



**ELLIS HOSPITAL**  
(d/b/a Ellis Medicine)

Financial Statements

December 31, 2009 and 2008

(With Independent Auditors' Report Thereon)

**ELLIS HOSPITAL**  
(d/b/a Ellis Medicine)  
Financial Statements  
December 31, 2009 and 2008

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KPMG LLP  
515 Broadway  
Albany, NY 12207

## Independent Auditors' Report

The Board of Trustees  
Ellis Hospital (d/b/a Ellis Medicine):

We have audited the accompanying balance sheet of Ellis Hospital (d/b/a Ellis Medicine) (the Hospital) as of December 31, 2009, and the related statements of operations and 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. The accompanying financial statements of the Hospital as of December 31, 2008, were audited by other auditors whose report thereon dated April 23, 2009, expressed an unqualified opinion on those statements.

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 2009 financial statements referred to above present fairly, in all material respects, the financial position of Ellis Hospital (d/b/a Ellis Medicine) as of December 31, 2009, and the results of its operations and 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*

April 9, 2010

**ELLIS HOSPITAL**  
(d/b/a Ellis Medicine)

Balance Sheets

December 31, 2009 and 2008

<b>Assets</b>	<b>2009</b>	<b>2008</b>
Current assets:		
Cash and cash equivalents	\$ 9,984,890	8,986,813
Patient accounts receivable (net of allowance for doubtful accounts of approximately \$24,620,000 in 2009 and \$19,785,000 in 2008)	43,156,413	46,051,078
Other receivables	874,958	1,241,122
Grants receivable	—	1,448,950
Assets limited as to use	13,068,214	7,870,919
Inventories	3,982,413	3,629,657
Prepaid expenses	1,339,875	1,450,953
Total current assets	72,406,763	70,679,492
Assets limited as to use	28,385,897	23,883,713
Interest in net assets of Ellis Hospital Foundation, Inc.	11,942,969	9,382,639
Property and equipment, net	88,163,843	82,318,982
Deferred financing costs, net	1,481,251	1,620,925
Grants receivable	7,261,504	9,699,150
	\$ 209,642,227	197,584,901

See accompanying notes to financial statements.

<b>Liabilities and Net Assets</b>	<b>2009</b>	<b>2008</b>
	<u>                    </u>	<u>                    </u>
Current liabilities:		
Current portion of long-term debt	\$ 4,228,569	5,740,275
Current portion of capital lease obligations	1,134,959	1,725,738
Accounts payable	22,112,845	26,441,852
Accrued vacation	7,363,142	6,199,660
Accrued salaries, wages and related expenses	5,618,403	5,969,243
Accrued interest payable	179,241	194,195
Other current liabilities	3,920,152	3,484,814
Estimated third-party payor settlements	4,683,000	292,900
	<u>                    </u>	<u>                    </u>
Total current liabilities	49,240,311	50,048,677
	<u>                    </u>	<u>                    </u>
Long-term debt, net of current portion	40,260,135	44,610,281
Capital lease obligations, net of current portion	703,119	1,684,041
Estimated liability for self-insurance claims	8,991,000	7,390,000
Estimated third-party payor settlements	2,000,000	1,500,000
Accrued sick pay	3,954,775	3,196,717
Accrued pension costs	11,581,040	23,464,278
Other liabilities	1,327,301	—
Deferred credit	3,488,191	3,998,658
	<u>                    </u>	<u>                    </u>
Total liabilities	121,545,872	135,892,652
	<u>                    </u>	<u>                    </u>
Net assets:		
Unrestricted	75,635,737	48,933,576
Temporarily restricted	8,541,108	8,939,236
Permanently restricted	3,919,510	3,819,437
	<u>                    </u>	<u>                    </u>
Total net assets	88,096,355	61,692,249
	<u>                    </u>	<u>                    </u>
Commitments and contingencies (notes 7, 10 and 14)		
	<u>                    </u>	<u>                    </u>
Total liabilities and net assets	\$ 209,642,227	197,584,901
	<u>                    </u>	<u>                    </u>

**ELLIS HOSPITAL**  
(d/b/a Ellis Medicine)

Statements of Operations and Changes in Net Assets

Years ended December 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Unrestricted revenue, gains and other support:		
Net patient service revenue	\$ 361,494,108	305,861,124
Other revenue	4,985,691	9,102,529
Net assets released from restrictions used for operations	167,305	111,528
Total revenue, gains and other support	<u>366,647,104</u>	<u>315,075,181</u>
Expenses:		
Salaries and wages	164,784,993	139,347,447
Employee benefits	29,425,058	23,976,271
Supplies and other expenses	106,727,665	90,266,995
Depreciation and amortization	13,338,855	12,454,627
Interest	1,891,757	2,240,268
Insurance	4,606,853	5,896,661
Provision for bad debts	38,097,350	32,224,873
Total expenses	<u>358,872,531</u>	<u>306,407,142</u>
Operating income	7,774,573	8,668,039
Nonoperating income (expense):		
Contributions	—	134,461
Investment loss	(569,233)	(201,265)
Gain on disposal of equipment	—	59,809
Excess of revenues over expenses	<u>\$ 7,205,340</u>	<u>8,661,044</u>

**ELLIS HOSPITAL**  
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Statements of Operations and Changes in Net Assets

Years ended December 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Unrestricted net assets:		
Excess of revenues over expenses	\$ 7,205,340	8,661,044
Change in net unrealized gains and losses on investments	4,467,275	(4,920,605)
Change in interest in net assets of Ellis Hospital Foundation, Inc.	812,806	(3,672,910)
Pension and post-retirement related changes other than net periodic benefit cost	4,418,595	(25,265,692)
Contributed property and equipment	—	4,365,295
Net assets released from restrictions used for purchase of property and equipment	<u>9,798,145</u>	<u>7,300,730</u>
Increase (decrease) in unrestricted net assets	<u>26,702,161</u>	<u>(13,532,138)</u>
Temporarily restricted net assets:		
Contributions, grants and contracts	7,902,385	12,071,424
Change in interest in net assets of Ellis Hospital Foundation, Inc.	1,647,451	537,792
Net assets released from restrictions used for purchase of property and equipment	(9,798,145)	(7,300,730)
Net assets released from restrictions used for operations	(167,305)	(111,528)
Restricted income (loss) from investments	<u>17,486</u>	<u>(4,754)</u>
(Decrease) increase in temporarily restricted net assets	<u>(398,128)</u>	<u>5,192,204</u>
Increase (decrease) in permanently restricted net assets – change in interest in net assets of Ellis Hospital Foundation, Inc.	<u>100,073</u>	<u>(323,844)</u>
Increase (decrease) in net assets	26,404,106	(8,663,778)
Net assets at beginning of year	<u>61,692,249</u>	<u>70,356,027</u>
Net assets at end of year	<u>\$ 88,096,355</u>	<u>61,692,249</u>

See accompanying notes to financial statements.

