

are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations. During 2014 and 2013, the Hospital recorded increases in net patient service revenue of approximately \$638,000 and \$400,000, respectively, related to changes in previously estimated third-party payor settlements.

The Hospital has established estimates based on information presently available of amounts due to or from Medicare, Medicaid, and other third-party payors for adjustments to current and prior year payment rates, based on industry-wide and Hospital-specific data. Such amounts are included in the accompanying balance sheets.

Patient service revenue, net of contractual allowances and charity care and before the provision for uncollectible accounts, recognized in the period from major payor sources is as follows:

	Year Ended September 30	
	2014	2013
Third-party payors	\$ 62,291,677	\$ 69,571,079
Self-pay patients	1,558,463	2,710,875
	<u>\$ 63,850,140</u>	<u>\$ 72,281,954</u>

It is the policy of the Hospital to provide necessary care to all persons seeking treatment, without discrimination on the grounds of age, race, creed, national origin, or any other grounds unrelated to an individual's need for the service or the availability of the needed service at the Hospital. A patient is classified as a charity care patient by reference to the established policies of the Hospital. Essentially, these policies define charity care services as those services for which no payment is anticipated. In assessing a patient's inability to pay, the Hospital utilizes the generally recognized Federal poverty income guidelines but also includes certain cases where incurred charges are significant when compared to a responsible party's income. Those charges are not included in net patient service revenue for financial reporting purposes.

The estimated cost of charity care provided was approximately \$346,300 and \$410,800 for the years ended September 30, 2014 and 2013, respectively. The estimated cost of charity care is based on the ratio of cost to charges, as determined by hospital-specific data.

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

3. Fair Values of Financial Instruments

For assets and liabilities required to be measured at fair value, the Hospital measures fair value based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are applied based on the unit of account from the Hospital's perspective. The unit of account determines what is being measured by reference to the level at which the asset or liability is aggregated (or disaggregated) for purposes of applying other accounting pronouncements.

The Hospital follows a valuation hierarchy that is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Observable inputs that are based on inputs not quoted in active markets, but corroborated by market data.

Level 3: Unobservable inputs that are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. In determining fair value, the Hospital uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible and considers non-performance risk in its assessment of fair value.

Financial assets carried at fair value in the accompanying balance sheets for the fiscal year ending September 30, 2014 and 2013, consist of cash and cash equivalents of \$1,731,840 and \$2,221,385, which are classified as Level 1 assets.

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

3. Fair Values of Financial Instruments (continued)

Financial assets carried at fair value included in the defined benefit pension plan (see Note 6) are classified in the table below in one of the three categories described above:

	September 30, 2014			Total
	Level 1	Level 2	Level 3	
Mutual funds:				
Domestic equity	\$ 21,672,701	\$ —	\$ —	\$ 21,672,701
International equity	3,149,928	—	—	3,149,928
Fixed income	25,159,289	—	—	25,159,289
Other	3,017,320	—	—	3,017,320
	<u>\$ 52,999,238</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 52,999,238</u>

	September 30, 2013			Total
	Level 1	Level 2	Level 3	
Mutual funds:				
Domestic equity	\$ 23,505,440	\$ —	\$ —	\$ 23,505,440
International equity	3,214,773	—	—	3,214,773
Fixed income	20,824,167	—	—	20,824,167
Other	2,906,636	—	—	2,906,636
	<u>\$ 50,451,016</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 50,451,016</u>

Fair value for Level 1 assets is based upon quoted market prices.

4. Commitments and Contingencies

Litigation

Malpractice claims have been asserted against the Hospital by various claimants. The claims are in various stages of processing and some may ultimately be brought to trial. In addition, the Hospital is a party to various lawsuits incidental to its business. Management believes that the claims and lawsuits will not have a material adverse effect on the Hospital's financial position.

The New Milford Hospital, Incorporated
Notes to Financial Statements (continued)

4. Commitments and Contingencies (continued)

Workers' Compensation Insurance

The Hospital is self-insured for workers' compensation benefits. Liabilities of \$124,615 and \$463,981, using a discount rate of 5.6%, have been accrued as of September 30, 2014 and 2013, respectively, based on expected future payments pertaining to such years.

Operating Leases

The Hospital leases various equipment and facilities under operating leases expiring at various dates through 2017. Total rental expense charged to operations amounted to \$661,641 and \$751,809 in 2014 and 2013, respectively.

