Fletcher Allen Partners, Inc. and Subsidiaries

Report on Federal Awards in Accordance with OMB Circular A–133
September 30, 2012
EIN 45–2880726

Fletcher Allen Partners, Inc. and Subsidiaries
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September 30, 2012

Part I

Financial Statements

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Report of Independent Auditors

To the Board of Trustees of
Fletcher Allen Partners, Inc.:

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of operations, changes in net assets, and cash flows present fairly, in all material respects, the financial position of Fletcher Allen Partners, Inc. and its Subsidiaries ("the Organization") as of September 30, 2012, and the results of their operations, their changes in net assets and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of Organization's management. Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 21, 2012 on our consideration of Organization's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards for the year ended September 30, 2012 is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. The information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The Schedule of Expenditures of Federal Awards has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or the financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

PricewaterhouseCoopers LLP

December 21, 2012

Fletcher Allen Partners, Inc. and Subsidiaries
Consolidated Balance Sheet
September 30, 2012

(in thousands)

Assets		
Current assets		
Cash and cash equivalents	$	173,865
Patient and other trade accounts receivable - net of allowance for doubtful accounts of $26,572		132,939
Short-term investments		1,932
Inventories		23,861
Current portion of assets whose use is limited or restricted		13,132
Estimated receivables from third-party payers		6,140
Prepaid and other current assets		25,156
Total current assets		377,025
Assets whose use is limited or restricted		
Board-designated assets		294,100
Assets held by trustee under bond indenture agreements		31,228
Restricted assets		37,319
Donor-restricted assets for specific purposes		25,351
Donor-restricted assets for permanent endowment		29,165
Total assets whose use is limited or restricted		417,163
Property and equipment, net		471,064
Other assets		
Deferred financing costs, net		13,150
Notes receivable and other assets		10,073
Investment in affiliated companies		5,131
Pledges receivable, net of current portion		584
Total other assets		28,938
Total assets	$	1,294,190
Liabilities and net assets		
Current liabilities		
Current installments of long-term debt	$	13,489
Accounts payable		25,671
Accrued expenses and other liabilities		50,807
Accrued payroll and related benefits		72,253
Estimated third-party payer settlements		16,916
Estimated amounts for incurred but not reported claims		24,631
Total current liabilities		203,767
Long-term liabilities		
Long-term debt - net of current installments		401,833
Reserve for outstanding losses on malpractice and workers' compensation claims		28,982
Pension and other postretirement benefit obligations		81,582
Other long-term liabilities		21,248
Total long-term liabilities		533,645
Total liabilities		737,412
Commitments and contingent liabilities		
Net assets		
Unrestricted		500,374
Temporarily restricted		27,239
Permanently restricted		29,165
Total net assets		556,778
	$	1,294,190

The accompanying notes are an integral part of these consolidated financial statements.

Fletcher Allen Partners, Inc. and Subsidiaries
Consolidated Statement of Operations
Year Ended September 30, 2012

(in thousands)

Unrestricted revenue and other support	
Net patient service revenue	$ 1,037,259
Less: Provision for bad debts	(35,856)
Net patient service revenue after provision for bad debts	1,001,403
Premium revenue	106,904
Other revenue	36,242
Total unrestricted revenue and other support	1,144,549
Expenses	
Salaries, payroll taxes, and fringe benefits	665,704
Supplies and other	264,803
Purchased services	45,660
Depreciation and amortization	57,104
Interest expense	19,951
Underwriting expenses	14,652
Medical claims	47,609
Total expenses	1,115,483
Income from operations	29,066
Nonoperating gains (losses)	
Investment income	21,668
Loss on interest rate swap agreements	(1,266)
Loss on the extinguishment of debt	(2,834)
Contribution revenue from acquisition	52,453
Other	5,885
Total nonoperating gains	75,906
Excess of revenue over expenses	104,972
Net change in unrealized gains on investments	30,945
Assets released from restrictions for capital purchases	334
Pension related adjustments	(18,343)
Increase in unrestricted net assets	$ 117,908

The accompanying notes are an integral part of these consolidated financial statements.

Fletcher Allen Partners, Inc. and Subsidiaries
Consolidated Statement of Changes in Net Assets
Year Ended September 30, 2012

(in thousands)

Unrestricted net assets	
Excess of revenue over expenses	$ 104,972
Net change in unrealized gains on investments	30,945
Assets released from restrictions for capital purchases	334
Pension related adjustments	(18,343)
Increase in unrestricted net assets	117,908
Temporarily restricted net assets	
Gifts, grants, and bequests	2,908
Investment income	180
Net change in unrealized gains on investments	3,099
Net realized gains on investments	617
Net assets released from restrictions used in operations	(1,522)
Net assets released from restrictions used for nonoperating purposes	(306)
Net assets released from restrictions used for capital purchases	(334)
Transfer of net assets	(64)
Contribution of temporarily restricted net assets	6,035
Increase in temporarily restricted net assets	10,613
Permanently restricted net assets	
Gifts, grants, and bequests	67
Change in beneficial interest in perpetual trusts	941
Transfer of net assets	64
Contribution of permanently restricted net assets	3,101
Increase in permanently restricted net assets	4,173
Increase in net assets	132,694
Net assets	
Beginning of year	424,084
End of year	$ 556,778

The accompanying notes are an integral part of these consolidated financial statements.

Fletcher Allen Partners, Inc. and Subsidiaries
Consolidated Statement of Cash Flows
Year Ended September 30, 2012

(in thousands)

Cash flows from operating activities		
Increase in net assets	$	132,694
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Depreciation and amortization		57,104
Contribution revenue from acquisition		(61,589)
Provision for bad debts		35,856
Contributions restricted for long-term use		(67)
Pension related adjustments		18,343
Loss on extinguishment of debt		2,834
Gain on disposal of property and equipment		(218)
Loss on interest rate swap agreements		1,266
Realized and unrealized gains on investments		(48,943)
Undistributed gains of affiliated companies		(226)
Change in beneficial interest in perpetual trusts		(941)
Changes in operating assets and liabilities		
Increase in patient and other accounts receivable		(28,747)
Increase in other current and noncurrent assets		(5,607)
Increase in estimated receivables from third-party payers		(901)
Increase in accounts payable and accrued expenses		16,843
Increase in accrued payroll and related expenses		7,743
Increase in other current and noncurrent liabilities		11,289
Decrease in estimated settlements with third-party settlements		(3,580)
Decrease in pension and other postretirement benefit obligations		(7,398)
Net cash provided by operating activities		125,755
Cash flows from investing activities		
Acquisitions of property and equipment		(39,488)
Purchase of investments		(213,760)
Proceeds from sale of investments		201,683
Proceeds from sale of affiliated company		397
Cash received through acquisition		7,336
Net cash used in investing activities		(43,832)
Cash flows from financing activities		
Contributions restricted for long-term use		67
Proceeds of debt issuance		67,559
Payment of long-term debt		(85,438)
Debt issuance costs		(547)
Net cash used in financing activities		(18,359)
Net increase in cash and cash equivalents		63,564
Cash and cash equivalents		
Beginning of year		110,301
End of year	$	173,865
Supplemental cash flow information		
Cash paid during the year for interest	$	19,459
Capital expenditures included in accounts payable		3,460
Increase in fair value of assets acquired		5,390
Assets acquired under capital lease		571

The accompanying notes are an integral part of these consolidated financial statements.

1. Organization

Fletcher Allen Partners, Inc. (FAP), established as of October 1, 2011, is a nonprofit, tax-exempt Vermont corporation and the sole corporate member of Fletcher Allen Health Care, Inc., and Central Vermont Medical Center, Inc. FAP's purpose is to establish an integrated regional health care system to engage in regional planning to develop a highly coordinated health care network that will improve the quality, increase the efficiencies, and lower the costs of health care delivery in the regions it serves.

Fletcher Allen Health Care, Inc (FAHC) is a tertiary care teaching hospital that, in affiliation with The University of Vermont (UVM), serves as Vermont's Academic Medical Center. As a regional referral center, FAHC provides advanced level care throughout Vermont and Northern New York, with a full time emergency department, also certified as a Level 1 Trauma Center. It is FAHC's mission to improve the health of the people in the communities that it serves by integrating patient care, education, and research in a caring environment. As a charitable organization, FAHC lives its mission through a number of community benefit programs, many done in collaborative partnership with other community based organizations. These include but are not limited to community wellness programs, education, direct grants, free access to a community health resource center, direct financial assistance to patients, and other subsidized programs.

FAHC is the sole member of the following subsidiaries: Fletcher Allen Health Ventures, Inc. (FAHV); University of Vermont Medical Group (UVM Medical Group); Fletcher Allen Coordinated Transport, LLC (FACT); Fletcher Allen Skilled Nursing Care, LLC (FASN); Fletcher Allen Health Care Foundation, Inc.; Fletcher Allen Executive Services, LLC (FAES) and VMC Indemnity Company Ltd. (VMCIC). Vermont Managed Care, Inc. (VMC) is a wholly owned subsidiary of FAHV. The following entities are partly owned or controlled by FAHC: Medical Education Center Condominium Association, Inc; OB Net Services, LLC; Copley Woodlands, Inc.; Fletcher Allen Medical Group, PLLC (FAMG); and OneCare Accountable Care Organization, LLC.

Central Vermont Medical Center, Inc. (CVMC) provides health care services under three distinct business units: Central Vermont Hospital, Woodridge Rehabilitation and Nursing, and Central Vermont Medical Group Practice. CVMC works collaboratively to meet the needs and improve the health of the residents of central Vermont. CVMC's hospital provides 24-hour emergency care, with a full spectrum of inpatient and outpatient services.

2. Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements have been prepared on the accrual basis of accounting and include the accounts of FAP and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation. The assets of members of the consolidated group may not be available to meet the obligations of another member of the group.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Significant estimates include the allowances for doubtful accounts and contractual allowances, receivables and accruals for estimated settlements with third-party payers, contingencies, self-insurance program liabilities, accrued medical claims, pension and postretirement costs, and the valuation of investments and interest rate swaps. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include all highly liquid investments with maturities of three months or less when purchased, excluding amounts classified as assets whose use is limited or restricted.

