# ELKHART GENERAL HOSPITAL, INC.

## FINANCIAL STATEMENTS
December 31, 2010 and 2009

ELKHART GENERAL HOSPITAL, INC.
Elkhart, Indiana

FINANCIAL STATEMENTS
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CONTENTS

Crowe Horwath.

Crowe Horwath LLP
Independent Member Crowe Horwath International

REPORT OF INDEPENDENT AUDITORS

Board of Directors
Elkhart General Hospital, Inc.
Elkhart, Indiana

We have audited the accompanying balance sheets of Elkhart General Hospital, Inc., (the Hospital) as of December 31, 2010 and 2009, and the related statements of operations and changes in net assets and cash flows for the years 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 audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Elkhart General Hospital, Inc. as of December 31, 2010 and 2009, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Crowe Horwath LLP

Crowe Horwath LLP

South Bend, Indiana
May 17, 2011

ELKHART GENERAL HOSPITAL, INC.
BALANCE SHEETS
December 31, 2010 and 2009

| | 2010 | 2009 |
|---|---|---|
| **ASSETS** | | |
| Current assets | | |
| Cash and cash equivalents | $ 8,897,071 | $ 14,845,519 |
| Short-term investments | 21,877,462 | 18,331,202 |
| Patient accounts receivable, less allowance for doubtful accounts of $7,443,000 in 2010 and $8,048,000 in 2009 | 53,017,982 | 43,339,222 |
| Inventories | 5,502,740 | 6,285,036 |
| Estimated receivables from third-party payors | 1,117,554 | - |
| Prepaid expenses and other current assets | 8,632,198 | 7,654,159 |
| Total current assets | 99,045,007 | 90,455,138 |
| Assets limited as to use | 161,091,466 | 140,623,789 |
| Long-term investments | 9,339,578 | 2,820,175 |
| Property and equipment, net | 139,234,692 | 149,017,749 |
| Investments in and advances to affiliates | 2,124,650 | 1,104,089 |
| Deferred bond issuance costs and other assets | 1,266,830 | 1,332,078 |
| | $ 412,102,223 | $ 385,353,018 |
| **LIABILITIES AND NET ASSETS** | | |
| Current liabilities | | |
| Accounts payable and accrued expenses | $ 12,685,643 | $ 11,697,806 |
| Employee compensation and related liabilities | 11,985,388 | 10,568,455 |
| Estimated payables to third-party payors | 1,092,579 | 1,845,452 |
| Current maturities of long-term debt | 2,085,000 | 2,000,000 |
| Accrued interest | 878,077 | 897,936 |
| Total current liabilities | 28,726,687 | 27,009,649 |
| Noncurrent liabilities | | |
| Accrued pension liability | 24,000,972 | 26,523,424 |
| Long-term debt | 84,470,000 | 86,555,000 |
| Other long-term benefit obligations | 5,716,511 | 5,424,414 |
| Total liabilities | 142,914,170 | 145,512,487 |
| Net assets | | |
| Unrestricted | 264,170,632 | 235,320,421 |
| Temporarily restricted | 4,617,421 | 4,120,110 |
| Permanently restricted | 400,000 | 400,000 |
| Total net assets | 269,188,053 | 239,840,531 |
| | $ 412,102,223 | $ 385,353,018 |

See accompanying notes to financial statements.

ELKHART GENERAL HOSPITAL, INC.
STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS
Years ended December 31, 2010 and 2009

| | 2010 | 2009 |
|---|---|---|
| **Unrestricted revenues, gains and other support** | | |
| Net patient service revenue | $ 251,458,257 | $ 257,359,870 |
| Other operating revenue | 11,081,490 | 10,316,483 |
| | 262,539,747 | 267,676,353 |
| **Expenses** | | |
| Salaries and wages | 82,147,651 | 84,554,031 |
| Employee benefits | 37,263,333 | 43,165,915 |
| Purchased services-medical laboratory | 10,726,509 | 11,109,487 |
| Supplies | 38,449,585 | 40,960,859 |
| Provision for doubtful accounts | 16,300,686 | 15,229,589 |
| Depreciation and amortization | 17,769,246 | 18,852,735 |
| Other expense | 53,071,519 | 50,353,460 |
| | 255,728,529 | 264,226,076 |
| **Operating revenue in excess of expenses** | 6,811,218 | 3,450,277 |
| Nonoperating | | |
| Nonoperating income/ expense, net | 3,290,273 | 2,250,196 |
| Other | 333,728 | (272,670) |
| | 3,624,001 | 1,977,526 |
| **Revenue in excess (deficit) of expenses** | 10,435,219 | 5,427,803 |
| Other changes in unrestricted net assets | | |
| Change in unrealized investment gains/losses, net | 15,042,754 | 26,700,870 |
| Pension adjustment | 3,372,238 | 12,781,076 |
| | 18,414,992 | 39,481,946 |
| **Change in unrestricted net assets** | 28,850,211 | 44,909,749 |
| **Temporarily restricted net assets** | | |
| Investment income, net of trustees | 78,028 | 83,208 |
| Realized investment gains/losses | 241,386 | (379,474) |
| Change in unrealized investment gains/ losses, net | 247,897 | 1,212,219 |
| Investment income released from restriction | (70,000) | - |
| Change in temporarily restricted net assets | 497,311 | 915,953 |
| **Change in net assets** | 29,347,522 | 45,825,702 |
| Net assets at beginning of year | 239,840,531 | 194,014,829 |
| **Net assets at end of year** | $ 269,188,053 | $ 239,840,531 |

See accompanying notes to financial statements.

