# Fletcher Allen Partners, Inc. and Subsidiaries

## Report on Federal Awards in Accordance with OMB Circular A–133

September 30, 2014

EIN 45–2880726

# Fletcher Allen Partners, Inc. and Subsidiaries
## Index
## September 30, 2014 and 2013

# Part I

# Financial Statements and Schedule of Expenditures of Federal Awards

## Independent Auditor's Report

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

### Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Fletcher Allen Partners, Inc. and Subsidiaries (the "Organization"), which comprise the consolidated balance sheets as of September 30, 2014 and 2013, and the related consolidated statements of operations, changes in net assets and of cash flows for the years then ended, and the related notes to the financial statements.

#### *Management's Responsibility for the Consolidated Financial Statements*

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

#### *Auditor's Responsibility*

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We did not audit the financial statements of Community Providers, Inc. and Affiliates ("Community Providers, Inc."), a subsidiary whose sole member is Fletcher Allen Partners, Inc., which statements reflect total assets constituting 16% of consolidated total assets at September 30, 2013 and total revenues constituting 16% of consolidated total revenues for the year then ended. The financial statements of Community Providers, Inc. as of September 30, 2013 and for the nine months then ended were audited by other auditors whose report thereon has been furnished to us, and our opinion expressed herein, insofar as it relates to the amounts included for Community Providers Inc., is based solely on the report of the other auditors. We conducted our audits 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Organization's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control. Accordingly, we express no such

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opinion.  An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.  We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***Opinion***

In our opinion, based on our audits and the report of the other auditors with respect to the consolidated financial statements as of and for the year ended September 30, 2013, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Fletcher Allen Partners, Inc. and Subsidiaries at September 30, 2014 and 2013, and the results of their operations, their changes in net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### **Other Matters**

*Other Information*

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole.  The accompanying schedule of expenditures of federal awards for the year ended September 30, 2014 is presented for purposes of additional analysis as required by 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 consolidated financial statements.  Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements.  The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated 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 consolidated financial statements as a whole.

### ***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated December 23, 2014 on our consideration of the 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 internal control over financial reporting or on compliance.  That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Organization's internal control over financial reporting and compliance.

PricewaterhouseCoopers LLP

December 23, 2014

# Fletcher Allen Partners, Inc. and Subsidiaries
## Consolidated Balance Sheets
## September 30, 2014 and 2013

| *(in thousands)* | 2014 | 2013 |
|---|---|---|
| **Assets** | | |
| Current assets | | |
| Cash and cash equivalents | $ 268,216 | $ 248,852 |
| Patient and other trade accounts receivable - net of allowance for doubtful accounts of $38,300 and $34,150, respectively | 202,182 | 175,792 |
| Inventories | 29,766 | 29,654 |
| Current portion of assets whose use is limited or restricted | 27,876 | 20,845 |
| Receivables from third-party payers | 4,329 | 4,951 |
| Prepaid, other current assets, and short-term investments | 37,187 | 55,831 |
| Total current assets | 569,556 | 535,925 |
| Assets whose use is limited or restricted | | |
| Board-designated assets | 349,054 | 317,715 |
| Assets held by trustee under bond indenture agreements | 28,405 | 26,013 |
| Restricted assets | 28,422 | 39,006 |
| Donor-restricted assets for specific purposes | 33,538 | 28,708 |
| Donor-restricted assets for permanent endowment | 31,373 | 29,775 |
| Total assets whose use is limited or restricted | 470,792 | 441,217 |
| Property and equipment, net | 599,973 | 608,519 |
| Other | 32,531 | 28,909 |
| Total assets | $ 1,672,852 | $ 1,614,570 |
| **Liabilities and net assets** | | |
| Current liabilities | | |
| Current installments of long-term debt | $ 28,233 | $ 27,688 |
| Accounts payable | 36,386 | 35,611 |
| Accrued expenses and other liabilities | 60,463 | 71,680 |
| Accrued payroll and related benefits | 96,219 | 90,903 |
| Third-party payer settlements | 16,441 | 20,926 |
| Incurred but not reported claims | 24,073 | 30,711 |
| Total current liabilities | 261,815 | 277,519 |
| Long-term liabilities | | |
| Long-term debt - net of current installments | 450,114 | 470,721 |
| Malpractice and workers' compensation claims net of current portion | 32,459 | 29,463 |
| Pension and other postretirement benefit obligations | 70,663 | 66,300 |
| Other | 30,671 | 25,027 |
| Total long-term liabilities | 583,907 | 591,511 |
| Total liabilities | 845,722 | 869,030 |
| Commitments and contingent liabilities | | |
| Net assets | | |
| Unrestricted | 755,263 | 681,708 |
| Temporarily restricted | 38,873 | 32,500 |
| Permanently restricted | 32,994 | 31,332 |
| Total net assets | 827,130 | 745,540 |
| | $ 1,672,852 | $ 1,614,570 |