**ELLIS HOSPITAL**  
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Statements of Cash Flows

Years ended December 31, 2009 and 2008

	<b>2009</b>	<b>2008</b>
Cash flows from operating activities:		
Change in net assets	\$ 26,404,106	(8,663,778)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	13,338,855	12,454,627
Pension and post-retirement related changes other than net periodic benefit cost	(4,418,595)	25,265,692
Contributed property and equipment	—	(4,365,295)
Amortization of deferred financing costs	139,674	139,673
Provision for bad debts	38,097,350	32,224,873
Amortization of deferred credits	(510,467)	(510,467)
Net realized loss on sale of investments	1,530,685	1,322,428
Change in net unrealized gains and losses on investments	(4,467,275)	4,920,605
Gain on disposal of equipment	—	(59,809)
Change in interest in net assets of Ellis Hospital Foundation, Inc.	(2,560,330)	3,458,962
Contributions and interest income restricted for long-term investments and property and equipment	(7,864,715)	(12,005,591)
Changes in operating assets and liabilities:		
Patient accounts receivable	(35,202,685)	(47,547,709)
Other receivables and prepaid expenses	477,242	(20,764)
Inventories	(352,756)	(1,208,183)
Grants receivable	3,886,596	(1,448,950)
Accounts payable, accrued expenses and other liabilities	(582,984)	12,302,712
Estimated third-party payor settlements	4,890,100	(2,207,718)
Estimated liability for self-insurance claims	1,601,000	2,846,667
Accrued pension costs	(7,464,643)	(2,536,101)
Net cash provided by operating activities	26,941,158	14,361,874
Cash flows from investing activities:		
Purchase of property and equipment	(19,713,377)	(9,785,278)
Proceeds from disposition of property and equipment	—	62,620
Purchase of investments	(18,466,917)	(23,139,059)
Proceeds on sale of investments	11,915,612	18,483,191
Net cash used in investing activities	(26,264,682)	(14,378,526)
Cash flows from financing activities:		
Contributions and interest income restricted for long-term investments and property and equipment	7,864,715	2,306,441
Payments on capital lease obligations	(1,681,262)	(1,765,392)
Proceeds from long-term debt	—	9,533,298
Payments on long-term debt	(5,861,852)	(6,104,992)
Net cash provided by financing activities	321,601	3,969,355
Net increase in cash and equivalents	998,077	3,952,703
Cash and cash equivalents at beginning of year	8,986,813	5,034,110
Cash and cash equivalents at end of year	\$ 9,984,890	8,986,813
Supplemental disclosures of cash flow information:		
Cash paid during the year for interest	\$ 2,191,670	2,634,585
Noncash investing and financing activities:		
Lease obligations incurred for capitalized equipment	109,561	69,896
Fixed asset purchases included in accounts payable	4,989,706	5,417,344

See accompanying notes to financial statements.

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Notes to Financial Statements

December 31, 2009 and 2008

**(1) Summary of Significant Accounting Policies**

**(a) Description of Organization**

Ellis Hospital (d/b/a Ellis Medicine) (the Hospital), located in Schenectady, New York, operates a 455 certified bed acute care not-for-profit hospital. Included as part of the Hospital is an 82-bed hospital based nursing facility and four primary care health centers. The Hospital is also financially interrelated to the Ellis Hospital Foundation, Inc., which seeks philanthropic support on behalf of the Hospital and grants funds to the Hospital under the direction of its Board of Trustees.

In November 2006, the New York Commission on Health Care Facilities in the 21<sup>st</sup> Century released its final report, which became law January 1, 2007, including two specific recommendations for changing how hospital services are provided in Schenectady County. One recommendation mandated the closure of Bellevue Woman's Hospital (Bellevue), which occurred and culminated in Bellevue's services and assets being transferred to the Hospital in November 2008. The other pertinent recommendation required St. Clare's Hospital (St. Clare's) and the Hospital to combine under a single governance structure and reduce their combined bed capacity. On June 16, 2008, St. Clare's surrendered its operating certificate and the New York Department of Health transferred responsibility for its services to the Hospital. Also since that date, the Hospital has leased St. Clare's healthcare assets and hospital campus for \$1 per month, until such time the related assets are able to be legally transferred to the Hospital.

The Hospital received \$14,578,100 in Health Care Efficiency and Affordability Law of New York State (HEAL) grants, and \$9,000,000 in interest-free loans from the state and Federal government to offset the negative financial impacts on it of these events.

**(b) Basis of Presentation**

In June 2009, the Financial Accounting Standards Board (FASB) authorized the *FASB Accounting Standards Codification* (ASC or the Codification) to become the single source of authoritative, nongovernmental U.S. generally accepted accounting principles (GAAP). The Codification brings together in one place the authoritative accounting standards that existed in a number of formats including FASB Statements and Interpretations, Emerging Issues Task Force Abstracts, FASB Staff Positions, and American Institute of Certified Public Accountants (AICPA) Statements of Positions and Accounting and Auditing Guides. The Codification is effective for financial statements issued for annual periods ending after September 15, 2009. Since the Codification is the accumulation of existing GAAP, it did not have any impact on the Hospital's financial statements.

The accompanying financial statements, which are presented on the accrual basis of accounting, have been prepared consistent with ASC 954, which addresses the accounting for healthcare entities. In accordance with the provisions of the ASC 954, net assets and revenue, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, unrestricted net assets are amounts not subject to donor-imposed stipulations and are available for operations. Temporarily restricted net assets are those whose use 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.

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The Hospital considers events or transactions that occur after the balance sheet date, but before the financial statements are issued, to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure. These financial statements were issued on April 9, 2010 and subsequent events have been evaluated through that date.

**(c) Use of Estimates**

The preparation of the accompanying financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions about future events. These estimates and underlying assumptions affect the reported amounts of assets and liabilities and disclosure of contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the allowance for doubtful accounts, contractual allowances, estimated third-party payor settlements, self-insurance liabilities, asset retirement obligations and the assumptions used to determine the pension and postretirement liabilities. These estimates and assumptions are based on management's best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. Management adjusts such estimates and assumptions when facts and circumstances dictate. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in those estimates resulting from continuing changes in the economic environment will be reflected in the financial statements in future periods.

**(d) Collective Bargaining Agreement**

At December 31, 2009 and 2008, the Hospital has approximately 23% of its employees working under a collective bargaining agreement. This agreement with the New York State Nurses Association (NYSNA) is set to expire on February 28, 2010. Terms for a new contract between the Hospital and NYSNA are still being negotiated.

**(e) Restricted Cash and Cash Equivalents**

For purposes of the statements of cash flows, the Hospital considers all highly liquid debt instruments with original maturities of three months or less to be cash and cash equivalents, excluding assets limited as to use. Cash includes restricted funds of approximately \$245,000 and \$251,000 at December 31, 2009 and 2008, respectively.