ELKHART GENERAL HOSPITAL, INC.
STATEMENTS OF CASH FLOWS
Years ended December 31, 2010 and 2009

| | 2010 | 2009 |
|---|---|---|
| **Cash flows from operating activities** | | |
| Change in net assets | $ 29,347,522 | $ 45,825,702 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities | | |
| Depreciation and amortization | 17,769,246 | 18,852,735 |
| Provision for doubtful accounts | 16,300,686 | 15,229,589 |
| Undistributed equity in earnings of investments in affiliates | (758,372) | (1,014,595) |
| Net realized and change in unrealized investment gains/losses, net | (15,484,297) | (28,005,470) |
| Proceeds (losses) from restricted contributions and gains (losses) on investments, net of investment income released from restrictions | (497,311) | (915,953) |
| Pension adjustment and adoption of provisions of FAS 158 | (3,372,238) | (12,781,076) |
| Loss on sale of property and equipment | (376,207) | 70,746 |
| Changes in operating assets and liabilities: | | |
| Patient accounts receivable | (25,979,446) | (8,637,995) |
| Prepaid expenses | (978,039) | 47,317 |
| Other assets | 782,296 | (206,476) |
| Accounts payable, accrued expenses, accrued pension and other | 5,099,213 | (2,875,201) |
| Estimated payables/receivables to/from third-party payors | (1,870,427) | 369,435 |
| Net cash provided by operating activities | 19,982,626 | 25,958,758 |
| **Cash flows from investing activities** | | |
| Purchases of investments | (79,813,595) | (22,333,566) |
| Sales of investments | 64,764,552 | 8,905,072 |
| Purchase of property and equipment | (9,137,761) | (9,208,425) |
| Proceeds from the sale of property and equipment | 20,608 | 16,719 |
| Change in investment in and advances to affiliates | (262,189) | 883,919 |
| Net cash used in investing activities | (24,428,385) | (21,736,281) |
| **Cash flows from financing activities** | | |
| Payments of long-term debt | (2,000,000) | (1,900,000) |
| Proceeds (loss) from restricted contributions and gains (losses) on investments, net of investment income released from restrictions | 497,311 | 915,953 |
| Cash paid for debt issuance costs | - | (132,748) |
| Net cash used in financing activities | (1,502,689) | (1,116,795) |
| Change in cash and cash equivalents | (5,948,448) | 3,105,682 |
| Cash and cash equivalents at beginning of year | 14,845,519 | 11,739,837 |
| **Cash and cash equivalents at end of year** | $ 8,897,071 | $ 14,845,519 |
| **Supplemental disclosures of cash flow information** | | |
| Cash paid during the year for interest | $ 2,282,778 | $ 2,799,399 |
| Property and equipment acquired through accounts payable | 1,572,419 | 1,506,141 |

See accompanying notes to financial statements.

## NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization: Elkhart General Hospital, Inc. (the Hospital), a not-for-profit corporation, is a community hospital located in Elkhart, Indiana, and is exempt from federal income taxes on related income pursuant to Section 501(c)(3) of the Internal Revenue Code.

Mission Statement: The Hospital's mission is to create a healthier community by being a premier provider of healthcare; promoting the health and well being of individuals and families by providing education that may aid in detection and prevention of disease; conducting its activities with compassion and respect; acting with the recognition that health is holistic and embraces the body, mind and spirit; seeking and partnering with those who share its mission, continuously improving the quality and cost-effectiveness of services; and maintaining the financial viability of the Hospital while continuing its charitable role in the community.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Although estimates are considered to be fairly stated at the time the estimates are made, actual results could differ from those estimates.

Fair Value of Financial Instruments: The Hospital's carrying amount for its financial instruments, which include cash and cash equivalents, investments and assets limited as to use, accounts receivable, and long-term debt at December 31, 2010 and 2009 are carried at their estimated fair values. The estimated fair value amounts have been determined by the Hospital using available market information and appropriate valuation methodologies. Considerable judgment is required in interpreting market data and developing these estimates. The fair value of the Hospital's debt based on quoted market prices for same or similar issues was $85,067,406 and $88,421,606 at December 31, 2010 and 2009, respectively.

Income Taxes: U.S. GAAP requires that a tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded.

Due to its tax-exempt status, the Hospital is not subject to U.S. federal income tax or state income tax. The Hospital is however subject to income taxes on income generated from activities that are un-related to its exempt purpose. The Hospital's Form 990 has not been subject to examination by the Internal Revenue Service or the State of Indiana for the last three years. The Hospital does not expect the total amount of unrecognized tax benefits to significantly change in the next 12 months. The Hospital recognizes interest and/or penalties related to income tax matters in income tax expense. The Hospital did not have any amounts recorded for interest and penalties at December 31, 2010 and 2009.

Cash and Cash Equivalents: Cash and cash equivalents include investments in highly liquid debt instruments with original maturities of three months or less when purchased, excluding amounts whose use is limited by board designation or other arrangements under trust agreements.

Patient Accounts Receivable, Estimated Payables to Third-Party Payors, and Net Patient Service Revenue: Patient accounts receivable and net patient service revenue are reported at the estimated net realizable amounts due from patients, third-party payors, and others (principally insurers) for services rendered.

**NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (Continued)

The Hospital evaluates the collectibility of its accounts receivable based on the length of time the receivable is outstanding, payor class, historical experience, an assessment of business and economic conditions, and trends in healthcare coverage. Accounts receivable are charged to the allowance for doubtful accounts when they are deemed uncollectible.

Estimated retroactive adjustments under reimbursement agreements with third-party payors, certain of which are subject to audit by administering agencies, are accrued on an estimated basis and are adjusted in future periods as final settlements are determined.

The Hospital charges interest on past due patient accounts receivable which totaled $5,499 and $18,869 as of December 31, 2010 and 2009, respectively.

Forgivable Loans: The Hospital has loans to employed and associated physicians that provide for forgiveness over a specified period of time. Compensation expense will be recorded in accordance with the agreement upon completion of the specified period. Forgivable loans are recorded in prepaid expenses and other current assets on the balance sheets at December 31, 2010 and 2009 and were $463,393 and $404,885, respectively.

Short-Term and Long-Term Investments: Investments in equity securities with readily determinable fair value and all investments in debt securities are measured at fair value in the balance sheets. Fair value is based on quoted market prices. Investment income is included in revenues in excess of expenses unless the income or loss is restricted by donor or law. The long-term investment represents assets held in trust related to a deferred compensation plan.

Assets Limited as to Use: Assets limited as to use consist of investments set aside by the Board of Directors (the Board) for specific projects or purposes, over which the Board retains control and may, at its discretion, subsequently use for other purposes. Assets limited as to use that are required to meet current liabilities are reported as current assets. Additionally, assets limited as to use include investments held by trustees under debt agreements.

Inventories: Inventories, primarily consisting of pharmaceuticals and other supplies, are stated at cost (first-in, first-out method) and are valued at lower of cost or market value.

Property and Equipment: Property and equipment are recorded on the basis of cost or, if donated, at fair value at the date of donation. Property and equipment are capitalized when the cost is equal to or greater than $2,500, in accordance with the Hospital's policy. Depreciation is provided by using the straight-line method based on expected useful lives, ranging from 3 to 40 years, of the various classes of assets. The amount of depreciation expense for the years ended December 31, 2010 and 2009 was $17,703,998 and $18,787,044, respectively. Routine maintenance, repairs, renewals, and replacement costs are charged to expense as incurred. Expenditures which materially increase values or extend useful lives are capitalized. Costs and related accumulated depreciation of property sold or otherwise retired are removed from the accounts.