Most of FAP's banking activity, including cash and cash equivalents, is maintained with several national banks and from time to time cash deposits exceed federal insurance limits. It is FAP's policy to monitor these banks' financial strength on an ongoing basis.

Inventories

Inventories are stated using the lesser of average cost or market value.

Prepaid and Other Current Assets

Prepaid and other current assets include miscellaneous nonpatient receivables and prepaid expenses primarily related to software maintenance and other contracts. The carrying value of prepaid and other current assets is reviewed if the facts and circumstances suggest that it may be impaired.

Contributions

Unconditional promises to give that are expected to be collected within one year are recorded at their estimated net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of estimated future cash flows. The present value of estimated future cash flows has been measured at the time of the contribution using rates indicative of the market and credit risk associated with the contribution. Conditional promises to give are not included as support until the conditions are substantially met.

Investments and Investment Income

Investments in equity securities, mutual funds, and common collective trusts with readily determinable fair market values and all investments in debt securities are recorded at fair value. Investment income or loss (including realized gains and losses on investments, interest, and dividends), to the extent not capitalized, is included in nonoperating gains (losses), unless the income or gain (loss) is restricted by donor or law. Realized gains or losses on the sale of investments are determined by use of average costs. Unrealized gains and losses on investments carried at fair value are excluded from the excess of revenue over expenses and reported as an increase or decrease in net assets. Declines in fair value that are judged to be other-than-temporary are reported as realized losses.

Investments, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. As such, it is reasonably possible that changes in the values of investments will occur in the near term and that such changes could materially affect the amounts reported in the consolidated balance sheet and statements of operations and changes in net assets.

FAP reviews its investments to identify those for which fair value is below cost. FAP then makes a determination as to whether the investment should be considered other-than-temporarily impaired. FAP recognized $778,000 in losses related to declines in value that were other-than-temporary in nature in the year ended September 30, 2012.

Investment in Affiliates

Investments in noncontrolled affiliates are accounted for using the equity method of accounting and reported within investment in affiliated companies on the consolidated balance sheet. These include Starr Farm Partnership, OB NET Services, LLC, and OneCare Vermont Accountable Care Organization, LLC.

Assets Whose Use is Limited or Restricted

Assets whose use is limited or restricted primarily include board-designated assets, assets held by trustees under indenture agreements, donor-restricted assets, and restricted assets which are held for insurance-related liabilities. Board-designated assets may be used at the Board’s discretion.

Property and Equipment

Property and equipment acquisitions are recorded at cost or, in the case of gifts, at fair market value at the date of the gift. Depreciation is provided over the estimated useful life of each class of depreciable assets and is computed using the straight-line method. Equipment under capital lease obligations is amortized using the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the consolidated financial statements.

Depreciation is calculated using the following estimated useful lives:

Land improvements	15 – 25 years
Building and improvements	7 – 40 years
Fixed equipment	5 – 20 years
Major moveable equipment	2 – 20 years

Gifts of long-lived assets, such as land, buildings, or equipment, are reported as unrestricted support and are excluded from the excess of revenue 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 these long-lived assets must be maintained, expiration of donor restrictions is reported when the donated or acquired long-lived assets are placed in service.

Impairment of Long-Lived Assets

Long-lived assets to be held and used are reviewed for impairment whenever circumstances indicate that the carrying amount of an asset may not be recoverable. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value, less costs to sell.

Costs of Borrowing
Interest cost incurred on borrowed funds during the period of construction of capital assets, net of investment income on borrowed assets held by trustees, is capitalized as a component of the cost of acquiring those assets. Approximately $339,000 of interest was capitalized during the year ended September 30, 2012. Net deferred financing costs totaled $13,150,000 at September 30, 2012. Such amounts are reported within other assets and are amortized over the period the related obligations are outstanding using the effective interest method. Accumulated amortization of deferred financing costs totaled $9,746,000 at September 30, 2012.

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

Consolidated Statement of Operations
For purposes of display, transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported as unrestricted revenue and other support and expenses. Peripheral or incidental transactions are reported as nonoperating gains.

Excess of Revenue Over Expenses
The consolidated statement of operations includes excess of revenue over expenses. Changes in unrestricted net assets which are excluded from the excess of revenue over expenses, consistent with industry practice, primarily include unrealized gains and losses on investments (other than those on which other-than-temporary losses are recognized), contributions of long-lived assets (including assets acquired using contributions restricted by donors for acquiring such assets), and pension related adjustments.

Net Patient Service Revenue
Net patient service revenue is reported at the estimated net realizable amounts due from patients, third-party payers, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers. Under the terms of various agreements, regulations, and statutes, certain elements of third-party reimbursement are subject to negotiation, audit, and/or final determination by the third-party payers. In addition, laws and regulations governing Medicare and Medicaid programs are 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. Differences between amounts previously estimated for retroactive adjustments and amounts subsequently determined to be recoverable or payable are included in net patient service revenue in the year that such amounts become known. Changes in prior-year estimates increased net patient service revenue by approximately $12,723,000 in the year ended September 30, 2012.

FAP has agreements with third-party payers that provide for payments to FAP at amounts different from its established rates. A summary of the payment arrangements with major third-party payers follows:

Medicare
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. Inpatient rehabilitation services are paid based on a prospective per discharge methodology. These rates vary according to a patient classification system based upon services provided, the patient's level of functionality and other factors. Outpatient services are paid based upon a prospective standard rate for procedures performed or services rendered. FAP is reimbursed for cost-reimbursable items at tentative rates, with final settlement determined after submission of annual cost reports by FAP and audits thereof by the Medicare Audit Contractor (MAC). Medicare reimbursement for professional billings is determined by a standard fee schedule that is determined by the Centers for Medicare and Medicaid Services of the U.S. Department of Health and Human Services. The percentage of net patient service revenue derived from the Medicare program was approximately 28% in the year ended September 30, 2012.

Medicaid

Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. As with Medicare, reimbursement is based on a diagnosis-related group (DRG) system that is based on clinical, diagnostic, and other factors. For inpatient rehabilitation and neonatal cases, additional reimbursement is paid through a per diem add-on. For inpatient psychiatric cases, reimbursement is based on a per diem rate calculation, including adjustments for diagnostic factors and length of stay. Outpatient services rendered to Medicaid beneficiaries are paid based upon a prospective standard rate. Certain laboratory, mammography, therapy, and dialysis services are paid on a fee schedule. Medicaid reimbursement for professional services is determined by a standard fee schedule that is determined by the State of Vermont. The Vermont Medicaid program accounts for approximately 11% of FAP's net revenue in the year ended September 30, 2012.

Managed Care and Commercial Insurers

Services rendered to patients with commercial insurance are generally reimbursed at standard charges, less a negotiated discount or according to DRG or negotiated fee schedules. Approximately 46% of FAP's net revenues were derived from contracted insurers in the year ended September 30, 2012. Approximately 9% of FAP's net revenues were derived from noncontracted insurers in the year ended September 30, 2012.

VMC negotiates contracts with insurers and other payers for the provision of health care services through participating providers associated with its network. As a result, VMC is currently managing and/or has entered into contracts with managed care plans on behalf of FAP and its network providers. Under the terms of these agreements, VMC provides managed care services to subscribers of the managed care plans who select VMC as their primary health plan provider. Payments to FAP from VMC for services on behalf of respective managed care plan subscribers are based on a discounted fee for service or a predetermined fee schedule.

VMC has agreements with various Health Maintenance Organizations (HMOs) to provide medical services to subscribing participants. Under these agreements, VMC receives monthly capitation payments based on the number of each HMO's participants regardless of services actually performed. These revenues are subsequently disbursed to participating providers based on both discounted fee for service schedules and predetermined payment rates. Participating providers share a limited degree of risk through a set withhold that is only paid if cost and utilization targets are met.

Other Revenue
Other revenue consists primarily of research revenue, sales of pharmaceuticals and related products, cafeteria sales, meaningful use revenue under governmental Electronic Health Records Incentive programs, parking garage income, net assets released from restrictions used for operations, and rental income.

Research Grants and Contracts
Revenue related to research grants and contracts is recognized as the related costs are incurred. Indirect costs relating to certain government grants and contracts are reimbursed at fixed rates negotiated with the government agencies. Research grants and contracts are accounted for as exchange transactions. Amounts received in advance of incurring the related expenditures are recorded as unexpended research grants and are included within accrued expenses. Amounts expended in advance of the receipt of funding are included within patient and other trade accounts receivable.

Reserves for Outstanding Losses and Loss-Related Expenses for Malpractice Claims
The liabilities for outstanding losses and loss-related expenses and the related provision for losses and loss-related expenses include estimates for malpractice losses incurred but not reported, as well as losses pending settlement. Such liabilities are necessarily based on estimates and, while management believes the amounts provided are adequate, the ultimate liability may be in excess of or less than the amounts provided. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The methods for making such estimates and the resulting liability are actuarially reviewed on an annual basis and any adjustments required are reflected in current operations.

Income Taxes
FAP, FAHC, CVMC, UVM Medical Group, and FAMG are incorporated and recognized by the Internal Revenue Service (IRS) as tax-exempt under Section 501(c) (3) of the Internal Revenue Code (the “Code”). Accordingly, the IRS has determined that FAP, FAHC, CVMC, UVM Medical Group, and FAMG are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. FACT, FAES and FASN are single-member limited liability corporations. As such, for tax purposes, FACT, FAES, and FASN are treated as divisions of FAHC. No provision for federal income taxes has been recorded in the accompanying consolidated financial statements for these organizations.

FAHV and VMC are for-profit subsidiaries subject to federal and state taxation. The tax provisions and related tax assets and liabilities for these entities are not material to the consolidated financial statements.

For tax years beginning after December 15, 2008, nonpublic companies adopted guidance under ASC 740, *Income Taxes*, that prescribe a model for the recognition and measurement of uncertain tax benefits. This guidance did not have an impact on FAP and its subsidiaries.

VMCIC is currently not a taxable entity under the provisions of the territory of Bermuda and, accordingly, no provision for taxes has been recorded by VMCIC. In the event that such taxes are levied, VMCIC has received an undertaking from the Bermuda Government exempting it from all such taxes until 2016.