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

## Fletcher Allen Partners, Inc. and Subsidiaries
### Consolidated Statements of Operations
### Years Ended September 30, 2014 and 2013

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| **Unrestricted revenue and other support** | | |
| Net patient service revenue | $ 1,455,153 | $ 1,285,667 |
| Less: Provision for bad debts | (42,386) | (37,524) |
| Net patient service revenue after provision for bad debts | 1,412,767 | 1,248,143 |
| Enhanced Medicaid Graduate Medical Education revenues-Hospital | 11,461 | 18,582 |
| Enhanced Medicaid Graduate Medical Education revenues-Professional | 18,818 | 48,639 |
| Net patient service revenue after provision for bad debts and enhanced Medicaid Graduate Medical Education revenues | 1,443,046 | 1,315,364 |
| Premium revenue | 42,925 | 120,303 |
| Other revenue | 81,580 | 66,963 |
| Total unrestricted revenue and other support | 1,567,551 | 1,502,630 |
| **Expenses** | | |
| Salaries, payroll taxes, and fringe benefits | 929,559 | 845,394 |
| Supplies and other | 399,380 | 389,719 |
| Purchased services | 58,501 | 59,844 |
| Depreciation and amortization | 76,654 | 70,338 |
| Interest expense | 21,184 | 21,332 |
| Underwriting expenses | 9,902 | 12,025 |
| Medical claims | 12,350 | 60,197 |
| Total expenses | 1,507,530 | 1,458,849 |
| Income from operations | 60,021 | 43,781 |
| **Nonoperating gains (losses)** | | |
| Investment income | 15,277 | 38,297 |
| Loss on interest rate swap agreements | (2,058) | 9,450 |
| Loss on the extinguishment of debt | - | (1,142) |
| Contribution revenue from acquisition | - | 45,479 |
| Other | 2,189 | 6,498 |
| Total nonoperating gains | 15,408 | 98,582 |
| Excess of revenue over expenses | 75,429 | 142,363 |
| Net change in unrealized gains on investments | 15,417 | (20,805) |
| Net assets released from restrictions for capital purchases | 3,281 | 7,195 |
| Pension related adjustments | (19,238) | 52,581 |
| Other adjustments | (1,334) | - |
| Increase in unrestricted net assets | $ 73,555 | $ 181,334 |

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

# Fletcher Allen Partners, Inc. and Subsidiaries
## Statements of Changes in Net Assets
## Years Ended September 30, 2014 and 2013

| *(in thousands)* | 2014 | 2013 |
|---|---|---|
| **Unrestricted net assets** | | |
| Excess of revenue over expenses | $ 75,429 | $ 142,363 |
| Net change in unrealized gains on investments | 15,417 | (20,805) |
| Net assets released from restrictions for capital purchases | 3,281 | 7,195 |
| Pension related adjustments | (19,238) | 52,581 |
| Other adjustments | (1,334) | - |
| Increase in unrestricted net assets | 73,555 | 181,334 |
| **Temporarily restricted net assets** | | |
| Gifts, grants, and bequests | 9,390 | 9,773 |
| Investment income | 339 | 192 |
| Net change in unrealized gains on investments | (281) | 1,197 |
| Net realized gains on investments | 3,149 | 1,728 |
| Net assets released from restrictions used in operations | (2,372) | (2,209) |
| Net assets released from restrictions used for nonoperating purposes | (188) | (1,150) |
| Net assets released from restrictions used for capital purchases | (3,281) | (7,195) |
| Transfer of net assets | (383) | (29) |
| Contribution of temporarily restricted net assets | - | 2,954 |
| Increase in temporarily restricted net assets | 6,373 | 5,261 |
| **Permanently restricted net assets** | | |
| Gifts, grants, and bequests | 63 | 75 |
| Change in beneficial interest in perpetual trusts | 1,216 | 506 |
| Transfer of net assets | 383 | 29 |
| Contribution of permanently restricted net assets | - | 1,557 |
| Increase in permanently restricted net assets | 1,662 | 2,167 |
| Increase in net assets | 81,590 | 188,762 |
| **Net assets** | | |
| Beginning of year | 745,540 | 556,778 |
| End of year | $ 827,130 | $ 745,540 |

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

# Fletcher Allen Partners, Inc. and Subsidiaries
## Consolidated Statements of Cash Flows
## Years Ended September 30, 2014 and 2013