Impairment of Long-Lived Assets: On an ongoing basis, the Hospital reviews long-lived assets for impairment whenever events or circumstances indicate that the carrying amounts may be overstated. The Hospital recognizes impairment losses if the undiscounted cash flows expected to be generated by the asset are less than the carrying value of the related asset. The impairment loss adjusts the assets to fair value. As of December 31, 2010 and 2009, the Hospital believes that no impairments existed.

Capitalized Interest: Interest costs capitalized during the construction period of various projects aggregated $116,768 and $127,180 at December 31, 2010 and 2009, respectively.

**NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (Continued)

Investment in Affiliates: The Hospital accounts for its investment in less than majority-owned and controlled affiliates using the equity method of accounting.

Deferred Financing Cost: Financing costs are capitalized and amortized by the effective interest method over the term of the related bonds. The gross costs being amortized are $1,841,461 December 31, 2010 and 2009. The accumulated amortization was $574,631 and $509,383 at December 31, 2010 and 2009, respectively. Amortization expense is estimated at approximately $65,000 per year for 2011 through 2015.

Restricted Net Assets: Permanently restricted net assets have been restricted by donors to be maintained by the Hospital in perpetuity. In accordance with the Hospital's restriction, a majority of the investment income and investment gains or losses from permanently restricted net assets are to be reinvested with the principal and are therefore temporarily restricted. A specified portion of income earned by temporarily restricted net assets is released from restriction and used for operations and, therefore, is included in the statements of operations and changes in net assets as other revenue.

In August 2008, the FASB issued FASB ASC 958-205, Endowments of Not-for-Profit Organizations: Net Asset Classification of classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds, which, among other things, provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Act of 2006 (UPMIFA) and additional disclosures about an organization's endowment funds. In 2007, the State of Indiana adopted UPMIFA. The following disclosures are made as required by FASB ASC 958-205.

The Hospital has one endowment established for patient care purposes. The Hospital has established investment and spending policies related to the preservation and appreciation of this endowment. Should the underlying assets fall below this targeted amount the Hospital pursues actions consistent with established policies to return the endowment to the targeted amount. Based upon these policies, endowment amounts are temporarily restricted until Board authorized release of funds for patient care purposes is approved.

Changes in the endowment funds, consisting principally of the funds included as temporarily restricted net assets of the Hospital, for the fiscal years ended December 31, 2010 and 2009, are detailed within the statements of operations and changes in net assets, respectively. At December 31, 2010 and 2009, other than the endowment described above, no other Board-designated assets limited as to use are being accounted for as Board-designated endowments as they do not meet applicable criteria.

Revenue in Excess of Expenses: The statements of operations and changes in net assets include revenue in excess of expenses. Changes in unrestricted net assets, which are excluded from revenue in excess of expenses, include the change in unrealized gains and losses on investments, pension adjustments, and net assets released from restrictions.

Nonoperating income/expense, net primarily consists of investment income, net of interest expense.

Community Commitment: The Hospital provides services without charge, or at amounts less than its established rates, to patients who meet the criteria of its charity care or uninsured policies. The criteria for charity care takes into consideration Health & Human Services Federal Poverty Guidelines, family assets, family size, employment status, ordinary family expenses, and other related information.

The net cost of charity care provided was approximately $4,402,000 in 2010 and $5,078,000 in 2009. This cost estimate was based upon the Hospital-wide cost to charge ratio.

**NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (Continued)

In 2008, the Hospital implemented a policy to provide discounts to the uninsured. The estimated unpaid costs of providing services under this program was approximately $4,464,000 in 2010 and $4,827,000 in 2009. This cost estimate was based upon the Hospital-wide cost to charge ratio.

Relative to gross charges, the Hospital provided charity care and uninsured discounts at a rate of 3.7% and 4.0% in 2010 and 2009, respectively.

In addition to charity care, the Hospital provided services under the Medicaid and Medicare programs for financially needy, elderly and disabled patients, for which the payments received were less than the cost of providing the services. The unpaid costs attributable to providing services under the Medicaid and Medicare programs were estimated to be:

| | 2010 | 2009 |
|---|---|---|
| Unreimbursed Medicare cost | $ 22,284,342 | $ 29,249,966 |
| Unreimbursed Medicaid cost | 19,372,701 | 18,684,153 |
| | $ 41,657,043 | $ 47,934,119 |

In addition, the Hospital is involved in many community-benefit activities. These activities are wide-ranging and include health education, health screenings, support groups, seminars, and speakers. These activities are conducted free of charge or below the cost of providing them. The estimated cost of these activities was approximately $1,856,000 and $1,956,000 in 2010 and 2009, respectively. The estimated cost of physician recruitment was approximately $178,000 and $71,000 in 2010 and 2009, respectively.

Medical Malpractice Insurance: Medical malpractice insurance coverage was provided under a claims-made policy, which had a $50,000 deductible effective February 15, 2005, and a $5,000 deductible prior to February 1, 2005. Upon termination of the claims-made policy, the Hospital has the option to purchase insurance for claims having occurred during its term but reported subsequently.

As of March 1, 2010, the Hospital became self insured for medical malpractice on all of the Hospital's medical liability claims. The Hospital remained a participant in the Indiana Patient Compensation Fund. In addition to the Patient Compensation Fund, the Hospital remained commercially insured for general liability exposure, physician malpractice coverage, and continued to purchase an umbrella/excess policy.

Prior to July 1, 1999, the Indiana Medical Malpractice Act provided for a maximum recovery of $750,000 per occurrence for professional liability, $100,000 of which would be paid through the Hospital's malpractice insurance coverage, and the balance would be paid by the State of Indiana Patient Compensation Fund. As of July 1999, the Indiana Medical Malpractice Act provides recovery up to $1,250,000 per occurrence, with the first $250,000 covered by the Hospital's insurance. While the ultimate result of any claim or action cannot be determined, management does not believe that the outcome of any claim or action will have a material adverse affect on the financial position or results of operations of the Hospital.

Advertising: Advertising costs are expensed as incurred. Advertising costs were $2,021,526 and $1,574,729 for 2010 and 2009, respectively.

Reclassifications: Certain prior year amounts have been reclassified to conform with the current year presentation. Such reclassifications have no affect on previously reported net assets or the change in net assets.