Future minimum payments required under non-cancellable operating leases with initial or remaining terms of one year or more consisted of the following as of September 30, 2014:

	<u>Operating Leases</u>
For the year ended September 30:	
2015	\$ 399,624
2016	64,908
2017	5,571
Total minimum lease payments	<u>\$ 470,103</u>

5. Related Party Transactions

The Hospital has recorded amounts due to (from) related parties as follows:

	<u>September 30</u>	
	<u>2014</u>	<u>2013</u>
Danbury Hospital	\$ 4,067,261	\$ 8,136,246
Western Connecticut Health Network, Inc.	795	(91,678)
Western Connecticut Medical Group, P.C.	<u>1,101,366</u>	<u>946,307</u>
	5,169,422	8,990,875
Less: current portion	<u>(4,086,934)</u>	<u>(6,514,591)</u>
	<u>\$ 1,082,488</u>	<u>\$ 2,476,284</u>

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

5. Related Party Transactions (continued)

Effective July 1, 2011, the Hospital entered into an agreement with Danbury Hospital to provide a term loan in the amount of \$6,640,229 for the payoff of the Hospital's term loans, interest rate swap, and promissory notes in June 2011. The term loan with Danbury Hospital bears interest at an annual rate of 4%. Payments of \$122,290 are due monthly beginning August 1, 2011 through July 1, 2016. The balance of the term loan was \$2,476,284 and \$3,815,517 as of September 30, 2014 and 2013, respectively. In addition, the Hospital has recorded a payable due to Danbury Hospital in the amount of \$1,590,977 and \$4,320,729 as of September 30, 2014 and 2013, respectively, for expenses such as insurance, administrative, and other services provided by Danbury Hospital on behalf of the Hospital.

6. Pension Plans

The Hospital has a defined benefit pension plan (the Plan) covering employees who meet certain eligibility requirements. The Plan benefits are based on years of service and the employees' compensation during the last five years of covered employment. Contributions are intended to provide not only for benefits attributed to service to date, but also for those expected to be earned in the future. The Hospital makes contributions in amounts sufficient to meet the Employee Retirement Income Security Act of 1974 minimum funding requirements.

Effective January 31, 2010, the Hospital amended the Plan to close the Plan to new participants and to freeze accruals for all participants, other than those who were fifty-six years old and had at least ten years of service. The Plan was amended effective October 31, 2012, to cease the future accrual of benefits to each highly compensated employee as defined by the Internal Revenue Service.

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

6. Pension Plans (continued)

The following tables set forth the changes in benefit obligations, changes in Plan assets, and components of net periodic benefit cost for the Plan:

	September 30	
	2014	2013
Changes in benefit obligations		
Benefit obligations at beginning of year	\$ 58,717,167	\$ 67,330,037
Service cost	134,869	247,338
Interest cost	3,021,008	2,694,999
Amendment	-	(127,811)
Assumption changes	7,749,946	(8,434,543)
Actuarial loss (gain)	434,024	(561,522)
Benefits paid	(2,621,854)	(2,431,331)
Benefit obligations at end of year	<u>67,435,160</u>	<u>58,717,167</u>
Changes in plan assets		
Fair value of plan assets at beginning of year	50,451,016	46,434,477
Actual return on plan assets	4,150,688	4,464,247
Employer contribution	1,178,868	2,107,867
Expenses	(159,480)	(124,244)
Benefits paid	(2,621,854)	(2,431,331)
Fair value of plan assets at end of year	<u>52,999,238</u>	<u>50,451,016</u>
Underfunded status	<u>\$ (14,435,922)</u>	<u>\$ (8,266,151)</u>
	Year Ended September 30	
	2014	2013
Components of net periodic benefit cost		
Service cost	\$ 134,869	\$ 247,338
Interest cost	3,021,008	2,694,999
Expected return on plan assets	(3,960,704)	(3,689,438)
Amortization of prior service cost	(42,604)	(42,604)
Recognized net loss	1,190,458	2,089,996
Net periodic benefit cost	<u>\$ 343,027</u>	<u>\$ 1,300,291</u>

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

6. Pension Plans (continued)

Assumptions

	<u>2014</u>	<u>2013</u>
Weighted-average assumptions used to determine benefit obligations		
Discount rate	4.56%	5.23%
Rate of increase in compensation	3.00	3.00
Weighted-average assumptions used to determine net periodic benefit cost		
Discount rate	5.23%	4.12%
Rate of increase in compensation	3.00	3.00
Expected long-term return on plan assets	8.00	8.00

The actuarial loss in 2014 primarily relates to changes in the discount rate and mortality table used to measure the benefit obligation, and the actuarial gain in 2013 primarily relates to changes in the discount rate used to measure the benefit obligation.

To develop the expected long-term rate of return on plan assets assumption, the Hospital considered the historical return and the future expectations for returns for each asset class, as well as the target asset allocation of the pension portfolio.

Amounts recorded in unrestricted net assets and not yet amortized as components of net periodic benefit costs total \$24,166,673 and \$17,161,061 as of September 30, 2014 and 2013, respectively, and represent unrecognized actuarial losses. The amortization of these components expected to be recognized in net periodic costs for the year ended September 30, 2015, is \$1,725,187.

The accumulated benefit obligation was \$66,887,612 and \$58,310,526 as of September 30, 2014 and 2013, respectively. The Plan's measurement date is September 30.

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

6. Pension Plans (continued)

Plan Assets

The Plan's investment objectives are to achieve long-term growth in excess of long-term inflation and to provide a rate of return that meets or exceeds the actuarial expected long-term rate of return on plan assets over a long-term time horizon. In order to minimize the risk, the Plan aims to minimize the variability in yearly returns. The Plan also aims to diversify its holdings among sectors, industries, and companies. The assets of the Plan are all held in mutual funds.