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| **Cash flows from operating activities** | | |
| Increase in net assets | $ 81,590 | $ 188,762 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities | | |
| Depreciation and amortization | 76,654 | 70,338 |
| Contribution revenue from acquisition | - | (49,990) |
| Provision for bad debts | 42,386 | 37,524 |
| Contributions and investment income restricted for long-term use | (3,104) | (5,478) |
| Pension related adjustments | 19,238 | (52,581) |
| Loss on extinguishment of debt | - | 1,142 |
| Gain on disposal of property and equipment | (2,396) | (264) |
| Loss (gain) on interest rate swap agreements | 2,058 | (9,450) |
| Realized and unrealized gains on investments | (29,649) | (13,301) |
| Undistributed (gains) losses of affiliated companies | (1,638) | 1,293 |
| Change in beneficial interest in perpetual trusts | (1,216) | (506) |
| Changes in operating assets and liabilities | | |
| Increase in patient and other accounts receivable | (68,776) | (39,878) |
| Decrease (increase) in other current and noncurrent assets | 6,142 | (3,584) |
| Decrease in estimated receivables from third-party payers | 622 | 1,189 |
| (Decrease) increase in accounts payable and accrued expenses | (10,999) | 17,249 |
| Increase in accrued payroll and related expenses | 5,316 | 5,658 |
| Decrease in other current and noncurrent liabilities | (56) | (8,668) |
| Decrease in estimated settlements with third-party settlements | (4,485) | (6,434) |
| Decrease in pension and other postretirement benefit obligations | (14,875) | (10,559) |
| Net cash provided by operating activities | 96,812 | 122,462 |
| **Cash flows from investing activities** | | |
| Acquisitions of property and equipment | (65,180) | (85,247) |
| Proceeds from sale of property and equipment | 2,770 | 1,399 |
| Purchase of investments | (232,403) | (295,904) |
| Proceeds from sale of investments | 226,478 | 314,003 |
| Proceeds from sale of affiliated company | - | 397 |
| Cash received through acquisition | - | 30,073 |
| Net cash used in investing activities | (68,335) | (35,279) |
| **Cash flows from financing activities** | | |
| Contributions and investment income restricted for long-term use | 3,104 | 5,478 |
| Proceeds of debt issuance | 9,903 | 36,419 |
| Payment of long-term debt | (23,005) | (53,843) |
| Borrowings on line of credit | 17,770 | - |
| Repayments on line of credit | (16,885) | - |
| Debt issuance costs | - | (250) |
| Net cash used in financing activities | (9,113) | (12,196) |
| Net increase in cash and cash equivalents | 19,364 | 74,987 |
| **Cash and cash equivalents** | | |
| Beginning of year | 248,852 | 173,865 |
| End of year | $ 268,216 | $ 248,852 |
| **Supplemental cash flow information** | | |
| Cash paid during the year for interest | $ 19,668 | $ 21,233 |
| Capital expenditures included in accounts payable | 5,322 | 4,765 |
| Increase in fair value of assets acquired | - | 2,634 |
| Assets acquired under capital lease | 2,165 | - |
| Noncash increase in other current assets and long term debt associated with debt issuance | - | 9,903 |

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 non-profit, tax-exempt Vermont corporation and the sole corporate member of Fletcher Allen Health Care, Inc., Central Vermont Medical Center, Inc., and Community Providers, Inc. FAP became the sole corporate member of Fletcher Allen Health Care, Inc. and Central Vermont Medical Center, Inc. on October 1, 2011, and Community Providers, Inc. on January 1, 2013. FAP's purpose is to establish an integrated regional health care system for the development of a highly coordinated health care network to 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 which is 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. ("FAHC Foundation"); 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"); OneCare Vermont Accountable Care Organization, LLC ("OCV"); and Adirondack Accountable Care Organization, LLC ("ADK ACO").

Central Vermont Medical Center, Inc. ("CVMC") provides health care services under three distinct business units: Central Vermont Hospital, Woodridge Rehabilitation and Nursing ("Woodridge"), 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 and has a full spectrum of inpatient and outpatient services.

Community Providers, Inc. ("CPI") is incorporated as a not-for-profit corporation under the laws of the state of New York. CPI's primary purpose is to develop and coordinate a community and regionally focused healthcare system that provides appropriate, cost-effective care, emphasizing wellness and prevention, and promising both public and patient education.

CPI includes Champlain Valley Physician Hospital Medical Center ("CVPH"), Mediquest Corp. ("Mediquest"), Emergency Medical Transport of CVPH, Inc. ("EMT"), Champlain Valley Health Network, Inc. ("CVHN"), and Elizabethtown Community Hospital ("ECH"). CVPH is the sole member of the CVPH Medical Center Foundation, Champlain Valley Open MRI, LLC, and Valcour Imaging, Inc., and is a partner with FAHC in ADK ACO.

On November 12, 2014, FAP changed its name to The University of Vermont Health Network ("UVM Health Network"). The UVM Health Network name better reflects the connection to The University of Vermont College of Medicine and College of Nursing and Health Sciences, and reminds those in its service delivery areas that nationally recognized health care is available right in their communities. As a result of this branding campaign, FAHC became The University of Vermont Medical Center, and the other hospitals in the network were branded as The UVM Health Network, with their traditional hospital names remaining in place. Other subsidiaries within the FAHC structure were renamed to reflect The University of Vermont Medical Center changes.

## 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 subsidiaries for which it serves as the sole corporate member. 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.

### Reclassifications

Certain amounts for the year ended September 30, 2013 have been reclassified to conform to the current year presentation.