## NOTE 2 - NET PATIENT SERVICE REVENUE

The Hospital provides care to certain patients under payment arrangements with Medicare, Medicaid, and various health maintenance and preferred provider organizations at amounts different from its established rates. Services provided under those arrangements are paid at prospectively determined rate per discharge, reimbursable costs, discounted charges, and per diem rates. Reported costs and/or services provided under certain arrangements are subject to the audit by the administering agencies. Changes in the Medicare and Medicaid programs and reduction of funding levels could have an adverse affect on the future amounts recognized as net patient service revenue.

Combined revenues received under the Medicare, Medicaid, and Wellpoint, Inc. payment arrangements account for 77.2% and 71.2% of net patient service revenue for the years ended December 31, 2010 and 2009, respectively. Provision has been made in the financial statements for contractual adjustments, representing the difference between standard charges for services and actual or estimated payments.

Net patient service revenue is summarized as follows for the years ended December 31:

| | 2010 | 2009 |
|---|---|---|
| Gross patient service revenue, excluding charity care and forgone charges | | |
| Inpatient | | |
| Routine | $ 88,191,004 | $ 88,636,303 |
| Ancillary | 229,166,923 | 229,724,278 |
| Total inpatient | 317,357,927 | 318,360,581 |
| Outpatient | 260,997,238 | 258,860,404 |
| | 578,355,165 | 577,220,985 |
| Less contractual allowances | 326,896,908 | 319,861,115 |
| Net patient service revenue | $ 251,458,257 | $ 257,359,870 |

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party agreements. Major components of gross patient accounts receivable include 37.8% from Medicare, 14.5% from Medicaid, and 13.5% from Wellpoint, Inc. at December 31, 2010 and 26.7% from Medicare, 11.9% from Medicaid, and 14.8% from Wellpoint, Inc. at December 31, 2009.

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

## NOTE 3 - ASSETS LIMITED AS TO USE AND OTHER FINANCIAL INSTRUMENTS

Accounting Standard Codification 820-10-05, Fair Value Measurement, defines fair value as the price that would be received for an asset or paid to transfer a liability (an exit price) in the Hospital's principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

FASB ASC 820-10-05 establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

**NOTE 3 - ASSETS LIMITED AS TO USE AND OTHER FINANCIAL INSTRUMENTS** (Continued)

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date. The fair values of equity securities are determined by obtaining quoted prices on nationally recognized securities exchanges.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The following is a description of the valuation methodology used for level 2 assets measured at fair value. There have been no changes in the methodology used at December 31, 2010 and 2009:

U.S. Government Securities: U.S. government securities are normally valued using a model that incorporates market observable data such as reported sales of similar securities, broker quotes, yields, bids, offers, and reference data. Certain securities are valued principally using dealer quotations. U.S. government securities are categorized in level 1 or level 2 of the fair value hierarchy depending on the inputs used and market levels for specific securities.

Money Market Accounts: The fair value of money market accounts are normally valued using amortized cost to the extent that periodic mark-to-market calculations indicates the the use of amortized cost approximates market value. Money market accounts are categorized as level 2.

The following tables present the Hospital's assets measured at fair value on a recurring basis under FASB ASC 820-10-05 at December 31:

| | Fair Value Measurements at December 31, 2010 Using Quoted Prices in: | | | |
|---|---|---|---|---|
| | Significant Active Markets for Identical Assets (Level 1) | Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
| Domestic Equities - securities | $ 10,383,235 | $ - | $ - | $ 10,383,235 |
| Domestic Equities - mutual funds | 99,143,230 | - | - | 99,143,230 |
| International Equities - securities | 1,019,819 | - | - | 1,019,819 |
| International Equities - mutual funds | 48,926,185 | - | - | 48,926,185 |
| Fixed income securities - mutual funds | 25,753,214 | - | - | 25,753,214 |
| Fixed income securities - corporate bonds | 345,937 | - | - | 345,937 |
| Fixed income securities - US Treasuries | - | 4,589,132 | - | 4,589,132 |
| Fixed income securities - mortgage backed and other government | 1,039,857 | - | - | 1,039,857 |
| Money Market | - | 1,107,897 | - | 1,107,897 |
| | $ 186,611,477 | $ 5,697,029 | $ - | $ 192,308,506 |

**NOTE 3 - ASSETS LIMITED AS TO USE AND OTHER FINANCIAL INSTRUMENTS** (Continued)

| | Fair Value Measurements at December 31, 2009 Using Quoted Prices in: | | | |
|---|---|---|---|---|
| | Significant Active Markets for Identical Assets (Level 1) | Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
| Assets: | | | | |
| Cash and cash equivalents | $ 1,325,731 | $ - | $ - | $ 1,325,731 |
| Mutual funds | 86,699,706 | - | - | 86,699,706 |
| Marketable equity securities | 8,087,672 | - | - | 8,087,672 |
| Bonds | 61,807,278 | 3,854,779 | - | 65,662,057 |
| | $ 157,920,387 | $ 3,854,779 | $ - | $ 161,775,166 |

The composition of assets limited as to use and short-term and long-term investments is as follows at December 31:

| | 2010 | | 2009 | |
|---|---|---|---|---|
| | Fair value | Cost | Fair value | Cost |
| Cash and cash equivalents | $ 1,107,897 | $ 1,107,824 | $ 1,325,731 | $ 1,324,679 |
| Mutual funds | 156,717,240 | 146,010,456 | 86,699,706 | 90,712,900 |
| Marketable equity securities | 12,393,835 | 10,150,574 | 8,087,672 | 7,165,381 |
| Bonds | 22,089,534 | 22,151,847 | 65,662,057 | 64,975,053 |
| | $ 192,308,506 | $ 179,420,701 | $ 161,775,166 | $ 164,178,013 |

Assets limited as to use, which are carried at fair value based on quoted market prices, consist of the following at December 31:

| | 2010 | 2009 |
|---|---|---|
| Temporarily restricted | $ 4,617,421 | $ 4,120,110 |
| Permanently restricted | 400,000 | 400,000 |
| Unrestricted-board-designated | 156,074,045 | 136,014,970 |
| Bond funds | - | 88,709 |
| | $ 161,091,466 | $ 140,623,789 |

The unrestricted board-designated assets represent funds designated by the Board for future replacement and acquisition of property and equipment and the payment of principal on long-term debt.