**(f) Inventories**

Inventories are stated at the lower of cost or market, determined on an average cost method.

**(g) Assets Limited as to Use**

Assets limited as to use include amounts held by bank trustees under indenture agreements and self-insurance trust arrangements, funds held in escrow, contributions from donors restricted for specific purposes (including unexpended income), endowment funds from donor-restricted resources

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(including unexpended income), the principal of which may not be expended by the governing board and assets set aside by the Board of Trustees over which the Board retains control and may, at its discretion, subsequently use for other purposes. Investment income from assets held by trustees related to the self-insurance programs is included within operating income, all other investment income is included in nonoperating income in the statements of operations and changes in net assets.

Investments are measured at fair value based on quoted market prices in the accompanying balance sheets. Investment income or loss (including realized gains or 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. Losses on other than temporarily impaired assets are included in the excess of revenues over expenses.

**(h) *Investment Risks***

Investment securities are exposed to various risks, such as interest rate, market and credit. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in values in the near term could materially affect the amounts reported in the accompanying balance sheets, statements of operations and changes in net assets.

The Hospital continually reviews investments for impairment conditions that indicate that an other than temporary decline in market value has occurred. In conducting this review, numerous factors are considered which, individually or in combination, indicate that a decline is other than temporary and that a reduction of the carrying value is required. These factors include specific information pertaining to an individual company or particular industry and general market conditions that reflect prospects for the economy as a whole. During 2009, the Hospital did not recognize any other than temporary losses as there were no significant unrealized losses. During 2008, the Hospital recognized \$362,801 in other than temporary losses.

**(i) *Property and Equipment***

Property and equipment are stated at cost, if purchased or at fair value at date of receipt, if acquired by gift, less accumulated depreciation. Depreciation is computed by use of the straight-line method over the estimated useful lives of the assets ranging from 3 to 40 years. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life. Such amortization is included in depreciation and amortization expense in the financial statements.

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.

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In 2008, the Hospital received approximately \$4,365,000 of property and equipment from the transfer of services of the former 40-bed Bellevue Women's Hospital. As of December 31, 2009, the Hospital has not yet received title to the property and equipment from the transfer of services of the other acute care hospital that occurred during 2008. The transfer of these assets is anticipated to occur during the second quarter of 2010.

**(j) *Deferred Financing Costs***

Deferred financing costs represent costs, relating to the 1995 and 2004 mortgage notes and the lease financing, which are amortized utilizing the straight-line method to expense over the life of the debt. Deferred financing costs are net of accumulated amortization of \$2,059,537 and \$1,919,858 as of December 31, 2009 and 2008, respectively. Amortization expense amounted to approximately \$140,000 in 2009 and 2008. Amortization expense for each of the four years ended through 2013 will be approximately \$140,000.

**(k) *Deferred Credit***

As a result of the 1995 Dormitory Authority of the State of New York (DASNY) mortgage refinancing, present value savings were escrowed for future capital expenditures. During 1997, DASNY made available these funds to the Hospital to be used in facility renovations in lieu of further lowering the mortgage interest rate. The Hospital has no obligation to repay these funds provided the mortgage balance is paid and operations continue at the Hospital. The Hospital has recorded the funds received as a deferred credit. This balance is being amortized, using the straight-line method, over the remaining life of the mortgage. The annual amortization is recorded as a reduction of mortgage interest expense.

**(l) *Accrued Sick Pay***

The Hospital has accrued a liability for employees' vested sick pay. Employees are vested when they become pension-eligible and have five years of service, accruing up to a maximum of 960 hours. At that time, they are entitled to receive compensation for their accumulated sick time when they retire at certain percentages depending on their age. Since it cannot be determined when employees will use their accumulated sick time or retire, the aforementioned accrual is classified as a noncurrent liability in the accompanying balance sheets.

**(m) *Excess of Revenues over Expenses***

The statements of operations and changes in net assets includes excess of revenues over expenses. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice, include change in net unrealized gains and losses on investments other than trading securities, change in unrestricted interest in net assets of Foundation, contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets), and pension and post-retirement related changes other than net periodic benefit cost.

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**(n) Net Patient Service Revenue**

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 and prospective adjustments under reimbursement agreements with third-party payors. Third-party payors retain the right to review and propose adjustments to amounts reported by the Hospital. Such 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.

**(o) Charity Care and Provision for Bad Debts**

The Hospital provides care to patients who meet certain criteria under its charity care policy without charges or at amounts less than its estimated rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The Hospital maintains records to identify and monitor the level of charity care they provide. Those records include the amount of charges for services and supplies furnished to patients at no charge.

The Hospital grants credit without collateral to patients, most of whom are local residents and are insured under third-party payor agreements. Additions to the allowance for doubtful accounts are made by means of the provision for bad debts. Accounts written off as uncollectible are deducted from the allowance. The amount of the provision for bad debts is based upon management's assessment of historical expected net collections, business and economic conditions, trends in Federal and state governmental health care coverage, and other collection indicators. Services rendered to individuals when payment is expected and ultimately not received are written off to the allowance for doubtful accounts.

**(p) 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. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. 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 to unrestricted net assets and reported in the statements of operations and changes in net assets as net assets released from restrictions.

**(q) Income Taxes**

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

**(r) Concentration of Credit Risk**

The Hospital maintains cash balances in depositories above FDIC insurance limitations amounting to approximately \$6,037,000 at December 31, 2009.

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(s) ***Reclassifications***

Certain amounts in the 2008 financial statements have been reclassified to conform to the 2009 presentation.

(t) ***Recently Adopted Accounting Pronouncements***

In May 2009, the FASB issued FASB ASC 855, *Subsequent Events*, which defines the circumstances under which the events or transactions subsequent to year-end should be recognized and disclosures regarding subsequent events or transactions. The subsequent event reporting requirements are effective for annual periods beginning after June 15, 2009. See the additional subsequent event disclosures included under *Basis of Presentation* above.

**(2) Net Patient Service Revenue**

Net patient service revenue and accounts receivable are reported at the estimated net realizable amounts from third-party payors, patients, 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 or adjustments become known or as years are no longer subject to audits, reviews, and investigations. See below for information relative to third-party reimbursement agreements.

Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

Under the New York Health Care Reform Act (NYHCRA), hospitals are authorized to negotiate reimbursement rates for inpatient acute care services with certain non-Medicare payors except for Medicaid, Workers' Compensation and No-Fault. These negotiated rates may take the form of rates per discharge, reimbursed costs, discounted charges or as per diem payments. Reimbursement rates for Medicaid, Workers' Compensation and No-Fault are determined on a prospective basis as determined by the New York State Prospective Hospital Reimbursement Methodology (NYPHRM), which was subsequently adopted under the provisions of NYHCRA. These rates also vary according to a patient classification system defined by NYPHRM that is based on clinical, diagnostic and other factors.