### 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 multiple regional 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 fair 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.

### 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. A significant portion of the assets are made up of investments.

### Investments and Investment Income

Investments in equity securities and mutual funds with readily determinable fair market values, common collective trusts, hedge funds 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 financial statements.

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 $828,000 and $1,047,000 in losses related to declines in value that were other-than-temporary in nature in the years ended September 30, 2014 and 2013, respectively.

### 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 | 2 - 25 years |
| Buildings and improvements | 5 - 40 years |
| Fixed equipment | 5 - 20 years |
| Major moveable equipment | 2 - 20 years |
| Automobiles | 4 - 15 years |
| Building service equipment | 5 - 30 years |
| Leasehold improvements | 2 - 30 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 $411,000 and $358,000 of interest was capitalized during the years ended September 30, 2014 and 2013, respectively. Net deferred financing costs totaled $11,063,000 and $11,735,000 at September 30, 2014 and 2013, respectively. 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 $6,461,000 and $5,789,000 at September 30, 2014 and 2013, respectively.

**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 (losses).

**Excess of Revenue Over Expenses**
The consolidated statements of operations include the 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 $2,377,000 and $3,202,000 in the years ended September 30, 2014 and 2013, respectively.

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 31% in each of the years ended September 30, 2014 and 2013.

***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. In Vermont additional reimbursement 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. The Medicaid program accounts for approximately 12% and 11% of FAP's net revenue for the years ended September 30, 2014 and 2013, respectively.

***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 49% and 44% of FAP's net revenues were derived from contracted insurers in the years ended September 30, 2014 and 2013, respectively. Approximately 8% and 9% of FAP's net revenues were derived from noncontracted insurers in the years ended September 30, 2014 and 2013, respectively.

VMC has agreements with various Health Maintenance Organizations ("HMO") 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. In April of 2014, VMC operations shifted from actively managing monthly capitation payments to providing contract run-out services for its last two payer partnerships. The final settlement of the last two contracts will occur in fiscal year 2015.

**Enhanced Medicaid Graduate Medical Education Revenues (Hospital and Professional)**
Under an Amendment to the Vermont State Medicaid Plan TN#11-019 (the "State Plan Amendment"), FAHC received increased Vermont Medicaid payments to support graduate medical education ("GME") beginning in fiscal year 2013. The State Plan Amendment was approved by the Centers for Medicare and Medicaid Services in May 2013 with an effective date of July 1, 2011, the date of submission by the State's Department of Vermont Health Access. The State Plan Amendment provided for enhanced Medicaid payments of GME through two funding mechanisms: (1) payments to "qualified teaching hospitals" and (2) payments to "qualified teaching physicians." Under the definitions contained in the State Plan Amendment, FAHC is a qualified teaching hospital and physicians employed by UVM Medical Group are qualified teaching physicians.

The nonfederal source of these payments was provided by payments from the University of Vermont ("UVM") from its governmental appropriations from the State of Vermont ("the State"). UVM has entered into a contract with the State to provide annual amounts during the State's fiscal year as the nonfederal share of GME payments for that year. FAHC expects that UVM will enter into similar contracts for subsequent years, though there is no assurance of this. FAHC entered into a contract with the State, by which FAHC agrees to assess and monitor program benefits to Medicaid beneficiaries and to report to the State annually on its performance on certain quality measures and improvement focus areas for Medicaid beneficiaries pertaining to FAHC's GME programs, and the State agrees to provide GME payments to FAHC during the State fiscal year. FAHC expects to enter into similar contracts with the State for future years, but these are subject to continued funding by UVM of the nonfederal source. The State, FAHC and UVM have also entered into a Memorandum of Understanding ("MOU"), dated June 10, 2013 that describes the State Plan Amendment and these funding arrangements.

FAHC received GME funding from the State under the State Plan Amendment totaling $30.3 million for the fiscal year ending September 30, 2014. The $30.3 million includes reimbursement to FAHC as a qualified teaching hospital in an amount of $11.5 million and reimbursement to the UVM Medical Group as qualified teaching physicians in an amount of $18.8 million. In 2013, FAHC received GME funding from the State under the State Plan Amendment totaling $67.2 million, which included retroactive amounts back to the effective date of July 1, 2011. Under the MOU, both UVM and the State retain the right to discontinue GME payments at any time in the future.

**Premium Revenue**
VMC has agreements with various insurers to provide medical services through its provider network to subscribing participants. Under these agreements, VMC receives monthly capitation payments based on the number of each insurer's participants, regardless of services actually performed by VMC's network of providers. The remaining two payer contracts under these agreements ended by the second quarter of fiscal year 2014. No additional payer contracts are anticipated in the near future under the VMC risk-arrangement model.

**Other Revenue**
Other revenue consists primarily of research revenue, non-patient related contract revenues, 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. 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 and Workers' Compensation 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, losses pending settlement, as well as for workers' compensation claims and underwriting expenses. Such liabilities are necessarily based on estimates and, while management believes the amounts provided are adequate, the ultimate liabilities 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 liabilities are actuarially reviewed on an annual basis and any adjustments required are reflected in current operations.