**NOTE 3 - ASSETS LIMITED AS TO USE AND OTHER FINANCIAL INSTRUMENTS** (Continued)

Investment returns for assets limited as to use, cash and cash equivalents, and short-term investments comprise the following for the years ended December 31:

| | 2010 | 2009 |
|---|---|---|
| Interest and dividend income | $ 6,931,977 | $ 5,367,922 |
| Interest expense | (1,368,533) | (1,287,552) |
| Net realized gains/(losses) | 193,646 | 92,381 |
| Net change in unrealized gains/(losses) | 15,290,651 | 27,913,089 |
| | $ 21,047,741 | $ 32,085,840 |

Investment returns are included in the statements of operations and changes in net assets for the years ended December 31 as follows:

| | 2010 | 2009 |
|---|---|---|
| Investment income and expense, and realized investment gains / (losses) included in nonoperating income / expense, net | $ 5,437,676 | $ 4,469,017 |
| Other changes in unrestricted net assets- net change in unrealized gains / (losses), net | 15,042,754 | 26,700,870 |
| Temporarily restricted net assets investment income, net of trust fees, realized investment gains / (losses), and change in unrealized gains / (losses), net | 567,311 | 915,953 |
| | $ 21,047,741 | $ 32,085,840 |

Nonoperating income/expense, net included $2,147,402 and $2,218,821 in interest expense related to long-term borrowing for 2010 and 2009, respectively.

Over the past several years, the public equity markets experienced significant fluctuations, which impacted investments held by the Hospital. Management continually reviews its investment portfolio and evaluates whether declines in the fair value of the securities should be considered other than temporary. Factored into this evaluation are the general market conditions, the issuer's financial condition and near-term prospects, conditions in the issuer's industry, the recommendation of advisors, and the length of time and extent to which the market value has been less than cost. Management recognized $12,657 of losses related to other-than-temporary impairments of investments in 2010. No amounts of losses related to other-than-temporary impairments of investments were recognized in 2009.

**NOTE 3 - ASSETS LIMITED AS TO USE AND OTHER FINANCIAL INSTRUMENTS** (Continued)

The following tables summarize the unrealized losses on investments held at December 31:

| | Less than Twelve Months | | Twelve Months or Longer | |
|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| 2010 | | | | |
| Common stock | $ 520,874 | $ 3,270 | $ - | $ - |
| Mutual funds | 96,730 | 20,776 | 8,691,806 | 901,357 |
| Bonds | 10,595,849 | 143,362 | 1,351,611 | 129,146 |
| Total | $ 11,213,453 | $ 167,408 | $ 10,043,417 | $ 1,030,503 |
| 2009 | | | | |
| Common stock | $ 89,658 | $ 13,437 | $ 2,280,821 | $ 294,432 |
| Mutual funds | 2,774,312 | 25,688 | 56,093,960 | 5,444,791 |
| Bonds | 9,976,157 | 55,909 | 29,442,560 | 510,655 |
| Total | $ 12,840,127 | $ 95,034 | $ 87,817,341 | $ 6,249,878 |

**NOTE 4 - PROPERTY AND EQUIPMENT**

Property and equipment at December 31 are summarized as follows:

| | 2010 | 2009 |
|---|---|---|
| Land and improvements | $ 2,687,613 | $ 2,706,311 |
| Property held for future expansion | 3,696,749 | 3,696,749 |
| Building and improvements | 170,717,680 | 170,055,462 |
| Equipment | 114,290,654 | 108,713,105 |
| Construction-in-progress | 4,466,731 | 5,847,122 |
| | 295,859,427 | 291,018,749 |
| Less allowance for depreciation | 156,624,735 | 142,001,000 |
| | $ 139,234,692 | $ 149,017,749 |

**NOTE 5 - LONG-TERM DEBT**

Long-term debt at December 31 is summarized as follows:

| | 2010 | 2009 |
|---|---|---|
| Hospital Authority of Elkhart County (the Authority), Hospital Revenue Bonds, Series 1998, interest rates ranging from 4.68% to 5.25% | $ 40,240,000 | $ 41,475,000 |
| Hospital Authority of Elkhart County, Hospital Revenue Bonds, Series 2008, interest rates ranging from 0.24% to 0.38% | 46,315,000 | 47,080,000 |
| | 86,555,000 | 88,555,000 |
| Less current maturities | 2,085,000 | 2,000,000 |
| | $ 84,470,000 | $ 86,555,000 |

The Authority issued $49,330,000 of Series 1998 Hospital Revenue Bonds (Series 1998 Bonds). The Hospital borrowed the proceeds of the sale of the Series 1998 Bonds and evidenced this loan with a loan agreement, issued under the Trust Indenture date November 15, 1998, between the Authority and Bank One, N.A., as trustee. A portion of the proceeds of the Series 1998 Bonds were issued to retire interest payments and principal payments of certain previously outstanding Series 1992 Bonds. The remaining proceeds were used to reimburse the Hospital for certain capital expenditures. The Series 1998 Bonds are unsecured general obligations of the Hospital. The Series 1998 Bonds mature in August 2028.

The Authority issued $47,800,000 of Series 2008 Hospital Revenue Bonds (Series 2008 Bonds). The Hospital borrowed the proceeds of the sale of the Series 2008 bonds and evidenced this loan with a loan agreement, issued under the Trust Indenture dated December 1, 2008. The proceeds of the Series 2008 Bonds was issued to retire interest and principal payments of previously outstanding bonds. The Series 2008 Bonds require the Hospital to hold a letter of credit with JP Morgan Chase Bank, N.A. in the amount of $47,045,889. The letter of credit expires on January 15, 2014. The letter of credit decreases by the principal payments made by the Hospital on the Series 2008 Bonds. The Series 2008 Bonds mature in December 2033.

The loan agreements require maintenance of a certain debt service coverage ratio, limit additional borrowings, and require compliance with various other restrictive covenants. The Hospital was in compliance with all covenants.

Required annual principal payments of long-term debt for each of the next five years are as follow: 2011-$2,085,000; 2012-$2,195,000; 2013-$2,450,000; 2014-$2,460,000; 2015-$2,595,000.

Interest paid during 2010 and 2009 was $2,282,778 and $2,799,399, respectively.

## NOTE 6 - LEASE OBLIGATIONS

The Hospital leases various equipment for use in operations. Total rental expense was $1,585,000 and $1,668,000 in 2010 and 2009, respectively. At December 31, 2010 minimum future rental payments under non-cancelable operating leases are as follows:

| | |
|---|---|
| 2011 | $ 523,203 |
| 2012 | 385,728 |
| 2013 | 209,688 |
| | $ 1,118,619 |

## NOTE 7 - BENEFIT PLAN

The Hospital maintains a defined-benefit pension plan that covers a majority of its employees as of December 31. A plan measurement date of January 1 is utilized for this plan.