Asset Retirement Obligations

FAP recognizes a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. Uncertainty about the timing and/or method of settlement of a conditional asset retirement obligation is factored into the measurement of the liability when sufficient information exists. The types of asset retirement obligations that FAP considers are those for which it has a legal obligation to perform an asset retirement activity, however, the timing and/or method of settling the obligation are conditional on a future event that may or may not be within its control. The fair value of a liability for the legal obligation associated with an asset retirement is recorded in the period in which the obligation is incurred. When the liability is initially recorded, the cost of the asset retirement is capitalized.

The estimated future undiscounted value of the asset retirement obligation is approximately $1,272,000 at September 30, 2012, substantially all of which relates to the estimated costs to remove asbestos that is contained within FAP's facilities. The initial asset retirement obligation was calculated using a discount rate of 4.5%. The recorded asset retirement obligation at September 30, 2012 was approximately $1,082,000.

Defined Benefit Pension and Other Postretirement Benefit Plans

FAP recognizes the overfunded or underfunded status of its defined benefit pension and other postretirement benefit plans (collectively, "postretirement benefit plans") in the balance sheet. Changes in the funded status of the plans are reported in the year in which the changes occur as a change in unrestricted net assets presented below the excess of revenue over expenses in the consolidated statements of operations and changes in net assets.

Adoption of New Accounting Guidance

In August 2010, the Financial Accounting Standards Board issued Accounting Standards Update 2010-23 (ASU 2010-23), *Health Care Entities: Measuring Charity Care for Disclosure*. The standard provides for consistency in practice within charity care disclosures. Under the new guidance, charity care disclosures must be based on estimated costs of providing the services. The estimated costs must include direct and indirect costs, a description of the measurement approach used, and the amount of any funds received to offset or subsidize charity care services provided. ASU 2010-23 is effective for fiscal years beginning after December 15, 2010. Charity care disclosures for FAP adhere to this new guidance.

Additionally in August 2010, the Financial Accounting Standards Board issued Accounting Standards Update 2010-24 (ASU 2010-24), *Health Care Entities: Presentation of Insurance Claims and Related Insurance Recoveries*. The standard provides for consistency in accounting for malpractice claims and similar liabilities by health care entities. Under the new guidance, medical malpractice claims liabilities must be reported at gross and not offset by anticipated insurance recoveries. ASU 2010-24 is effective for fiscal years beginning after December 15, 2010. The adoption of the standard had no impact on excess of revenues over expenses. Included within prepaid and other current assets are $3,376,000 of reinsurance receivables as of September 30, 2012.

3. Formation of Fletcher Allen Partners, Inc.

On October 1, 2011 Fletcher Allen Health Care, Inc. (FAHC) and Central Vermont Medical Center, Inc., (CVMC) contributed their net assets to form Fletcher Allen Partners, Inc. (FAP). In accordance with applicable accounting guidance on not-for-profit mergers and acquisitions, FAP recorded contribution income of $61,589,000 reflecting the fair value of the contributed net assets of CVMC on the transaction date. Of this amount, $52,453,000 represents unrestricted net assets and is included as a nonoperating gain in the accompanying consolidated statement of operations. Temporarily restricted net assets and permanently restricted net assets of $6,035,000 and $3,101,000, respectively, were recorded as restricted contribution income in the accompanying consolidated statement of changes in net assets.

The consolidated statement of operations reflects the activity of FAHC and CVMC from the date of the transaction (October 1, 2011) to September 30, 2012. No consideration was exchanged for the net assets contributed. The fair value of assets, liabilities, and net assets contributed by CVMC at October 1, 2011 were as follows:

(in thousands)

Assets		
Cash and cash equivalents	$	7,336
Assets limited as to use and investments		40,120
Patient accounts receivable, net		16,352
Property plant and equipment		74,742
Other assets		8,571
Total assets acquired	$	147,121
Liabilities		
Accounts payable and accrued expenses	$	11,616
Estimated amounts due to third party payers		2,264
Long-term debt		31,463
Accrued pension and post-retirement benefits		39,158
Other liabilities		1,031
Total liabilities assumed		85,532
Net assets		
Unrestricted		52,453
Temporary restricted		6,035
Permanently restricted		3,101
Total net assets		61,589
	$	147,121

A summary of the financial results of CVMC included in the consolidated statement of operations and changes in net assets for the year ended September 30, 2012 is as follows:

(in thousands)

Total operating revenues	$	150,983
Total operating expenses		146,036
Operating income		4,947
Nonoperating gains		1,152
Excess of revenues over expenses		6,099
Net assets released from restriction used for capital purchases		190
Net unrealized gain on investments		1,788
Pension adjustment		(10,208)
Transfer of net assets		52,453
Increase in unrestricted net assets	$	50,322

4. Charity Care and Community Service

FAP provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because FAP does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

The amount of charges foregone for services and supplies furnished under FAP's charity care policy aggregated approximately $27,685,000.

Of FAP's total expenses reported of $1,115,483,000, an estimated $11,640,000 arose from providing services to charity patients. The estimated costs of providing charity services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on FAP's total expenses divided by gross patient service revenue. For the year ended September 30, 2012, FAP used $285,000 in charitable endowment earnings to help defray the costs of indigent care.

5. Assets Whose Use is Limited or Restricted

Assets whose use is limited or restricted at September 30, 2012 consisted of the following:

(in thousands)

Equities	$ 1,247
Mutual funds	98,922
Money market funds	22,006
Bonds and notes	41,865
Common collective trusts	253,633
Beneficial interest in perpetual trusts	10,093
Hedge Funds	2,229
Real estate	300
	430,295
Less: Current portion	(13,132)
	$ 417,163

Investment income and gains for the years ended September 30, 2012 consisted of the following:

(in thousands)

Nonoperating revenue and expenses	
Investment income	$ 7,386
Net realized gains	14,282
	21,668
Net change in unrealized gains on investments	30,945
Changes in temporarily restricted net assets	
Investment income	180
Net change in unrealized gains on investments	3,099
Net realized gains on investments	617
	3,896
Changes in permanently restricted net assets	
Change in beneficial interest in perpetual trusts	941
	$ 57,450

As a result of the recognition of $778,000 in losses related to declines in value that were other-than-temporary in nature during the year ended September 30, 2012, there were no investments that had a fair value less than cost at September 30, 2012.

The cost and estimated fair value of securities classified as available-for-sale by the organization, which excludes beneficial interest in perpetual trusts of $10,093,000, and includes short-term investments of $1,932,000 as of September 30, 2012, is as follows:

(in thousands)	Cost	Gross Unrealized Gains	Estimated Fair Value
Mutual funds	$ 91,027	$ 9,827	$ 100,854
Equities	1,073	174	1,247
Real estate	165	135	300
Hedge funds	2,143	86	2,229
Money market funds	22,006	-	22,006
Bonds and notes	41,439	426	41,865
Common collective trusts	218,061	35,572	253,633
	$ 375,914	$ 46,220	$ 422,134

6. Property and Equipment

A summary of property and equipment at September 30, 2012 is as follows:

(in thousands)	
Land	$ 13,526
Land improvements	14,119
Leasehold improvements	40,236
Buildings	568,057
Equipment, furniture, and fixtures	295,786
	931,724
Less: Accumulated depreciation	(472,163)
	459,561
Construction–in–progress	11,503
	$ 471,064

FAP wrote off approximately $3,683,000 in assets in the year ended September 30, 2012. In conjunction with these write offs, a gain on disposal of property and equipment of $218,000 was recorded, and is included in supplies and other expense. At September 30, 2012, FAP had commitments to purchase approximately $3,460,000 of property and equipment.

FAP recorded depreciation expense of $56,436,000 for the year ended September 30, 2012.

7. Investment in Affiliated Companies

Investment in affiliated companies at September 30, 2012 consisted of the following:

(in thousands)		
Starr Farm Partnership	$	4,914
OB Net Services, LLC		192
OneCare Vermont Accountable Care Organization, LLC		25
	$	5,131

Distributions from these affiliated organizations totaled $500,000 for the year ended September 30, 2012. FAP's share of the income of these affiliates is reported as other nonoperating gains and totaled approximately $701,000 for the year ended September 30, 2012.

Starr Farm Partnership's beginning net assets as of September 30, 2011, were $9,425,000. Summarized financial information from the unaudited financial statements of the Starr Farm Partnership as of and for the year ended September 30, 2012 was as follows:

(in thousands)	**Ownership Percentage**		**Total Assets**		**Net Assets**		**Change in Net Assets**
Starr Farm Partnership	50 %	$	10,880	$	9,827	$	402

The accompanying notes are an integral part of these consolidated financial statements.

8. Long-Term Debt

Long-term debt at September 30, 2012 consisted of the following:

(in thousands)

Vermont Educational and Health Buildings Financing Agency Hospital Revenue Bonds		
Series 2009A loan, fixed rate (5.08% to 7.23%), payable through 2024	$	12,642
Series 2009B loan, fixed rate (3.72% at September 30, 2012), payable through 2014		1,771
Series 2008A Bonds, variable rate (0.17% at September 30, 2012), payable through 2030		54,705
Series 2007A Bonds, fixed rate (4.00% to 4.75%), payable through 2037 (including unamortized premium of $93)		56,098
Series 2004B Bonds, fixed rate (4.00% to 5.50%), payable through 2035 (including unamortized premium of $130)		149,580
Series 2004A Bonds, fixed rate (3.00% to 5.00%), payable through 2025 (including unamortized premium of $1,098)		35,513
Series 2000A Bonds, fixed rate (5.50% to 6.13%), payable through 2028 (including unamortized discount of $174)		32,376
Series 1996 loan, fixed rate (4.23% at September 30, 2012), payable through 2021		11,052
Select Auction Variable-Rate Securities (SAVRS) 1994 Bonds, variable rate (4.93% at September 30, 2012), payable through 2013 (including unamortized discount of $35)		2,915
Other long-term debt		
KeyBank loan, fixed rate (3.49% at September 30, 2012), payable through 2023		53,110
KeyBank loan, fixed rate (2.90% at September 30, 2012), payable through 2022		1,750
People's United Bank loan, fixed rate (4.19% at September 30, 2012), payable through 2017		2,710
People's United Bank Revolving Line of Credit, variable rate (3.25% at September 30, 2012), payable through 2013		1,100
		415,322
Less: Current portion		(13,489)
Long–term debt	$	401,833

Fletcher Allen Obligated Group
Fletcher Allen Health Care and Central Vermont Medical Center presently are the sole members of the Fletcher Allen Obligated Group (Obligated Group).