**Income Taxes**
FAP, FAHC, CVMC, UVM Medical Group, FAMG, FAHC Foundation, CVPH, EMT, ECH and CPI 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, FAMG, FAHC Foundation, CVPH, EMT, ECH and CPI 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. OCV is a limited liability company taxed as a partnership. Earnings and losses are passed through to the owners, both of which are tax-exempt, and are treated in the same manner for tax purposes. No provision for federal income taxes has been recorded in the accompanying consolidated financial statements for these organizations.

FAHV, VMC, Mediquest and CVHN 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.

FAP accounts for recognition and measurement of uncertain tax positions in accordance with ASC 740. No provision for uncertain tax positions is recorded in the accompanying consolidated financial statements.

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 March 31, 2035.

**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 $3,103,000 and $2,796,000 at September 30, 2014 and 2013, respectively, 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%-6.0%. The recorded asset retirement obligation at September 30, 2014 and 2013 was approximately $1,665,000 and $1,616,000, respectively.

**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.

**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 identical or similar assets in nonactive 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 within the fund. There are no unfunded commitments or liquidity restrictions related to these common collective trusts at September 30, 2014. 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 within the trust, 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.

## 3. 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 $27,777,000 and $36,666,000 for the years ended September 30, 2014 and 2013, respectively.

Approximately $10,763,000 and $15,215,000 of FAP's total expenses for the years ended September 30, 2014 and 2013 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 years ended September 30, 2014 and 2013, respectively, FAP used $250,000 and $240,000 in charitable endowment earnings to help defray the costs of indigent care.

## 4. Assets Whose Use is Limited or Restricted

Assets whose use is limited or restricted at September 30, 2014 and 2013 consisted of the following:

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| Equities | $ 14,450 | $ 13,323 |
| Mutual funds | 88,687 | 79,044 |
| Money market funds | 21,153 | 21,900 |
| Bonds and notes | 39,861 | 37,536 |
| Common collective trusts | | |
| Bond funds | 130,588 | 137,619 |
| U.S. treasury obligation funds | 38,507 | 37,634 |
| International equity funds | 68,149 | 53,127 |
| Domestic equity funds | 29,805 | 25,121 |
| Commodity funds | 23,155 | 26,448 |
| Real estate funds | 27,672 | 14,908 |
| Total common collective trusts | 317,876 | 294,857 |
| Beneficial interest in perpetual trusts | 14,072 | 12,856 |
| Hedge funds | 2,569 | 2,416 |
| Real estate | - | 130 |
| | 498,668 | 462,062 |
| Less: Current portion | (27,876) | (20,845) |
| | $ 470,792 | $ 441,217 |

Investment income and gains (losses) for the years ended September 30, 2014 and 2013 consisted of the following:

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| **Nonoperating gains (losses)** | | |
| Investment income | $ 3,913 | $ 7,116 |
| Net realized gains on investments | 11,364 | 31,181 |
| Investment income recorded in nonoperating gains (losses) | 15,277 | 38,297 |
| Net change in unrealized gains on investments | 15,417 | (20,805) |
| **Changes in temporarily restricted net assets** | | |
| Investment income | 339 | 192 |
| Net change in unrealized gains on investments | (281) | 1,197 |
| Net realized gains on investments | 3,149 | 1,728 |
| | 3,207 | 3,117 |
| **Changes in permanently restricted net assets** | | |
| Change in beneficial interest in perpetual trusts | 1,216 | 506 |
| | $ 35,117 | $ 21,115 |

FAP recognized $828,000 and $1,047,000 in losses related to declines in value that were other-than-temporary in nature during the years ended September 30, 2014 and 2013, respectively.

The cost and estimated fair value of securities classified as available-for-sale by the organization, which excludes beneficial interest in perpetual trusts of $14,072,000 and $12,856,000, and includes short-term investments of $6,205,000 and $5,568,000 as of September 30, 2014 and 2013, respectively, and long-term investments of $4,222,000 and $4,002,000 as of September 30, 2014 and 2013, respectively, is as follows:

| | 2014 | | |
|---|---|---|---|
| *(in thousands)* | **Cost** | **Gross Unrealized Gains** | **Estimated Fair Value** |
| Mutual funds | $ 80,845 | $ 11,788 | $ 92,633 |
| Equities | 16,531 | 2,364 | 18,895 |
| Real estate | 192 | 13 | 205 |
| Hedge funds | 2,597 | 431 | 3,028 |
| Money market funds | 21,670 | 131 | 21,801 |
| Bonds and notes | 40,546 | (233) | 40,313 |
| Common collective trusts | 289,418 | 28,730 | 318,148 |
| | $ 451,799 | $ 43,224 | $ 495,023 |

| | 2013 | | |
|---|---|---|---|
| *(in thousands)* | **Cost** | **Gross Unrealized Gains** | **Estimated Fair Value** |
| Mutual funds | $ 73,369 | $ 10,077 | $ 83,446 |
| Equities | 15,298 | 2,677 | 17,975 |
| Real estate | 129 | 1 | 130 |
| Hedge funds | 2,142 | 274 | 2,416 |
| Money market funds | 22,039 | - | 22,039 |
| Bonds and notes | 38,279 | (366) | 37,913 |
| Common collective trusts | 279,813 | 15,044 | 294,857 |
| | $ 431,069 | $ 27,707 | $ 458,776 |