In connection with the Hospital's adoption of FASB ASC 715, Compensation - Retirement Plans, the hospital recognizes the overfunded or underfunded status of a defined benefit post-retirement plan as an asset or liability in its statement of operations and change in net assets and recognizes the changes in that funded status in the year in which the changes occur through the statement of operations and change in net assets.

A summary of the changes in the projected benefit obligation and plan assets and the resulting funded status of the defined-benefit pension plan are as follows:

| | 2010 | 2009 |
|---|---|---|
| Change in projected benefit obligation: | | |
| Benefit obligation at beginning of year | $ 107,953,525 | $ 101,711,207 |
| Service cost | 972,849 | 1,028,427 |
| Interest cost | 6,634,111 | 6,373,329 |
| Actuarial (gain) loss | 2,929,816 | 2,129,189 |
| Benefits paid | (3,644,131) | (3,288,627) |
| Projected benefit obligation at year-end | $ 114,846,170 | $ 107,953,525 |
| | | |
| Change in plan assets: | | |
| Fair value of plan assets at beginning of year | $ 81,430,101 | $ 65,747,046 |
| Actual return on plan assets | 11,376,057 | 17,540,904 |
| Employer contributions | 1,683,171 | 1,430,778 |
| Benefits paid | (3,644,131) | (3,288,627) |
| Fair value of plan assets at year-end | $ 90,845,198 | $ 81,430,101 |

**NOTE 7 - BENEFIT PLAN** (Continued)

| | 2010 | 2009 |
|---|---|---|
| Funded status of the plan | $ (24,000,972) | $ (26,523,424) |
| Unrecognized prior service cost | 11,120 | 14,032 |
| Unrecognized net loss | 26,447,081 | 29,764,930 |
| Prepaid benefit cost | $ 2,457,229 | $ 3,255,538 |
| Net periodic pension cost comprises the following | | |
| Service cost | $ 972,849 | $ 1,028,427 |
| Interest cost | 6,634,111 | 6,373,329 |
| Expected return on plan assets | (6,852,899) | (5,489,989) |
| Recognized loss | 1,724,507 | 2,951,553 |
| Net amortization and deferrals | 2,912 | 2,912 |
| Net periodic pension cost | $ 2,481,480 | $ 4,866,232 |

| | |
|---|---|
| Estimated benefit costs in the next fiscal year: | |
| Prior service Cost | $ 2,026 |
| Net loss | 1,496,246 |

The accumulated benefit obligation for the defined-benefit pension plan was $111,252,604 and $103,630,065 at December 31, 2010 and 2009, respectively.

Weighted-average assumptions used to determine benefit obligations at December 31 are as follows:

| | 2010 | 2009 |
|---|---|---|
| Discount rate | 6.00 % | 6.25 % |
| Rate of compensation increase | 3.00 | 3.00 |

Weighted average assumptions used to determine net periodic pension cost for years ended December 31 are as follows:

| | 2010 | 2009 |
|---|---|---|
| Discount rate | 6.25 % | 6.25 % |
| Expected long-term return on plan assets | 8.50 | 8.50 |
| Rate of compensation increase (until 40/thereafter) | 3.00 | 3.00 |

**NOTE 7 - BENEFIT PLAN** (Continued)

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

| | 2010 Target | Actual 2010 | Actual 2009 |
|---|---|---|---|
| Asset category | | | |
| Equity securities | 75.00 % | 64.00 % | 61.00 % |
| Debt securities | 24.00 | 35.00 | 38.00 |
| Other | 1.00 | 1.00 | 1.00 |
| | 100.00 % | 100.00 % | 100.00 % |

The plan exists to provide retirement benefits for covered employees of the Hospital consistent with the long-term interests of plan participants and their beneficiaries. The plan's investment objectives may include, but are not limited to maintaining, the purchasing power of current assets and all future contributions by producing positive real rates of return on plan assets; having the ability to pay all benefit and expense obligations when due; maximizing return within reasonable and prudent levels of risk in order to minimize contributions; and controlling costs in administering the plan and managing the investments. Effective December 31, 2007 the Hospital froze the plan for all participants who have not attained the age of 50 and accumulated 15 years of vesting service as of December 31, 2007. Participants who are at least 50 years old and had accumulated 15 years of vesting service at December 31, 2007 will continue to accrue benefits under the terms of the plan. No new participants are allowed to enter the plan. A new employee benefit plan was initiated (Note 8).

Fair Value of Plan Assets: Fair value is the exchange price that would be received for an asset in the principal or most advantageous market for the asset in an orderly transaction between market participants on the measurement date.

The Hospital used the following methods and significant assumptions to estimate the fair value of each type of plan asset:

Equity, Debt, Investment Funds and Other Securities: The fair values for investment securities are determined by quoted market prices, if available (Level 1). For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3).

**NOTE 7 - BENEFIT PLAN** (Continued)

The fair value of the plan assets at December 31, 2010, by asset category, is as follows:

| | Fair Value Measurements at December 31, 2010 Using Quoted Prices in: | | | |
|---|---|---|---|---|
| | Significant Active Markets for Identical Assets (Level 1) | Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
| Domestic Equities - securities | $ 2,906,660 | $ - | $ - | $ 2,906,660 |
| Domestic Equities - mutual funds | 46,689,833 | - | - | 46,689,833 |
| International Equities - securities | 106,848 | - | - | 106,848 |
| International Equities - mutual funds | 27,212,254 | - | - | 27,212,254 |
| Fixed income securities - mutual funds | 12,847,815 | - | - | 12,847,815 |
| Money Market | - | 1,081,788 | - | 1,081,788 |
| | $ 89,763,410 | $ 1,081,788 | $ - | $ 90,845,198 |

| | Fair Value Measurements at December 31, 2009 Using Quoted Prices in: | | | |
|---|---|---|---|---|
| | Significant Active Markets for Identical Assets (Level 1) | Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
| Cash and cash equivalents | $ 1,083,169 | $ - | $ - | $ 1,083,169 |
| Mutual Funds | 78,242,945 | - | - | 78,242,945 |
| Marketable securities | 2,103,987 | - | - | 2,103,987 |
| | $ 81,430,101 | $ - | $ - | $ 81,430,101 |

Contributions: Plan contributions made for 2010 and 2009 were $1,683,171 and $1,430,778, respectively. Any contributions made for the 2011 plan year will be discretionary or as required by applicable law.