For all payors except Medicare, outpatient services are paid under various reimbursement methods including cost reimbursement, fee schedules and charges. Outpatient services rendered to Medicare beneficiaries are paid under a prospective payment system (PPS). Under the Medicare outpatient PPS, services provided to a beneficiary on the same day are grouped into ambulatory payment classifications (APCs) and paid at predetermined amounts.

Payments to the Hospital under both Medicaid and Medicare – Part A for nursing facility patients are made utilizing a PPS reimbursement methodology. With the exception of Medicaid capital, the reimbursement is made at a predetermined rate depending on intensity of services rendered to patients regardless of the cost of delivering those services.

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The Hospital is eligible to receive funds from several pools established under NYHCRA. Amounts received or to be received from the pools have been included as increases to net patient service revenue. Differences between amounts recorded and final distributions from the pools will be included as adjustments to net patient service revenue in the year that such distributions are finalized.

Revenue from Medicare and Medicaid accounted for 47% of net patient service revenue for the year ended December 31, 2009 and 45% for the year ended December 31, 2008. As such, the Hospital is dependent on these payors to carry out its operating activities. Cost reports supporting third-party patient service revenue have been audited and finalized through December 31, 2006 by the designated intermediaries.

The laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Compliance with laws and regulations can be subject to future government review and interpretation as well as significant regulatory action; failure to comply with such laws and regulations can result in fines, penalties and exclusion from the Medicare and Medicaid programs. The Hospital believes it is in compliance with applicable laws and regulations and retroactive adjustments, if any, would not be material to the financial position or results of operations of the Hospital. The Hospital has classified a portion of the accrual for estimated third-party payor settlements as long term liabilities because such amounts, by their nature or by virtue of regulations or legislation will not be paid within one year.

In 2009 and 2008, the Hospital's revenue was impacted by approximately \$(487,000) and \$197,000, respectively, due to funds received and the removal of allowances previously estimated that are no longer necessary related to prior periods as a result of the tentative and final settlements and years that are no longer subject to audits, reviews and investigations.

At December 31, 2009 and 2008, significant concentrations of patient accounts receivable include 26% and 29% due from government related programs, 48% and 42% due from Blue Cross/Blue Shield and other commercial insurers, and 26% and 29% from self-pay patients, respectively.

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**(3) Charity Care**

In pursuing its mission the Hospital provides services to the financially disadvantaged, to other individuals, and to the broader community, despite the lack of adequacy of reimbursement for those services. This expresses the Hospital's continued commitment and willingness to assist those individuals who cannot afford to pay for necessary services rendered. The Hospital maintains records to identify and monitor the level of community benefits provided in accordance with its formal policies. The value of services to financially disadvantaged persons which qualified as charity care amounted to approximately \$3,047,000 and \$1,073,000 for the years ended December 31, 2009 and 2008, respectively.

**(4) Assets Limited as to Use**

Assets limited as to use at December 31 include the following:

	<b>2009</b>		<b>2008</b>	
	<u>Cost</u>	<u>Market</u>	<u>Cost</u>	<u>Market</u>
Cash and cash equivalents	\$ 5,387,018	5,387,018	\$ 3,319,515	3,319,515
Mutual funds	2,783,406	2,871,080	1,583,926	1,067,283
Equity securities	13,637,598	14,895,865	13,552,453	10,717,844
Corporate debt securities	4,057,892	4,158,662	2,359,513	2,343,617
U.S. treasury obligations	13,537,339	14,141,486	13,365,283	14,306,373
	<u>\$ 39,403,253</u>	<u>41,454,111</u>	<u>\$ 34,180,690</u>	<u>31,754,632</u>
Current portion		<u>(13,068,214)</u>		<u>(7,870,919)</u>
Long-term portion		<u>\$ 28,385,897</u>		<u>\$ 23,883,713</u>

Unrestricted investment income and gains and losses from assets limited as to use are comprised of the following at December 31:

	<u>2009</u>	<u>2008</u>
Investment income (loss) in other operating revenue:		
Interest and dividends	\$ 258,806	216,566
Realized losses on sales of investments, net	(320,574)	(195,789)
	<u>\$ (61,768)</u>	<u>20,777</u>
Investment income (loss) in nonoperating income (expense):		
Interest and dividends	\$ 640,878	925,374
Realized losses on sales of investments, net	(1,210,111)	(1,126,639)
	<u>\$ (569,233)</u>	<u>(201,265)</u>

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The following is a summary of assets limited as to use at December 31:

	<u>2009</u>	<u>2008</u>
Mortgage reserve fund	\$ 8,766,360	9,853,312
Funds held in escrow	230,861	222,188
Funds held in trust for self-insurance	12,910,745	8,371,785
Funds held for board-designation	11,851,353	6,662,731
Donor restricted principal and accumulated earnings	7,694,792	6,644,616
Total assets limited as to use	<u>\$ 41,454,111</u>	<u>31,754,632</u>

The Hospital considers funds held for board-designations and other funds that are anticipated to be used in the following year as current.

The Mortgage Reserve Fund Agreement for the 1995 debt requires the fund hold two years' worth of debt service payments. Based on this requirement, the Mortgage Reserve Fund for this debt was required to be \$8,033,649 as of December 31, 2009 and 2008. The Hospital met the funding requirements for 2009 and 2008.

The requirement for the 2004 debt for the ICU project was to start funding the Mortgage Reserve Fund in 2006, with the requirement that the balance be \$768,912 as of May 31, 2010. The balance of this Mortgage Reserve Fund was \$673,771 and \$474,332 at December 31, 2009 and 2008, respectively.

At December 31, 2009 and 2008, the Hospital's investment portfolio has equity and debt securities in an aggregate unrealized loss position of \$(835,721) and \$(3,575,671) and an aggregate fair value of \$11,396,697 and \$12,130,081, respectively. The following table presents the gross unrealized losses and fair value of the Hospital's investments with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2009:

	<u>Gross unrealized loss</u>	<u>Fair value</u>
Debt securities:		
Loss position continuous for less than 12 months	\$ (41,974)	4,727,081
Loss position continuous for 12 months or greater	(26,649)	505,443
Total	<u>\$ (68,623)</u>	<u>5,232,524</u>
Equity securities:		
Loss position continuous for less than 12 months	\$ (130,343)	2,285,510
Loss position continuous for 12 months or greater	(636,755)	3,878,663
Total	<u>\$ (767,098)</u>	<u>6,164,173</u>

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The following table presents the gross unrealized losses and fair value of the Hospital's investments with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2008:

	<b>Gross unrealized loss</b>	<b>Fair value</b>
Debt securities:		
Loss position continuous for less than 12 months	\$ (67,255)	2,129,136
Loss position continuous for 12 months or greater	(13,324)	211,019
Total	\$ (80,579)	2,340,155
Equity securities:		
Loss position continuous for less than 12 months	\$ (3,284,194)	9,369,119
Loss position continuous for 12 months or greater	(210,898)	420,807
Total	\$ (3,495,092)	9,789,926

Management reviewed the investments with unrealized losses, summarized in the preceding tables, and determined that the investments were not other than temporarily impaired. Management reached this conclusion in consultation with its investment advisors and portfolio managers, who relied on industry analyst reports, credit ratings, current market conditions, and other information they deemed relevant to their assessment.