The following table presents information as of September 30, 2014 and 2013, about FAP's financial assets and liabilities that are measured at fair value on a recurring basis:

| | 2014 | | | |
|---|---|---|---|---|
| *(in thousands)* | **Quoted Prices in Active Markets (Level 1)** | **Other Observable Inputs (Level 2)** | **Unobservable Inputs (Level 3)** | **Fair Value** |
| Mutual funds | $ 92,633 | $ - | $ - | $ 92,633 |
| Equities | 18,895 | - | - | 18,895 |
| Money market funds | 21,801 | - | - | 21,801 |
| Hedge funds | - | 459 | 2,569 | 3,028 |
| Bonds and notes | 30,468 | 9,845 | - | 40,313 |
| Common collective trusts | - | 318,148 | - | 318,148 |
| Beneficial interest in perpetual trusts | - | - | 14,072 | 14,072 |
| Real estate | - | 205 | - | 205 |
| | $ 163,797 | $ 328,657 | $ 16,641 | $ 509,095 |
| Interest rate swap agreements | $ - | $ 19,120 | $ - | $ 19,120 |

| | 2013 | | | |
|---|---|---|---|---|
| *(in thousands)* | **Quoted Prices in Active Markets (Level 1)** | **Other Observable Inputs (Level 2)** | **Unobservable Inputs (Level 3)** | **Fair Value** |
| Mutual funds | $ 82,693 | $ 753 | $ - | $ 83,446 |
| Equities | 17,975 | - | - | 17,975 |
| Money market funds | 22,039 | - | - | 22,039 |
| Hedge funds | - | - | 2,416 | 2,416 |
| Bonds and notes | 12,476 | 25,437 | - | 37,913 |
| Common collective trusts | - | 294,857 | - | 294,857 |
| Beneficial interest in perpetual trusts | - | - | 12,856 | 12,856 |
| Real estate | - | 130 | - | 130 |
| | $ 135,183 | $ 321,177 | $ 15,272 | $ 471,632 |
| Interest rate swap agreements | $ - | $ 17,062 | $ - | $ 17,062 |

The table above has been revised from the previous presentation in FAP's consolidated financial statements to correctly present $2,257,000 of equities, money market funds, bonds and notes, and real estate investments previously disclosed as Level 1 or Level 2 investments to Level 3 beneficial interest in perpetual trusts as of September 30, 2013. The table has also been revised to correctly present $19,409,000 of mutual funds previously disclosed as Level 2 investments to Level 1 investments as of September 30, 2013. FAP has concluded that these revisions do not have a material impact to the prior period financial statements.

A roll forward of Level 3 fair value measurements (defined above) for the years ended September 30, 2014 and 2013, is as follows:

| *(in thousands)* | 2014 Beneficial Interest in Perpetual Trusts | 2014 Hedge Funds | 2014 Total Level 3 Assets |
|---|---|---|---|
| **Beginning of year** | $ 12,856 | $ 2,416 | $ 15,272 |
| Purchases | - | - | - |
| Sales | - | - | - |
| Unrealized gains | 1,216 | 153 | 1,369 |
| Unrealized losses | - | - | - |
| **End of the year** | $ 14,072 | $ 2,569 | $ 16,641 |
| Increase in fair value of Level 3 investments held at September 30, included in the statement of changes in net assets | $ 1,216 | $ 153 | $ 1,369 |

| *(in thousands)* | 2013 Beneficial Interest in Perpetual Trusts | 2013 Hedge Funds | 2013 Total Level 3 Assets |
|---|---|---|---|
| **Beginning of year** | $ 12,350 | $ 2,229 | $ 14,579 |
| Purchases | - | - | - |
| Sales | - | - | - |
| Unrealized gains | 506 | 187 | 693 |
| Unrealized losses | - | - | - |
| **End of the year** | $ 12,856 | $ 2,416 | $ 15,272 |
| Increase in fair value of Level 3 investments held at September 30, included in the statement of changes in net assets | $ 506 | $ 187 | $ 693 |

## 5. Property and Equipment

A summary of property and equipment at September 30, 2014 and 2013 is as follows:

| *(in thousands)* | **2014** | **2013** |
| --- | --- | --- |
| Land | $ 20,461 | $ 20,234 |
| Land improvements | 17,125 | 17,062 |
| Leasehold improvements | 45,786 | 44,204 |
| Buildings | 694,424 | 664,949 |
| Equipment, furniture, and fixtures | 414,939 | 383,061 |
| | 1,192,735 | 1,129,510 |
| Less: Accumulated depreciation | (608,611) | (538,876) |
| | 584,124 | 590,634 |
| Construction–in–progress | 15,849 | 17,885 |
| | $ 599,973 | $ 608,519 |