On November 1, 2011, CVMC withdrew from the D-H Obligated Group, and was admitted as a member to the Obligated Group pursuant to the Obligated Group Master Trust Indenture. In connection with CVMC's admission to the Obligated Group, the Series 1996, 2009A and 2009B Bonds, totaling $27,875,000, issued by the D-H Obligated Group for benefit of CVMC was refinanced or modified such that it has become an obligation of the Obligated Group. The Master Trust Indenture contains provisions permitting the addition, withdrawal or consolidation of members of the Obligated Group under certain conditions. The Master Trust Indenture constitutes joint and several obligations of the members of Obligated Group.

For presentation purposes, the financial statements of the Obligated Group are presented from the date of affiliation (October 1, 2011) and not from the date of CVMC's admission into the Obligated Group. The inclusion of the one month (October 2011) is deemed immaterial for presentation purposes.

Revenue Bonds

On May 21, 2008, FAHC converted the Series 2004B auction rate bonds from 35-day variable-rate bonds to fixed-rate bonds through a mandatory tender of the bonds as provided for under the original bond agreement. The tender was financed through the reissuance of $160,525,000 of Series 2004B bonds as tax-exempt fixed-rate bonds, and a payment of $2,700,000 from FAHC's debt service reserve funds. The Series 2004B bonds require FAHC to maintain a debt service reserve fund. As of September 30, 2012, the reserve fund balance was approximately $13,924,000.

Also on May 21, 2008, FAHC in connection with the Vermont Educational and Health Buildings Financing Agency (the "Agency"), issued $54,705,000 of tax-exempt variable-rate hospital revenue bonds ("Series 2008A"), the proceeds of which were used to refund its Series 2000B bonds in the amount of $50,000,000, pay an early termination payment in the amount of $3,128,000 on a related interest rate swap, and pay issuance costs in the amount of $1,577,000. The Series 2008A bonds are collateralized by an irrevocable letter of credit from a bank in the amount of $55,334,000 (covers principal of $54,705,000 and interest of $629,000), which expires in 2016. The interest rate on the Series 2008A bonds is set weekly. Series 2008A bondholders have the option to put the bonds back to FAHC. Such bonds would be subject to remarketing efforts by FAHC's remarketing agent. To the extent that such remarketing efforts were unsuccessful, the nonmarketable bonds would be purchased from the proceeds of the letter of credit. Monthly payments of principal on the letter of credit borrowings would commence on the first calendar day of the first month that commences more than one year after the borrowing. Repayment in full of the letter of credit would be required by the earlier of four years from the date of the borrowing under the letter of credit or the stated expiration date, currently, April 30, 2016.

In conjunction with these transactions, the notional amount of the original swap agreement covering the 2004B bonds was reduced from $135,000,000 to $55,190,000 and transferred to 2008A bonds in exchange for the payment of $3,128,000.

FAHC and certain of its subsidiaries are obligated under various other revenue bonds, capital leases, and notes payable. Various trustee-held funds are required under the terms of the loan agreements. Under one of the loan agreements, a reserve fund is required only upon the failure to meet certain financial ratios. As of September 30, 2012, no funding has been required under this agreement.

FAHC has granted a mortgage on substantially all of its property and an interest in its gross receipts, as defined in connection with the issuance of its long-term debt.

Series 1996 Bond Refinancing
In November 2011, the Series 1996 Bonds were redeemed with the proceeds of a term loan made to CVMC by People's United Bank in the amount of $11,600,000. The term loan has a fixed rate of interest of 4.23% and matures November 1, 2021. Interest payments are made monthly and principal payments in the amount of $582,000 are made semi-annually each May and November, beginning May 1, 2012 and ending on November 1, 2021. The term loan is collateralized with assets, mortgage, and all other collateral securing repayment of the Obligation as defined in the Master Trust Indenture of the Obligated Group. This refinancing resulted in a loss on extinguishment of debt of $529,000.

Series 2000A Bond Partial Refunding
In December 2011, the Series 2000A Bonds with maturities from 2012 through 2023 were refunded and replaced with a taxable private placement loan in the aggregate principal amount of $54,175,000 with a final maturity date in December 2023. In addition, a portion of the Series 2000A Bonds maturing on December 1, 2027 was redeemed in the aggregate principal amount of $6,745,000. The remaining balance of the initial aggregate principal amount of the Series 2000A Bonds is $32,550,000 with maturities between December 2025 and December 2027. Bond issuance costs of $547,000 are recorded in deferred financing costs, net and will be amortized over the life of the loan. The Series 2000A Bonds were issued with an original issue discount totaling $917,044 which is recorded in long-term debt. The discount will be amortized using the effective interest method over the life of the respective Bonds. The partial refunding resulted in a loss on extinguishment of debt of $2,305,000.

Scheduled Maturities of Long-Term Debt
As of September 30, 2012, scheduled maturities of long-term debt, not including a net unamortized premium of $1,112,000, for the next five years and thereafter are as follows:

(in thousands)

Years Ending September 30		
2013	$	13,489
2014		12,429
2015		12,553
2016		12,972
2017		13,404
Thereafter		349,363
	$	414,210

Loan Covenants
Under the terms of a master indenture, FAHC and CVMC are required to meet certain covenant requirements. In addition, the indenture provides for restrictions on, among other things, additional indebtedness and dispositions of property.

Line of Credit
A bank line of credit exists with a maximum borrowing of $2,000,000. The line matures on May 30, 2013, and bears interest at the Wall Street Journal prime rate adjusted daily with a floor of 3.25%, with advances secured by a portion of board designated funds. The outstanding advance at September 30, 2012 was $1,100,000.

Letter of Credit
The 2008A letter of credit was not drawn upon as of September 30, 2012, and the scheduled maturities of long-term debt assumes the Series 2008A bonds are not put back to FAP. If the letter of credit was drawn upon, the repayment would begin one year and one day from the date of the letter of credit being drawn upon. The repayment schedule would occur over the remaining three years of the letter of credit term. The repayment of principal would be as follows: $21,176,000 in year two, $21,176,000 in year three and $12,353,000 in the final year.

9. Interest Rate Swap Agreements

FAHC utilizes interest rate swap agreements to manage interest rate risk related to the variable rate Series 2008A Bonds and variable rate SAVRS 1994 Bonds. These agreements had aggregate notional amounts of $55,190,000 and $5,750,000, respectively, as of September 30, 2012. Pursuant to each agreement, FAHC is obligated to pay the applicable swap counterparty amounts based on a fixed interest rate and is to receive payment from such swap counterparty based on variable interest rates.

FAHC and the counterparties in the interest rate swap agreements are exposed to credit risk in the event of nonperformance or early termination of the agreements. Under certain circumstances, FAHC may be required to post collateral to secure its obligations under the 1994 interest rate swap agreement. In addition, each agreement may be terminated following the occurrence of certain events, at which time FAHC may be required to make a termination payment to the applicable swap counterparty.

In connection with the issuance of the Series 2008A bonds, FAHC entered into two interest rate swap agreements in the notional principal amount of $27,595,000 each. Under these agreements, FAHC will pay a fixed rate of 3.76% on a notional amount equal to the outstanding amount of the Series 2008A bonds for the term of the Series 2008A bonds and receive an alternative floating rate derived from a LIBOR based formula, which may or may not equal the rate on the Series 2008A bonds. The termination date of these swap contracts is December 1, 2034.

FAHC and its counterparty under the 1994 swap agreement entered into a bilateral pledge agreement whereby, on a monthly basis, the counterparty calculates the aggregate exposure amount based on current market value of replacing the interest rate swap agreement with a like financial instrument should either party default. The replacement of fair value of the interest rate swap agreement with a like instrument would cause FAHC to pay approximately $128,000 at September 30, 2012, to the counterparty. The counterparty to the 1994 swap agreement has declared bankruptcy and FAHC has made payments to the trustee in the bankruptcy during the year ended September 30, 2012. FAHC's payment is based on a 4.93% interest rate; however, FAHC pays net the 35 day floating amount due from Lehman Brothers Special Finance, Inc. FAHC receives no payment from Lehman Brothers Special Finance, Inc. for this transaction. The termination date of the 1994 swap agreement is September 12, 2013.

The fair value of interest rate swap agreements at September 30 is as of follows:

(in thousands)	**Balance Sheet Location**	**Fair Value**
1994 Swap	Other long-term liabilities	$ (128)
2008A Swap	Other long-term liabilities	$ (14,214)

The effect of interest rate swap agreements on the consolidated statement of operations and changes in net assets for 2012 are as follows:

(in thousands)	**Location of Gain/Loss Recognized in Statement of Operations**	**Amount of Gain/Loss Recognized in Statement of Operations**
1994 Swap	Gain/Loss on interest rate swap contracts	$ 234
2008A Swap	Gain/Loss on interest rate swap contracts	(1,500)
		$ (1,266)

10. Operating Leases

FAP has entered into certain operating lease agreements for the rental of building space and equipment. Rental expense, inclusive of common area maintenance charges amounted to $12,654,000 for the year ended September 30, 2012.

Minimum future lease payments required under noncancelable operating leases at September 30, 2012, were as follows:

(in thousands)

Years Ending September 30	
2013	$ 7,578
2014	6,613
2015	6,045
2016	5,120
2017	2,473
Thereafter	3,960
	$ 31,789

11. Net Assets

Temporarily Restricted Net Assets

At September 30, 2012, temporarily restricted net assets are available for the following purposes:

(in thousands)

Indigent care	$	1,005
Education and research		10,951
Children's programs		2,437
Capital projects		710
Other health case services		10,501
Long-term care services at Woodridge		1,635
	$	27,239

At September 30, 2012, temporarily restricted net assets include approximately $16,126,000 of accumulated gains on permanently restricted net assets, which are subject to board appropriation in accordance with state law.