**NOTE 7 - BENEFIT PLAN** (Continued)

Estimated Future Benefit Payments: The following benefit payments, which reflect expected future services, as appropriate, are expected to be paid:

| | Pension Benefits |
|---|---|
| 2011 | $ 4,007,819 |
| 2012 | 4,482,280 |
| 2013 | 4,947,885 |
| 2014 | 5,412,209 |
| 2015 | 5,861,190 |
| Thereafter | 37,294,764 |
| | $ 62,006,147 |

**NOTE 8 - EMPLOYEE BENEFIT PLANS**

The Hospital maintains two tax sheltered annuity plans, provided for in Internal Revenue Code Sections 401(a) and 403(b), for all eligible employees. For the 403(b) plan, the Hospital matches 50% of an employee's contribution up to 6% of compensation. For the 401(a) plan, the Hospital's contribution is based upon the employee's age and years of service. For the years ended December 31, 2010 and 2009, Hospital contributions were $4,152,313 and $4,397,999, respectively. The Hospital has accrued $2,586,228 and $2,742,697 in employer contributions and related liabilities at December 31, 2010 and 2009, respectively.

**NOTE 9 - FUNCTIONAL EXPENSES**

The Hospital provides general inpatient and outpatient healthcare services to its surrounding community. Expenses related to providing these services are as follows:

| | 2010 | 2009 |
|---|---|---|
| Healthcare services | $ 232,890,520 | $ 244,787,354 |
| General and administrative | 22,838,009 | 19,438,722 |
| | $ 255,728,529 | $ 264,226,076 |

**NOTE 10 - INVESTMENTS IN NONCONSOLIDATED AFFILIATES**

The Hospital owned a 33% interest in Partners National Health Plans of Indiana, Inc., a health maintenance organization (HMO), at December 31, 2010 and 2009. On January 23, 2003, the HMO announced a phase-out plan. In March 2007, the Hospital received a $700,000 return of investment. The phase out was finalized during 2010. The dissolution of the HMO did not have a material adverse affect on the operations or financial condition of the Hospital.

**NOTE 10 - INVESTMENTS IN NONCONSOLIDATED AFFILIATES** (Continued)

The Hospital owns a 40% interest in Northern Indiana Ambulatory Surgery Center, LLC, d/b/a RiverPointe Surgery Center (the Surgery Center). The Surgery Center was formed during 1996 by the Hospital and individual physicians to own and operate an ambulatory surgery center in space leased from the Hospital.

The Hospital owns 50% of RiverPointe Cardiovascular Lab, LLC (the Cardiovascular Lab). The Cardiovascular Lab is owned by the Hospital and the Elkhart Clinic to operate a cardiovascular laboratory in space leased from the Hospital.

The Hospital owns 25% of Community Occupational Medicine, LLC, an occupational healthcare facility located in Elkhart, Indiana.

The Hospital owns 42% of Wakarusa Medical Clinic, LLC, which owns the Wakarusa Medical Clinic facility and leases it to the Hospital.

The Hospital owns 50% of WaNee Walk In Clinic, LLC, a physician practice facility located in Wakarusa, Indiana.

The Hospital owns 50% of Michiana Linen Service, LLC, a laundry facility located in Elkhart, Indiana. The Hospital provides contract services to the LLC, and purchases laundry services in return.

The Hospital is a guarantor for a portion the debt of an unconsolidated joint venture, Community Occupational Medicine, LLC, in which the Hospital records an equity interest. The portion of the debt guaranteed by the Hospital is estimated at $611,000 at December 31, 2010. No amounts have been paid or accrued pursuant to this guarantee as of December 31, 2010. Community Occupational Medicine, LLC subsequently paid approximately $200,000 under the obligation as of , the date the financial statements were issued. The Hospital has set aside corresponding funds, which are recorded as short-term investments on the balance sheets.

Aggregate financial information (unaudited) relating to these investments is as follows:

| | 2010 | 2009 |
|---|---|---|
| Assets | $ 8,381,509 | $ 6,320,192 |
| Liabilities | 4,019,159 | 3,715,923 |
| Net income | 1,887,418 | 2,500,967 |

**NOTE 11 - RELATED PARTY TRANSACTIONS**

Elkhart General Hospital Foundation (the Foundation) was founded in 1966 to obtain funds through charitable contributions and is authorized by the Hospital to solicit contributions on its behalf. In the absence of donor restrictions, the Foundation has discretionary control over the amounts to be distributed to the Hospital, the timing of such distributions, and the purposes for which such funds are to be used. In addition, the Foundation directs the investment activities of the Jonathan Primley Fund (restricted assets), which released $70,000 in 2010. No such funds were released in 2009.

**NOTE 11 - RELATED PARTY TRANSACTIONS** (Continued)

The Hospital provides certain services in the ordinary course of business to the Surgery Center. Revenue recognized by the Hospital in connection with this arrangement for the years ended December 31, 2010 and 2009, was $85,000 and $89,000, respectively. In addition, the Hospital received rental income from physicians and the Surgery Center occupying the RiverPointe Medical Office Building of $1,459,000 and $1,538,000 for the years ended December 31, 2010 and 2009, respectively. Revenue recognized by the Hospital in connection with both arrangements is included in other operating revenue in the statements of operations and changes in net assets.

The Hospital provides employees to Michiana Linen, LLC under a leased employee agreement. The Hospital also provides certain services in the ordinary course of business to Michiana Linen Service, LLC. Either party may terminate the agreement upon a 90 day notice. Revenue and expenses recognized by the Hospital in connection with this arrangement for the year ended December 31, 2010 is $1,870,000. Related party receivables of $1,137,000 related to these services are outstanding at December 31, 2010. Revenue recognized by the Hospital in connection with these services is included in other operating revenue in the statements of operations and changes in net assets. Expenses recognized by the Hospital in connection with these services is included in salaries and wages, employee benefits and other expenses in the statements of operations and changes in net assets.

The Hospital entered into an agreement with Michiana Linen Service, LLC to purchase laundry service. The agreement is for the period of 3 years commencing in May of 2010. The Hospital purchased services from Michiana Linen Service, LLC of $810,000 for 2010. Approximately $100,000 was due to Michiana Linen, LLC related to service provided to the Hospital at December 31, 2010.