FAP wrote off approximately $3,035,000 and $3,266,000 in gross property and equipment in the years ended September 30, 2014 and 2013, respectively. FAP received $2,770,000 and $1,399,000 in proceeds for these assets for the years ended September 30, 2014 and 2013, respectively, and recorded a gain on disposal of property and equipment of $2,396,000 and $264,000 in the years ended September 30, 2014 and 2013, respectively. These gains are included in supplies and other expense. At September 30, 2014 and 2013, FAP had commitments to purchase approximately $19,397,000 and $4,765,000, respectively, of property and equipment.

FAP recorded depreciation expense of $76,074,000 and $69,672,000 for the years ended September 30, 2014 and 2013, respectively.

## 6. Long-Term Debt

Long-term debt at September 30, 2014 and 2013 consisted of the following:

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| **Vermont Educational and Health Buildings Financing Agency** | | |
| **Hospital Revenue Bonds** | | |
| Series 2009A loan, fixed rate (5.08% to 7.23%), payable through 2024 | $ 10,999 | $ 11,841 |
| Series 2008A Bonds, variable rate (0.04% at September 30, 2014), payable through 2030 | 54,705 | 54,705 |
| Series 2007A Bonds, fixed rate (4.00% to 4.75%), payable through 2037 (including unamortized premium of $86 and $90 at September 30, 2014 and 2013, respectively) | 55,791 | 55,945 |
| Series 2004B Bonds, fixed rate (4.00% to 5.50%), payable through 2035 (including unamortized premium of $119 and $125 at September 30, 2014 and 2013, respectively) | 143,843 | 147,100 |
| Series 2004A Bonds, fixed rate (3.00% to 5.00%), payable through 2025 (including unamortized premium of $903 and $1,000 at September 30, 2014 and 2013, respectively) | 31,383 | 33,535 |
| Series 2013A Bonds, fixed rate (2.597%) payable through 2027 | 29,012 | 29,337 |
| Series 1996 loan, fixed rate (4.23%), payable through 2021 | 8,683 | 9,889 |
| **County of Clinton Industrial Development Agency** | | |
| **Hospital Revenue Bonds** | | |
| Series 2006A & 2006B Bonds, variable rate (3.65% at September 30, 2014), payable through 2017 | 4,115 | 5,375 |
| Series 2007B Bonds, variable rate (0.11% at September 30, 2014), payable through 2042 | 11,395 | 11,595 |
| **Essex County Capital Resource Corporation** | | |
| **Hospital Revenue Bonds** | | |
| Series 2011 Bonds, variable rate (1.67% at September 30, 2014), payable through 2032 | 5,590 | 5,810 |
| **Other long-term debt** | | |
| Series 2002A Key Bank Bonds, variable rate (1.65% at September 30, 2014), payable through 2024 | 5,950 | 6,450 |
| Series 2007A Key Bank Bonds, variable rate (4.10% at September 30, 2014), payable through 2042 | 17,895 | 18,195 |
| Associates in Radiology of Plattsburg, LLC Note Payable, fixed rate (3.00%), payable through 2017 | 3,334 | 4,218 |
| Community Bank Loan Payable, fixed rate (3.50%), payable through 2017 | 15,944 | 16,555 |
| Capital lease, fixed rate (0.30% to 19.51%), payable through 2020 | 8,489 | 10,940 |
| KeyBank loan, variable rate (2.00% at September 30, 2014), payable through 2023 | 4,885 | 5,000 |
| KeyBank loan, fixed rate (3.49%), payable through 2023 | 48,310 | 51,870 |
| People's United loan, fixed rate (2.67%) payable through 2028 | 9,446 | 9,903 |
| Other debt | 8,578 | 10,146 |
| | 478,347 | 498,409 |
| Less: Current portion | (28,233) | (27,688) |
| Long–term debt | $ 450,114 | $ 470,721 |

### Obligated Group

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

An obligated group does not exist for the CPI entities.

**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, 2014 and 2013, the reserve fund balances were approximately $15,031,000 and $14,497,000, respectively.

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 the 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, 2014 and 2013, 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.

**Series 2002A Bonds**
The Series 2002A bonds are bank qualified bonds held by Key Bank, payable in annual installments ranging from $500,000 to $700,000, plus interest at one month LIBOR times 0.6501 plus 153 basis points (1.65% at September 30, 2014) through July 2024.