Permanently Restricted Net Assets
At September 30, 2012, income earned on permanently restricted net assets are restricted to:

(in thousands)

Indigent care	$	4,143
Education and research		6,902
Other health care services		17,391
Long-term care services		729
	$	29,165

Endowment Funds
FAP's endowment consists of approximately 79 funds established for a variety of purposes. FAP does not currently have any unrestricted funds designated by the Board of Trustees (the "Board") to function as endowment. Accordingly, for the purposes of this disclosure, endowment funds include only donor-restricted endowment funds. As required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law
FAP has interpreted state law as requiring realized and unrealized gains of permanently restricted net assets to be retained in a temporarily restricted net asset classification until appropriated by the Board and expended. State law allows the Board to appropriate the net appreciation of permanently restricted net assets as is prudent considering FAP's long and short-term needs, present and anticipated financial requirements, and expected total return on its investments, price level trends, and general economic conditions. In the year ended September 30, 2012, $751,000 was appropriated.

As a result of this interpretation, FAP classifies as permanently restricted net assets (a) the original value of the gifts donated to the permanent endowment when explicit donor stipulations requiring permanent maintenance of the historical fair value are present, and (b) the original value of subsequent gifts to the permanent endowment when explicit donor stipulations requiring permanent maintenance of the historical fair value are present. The remaining portion of the donor-restricted endowment fund is comprised of accumulated gains not required to be maintained in perpetuity. These amounts are classified as temporarily restricted net assets until those amounts are appropriated for expenditure in a manner consistent with the donor's stipulations. FAP considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: duration and preservation of the fund, purposes of the donor-restricted endowment funds, general economic conditions, the possible effect of inflation and deflation, and the expected total return from income and the appreciation of investments, other resources of FAP, and the investment policies of FAP.

Endowment Net Asset Composition and Changes in Endowment Net Assets
The following is a summary of the endowment net asset composition by type of fund at September 30, 2012, and the changes therein for the year then ended:

Endowment net asset composition by type of fund

(in thousands)	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
September 30, 2012				
Donor-restricted endowment funds	$ -	$ 16,126	$ 19,072	$ 35,198
Adjustments for funds with deficiencies	(44)	44	-	-
Total	$ (44)	$ 16,170	$ 19,072	$ 35,198

Changes in endowment net assets

(in thousands)	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets at September 30, 2011	$ -	$ 8,891	$ 15,839	$ 24,730
Acquired endowment net assets at October 1, 2011	(163)	4,408	3,101	7,346
Investment return				
Investment income	-	251	-	251
Net appreciation	-	3,555	-	3,555
Total investment return	-	3,806	-	3,806
Appropriations of endowment assets for expenditure	-	(751)	-	(751)
Adjustment for funds with deficiencies	119	(119)	-	-
Other	-	(65)	132	67
Endowment net assets at September 30, 2012	$ (44)	$ 16,170	$ 19,072	$ 35,198

Beneficial Interest in Perpetual Trusts
The above amounts exclude FAP's beneficial interest in perpetual trusts, which are not within management's investment control. Such beneficial interests totaled $10,093,000 at September 30, 2012.

Charitable Remainder Trust
FAP has received an irrevocable charitable remainder trust, for which FAP does not serve as trustee. For this trust, FAP recorded its beneficial interest in those assets as contributions revenue and pledges receivable at the present value of the expected future cash inflows. Trusts are recorded at the date FAP has been notified of the trust's existence and sufficient information regarding the trust has been accumulated to form the basis for an accrual. Changes in the value of these assets are recorded in either temporarily or permanently restricted net assets.

Funds with Deficiencies
From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor requires FAP to retain as a fund of perpetual duration. The deficiencies at September 30, 2012 were $44,000, associated with one permanently restricted endowment fund which is managed by a trustee outside of the control of FAP management.

Investment Return Objectives and Spending Policy
FAP has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to the programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity or for a donor-specified period(s). Under this policy, the endowment assets are invested in a manner to generate returns at least equal to and preferably greater than the consumer price index. To satisfy its return objective, FAP targets a diversified asset allocation that provides for a balanced portfolio.

12. Malpractice and Other Contingencies

Malpractice and Workers' Compensation
FAP is insured against malpractice losses under a claims-made insurance policy with VMCIC, its wholly owned subsidiary. VMCIC has reinsurance with commercial carriers for coverage above a self-insured retainage amount of $5,000,000 per claim with a $20,000,000 aggregate, with limits on such reinsurance. VMCIC provides claims-made coverage to certain affiliates of FAHC for periods prior to the merger that created FAHC. CVMC purchased comprehensive general and professional liability coverage on an occurrence basis and claims made basis, respectively, from a commercial insurance carrier during fiscal year 2012; however, as of September 30, 2012, tail coverage for CVMC is provided by VMCIC.

FAP is also self-insured for workers' compensation claims, and maintains an excess insurance policy to limit its exposure on claims up to $750,000 per occurrence in the year ended September 30, 2012, with a $25,000,000 aggregate.

The reserves for outstanding losses have been discounted at a rate of 3% at September 30, 2012, resulting in a reduction in the reserve of approximately $1,810,000 in the year ended September 30, 2012, for professional liability and a reduction in the reserve of approximately $310,000 at September 30, 2012, for worker's compensation.

As a result of changes in estimates of incurred events in prior years, primarily professional liability, the estimate of incurred losses increased by approximately $7,852,000 for the year ended September 30, 2012.

Employee Health and Dental Insurance
FAP maintains a self-insurance plan for employee health and dental insurance. Under the terms of the plan, employees and their dependents are eligible for participation and, as such, FAP is responsible for the administration of the plan and any resultant liability incurred. FAP maintained a stop-loss insurance policy to limit its exposure on cumulative claims between $100,000 and $150,000 per member per year in the year ended September 30, 2012, with a per-year benefit maximum equal to the amount of premiums paid under the policy. In addition to the self-insurance

plan, FAP maintained a commercial policy to limit its exposure on cumulative claims exceeding $225,000 per member per year for the year ended September 30, 2012.

Other Contingencies
FAP and its subsidiaries are parties in various legal proceedings and potential claims arising in the ordinary course of business. In addition, the health care industry as a whole is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations is subject to government review and interpretation, as well as regulatory actions, which could result in the imposition of significant fines and penalties, as well as significant repayments of previously billed and collected revenue from patient services. Management does not believe that these matters will have a material adverse effect on FAP's consolidated financial position or results of operations.

Collective Bargaining Agreements
FAHC is subject to a collective bargaining agreement with respect to its Registered Nurse ("RN") and Licensed Practical Nurse ("LPN") nursing staff. The current agreement runs through July 9, 2015, and covers approximately 1,697 staff at September 30, 2012. FAHC is also subject to a collective bargaining agreement with the technical bargaining unit. The current agreement runs from March 19, 2010 through March 1, 2013 and covers approximately 295 staff in various technical positions at September 30, 2012.

13. Statutory Capital and Surplus

VMCIC is registered under the Bermuda Insurance Act of 1978 and related regulations (the "Act") and is obligated to comply with various provisions of the Act regarding minimum levels of solvency and liquidity. Statutory capital and surplus at September 30, 2012, was $17,181,535. The required minimum statutory capital at September 30, 2012 was $3,263,597. The required minimum surplus as of September 30, 2012 was $2,263,597. In addition, a minimum liquidity ratio must be maintained whereby liquid assets, as defined by the Act, must exceed 75% of defined liabilities. The minimum required level of liquid assets was $24,617,240 at September 30, 2012. The measurement of this at September 30, 2012, is $50,004,522. FAP reports all of VMCIC's investments in marketable securities as restricted assets in the accompanying consolidated balance sheets.

14. Pension Plans and Other Postretirement Benefits

Fletcher Allen Healthcare Defined Benefit Pension and Postretirement Health Care Plans
Employees of the former Medical Center Hospital of Vermont (MCHV) are covered by a pension plan (the "FAHC Plan"), formerly the Pension Plan for Employees of Vermont Health Foundation, Inc. The FAHC Plan is a defined benefit final average pay plan, and the benefit accruals provided for a small group of grandfathered employees are based on a percentage of five year average pay. It is FAHC's policy to fund at least the required minimum contribution under Internal Revenue Code, Section 412.

The FAHC Plan was amended effective January 1, 1995, to provide for the continued participation in the FAHC Plan of any eligible employee who was a member on December 31, 1994, and who was an employee on January 1, 1995. The amendment also provided that no person could become a member on and after January 1, 1995. Effective July 1, 1996, the FAHC Plan was further amended to account for a curtailment of benefits for certain other employees.

In addition to providing pension benefits, FAHC sponsors a defined benefit postretirement health care plan for retired employees. Substantially all of FAHC's employees who are at least age 55 with 15 years of service and all employees who are eligible for retirement may become eligible for such benefits. The postretirement health care plan is contributory with retiree contributions adjusted annually. The marginal cost method is used for accounting purposes for postretirement healthcare benefits.