**(5) Grants Receivable**

As a result of the Berger Commission mandates, the Hospital received HEAL grants to help in the transition to combine services from three campuses. The first HEAL award was for a total of \$5,878,100 to assist with capital expenditures amounting to \$1,444,150 and operating needs amounting to \$4,433,950 associated with the assumption of women's health services. The second HEAL grant was awarded to assist in the transfer of services from the former St. Clare's Hospital. This amount totaled \$8,700,000 of which \$8,200,000 was for capital and \$500,000 was for operating needs. The Hospital also received a third HEAL grant for \$5,000,000 for capital expenditures related to the establishment of a medical home. In 2009, the Hospital released approximately \$6,946,000 for capital acquisition related to these grants. This amount is included in net assets released from restrictions used for purchase of property and equipment on the statements of operations and changes in net assets.

As of December 31, 2009 and 2008, the Hospital has recorded grant receivables for approximately \$7,262,000 and \$11,148,000 for operating expenses and capital expenditures, respectively.

**(6) Interest in Net Assets of Foundation**

In accordance with ASC 958, *Not-for-Profit Entities*, the Hospital records its interest in the net assets of Ellis Hospital Foundation, Inc. (Foundation). ASC 958-20 requires a beneficiary (Hospital) of financially

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interrelated organizations to recognize their interest in the net assets of the recipient organization (Foundation) and adjust that interest for its share of the change in net assets of the recipient organization.

The Foundation was incorporated for the purpose of receiving gifts and bequests from the general public for the benefit of the Hospital. A summary of the Foundation's assets, liabilities, net assets and changes in net assets are as follows:

	<u>2009</u>	<u>2008</u>
Cash and investments	\$ 11,011,491	8,879,756
Pledges and other receivables	<u>1,369,680</u>	<u>1,154,898</u>
Total assets	<u>\$ 12,381,171</u>	<u>10,034,654</u>
Total liabilities	<u>\$ 438,202</u>	<u>652,015</u>
Net assets:		
Unrestricted	\$ 5,203,193	4,390,387
Temporarily restricted	3,512,940	1,865,489
Permanently restricted	<u>3,226,836</u>	<u>3,126,763</u>
Total net assets	<u>\$ 11,942,969</u>	<u>9,382,639</u>
Change in unrestricted net assets	\$ 812,806	(3,672,910)
Change in temporarily restricted net assets	1,647,451	537,792
Change in permanently restricted net assets	<u>100,073</u>	<u>(323,844)</u>
Total change in interest in net assets of Foundation	<u>\$ 2,560,330</u>	<u>(3,458,962)</u>

The Foundation distributed approximately \$1,788,000 and \$2,182,000 in 2009 and 2008, respectively, to the Hospital for the purchase of certain Hospital equipment and operating expenses.

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**(7) Property and Equipment**

Property and equipment at December 31 is as follows:

	<u>2009</u>	<u>2008</u>
Land	\$ 590,661	590,661
Land improvements	3,737,499	3,705,408
Buildings	87,916,227	85,467,551
Fixed equipment	60,710,232	58,561,899
Moveable equipment	103,598,809	98,249,241
Leasehold improvements	1,177,542	1,177,542
Construction in progress	15,012,138	5,904,157
	<u>272,743,108</u>	<u>253,656,459</u>
Less accumulated depreciation and amortization	<u>184,579,265</u>	<u>171,337,477</u>
Net property and equipment	<u>\$ 88,163,843</u>	<u>82,318,982</u>

Costs to complete the construction in progress as of December 31, 2009 and 2008 approximate \$9,143,000 and \$3,646,000, respectively.

Included in property and equipment are the following amounts applicable to the capital leases:

	<u>2009</u>	<u>2008</u>
Moveable equipment	\$ 5,791,379	9,673,124
Less accumulated amortization	<u>3,536,065</u>	<u>4,379,749</u>
	<u>\$ 2,255,314</u>	<u>5,293,375</u>

Depreciation expense was \$11,895,254 and \$10,926,704 for the years ended December 31, 2009 and 2008, respectively. Amortization of assets under capital lease was \$1,443,601 and \$1,527,923 for the years ended December 31, 2009 and 2008, respectively.

**(8) Credit Facilities**

The Hospital has a \$4,000,000 working capital line of credit available for use. The line of credit expires on June 30, 2010 and is renewable annually. Advances under the line are subject to interest at the LIBOR rate plus 0.50% (0.73% and 0.94% at December 31, 2009 and 2008, respectively). There were no amounts outstanding at December 31, 2009 and 2008. Included in assets limited as to use are amounts which have been designated by the Board as collateral for outstanding borrowings under the line of credit agreement. In addition, the line of credit is used as collateral for two Stand By Letters of Credit for \$219,365 and \$370,000; these letters of credit were required by the debt issued in November 2004.

The Hospital has \$180,000 of outstanding letters of credit at December 31, 2009 and 2008, relating to the Hospital's worker's compensation and disability programs.

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**(9) Long-Term Debt**

Long-term debt is comprised of the following at December 31:

	<b>2009</b>	<b>2008</b>
Mortgage payable (a)	\$ 22,129,660	24,624,061
ICU financing loan (b)	13,894,758	14,278,395
Restructuring loan (c)	8,464,286	11,448,100
Total	44,488,704	50,350,556
Less current portion	4,228,569	5,740,275
	\$ 40,260,135	44,610,281

- (a) In November 1995, the Hospital entered into a loan agreement for approximately \$58.0 million with the Dormitory Authority of the State of New York (DASNY) in order to refinance approximately \$58.0 million of debt. This agreement resulted in the issuance of the Dormitory Authority of the State of New York Ellis Hospital FHA – Insured Mortgage Hospital Revenue Bonds, Series 1995 by DASNY. Debt service payments on the loan commenced on December 1, 1995 and are payable monthly through October 1, 2016. Interest on the loan is 6.48%. The debt service payments on the loan are insured by the U.S. Department of Housing and Urban Development (HUD). The loan agreement has financial covenants, which the Hospital was in compliance with at December 31, 2009.
- (b) In November 2004, the Hospital entered into a loan agreement for approximately \$15.6 million with the Dormitory Authority of the State of New York (DASNY) in order to finance the construction of a new Intensive Care Unit. This agreement resulted in the issuance of the Dormitory Authority of the State of New York Ellis Hospital FHS – Insured Mortgage Hospital Revenue Bonds, Series 2004 by DASNY. As of December 31, 2009, \$15,269,181 had been drawn down from bond proceeds. It is expected that the remaining \$282,729 will be drawn down during 2010. During construction, the interest rate was 7%, and no principal was paid. Debt service payments commenced on June 1, 2006 and are payable monthly through May 1, 2031. Interest on the loan is 5.06%. The debt service payments on the loan are insured by the U.S. Department of Housing and Urban Development (HUD). The loan agreement has various financial covenants, which the Hospital was in compliance with at December 31, 2009.
- (c) In November 2007, the Hospital entered into an interest free loan agreement to borrow \$11,878,100 from the Health Facility Restructuring Program. In December 2008, the loan agreement was amended where by an additional \$3,000,000 interest free loan was provided by DASNY. The terms of the restructuring loan are \$9,000,000 to be repaid in 84 monthly installments of \$107,142, which commenced on September 1, 2009. Including lump-sum and installment payments, \$3,430,000 was repaid by the Hospital in 2008 and \$2,983,814 in 2009.