As discussed in Note 3, the Hospital follows a three-level hierarchy to categorize assets measured at fair value. In accordance with the hierarchy, as of September 30, 2014 and 2013, 100% of the Plan assets were categorized as Level 1 investments. Securities with readily determinable values are carried at fair value as determined based on independent public sources.

Contributions

Management expects to contribute \$1,655,000 to the Plan during fiscal year 2015.

Estimated Future Benefit Payments

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

2015	\$ 3,033,230
2016	3,264,085
2017	3,411,422
2018	3,698,405
2019	3,908,538
Years 2020 – 2024	21,392,670

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

6. Pension Plans (continued)

Tax Sheltered Annuity

A Tax Shelter Annuity (TSA) plan is available to substantially all employees. New participants may elect to contribute up to 20% of pretax compensation, not to exceed \$17,500 in calendar year 2014 and 2013, respectively, with certain “catch-up” provisions for employees over fifty years of age. The participants are fully vested in their contributions from the date of contribution. Effective January 1, 2003, employees with hire dates after October 1, 1988, are eligible to receive a Hospital TSA matching contribution equal to 1% of their salary, provided the employee deposits at least that same amount to their TSA account. This percentage increased to 2% in calendar year 2004 and to 3% beginning in calendar year 2005. The TSA was frozen to new contributions as of December 31, 2011. The Hospital established a new defined contribution plan for all employees during fiscal year 2012. The expense related to the defined contribution plans was \$1,030,773 and \$1,246,644 for the years ended September 30, 2014 and 2013, respectively.

Supplemental Executive Retirement Plan (SERP)

Effective December 21, 2007, the Hospital adopted a SERP under section 457(b) of the Internal Revenue Code of 1986, as amended. The Hospital adopted a second SERP, effective June 30, 2008, under section 457(f) of the Internal Revenue Code of 1986, as amended. The SERP is pursuant to the Employee Retirement Income Security Act of 1974. The SERP has been established to supplement the retirement benefits of eligible employees designated by the Hospital’s Board of Directors. The accrued liability relating to the SERP amounted to \$101,001 and \$72,459 as of September 30, 2014 and 2013, respectively, and is included within other accrued expenses on the accompanying balance sheets. The expenses incurred related to the SERP amounted to \$3,304 and \$4,030 for the years ended September 30, 2014 and 2013, respectively. Effective October 1, 2009, the SERP was frozen. Provisions have been made to “grandfather” those participants in the plan that are sixty years old and have at least ten years of service.

7. Net Assets

Temporarily restricted net assets of \$3,596,815 and \$4,125,215 as of September 30, 2014 and 2013, respectively, are available to the Hospital for capital expenditures. Permanently restricted net assets total \$4,326,165 and \$4,269,475 as of September 30, 2014 and 2013, respectively, and represent the Hospital’s interest in Western Connecticut Health Network Foundation, Inc. assets held in trust by others to be maintained in perpetuity, the income from which is expendable to support health care services.

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

8. Changes in Components of Working Capital Other Than Cash and Cash Equivalents

	Year Ended September 30	
	2014	2013
(Increase) decrease in operating assets:		
Accounts receivable, net	\$ (1,511,233)	\$ (1,573,136)
Inventories	(67,553)	123,909
Prepaid expenses and other assets	(175,980)	234,989
	<u>(1,754,766)</u>	<u>(1,214,238)</u>
Increase (decrease) in operating liabilities:		
Accounts payable	961,218	(536,162)
Payroll-related accruals	3,509	(811,697)
Due to third-party payors	803,145	(488,062)
Other accrued expenses	(75,180)	(102,437)
Accrued pension liabilities and other	(1,758,658)	(1,135,168)
	<u>(65,966)</u>	<u>(3,073,526)</u>
Change in working capital other than cash and cash equivalents	<u>\$ (1,820,732)</u>	<u>\$ (4,287,764)</u>

9. Functional Expenses

The Hospital provides healthcare services to residents within its geographic location. Expenses related to providing these services are as follows:

	Year Ended September 30	
	2014	2013
Patient care services	\$ 46,250,569	\$ 50,642,213
General and administrative	18,575,342	22,020,763
	<u>\$ 64,825,911</u>	<u>\$ 72,662,976</u>

The New Milford Hospital, Incorporated

Notes to Financial Statements (continued)

10. Other Operating Revenue

Other operating revenue consisted of the following:

	Year Ended September 30	
	2014	2013
Rental income	\$ 86,305	\$ 102,134
Grants	334,803	249,941
Dietary/nutrition	324,222	293,864
Other income	242,614	98,163
	<u>\$ 987,944</u>	<u>\$ 744,102</u>

11. Subsequent Events

Subsequent events have been evaluated through February 27, 2015, which represents the date the financial statements were issued. Except as disclosed below, no events have occurred that require disclosure in or adjustment to the financial statements.

On October 1, 2014, Danbury Hospital received a single provider license to include the Hospital. As a result, the Hospital operations became a department of Danbury Hospital effective October 1, 2014, and all of the Hospital's assets and liabilities were transferred to Danbury Hospital on that date. The Hospital became an inactive entity as of that date.

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