**NOTE 12 - COMMITMENTS AND CONTINGENCIES**

Laboratory Services: The Hospital entered into a pathology and clinical laboratory services agreement (agreement) effective July 2007 through June 2012 which was amended in July 2010 to extend the contract through June 2014. The agreement requires base compensation for services rendered of $10,335,000 adjusted annually on July 1st by the CPI but not to exceed upper level range determined by an agreed upon benchmarking tool. The benchmarking tool used are operational data reports provided to the Hospital by a third-party. The Hospital paid $10,412,000 and $10,800,000 for pathology and clinical laboratory services under the agreement as of December 31, 2010 and 2009, respectively.

Self Funded Health Insurance: The Hospital provides a self-funded health insurance plan to its employees. The Hospital has stop-loss insurance to reduce its exposure under this plan. For 2009, the plan included a $250,000 specific stop-loss insurance per individual per year with an aggregate limit of $2,000,000. For 2010, the plan included a $350,000 specific stop-loss insurance per individual per year with no aggregate limit. The individual is responsible for all claims after the $2,000,000 aggregate limit. The Hospital accrues for the estimated uninsured portion of pending claims, both known and incurred but not reported. These accruals are provided based on management's evaluation of the nature and severity of claims and the Hospital's historical claims experience. The liability accrued at December 31, 2010 and 2009 was $2,373,989 and $1,912,788, respectively, and is included in accounts payable and accrued expenses. The expense, which is included in employee benefits in operating expenses, associated with the self-funded health insurance plan was $12,687,456 and $16,198,710 for 2010 and 2009, respectively.

Non-Compete: For a period of one year after termination of employment from the Hospital, no former physician may establish, operate, or provide medical services within a certain geographic area, as further described in the operating agreement.

**NOTE 12 - COMMITMENTS AND CONTINGENCIES** (Continued)

IT Services: The Hospital entered into an Information Services agreement (ISA) with CareTech Solutions, Inc. effective February 2008 to provide information technology services through January 2012. The agreement automatically renews for two successive three year terms unless either party provides 180 days written notice. The Hospital may terminate the agreement for any reason with 180 days written notice. The agreement requires a base service fee of $3,975,000 in year one, which will be reduced by 0.5% in years two and three and 0.25% in years four and five. The agreement calls for an annual increase of the base fee by the Consumer Price Index, as defined in the agreement, after the reduction in the base fee each year. Base fees paid totaled $3,820,663 and $3,845,655 for the year ended December 31, 2010 and 2009, respectively.

During 2010, the Hospital amended the agreement with CareTech Solutions for disaster recovery and remote hosting services. Monthly base services fee will be $309,089, adjusted annually, beginning 2011 using CPI as an escalator.

Hospitalist Services: Effective January, 2009, the Hospital entered into a Hospitalist Services Coverage agreement (Hospitalist Agreement) with a third party provider. The Hospitalist Agreement guarantees $328,400 of annual cash receipts per full time equivalent (FTE) physician. The Hospitalist Agreement stipulates a mutual intent of 8 FTE physicians. The term of the Hospitalist Agreement is through December 31, 2011 with automatic one year extensions unless terminated by either party within a 120 days written notice. Payments during 2010 and 2009 under the Hospitalist Agreement totaled $1,114,595 and $790,504, respectively.

Self-Funded Medical Malpractice: Professional liability claims that fall within the Hospital's range of self-insurance have been asserted by various claimants. The claims are in various stages of processing and some may ultimately be brought to trial. There are also known incidents that have occurred through December 31, 2010 that may result in the assertion of additional claims, as well as claims, from unknown incidents that may be asserted. The Hospital provides for an estimate of the ultimate costs, if any, relating to the settlement of such claims and remains liable for losses, if any, in excess of the amounts recorded; however, in management's opinion, such losses, if any, would not have a material adverse effect on the financial position or results of operations of the Hospital.

The liability accrued at December 31, 2010 and 2009 was $397,318 and $250,000, respectively, and is included in accounts payable and accrued expenses. The expense, which is included in operating expenses, associated with medical malpractice was $218,375 and $76,424 for 2010 and 2009, respectively.

Anesthesia Services: The Hospital contracts anesthesia services with a third party provider. The Hospital guarantees approximately $7,200,000 of annual cash receipts to the third party provider. On January 1st of each year, the guaranteed amount shall be increased by a prescribed percentage. Payments made by the Hospital for amounts guaranteed to the third party totaled $3,926,182 and $3,260,737 during 2010 and 2009, respectively.

**NOTE 13 - SUBSEQUENT EVENTS**

Hospital Affiliation: On March 17, 2011 the Hospital signed a Memorandum of Understanding (MOU) with Memorial Health System (MHS). The MOU is an exclusive agreement to create a parent company that will be the sole member of both the Hospital and MHS. The related entities of the Hospital and MHS will still be administered by the respective companies management. The Hospital and MHS will remain separate legal entities and maintain their separate provider numbers.

Home Care Partnership: The Hospital has entered into a 50/50 partnership agreement with American Nursing Care for Home Health Care, Durable Medical Equipment and Home Infusion Therapy Services. This new partnership will be effective on July 1, 2011.

Under this new partnership, EGH Home Care, Durable Medical Equipment and Home Infusion staff will become employees of American Nursing Care on the effective date.

Center for Wound Care: The Hospital entered into an agreement with the Center For Wound Healing, Inc to facilitate the construction, operation, and maintenance of a wound care facility under the auspices of the Hospital. The Hospital is to pay 75% and 50% of amounts collected for treatment of patients for Hyperbaric Oxygenation and Wound Care treatments, respectively. The Hospital is responsible for all billing and collection functions, medical supplies, cleaning, laundry services, utility services, computers, office supplies, telecommunications, information technology and oxygen. The initial term is for 5 years commencing after the opening of the Center for Wound Care (CWC) facility. The agreement auto renews for 3 year terms. A 180 day termination notice is required prior to the renewal date. Each party is required to maintain commercial insurance of $1,000,000 per occurrence and $3,000,000 in aggregate.

Cardiology Agreement: The Hospital has entered into various agreements with the Elkhart Clinic to purchase the assets of a cardiology practice, to rent space to operate a cardiology specialist practice, and to purchase cardiology professional services and other services to staff a Hospital owned cardiology practice. The agreements were effective on May 1, 2011

Subsequent Event Analysis: The Hospital has performed an analysis of activities and transactions subsequent to December 31, 2010 to determine the need for any adjustments to and/or disclosures within the audited financial statements for the year ended December 31, 2010. The Hospital has performed their analysis through May 17, 2011, the date the financial statements were issued.