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Principal maturities of long-term debt for the five years subsequent to December 31, 2009 are as follows:

2010	\$	4,228,569
2011		4,533,505
2012		4,744,200
2013		4,968,645
2014		5,207,739
Thereafter		<u>20,806,046</u>
	\$	<u><u>44,488,704</u></u>

**(10) Capital and Operating Lease Obligations**

The Hospital leases certain equipment under capital leases and medical and nonmedical equipment and office space under cancelable and noncancelable operating leases that expire over the next several years.

Future minimum lease payments, by year and in the aggregate, under the capital leases and cancelable and noncancelable operating leases as of December 31, 2009 are:

	<u>Capital leases</u>	<u>Operating leases</u>
Year ending December 31:		
2010	\$ 1,236,054	5,791,964
2011	675,374	4,127,974
2012	41,087	1,920,491
2013	13,945	1,019,176
2014	1,496	1,004,609
Thereafter	<u>—</u>	<u>4,056,468</u>
	1,967,956	\$ <u><u>17,920,682</u></u>
Less imputed interest (interest rates ranging from 4.8% to 7.8%)	<u>(129,878)</u>	
Present value of net minimum capital lease payments	1,838,078	
Less current obligations under capital leases	<u>1,134,959</u>	
Long-term obligations under capital leases	<u><u>\$ 703,119</u></u>	

Total rent expense was approximately \$6,800,000 and \$5,515,000 in 2009 and 2008, respectively.

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**(11) Pension and Other Postretirement Benefit Plans**

The Hospital has a noncontributory defined benefit pension plan (Plan) covering substantially all of its full-time employees prior to May 15, 2006. The plan provides pension benefits that are based on years of service, age and the employee's compensation. The Hospital's funding policy is to contribute annually an amount within the range established by the Employment Retirement Income Security Act (ERISA) of 1974. Contributions for the defined benefit plan are intended to provide for benefits attributed to service to date. Based upon the actuarial computation for funding of the Plan, the Hospital is expected to make a contribution amounting to \$3,600,000 to the Plan in 2010.

In 2006, the Hospital redesigned pension benefits, by freezing the defined benefit plan and establishing a defined contribution plan. The defined benefit plan was frozen on May 15, 2006. As such, no new members may be added to the Plan and no additional benefits will accrue to current plan participants. Retirees currently receiving benefits and terminated vested employees will not see any change to their benefit.

The defined contribution plan became effective on June 1, 2006. The Plan is designed to provide a basic 2% of pay contribution to all participants based on gross wages. There is an additional matching component which will provide a 50% match on the first 4% of employees' contributions (50% on the first 6% for longer service employees). The investment vehicle for this plan is a 403(b). There is a two-year waiting period for eligibility in which an employee must work 1,000 hours in each year. At the end of the accrual of 1,000 hours in the second year, an employee becomes a participant and is immediately 100% vested in any contributions. The Hospital's contributions to the Plan were approximately \$5,040,000 and \$4,237,000 in 2009 and 2008, respectively.

Effective January 1, 2006, the Hospital also redesigned their post-retirement health benefits. Under the amended plan, the Hospital contributes a frozen flat dollar benefit to retirees 65 years of age and older. This benefit will not increase in future years. The Hospital's policy is to fund the costs of this plan on a pay-as-you go basis and, as such, there are no plan assets at the balance sheet date. The Hospital expects to contribute approximately \$49,000 to the post-retirement plan in 2010.

**(a) Pension**

Included in unrestricted net assets at December 31, 2009, are the following amounts that have not yet been recognized in net periodic pension cost: unrecognized prior service cost of \$29,598 and unrecognized actuarial losses of \$21,748,567. The prior service cost and actuarial loss included in unrestricted net assets and expected to be recognized in net periodic pension cost during the year ending December 31, 2010, are \$3,188 and \$565,971, respectively.

**(b) Post-Retirement**

Included in unrestricted net assets at December 31, 2009, are the following amounts that have not yet been recognized in net periodic post-retirement cost: unrecognized prior service credit of \$4,288,722, unrecognized actuarial losses of \$5,609,608. The unrecognized prior service credit included in unrestricted net assets and expected to be recognized in net periodic post-retirement cost during the year ending December 31, 2010, are \$884,411. The unrecognized actuarial losses of \$619,198 will

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be recognized as a component of net periodic post-retirement cost during the year ending December 31, 2010.

A summary of the pension and post-retirement plans' funded status and amounts recognized in the Hospital's balance sheets for the years ended December 31 is as follows:

	<b>Pension benefits</b>		<b>Post-retirement benefits</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Change in benefit obligation:				
Benefit obligation at beginning of period	\$ 79,278,008	76,672,229	327,452	353,859
Service cost	500,000	250,000	—	—
Interest cost	4,839,729	4,784,156	18,532	20,407
Actuarial loss	3,401,522	1,698,159	29,023	8,599
Benefits paid	(4,413,904)	(3,612,874)	(54,450)	(55,413)
Administrative expenses	(687,748)	(513,662)	—	—
Benefit obligation at end of period	<u>82,917,607</u>	<u>79,278,008</u>	<u>320,557</u>	<u>327,452</u>
Change in plan assets:				
Fair value of plan assets at beginning of period	55,813,730	75,805,741	—	—
Actual return on plan assets	13,924,488	(17,482,140)	—	—
Administrative expenses	(687,748)	(513,662)	—	—
Employer contributions	6,700,001	1,616,665	54,450	55,413
Benefits paid	(4,413,904)	(3,612,874)	(54,450)	(55,413)
Fair value of plan assets at end of period	<u>71,336,567</u>	<u>55,813,730</u>	<u>—</u>	<u>—</u>
Accrued benefit costs	<u>\$ (11,581,040)</u>	<u>(23,464,278)</u>	<u>(320,557)</u>	<u>(327,452)</u>