The premiums paid by retirees participating in the FAHC postretirement health care plan exceed the cost covered by FAHC. Therefore, the projected benefit obligation has been reduced to zero. A reconciliation of the changes in the FAHC defined benefit plan projected benefit obligations and the fair value of assets for the year ended September 30, 2012 is as follows:

(in thousands)	**FAHC Defined Benefit Plan**
Changes in benefit obligations	
Projected benefit obligations - beginning of year	$ (137,305)
Service cost	(527)
Interest cost	(7,194)
Benefits paid	6,908
Actuarial loss	(23,044)
Administrative expenses paid	442
Projected benefit obligation - end of year	(160,720)
Accumulated benefit obligation	(160,104)
Changes in plan assets	
Fair value of plan assets - beginning of year	105,826
Actual gain on plan assets	20,348
Contributions	5,975
Benefits paid	(6,908)
Administrative expenses paid	(442)
Fair value of plan assets - end of year	124,799
Funded status of the plan (long-term)	$ (35,921)

Unrestricted net assets at September 30, 2012 include unrecognized actuarial losses of $67,679,000 related to the defined benefit plan. Of this amount, $2,265,000 was recognized in net periodic pension costs in the year ended September 30, 2012. The reconciliation of the unrecognized actuarial losses for the year ended September 30, 2012, is as follows:

(in thousands)		
Unrecognized actuarial losses - beginning of year	$	59,527
Net loss amortized during year		(1,821)
Net loss during year		9,973
Unrecognized actuarial losses - end of year	$	67,679

The cost components of the net periodic benefit cost for the year ended September 30, 2012 are as follows:

(in thousands)		**FAHC Defined Benefit Plan**
Service cost	$	527
Interest cost		7,194
Expected return on plan assets		(7,277)
Amortization of unrecognized net loss		1,821
Net periodic benefit cost	$	2,265

The assumptions used in accounting for the defined benefit pension plan are as follows:

	FAHC Defined Benefit Plan
Weighted-average assumptions used to determine the benefit liability	
Discount rates	4.03 %
Rates of increase in future compensation levels	3.50
Weighted-average assumptions used to determine expense	
Discount rates	5.39
Rates of increase in future compensation levels	3.50
Expected long-term rate of return on plan assets	7.00

The expected long-term rate of return for the FAHC Plans' total assets is based on the expected return of each of its asset categories, weighted based on the median of the allocation for each class. Equity securities are expected to return 9% to 11% over the long-term, while cash and fixed income is expected to return between 5% and 6%. Based on historical experience, FAHC expects that the plans' asset managers will provide a modest (0.5% to 1.0% per annum) premium to their respective market benchmark indices.

Plan Assets

FAHC's pension plan weighted-average asset allocations as of September 30, 2012, by asset category, are as follows:

Asset Category	
Money market	1 %
Mutual funds	12
Common collective trusts	87
	100 %

The following table presents information, as of September 30, 2012, about FAHC's pension assets that are measured at fair value on a recurring basis:

(in thousands)	**Quoted Prices in Active Markets (Level 1)**	**Other Observable Inputs (Level 2)**	**Unobservable Inputs (Level 3)**	**Fair Value**
2012				
Money market	$ 1,063	$ -	$ -	$ 1,063
Mutual funds	14,818	-	-	14,818
Common collective trusts	-	108,918	-	108,918
Total	$ 15,881	$ 108,918	$ -	$ 124,799

The investment strategy established by FAP's Finance Committee for pension plan assets is to meet present and future benefit obligations to all participants and beneficiaries, cover reasonable expenses incurred to provide such benefits, and provide a total return that maximizes the ratio of assets to liabilities by maximizing investment return at the appropriate level of risk.

There was no Level 3 activity for the year ended September 30, 2012.

Cash Flows - Contributions
FAHC expects to contribute $6,000,000 to its pension plan in the year ending September 30, 2013.

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

(in thousands)

Years Ending September 30	
2013	$ 8,212
2014	8,702
2015	9,110
2016	9,490
2017	9,819
2018–2022	51,589

Central Vermont Medical Center Defined Benefit Pension Plan
Most employees of CVMC who meet certain age and service requirements are covered by a defined benefit pension plan. The benefits are based on years of service and the employee's average compensation. Contributions are intended to provide not only the benefits attributed to the service to date, but also for those expected to be earned in the future. It is CVMC's intent to fund at least the required minimum contribution under Internal Revenue Code, Section 412.

CVMC froze the defined benefit pension plan for employees under the age of 50, effective January 1, 2012. The defined benefit pension plan will continue to accrue and vest for future services for employees who are participants of the plan and are 50 years and older before January 1, 2012. For employees who are participants of the defined benefit plan and are under 50 years of age before January 1, 2012, accruing and vesting of services under this plan were frozen as of January 1, 2012. The employees along with newly hired employees are covered under a CVMC sponsored ERISA defined contribution pension plan. The defined contribution plan is an IRS Section 403(b) retirement plan in which CVMC contributes and matches discretionary and nondiscretionary funds in accordance with plan participation guidelines.

The following table sets forth the change in the projected benefit obligation and in fair value of the CVMC defined benefit pension plan assets based on the measurement date as of September 30, 2012:

(in thousands)	**CVMC Defined Benefit Plan**
Changes in benefit obligations	
Projected benefit obligations - beginning of year	$ (94,645)
Service cost	(3,930)
Interest cost	(4,942)
Benefits paid	2,788
Actuarial loss	(17,746)
Administrative expenses paid	272
Projected benefit obligation - end of year	(118,203)
Accumulated benefit obligation	(110,052)
Changes in plan assets	
Fair value of plan assets - beginning of year	55,487
Actual gain on plan assets	10,074
Contributions	10,041
Benefits paid	(2,788)
Administrative expenses paid	(272)
Fair value of plan assets - end of year	72,542
Funded status of the plan (long-term)	$ (45,661)

Unrestricted net assets at September 30, 2012 include unrecognized actuarial losses of $37,592,000 related to the defined benefit plan. Of this amount, $6,190,000 is recognized in net periodic pension costs in the year ending September 30, 2012. The reconciliation of the unrecognized actuarial losses for the year ended September 30, 2012, is as follows:

(in thousands)		
Unrecognized actuarial losses - beginning of year	$	27,237
Net loss amortized during year		(1,671)
Net prior service cost amortized during year		(107)
Net loss during year		12,133
Unrecognized actuarial losses - end of year	$	37,592

The cost components of the net periodic benefit cost for the years ended September 30, 2012 are as follows:

(in thousands)		**CVMC Defined Benefit Plan**
Service cost	$	3,930
Interest cost		4,942
Expected return on plan assets		(4,460)
Amortization of unrecognized net loss		1,671
Amortization of prior service cost		107
Net periodic benefit cost	$	6,190

The assumptions used in accounting for the defined benefit pension plan are as follows:

	CVMC Defined Benefit Plan
Weighted-average assumptions used to determine the benefit liability	
Discount rates	4.15 %
Rates of increase in future compensation levels	3.75
Weighted-average assumptions used to determine expense	
Discount rates	5.30
Rates of increase in future compensation levels	3.75
Expected long-term rate of return on plan assets	8.00

The expected long-term rate of return for the Plan's total assets is based on the expected return of each of its asset categories, weighted based on the median of the allocation for each class. Equity securities are expected to return 9% to 11 % over the long-term, while cash and fixed income is expected to return between 4% and 6%. Based on historical experience, CVMC expects that the plan's asset managers will provide a modest (0.5% to 1.0% per annum) premium to their respective market benchmark indices.

Plan Assets

CVMC's pension plan weighted-average asset allocations as of September 30, 2012, by asset category, are as follows:

Assets Category	
Bonds	40 %
Equities	39
Real estate	8
Mutual funds	13
	100 %

The following table presents information as of September 30, 2012, about CVMC's pension assets that are measured at fair value on a recurring basis:

(in thousands)	**Quoted Prices in Active Markets (Level 1)**	**Other Observable Inputs (Level 2)**	**Unobservable Inputs (Level 3)**	**Fair Value**
Bonds	$ 17,502	$ 11,770	$ -	$ 29,272
Equities	23,436	4,687	-	28,123
Real estate	5,750	-	-	5,750
Mutual funds	9,397	-	-	9,397
Total	$ 56,085	$ 16,457	$ -	$ 72,542

The investment strategy established by FAP's Finance Committee for pension plan assets is to meet present and future benefit obligations to all participants and beneficiaries, cover reasonable expenses incurred to provide such benefits, and provide a total return that maximizes the ratio of assets to liabilities by maximizing investment return at the appropriate level of risk.

There was no Level 3 activity for the years ended September 30, 2012.

Cash Flows - Contributions

CVMC expects to contribute $5,200,000 to its pension plan in the year ending September 30, 2013.

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

(in thousands)

Years Ending September 30		
2013	$	3,175
2014		3,575
2015		3,900
2016		4,475
2017		5,275
2018–2022		35,775

Other FAP Retirement Plans
The plans that follow are other retirement plans that are not defined benefit plans. These plans are described in the remainder of the footnote, followed by required disclosures of total retirement benefit costs.

Medical Center of Vermont (MCHV) - Retirement Plan
A tax-sheltered annuity benefit plan is maintained covering substantially all of the employees of the former MCHV who have at least one year of continuous service. Contributions are determined based on a percentage of employees' salaries up to 1.5% of pay.

Fanny Allen Hospital (FAH) - Pension Plan
Substantially all of the employees of the former FAH were covered by a defined contribution retirement plan. Eligibility begins after one year of service. A contribution of 4% of each eligible employee's compensation is made to the plan. A tax-deferred annuity plan covering substantially all employees is also provided. Matching contribution is discretionary.

The plan was amended on January 1, 1996, to discontinue all contributions effective July 1, 1996. All participants became 100% vested as of that date. The amendment also provided that no person may become a member on and after January 1, 1996.

University Health Center (UHC) - Retirement Plan
A tax-sheltered annuity benefit plan is maintained covering substantially all of the employees of the former UHC who have at least two years of continuous service. Contributions are determined based on a percentage of employees' salaries.

Fletcher Allen Healthcare, Inc. - Retirement Plan
In accordance with ERISA guidelines, FAHC provided a new retirement plan for employees of the former MCHV, FAH, and UHC, effective July 1, 1996. FAHC maintains a tax-sheltered annuity benefit plan covering substantially all of its employees who have at least six months of continuous service. Contributions are determined based on a percentage of employees' salaries up to 10% of pay.

Central Vermont Medical Center Retirement Plan

In accordance with ERISA guidelines, CVMC provided a new retirement plan effective January 1, 2012. CVMC maintains a tax sheltered annuity benefit plan for its employees. Employees who were not grandfathered into the Defined Benefit Plan, and who have met eligibility requirements, receive discretionary and nondiscretionary contributions based on a percentage of their salaries up to 6% of pay.

Benefit Plan Costs

FAP generally funds the benefit costs related to the above retirement plans, including defined contribution plans and postretirement benefit plans, as incurred. Benefit plan costs amounted to $37,992,000 for the year ended September 30, 2012.

15. Concentrations of Credit Risk

FAP grants credit without collateral to its patients, most of whom are local residents and are insured under third-party agreements. The mix of gross receivables from patients and third-party payers at September 30, 2012 is as follows:

Medicare	23 %
Medicaid	10
Blue cross	15
Other third-party payers	31
Patients	21
	100 %

16. Transactions With UVM

FAHC has an Affiliation Agreement with UVM that was most recently renewed as of August 1, 2010, for a five year term. The Agreement automatically renews for subsequent five-year terms unless either party gives written notice of nonrenewal at least one year prior to the end of a five-year term. The Affiliation Agreement expresses the shared goals of UVM and FAHC for teaching, clinical care and research, documents the many points of close collaboration between the two organizations, provides the underpinnings for FAHC's status as an academic medical center, and obligates FAHC to provide substantial, annual financial support to UVM.

Under the Affiliation Agreement, UVM recognizes UVM Medical Group, a FAHC subsidiary, as the clinical practice group for physician faculty of UVM's College of Medicine, and FAHC agrees to meet its physician-employee staffing needs primarily through physicians who are employed by UVM Medical Group and are eligible for faculty appointments to the College of Medicine. The Agreement provides that the chairs of academic departments in the College of Medicine will be appointed by FAHC as the clinical leaders of the corresponding clinical services.

The current Affiliation Agreement provides for four components of financial support to UVM: (1) monthly payments by FAHC, known as the "commitment," to fund a portion of the salary, benefits and related expenses paid through UVM to physician-faculty who are jointly employed by both UVM and UVM Medical Group; (2) an academic support payment paid by FAHC; (3) a Dean's Tax paid by UVM Medical Group; and (4) reimbursement by FAHC of certain UVM expenses for joint functions.

The commitment is an annual undertaking by FAHC to fund a portion of the salary, benefits and related expenses of physician-faculty paid through UVM's payroll process. The minimum commitment payment for each full-time faculty member is $30,000 for salary plus the cost of UVM benefits. The total amount of the commitment is subject to variation each year based upon the needs of FAHC and UVM for physician staffing; the availability of funding sources apart from FAHC to pay for such personnel; and the allocation of the time and effort of physician-faculty among clinical, teaching, research and administrative activities. The amounts of the commitment for physician-faculty salaries and fringe benefits approximated $20,235,000 in the year ended September 30, 2012. In addition, FAHC reimburses UVM for equipment rental, research, and certain other administrative expenses through the commitment.

In addition to the commitment, FAHC also makes academic support payments. The academic support payment is paid to UVM in monthly installments. The amount of the academic support payment was $4,837,000 in the year ended September 30, 2012. This payment increases to $4,927,000 for the year ending September 30, 2013 and includes a $434,000 payment to support UVM's Dana Medical Library. The payment increases on each anniversary date of the Agreement by a percentage published by the Centers for Medicare and Medicaid Services, if available, or by the percentage increase in FAHC's Medicare inpatient hospital reimbursement.

Under the Affiliation Agreement, the Dean's Tax is paid to UVM by FAHC in an amount equal to the greater of two percent (2.0%) of the Medical Group's net patient service revenues for that fiscal year or $4,600,000. The amount of the Dean's Tax was $4,624,000 in the year ended September 30, 2012. Approximately 50% of the Dean's Tax may be expended, with the approval of the Dean, on research and education initiatives of FAHC's health care services as long as the research and education initiatives are consistent with the shared goals within the Affiliation Agreement. For the year ended September 30, 2012, approximately $32,000 of the $4,624,000 Dean's Tax was appropriated to research and education initiatives within FAHC.

In addition to providing financial support of UVM's Dana Medical Library, FAHC also pays UVM's Institutional Review Board a fee, currently $2,500 per review, for review of clinical trials and reimburses UVM for its expenses in the administration of FAHC-conducted clinical trials.

17. Functional Expenses

FAP provides general health care services to residents within its geographic location. Expenses related to providing these services for the year ended September 30, 2012, are as follows:

(in thousands)

Education and research	$ 1,788
Health care services	763,112
Management and general	352,209
Total functional expenses	1,117,109
Less: Nonoperating expenses	1,626
Total operating expenses	$ 1,115,483

18. Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (also referred to as an “exit price”). A fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. In determining fair value, the use of various valuation approaches, including market, income, and cost approaches, is permitted.

GAAP establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity’s own assumption about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

FAP uses the following fair value hierarchy to present its fair value disclosures:

Level 1 - Quoted (unadjusted) prices for identical assets or liabilities in active markets. Active markets are those in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 - Other observable inputs, either directly or indirectly, including:

- Quoted prices for similar assets in active markets
- Quoted prices for identical or similar assets in nonnative markets (few transactions, limited information, noncurrent prices, high variability over time)
- Inputs other than quoted prices that are observable for the asset (interest rates, yield curves, volatilities, default rates)
- Inputs that are derived principally from or corroborated by other observable market data

Level 3 - Unobservable inputs that cannot be corroborated by observable market data.

The following is a description of the valuation methodologies used for assets and liabilities measured at fair value:

Mutual Funds
The fair values of mutual funds are based on quoted market prices for identical assets in active markets.

Money Market Funds
The fair values of money market funds are based on quoted market prices.

Bonds and Notes
The estimated fair values of debt securities are based on quoted market prices and/or other market data for the same or comparable instruments and transactions in establishing the prices. The marketable debt securities classified as Level 2 were classified as such due to the usage of observable market prices for similar securities that are traded in less active markets or when observable market prices for identical securities are not available. Marketable debt instruments are priced using: nonbinding market consensus prices that are corroborated with observable market data; quoted market prices for similar instruments; or pricing models, such as a discounted cash flow model, with all significant inputs derived from or corroborated with observable market data. These Level 2 debt securities primarily include corporate bonds, notes and other debt securities.

Common Collective Trusts and Hedge Funds
The estimated fair values of common collective trusts and hedge funds are determined based upon the net asset value ("NAV") provided by the fund managers and assessed for reasonableness by management. Such information is generally based on the pro-rata interest in the net assets of the underlying investments. There are no unfunded commitments or liquidity restrictions related to these common collective trusts at September 30, 2012. FAP is able to redeem its investment in hedge funds on a calendar quarter basis after providing 90 days notice.

Beneficial Interest in Perpetual Trusts
The estimated fair values of FAP's beneficial interests in perpetual trusts are determined based upon information provided by the trustees and assessed for reasonableness by management. Such information is generally based on the pro-rata interest in the net assets of the underlying investments, which approximates fair value.

Interest Rate Swap Agreements
Interest rate swap agreements are valued at the present value of the estimated series of cash flows resulting from the exchange of fixed rate payments for floating rate payments from the counterparty over the remaining life of the contract from the balance sheet date. Each floating rate payment is calculated based on forward market rates at the valuation date for each respective payment date. The valuation based on the estimated series of cash flows is obtained from third parties and assessed by management for reasonableness. Because the inputs used to value the contract can generally be corroborated by market data, the fair value is categorized as Level 2.

Long-Term Debt
The estimated fair values of FAP's long-term debt is based on current traded value or a discounted cash flow private placement debt. Such amounts at September 30, 2012, are approximately $355,212,000.

The following table presents information as of September 30, 2012, about FAP's financial assets and liabilities that are measured at fair value on a recurring basis:

(in thousands)	**Quoted Prices in Active Markets (Level 1)**	**Other Observable Inputs (Level 2)**	**Unobservable Inputs (Level 3)**	**Fair Value**
Mutual funds	$ 72,319	$ 28,535	$ -	$ 100,854
Equities	1,247	-	-	1,247
Money market funds	22,006	-	-	22,006
Hedge funds	-	-	2,229	2,229
Bonds and notes	7,731	34,134	-	41,865
Common collective trusts	-	253,633	-	253,633
Beneficial interest in perpetual trusts	-	-	10,093	10,093
Real estate	-	300	-	300
	$ 103,303	$ 316,602	$ 12,322	$ 432,227
Interest rate swap agreements	$ -	$ 14,342	$ -	$ 14,342

A roll forward of Level 3 (defined above) for the year ended September 30, 2012, is as follows:

(in thousands)	**Beneficial Interest in Perpetual Trusts**	**Hedge Funds**	**Total Level 3 Assets**
Beginning of year	$ 9,152	$ -	$ 9,152
Purchases	-	2,254	2,254
Sales	-	(111)	(111)
Unrealized gains	952	86	1,038
Unrealized losses	(11)	-	(11)
End of the year	$ 10,093	$ 2,229	$ 12,322
Increase in fair value of Level 3 investments held at September 30, included in the statement of changes in net assets	$ 941	$ 86	$ 1,027

19. Pledges Receivable

Pledges receivable represent unconditional promises to give and are net of allowances for uncollectible amounts. Pledges are recorded at the present value of their estimated future cash flows, which has been measured at the time of the contribution using rates indicative of the market and credit risk associated with the pledge. Pledges collectible within one year are classified as other current assets and total $940,000 as of September 30, 2012. Estimated cash flows due after one year are discounted using a risk adjusted rate for the year ended September 30, 2012.

Pledges are expected to be collected as follows:

(in thousands)

Amounts due		
Within one year	$	986
In one to five years		342
In more than five years		648
		1,976
Less: Unamortized discount		359
		1,617
Less: Allowance for uncollectables		93
Net pledges receivables	$	1,524

20. Allowance for Doubtful Accounts

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, FAP analyzes its past history and identifies trends for each of its major categories of revenue (inpatient, outpatient, and professional) to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major categories of revenue in evaluating the sufficiency of the allowance for doubtful accounts. Throughout the year, FAP, after all reasonable collection efforts have been exhausted, will write off the difference between the standard rates (or discounted rates if negotiated) and the amounts actually collected against the allowance for doubtful accounts. In addition to the review of the categories of revenue, management monitors the write offs against established allowances as of a point in time to determine the appropriateness of the underlying assumptions used in estimating the allowance for doubtful accounts.