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A summary of the components of net periodic income and post-retirement benefit income for the years ended December 31 is presented below:

	<b>Pension benefits</b>		<b>Post-retirement benefits</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Component of net periodic benefit cost:				
Service cost	\$ 500,000	250,000	—	—
Interest cost	4,839,729	4,784,156	18,532	20,407
Expected return on assets	(5,954,558)	(5,956,780)	—	—
Net actuarial loss amortization	75,773	—	684,688	761,209
Prior service cost amortization	3,188	3,188	(884,411)	(884,411)
Net periodic benefit income	<u>\$ (535,868)</u>	<u>(919,436)</u>	<u>(181,191)</u>	<u>(102,795)</u>

	<b>2009</b>	<b>2008</b>
Additional information for pension plans with accumulated benefit obligations in excess of plan assets:		
Projected benefit obligation	\$ (82,917,607)	(79,278,008)
Accumulated benefit obligation	(82,917,607)	(79,278,008)
Fair value of plan assets	71,336,567	55,813,730

(c) **Actuarial Assumptions**

The actuarial assumptions used in developing the benefit obligations and net periodic pension costs are as follows:

Weighted-average assumptions used to determine benefit obligations for years ended:

	<b>Pension benefits</b>		<b>Post-retirement benefits</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Discount rate	5.875%	6.25%	5.25%	6.12%

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Weighted-average assumptions used to determine net periodic benefit costs for years ended:

	<b>Pension benefits</b>		<b>Post-retirement benefits</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Discount rate	6.25%	6.375%	6.12%	6.23%
Rate of compensation increase	N/A	N/A	N/A	N/A
Expected return on assets	8.0%	8.25%	N/A	N/A
Mortality table	2008 PPA	2008 PPA	RP2000	RP2000

The assumption for long-term expected return is based on an analysis of expected returns, based on the plan's asset allocation as of January 1, 2009. This forecast reflects the expected long-term rates of return for each significant asset class or economic indicator. The range of returns developed relies both on forecasts and on broad-market historical benchmarks for expected return, correlation and volatility for each asset class.

Due to the plan amendment effective January 1, 2006, healthcare trend rates are not used in this valuation and therefore changes will not have an impact on service cost, interest cost or the post-retirement benefit obligation.

The Hospital did not apply, nor does it intend to apply, for the Medicare Part D prescription drug federal subsidy, therefore the above disclosure does not reflect any adjustment for future subsidy payments.

**(d) Plan Assets**

Investment objectives for pension plan assets have been established by the Hospital's management in recognition of the fact that any invested fund is subject to three major risks: capital risk, reinvestment rate risk and inflation risk. The primary objective for the investment portfolio is long-term growth when stock-market valuation levels are favorable versus the risk-free alternative of current five year treasury and yields. The secondary objective is preservation of capital when the stock market valuation levels are no longer competitive against yields of five year treasury bonds. The third objective is exceeding the rate of inflation over the long term.

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The Hospital's pension plan weighted average asset allocations at December 31 by asset categories are as follows:

	<b>2010 Target Ranges</b>	<b>2009</b>	<b>2008</b>
Equity securities	50 - 75%	64%	66%
Fixed income securities	20 - 48	30	30
Cash and cash equivalents	2 - 5	6	4
		100%	100%

*(e) Contributions*

The Hospital's funding policy is to contribute amounts to the Plan sufficient to meet the minimum funding requirements set forth in the Employee Retirement Income Security Act of 1974, plus such additional amounts as the Hospital may determine to be appropriate from time to time. 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.

*(f) Estimated Future Benefit Payments*

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

	<b>Pension benefits</b>	<b>Post- retirement benefits</b>
2010	\$ 3,853,560	48,681
2011	4,026,355	44,805
2012	4,291,588	41,031
2013	4,526,598	37,385
2014	4,757,467	33,891
Years 2015 – 2019	27,464,659	123,577

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**(12) Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets are available for the following purposes:

	<u>2009</u>	<u>2008</u>
Health care services	\$ 6,648	6,648
Purchase of equipment	4,252,113	6,185,544
School of Nursing scholarships, awards and education	444,647	545,528
Health education and research	247,273	258,540
Home health care	77,487	77,487
Net assets held by Foundation	<u>3,512,940</u>	<u>1,865,489</u>
	<u>\$ 8,541,108</u>	<u>8,939,236</u>

Permanently restricted net assets are restricted to:

	<u>2009</u>	<u>2008</u>
Investments to be held in perpetuity, the income from which is expendable to support health care services (reported as other operating income)	\$ 692,674	692,674
Net assets held by Foundation (including \$1,165,883 for beneficial interest in perpetual trusts in 2009)	<u>3,226,836</u>	<u>3,126,763</u>
	<u>\$ 3,919,510</u>	<u>3,819,437</u>

**(a) Interpretation of Relevant Law**

Under New York State law, the historic dollar value of an endowment fund must be preserved. The historic dollar value is defined as the aggregate fair value in dollars at the time it becomes an endowment fund, each subsequent donation to the fund at the time it is made; and each accumulation made pursuant to a direction in applicable gift instrument at the time an accumulation is added to the fund.

To constitute an endowment under New York State law, the restriction must arise from a clearly expressed donor limitation, not a limitation from within the beneficiary organization. However, the Board of Trustees may, (absent an explicit donor restriction to the contrary) appropriate for expenditure as much as the Board deems prudent of the net appreciation realized (with respect to all assets) and unrealized (with respect only to readily marketable assets) from investments of an endowment fund over its historical dollar value. The amounts in excess of the historical dollar value of the endowment fund are classified as temporarily restricted net assets, if restricted under the agreement, until those amounts are appropriated for expenditure by the Hospital in a manner consistent with a standard of prudence. The Hospital considers such factors as the duration and preservation of the fund, the purposes of the Hospital and the donor-restricted endowment fund and the investment policies of the Hospital when, making a determination to appropriate or accumulate donor-restricted endowment funds.

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**(b) Funds with Deficiencies**

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level the donor requires the Hospital to retain as a fund of perpetual duration. Losses on the investment of a donor-restricted endowment fund shall reduce temporarily restricted net assets to the extent that donor-imposed restrictions on net appreciation of the funds have not been met before the loss occurs. Any remaining loss shall reduce unrestricted net assets. There were no such deficiencies as of December 31, 2009 or 2008.

**(c) Return Objectives, Strategies, Spending Policy and Investment Objectives**

The Hospital has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of the S&P 500 and the Barclay Intermediate Aggregate Index. To satisfy its long-term rate of return objectives, the Hospital 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 Hospital targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

The Hospital has a policy that allows it to spend the current yield (interest and dividends) of permanently restricted endowments to purchase capital assets or to support health care services based on the donor's request and that preserves the endowments purchasing power through maintaining all capital appreciation (realized and unrealized) within the endowment funds.