Accounts receivable, prior to adjustment for doubtful accounts, is summarized as follows at September 30, 2012:

(in thousands)

Receivables		
Patients	$	34,034
Third-party payers		125,477
	$	159,511

The allowance for doubtful accounts is summarized as follows at September 30, 2012:

(in thousands)

Allowance for doubtful accounts		
Patients	$	9,749
Third-party payers		16,823
	$	26,572

Bad debt expense for nonpatient related accounts receivable is reflected in total operating expenses on the statement of operations. Patient related bad debt is reflected as a reduction in patient service revenues on the statement of operations.

Net patient service revenue before the provision for bad debts for the years ended September 30, 2012, is summarized as follows:

(in thousands)

Net patient service revenue		
Patients	$	38,817
Third-party payers		998,442
	$	1,037,259

21. Subsequent Events

FAP has evaluated subsequent events through December 21, 2012, which is the date the financial statements were issued and has concluded that aside from the following item, there were no such events that require adjustments to the consolidated financial statements or disclosure in the notes to the consolidated financial statements.

On July 1, 2012, FAP approved an affiliation agreement between FAP and Community Providers, Inc. (“CPI”). Under the terms of this agreement, FAP will become the sole corporate member of CPI, continuing to serve its purpose of establishing an integrated regional health care system. This agreement was subject to due diligence and regulatory approval which was completed in the quarter ending December 31, 2012. CPI is the parent organization of Champlain Valley Physicians Hospital Medical Center (CVPH) in Plattsburgh, NY and Elizabethtown Community Hospital (ECH) in Elizabethtown, NY. With approval pending from the New York State Department of Health, the anticipated effective date of affiliation is January 1, 2013.

Fletcher Allen Partners, Inc. and Subsidiaries
Schedule of Expenditures of Federal Awards
Year Ended September 30, 2012

Federal Agency/Program	Federal CFDA No.	Pass-Through Awards Organization	Pass-Through Awards Number	Total Expenditures
U.S. Department of Health and Human Services				
Direct Awards				
OP Early Intervention Services	93.918	N/A	N/A	$ 584,819
Total Direct Awards				584,819
Passed through other organizations				
Public Health Emergency Prepardness	93.069	VT Dept of Health		12,160
Prevention of Complications of Hemophilia	93.110	UMASS-Worcester Medical School	6H30MC00037-13-03	22,900
CDC	93.110	VT Dept of Health	03420-XXXXs	11,376
Maternal & Child Health Fed Consolidated Program	93.110	VT Dept of Health	03420-5764S	5,000
	93.110 Total			39,276
Disabilities Prevention	93.184	VT Dept of Health	6137309/RF52012087	16,240
Universal Newborn Hearing Screening	93.251	VT Dept of Health	03420-5416	95,536
Universal Newborn Hearing Screening	93.251	VT Dept of Health	03420-5555S	28,151
Universal Newborn Hearing Screening	93.251	VT Dept of Health	03420-5780S	293,848
Universal Newborn Hearing Screening	93.251	VT Dept of Health	03420-5957S	62,908
	93.251 Total			480,443
Poison Control and Stabilization Program	93.253	Northern New England Poison Control Center		(426)
Poison Control and Stabilization Program	93.253	Northern New England Poison Control Center		45,527
	93.253 Total			45,101
Gynological Oncology Group	93.395	HRI Roswell Park Cancer Institute Division	5U10CA027469-31	37,441
CD10-10011 Strengthening Public Health Infrastructure for Improved Health Outcomes	93.507	VT Dept of Health	03420-5793S	5,118
Refugee Preventative Health Discretionary Grant	93.576	VT Dept of Health	03420-5794S	4,435
BluePrint for Health	93.778	VT Dept of Health	03420-5384	85
BluePrint for Health	93.778	VT Dept of Health	03410-6111-11	16,910
	93.778 Total			16,995
Emergency Training	93.889	VT Dept of Health	03420-5810S	26,011
Emergency Training	93.889	VT Dept of Health	03420-5979S	2,119
VT Bioterrorism Preparedness Program	93.889	VT Dept of Health	03420-5811S	63,035
	93.889 Total			91,165
Ryan White Title 2 69-170	93.917	VT Dept of Health	03420-5918P	50,675
Ryan White Title 2 69-170	93.917	VT Dept of Health	03420-5713P	191,693
	93.917 Total			242,368
SAFE Title II Grant	93.940	VT Dept of Health	03420-5638P	43,627
SAFE Title II Grant	93.940	VT Dept of Health	03420-5827P	45,950
	93.940 Total			89,577
OADAP Day One Program	93.959	VT Dept of Health	03420-A13050P	6,025
OADAP Day One Program	93.959	VT Dept of Health	03420-A11109P	19,389
	93.959 Total			25,414
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-5849S	40,000
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-xxxxs	10,000
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-5843S	105,042
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-5579S	384
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-xxxxs	35,014
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-5717S	39,761
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-5755S	8,405
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-5878S	15,000
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-5954S	12,041
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-5699S	(10,000)
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-xxxxs	20,399
MCH Services Title V Block Grant Program	93.994	VT Dept of Health	03420-5763S	55,030
	93.994 Total			331,076
Total passed through other organizations				1,436,809
Total U.S. Department of Health and Human Services				2,021,628
U.S. Department of Transportation				
Passed through other organizations				
Governor's Highway Safety	20.600	VT Dept of Public Safety	02140-1012-6219	90,702
Governor's Highway Safety	20.600	VT Dept of Public Safety	02140-1111-6000	47,108
	20.600 Total			137,810
Governor's Highway Safety	20.613	VT Dept of Public Safety	02140-1112-6000	141,579
Total passed through other organizations				279,389
Total U.S. Department of Transportation				279,389
Total Expenditures of Federal Awards				$ 2,301,017

The accompanying notes are an integral part of the schedule of expenditures of federal awards

Fletcher Allen Partners, Inc. and Subsidiaries
Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2012

1. Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards presents the federal grant transactions of the Organization for the year ended September 30, 2012.

Federal program expenditures included in the accompanying schedule are presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations.* Therefore, some amounts presented in the schedule may differ from amounts presented in or used in the preparation of the basic financial statements. Full CFDA and pass through numbers are provided where available. Negative amounts represent adjustments to prior reported amounts in the normal course of business.

2. Subrecipients

During fiscal 2012, the Organization provided $162,733 to subrecipients of the OP Early Intervention Services award (CFDA #93.918) as follows. These amounts are included in the accompanying Schedule of Expenditures of Federal Awards:

Brattleboro Memorial Hospital	$ 82,074
Northern Counties Health Care, Inc.	33,364
Rutland Regional Medical Center	47,295
	$ 162,733

Part II

Reports on Compliance and Internal Controls

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

To the Board of Trustees of
Fletcher Allen Partners, Inc.:

We have audited the consolidated financial statements of Fletcher Allen Partners, Inc. and its Subsidiaries ("the Organization") as of and for the year ended September 30, 2012, and have issued our report thereon dated December 21, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Organization's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Organization's consolidated financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

PricewaterhouseCoopers LLP, 125 High Street, Boston, MA 02110
T: (617) 530 5000, F: (617) 530 5001, www.pwc.com/us

Compliance and Other Matters

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

We noted certain matters that we reported to management of the Organization in a separate letter dated November 27, 2012.

This report is intended solely for the information and use of the Organization's management, the Organization's Board of Trustees, state and federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

PricewaterhouseCoopers LLP

December 21, 2012

Report of Independent Auditors on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133

To the Board of Trustees of
Fletcher Allen Partners, Inc.:

Compliance

We have audited the compliance of Fletcher Allen Partners, Inc. and its Subsidiaries ("the Organization") with the types of compliance requirements described in the Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2012. The Organization's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Organization's management. Our responsibility is to express an opinion on the Organization's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations.* Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Organization's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Organization's compliance with those requirements.

In our opinion, the Organization complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2012.

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Internal Control Over Compliance

Management of the Organization is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Organization's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly we do not express an opinion on the effectiveness of the Organization's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the Organization's management, the Organization's Board of Trustees, state and federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

PricewaterhouseCoopers LLP

February 8, 2013

Part III

Federal Award Findings and Questioned Costs

Fletcher Allen Partners, Inc. and Subsidiaries
Schedule of Findings and Questioned Costs
Year Ended September 30, 2012

I. Summary of Auditor's Results

Financial Statements

Type of auditor's report issued:	Unqualified	
Internal control over financial reporting: Material weakness(es) identified	___ yes	_x_ no
Significant deficiency(ies) identified that are not considered to be material weaknesses?	___ yes	_x_ none reported
Noncompliance material to financial statements noted?	___ yes	_x_ no

Federal Awards

Internal control over major programs: Material weakness(es) identified?	___ yes	_x_ no
Significant deficiency(ies) identified that are not considered to be material weakness(es)?	___ yes	_x_ none reported
Type of auditor's report issued on compliance for major programs	Unqualified	
Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of OMB Circular A-133?	___ yes	_x_ no

Identification of major programs

Name of Federal Program	CFDA No.
OP Early Intervention Services	93.918
MCH Services Title V Block Grant Program	93.994
Governor's Highway Safety	20.600

Dollar Threshold used to Distinguish Type A and Type B Programs:	$300,000	
Auditee qualifies as a Low-Risk Auditee?	_x_ yes	___ no

II. Findings Related to Financial Statements

No findings have been reported.

III. Federal Award Findings and Questioned Costs

Part A - No findings have been reported by PricewaterhouseCoopers, LLP.

Part B – Other matters:

During the year ended September 30, 2012, the State of Vermont Department of Public Safety performed an audit of the Governor's Highway Safety programs (CDFA's #20.600 and #20.613) in the normal course of business. The Vermont state auditor prepared a letter dated October 18, 2012, inquiring about certain expenditures as the Organization administered these programs. On January 3, 2013, after the Organization worked with the state auditor to address the points contained in the letter, the matter was settled resulting in $5,266 that was disallowed by the Vermont Department of Public Safety from these programs.

Fletcher Allen Partners, Inc. and Subsidiaries
Summary Schedule of Status of Prior Audit Findings
Year Ended September 30, 2012

There are no findings from prior year that require an update in this report.