**(13) Fair Value of Financial Instruments**

The Hospital estimates fair value based on a valuation framework that uses a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of fair value hierarchy defined in FASB ASC 820 are described below:

- (a) Level 1** – Quoted prices in active markets that are accessible at the measurement date for identical assets and liabilities.
- (b) Level 2** – Inputs, other than quoted prices in active markets, that are observable either directly or indirectly and fair value is determined through the use of models or other valuation methodologies.
- (c) Level 3** – Unobservable inputs that are supported by little or no market activity and require significant management judgment or estimation in the determination of fair value.

The following discussion describes the valuation methodologies used for financial assets and liabilities measured at fair value.

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Fair value for equity securities, mutual funds, and certain U.S. government and agency obligations and corporate bonds are based on quoted market prices or dealer quotes, where available. When quoted market prices are not available, fair values are based on quoted market prices of comparable instruments. For certain U.S. government and agency obligations and corporate bonds held by the Hospital and by the pension plan, the Hospital utilizes matrix pricing from a third party pricing vendor to determine fair value pricing. Matrix prices are based on quoted prices for securities with similar coupons, ratings, and maturities, rather than on specific bids and offers for the designated security.

The following table presents the Hospital's investments that are measured at fair value at December 31, 2009 on a recurring basis. Investments are classified in their entirety based on the lowest level of input that is significant to the fair value measurements.

	<b>Fair value measurements at December 31, 2009</b>			
	<b>Total</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>
<b>Assets:</b>				
Cash and cash equivalents	\$ 15,371,908	15,371,908	—	—
Mutual funds	2,871,080	2,871,080	—	—
Equity securities	14,895,865	14,895,865	—	—
Corporate debt securities	4,158,662	1,707,041	2,451,621	—
U.S. Treasury obligations	14,141,486	12,226,791	1,914,695	—
Total	<u>\$ 51,439,001</u>	<u>47,072,685</u>	<u>4,366,316</u>	<u>—</u>
<b>Pension related assets:</b>				
Cash and cash equivalents	\$ 4,657,258	4,657,258	—	—
Mutual funds	6,638,105	6,638,105	—	—
Equity securities	38,923,551	38,923,551	—	—
Corporate debt securities	8,361,152	—	8,361,152	—
U.S. Treasury obligations	12,756,501	—	12,756,501	—
Total	<u>\$ 71,336,567</u>	<u>50,218,914</u>	<u>21,117,653</u>	<u>—</u>

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The following table presents the Hospital's investments that are measured at fair value at December 31, 2008 on a recurring basis. Investments are classified in their entirety based on the lowest level of input that is significant to the fair value measurements.

<b>Fair value measurements at December 31, 2008</b>				
	<b>Total</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>
<b>Assets:</b>				
Cash and cash equivalents	\$ 12,306,328	12,306,328	—	—
Mutual funds	1,067,283	1,067,283	—	—
Equity securities	10,717,844	10,717,844	—	—
Corporate debt securities	2,343,617	937,414	1,406,203	—
U.S. Treasury obligations	14,306,373	12,875,066	1,431,307	—
Total	\$ 40,741,445	37,903,935	2,837,510	—

At December 31, 2009 and 2008, the recorded value approximates the fair value for financial assets and liabilities which are not measured at fair value on a recurring basis, except for long-term debt. The fair value of long-term debt was determined by a current quotation obtained from the original bond underwriter in consideration of similar issues at current borrowing rates. The recorded value of revenue bonds outstanding on the balance sheet at December 31, 2009 was approximately \$36,024,000 and the estimated fair value was approximately \$45,116,000. The recorded value of revenue bonds outstanding on the balance sheet at December 31, 2008 was approximately \$38,902,000 and the estimated fair value was approximately \$45,962,000.

**(14) Contingencies**

**(a) *Malpractice and Comprehensive General Liability***

The Hospital is defending several malpractice claims which allege negligent treatment of patients in prior years under which the amounts of damages sought are not presently determinable. The final outcome of these claims is also not presently determinable. However such claims have been included in the estimated liability for self-insurance claims as determined by the Hospital's actuary. The Hospital's management believes that none of these claims will expose the Hospital above the insurance limits or self-insurance reserves applicable at the dates of the alleged incidents.

The Hospital is self-insured for the deductible portion of its malpractice and comprehensive general liability coverage. The Hospital has entered into an irrevocable trust for its deductible portion of malpractice and comprehensive general liability losses occurring during 1986 through 2009 and between April 1, 1983 and December 31, 1984. Under the terms of the trust agreement, the trustee makes payments from the funds for the aforementioned losses to the extent of the excess policy coverages as follows: \$3,000,000 per occurrence and \$6,000,000 in the aggregate per annum for 2009 and 2008; \$2,000,000 per occurrence and \$4,000,000 in the aggregate per annum for 2002 through 2007; \$1,000,000 per occurrence and \$3,000,000 in the aggregate per annum for 1996 through 2001; \$3,000,000 per occurrence and \$6,000,000 in the aggregate per annum for 1987 through 1995; \$2,000,000 per occurrence and \$4,000,000 in the aggregate per annum for 1986;

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\$50,000 per occurrence and \$150,000 in the aggregate per annum for 1984; and \$300,000 in the aggregate per annum for 1983.

Liabilities for the self-insurance portion of claims have been estimated by the Hospital's actuary in accordance with accepted actuarial principles. The estimated liabilities for self-insurance claims of approximately \$9,977,000 and \$8,376,000 have been recorded as of December 31, 2009 and 2008, respectively. Those amounts estimated to be paid during the following year are included in other current liabilities in the accompanying financial statements, the remainder is recorded as a noncurrent liability. Assets limited as to use in an amount equal to the self-insurance claims anticipated to be paid during the next fiscal year are classified as current assets in the accompanying financial statements to match the corresponding current liabilities.

**(b) Medical Claims**

The Hospital is self-insured for employee healthcare claims. An accrual for claims liability including those incurred but not reported, amounted to approximately \$1,597,000 and \$1,443,000 as of December 31, 2009 and 2008, respectively, and is included in other current liabilities in the accompanying balance sheets.

**(c) Workers' Compensation**

The Hospital participates in a risk pool with an area health system for their worker's compensation insurance and retains an amount of risk under this program. The Hospital has accrued approximately \$216,000 and \$614,000 of estimated unfunded losses under this program for the years ended December 31, 2009 and 2008, respectively. For the years ended December 31, 2009 and 2008, these claims have been recorded at their estimated present value using a discount rate of 3.85% and 2.5%, respectively.

**(15) Functional Expenses**

The Hospital provides general healthcare services to residents within its geographic location. Expenses related to providing these services at December 31 are as follows:

	<u>2009</u>	<u>2008</u>
Healthcare services	\$ 320,858,951	274,603,367
General and administrative	37,506,253	31,803,775
	<u>\$ 358,365,204</u>	<u>306,407,142</u>