**Series 2006A & 2006B Bonds**
The Series 2006A and 2006B bonds are County of Clinton Industrial Development Agency, Variable Rate Demand Civic Facility Revenue Bonds, Series 2006A (tax-exempt) of $12,650,000 and Series 2006B (taxable) of $100,000, payable in annual installments ranging from $1,210,000 to $1,430,000 plus interest. Interest is payable semi-annually at a variable rate reset weekly by a remarketing agent (3.65% at September 30, 2014) from July 1, 2007 through July 1, 2017. The bonds are collateralized by a direct-pay letter of credit with a bank aggregating the outstanding principal amount plus 35 days interest at an assumed rate of 8% per annum for the term of the bonds.

**Series 2007A Bonds**
The Series 2007A bonds are bank qualified bonds held by Key Bank, payable in annual installments ranging from $285,000 to $1,125,000, plus interest at one month LIBOR times 0.6501 plus 153 basis points (4.10% at September 30, 2014) through July 2042.

**Series 2007B Bonds**
The Series 2007B bonds are County of Clinton Industrial Development Agency, Variable Rate Demand Civic Facility Revenue Bonds, Series 2007B (tax-exempt), payable in annual installments ranging from $150,000 to $700,000, plus interest at one month LIBOR times 0.68 (0.11% at September 30, 2014) through July 2042. The bonds are collateralized by a direct-pay letter of credit with a bank aggregating the outstanding principal amount plus 35 days interest at an assumed rate of 8% per annum for the term of the bonds.

**Series 2011 Bonds**
On December 1, 2011, ECH issued Essex County Capital Resource Corporation Revenue Bonds, Series 2011 in the amount of $6,160,000. The Series 2011 bonds were purchased by Key Bank, N.A. under a bond purchase agreement. As part of the agreement, the Series 2011 bonds are subject to mandatory redemption and are subject to optional tender by the bank for purchase by ECH at a price equal to the principal plus accrued and unpaid interest beginning on June 1, 2017. The Series 2011 bonds are collateralized by a mortgage that Key Bank holds with ECH. The Series 2011 bonds carry a variable interest rate of 65% of 1-month LIBOR plus 155 basis points (1.67% at September 30, 2014) due in quarterly installments through March 1, 2032.

**Series 2013A Bonds**
The 2000A Bonds were partially refunded in 2011. The remaining $32,550,000 balance of the initial aggregate principal amount of the Series 2000A Bonds with maturities between December 2025 and December 2027 were refunded in March 2013 and replaced with a tax-exempt direct bank private placement with TD Bank (the 2013A bonds), in the aggregate principal amount of $29,500,000 with a final maturity date in December 2027. Bond issuance costs of $250,000 are recorded as deferred financing costs, net and will be amortized over the life of the loan. The 2013 refunding resulted in a loss on extinguishment of debt of $1,142,000.

**People's United Loan**
On September 30, 2013, FAHC entered into a mortgage for property ("Holly Court") in the amount of $9,903,000. The mortgage is payable through September 2028, and bears interest at a variable rate equal to one month LIBOR plus 105 basis points (1.21% at September 30, 2014). Concurrent with the issuance of the Holly Court mortgage payable, an interest rate swap was entered into whereby FAHC pays a fixed rate of 2.67% and receives a variable rate of one month LIBOR.

**Scheduled Maturities of Long-Term Debt**
As of September 30, 2014, scheduled maturities of long-term debt, not including a net unamortized premium of $1,108,000 for the next five years and thereafter are as follows:

*(in thousands)*

| Years Ending September 30, | | |
|---|---|---|
| 2015 | $ | 28,233 |
| 2016 | | 21,021 |
| 2017 | | 20,945 |
| 2018 | | 31,078 |
| 2019 | | 16,950 |
| Thereafter | | 359,012 |
| | $ | 477,239 |

**Loan Covenants**
Under the terms of the master indenture agreement, the FA Obligated Group is required to meet certain covenant requirements, as are CVPH and ECH for their respective long-term debt. In addition, the indenture provides for restrictions on, among other things, additional indebtedness and dispositions of property of the FA Obligated Group.

**Letter of Credit**
The 2008A letter of credit was not drawn upon as of September 30, 2014, and the scheduled maturities of long-term debt assumes the Series 2008A bonds are not put back to the FA Obligated Group. 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.

The 2007B letter of credit was not drawn upon as of September 30, 2014, and the scheduled maturities of long-term debt assumes the Series 2007B bonds are not put back to the borrower. If the letter of credit was drawn upon and the bond is not remarketed for 180 days, such bond shall be subject to mandatory redemption on the first business day of each month, commencing with the first such business day of the first full month after the bond redemption commencement date over 60 consecutive months in equal principal amounts plus accrued interest at the bank rate. Subsequent to year-end, but prior to the issuance of the financial statements, CVPH's letter of credit was extended through March 2, 2016.

The 2006A letter of credit was not drawn upon as of September 30, 2014, and the scheduled maturities of long-term debt assumes the Series 2006A bonds are not put back to the borrower. If the letter of credit was drawn upon, the repayment term would continue to follow the original amortization schedule of the bonds to be repaid not later than the scheduled payments described in the original bond agreement.

**Line of Credit**

CVMC has a bank line of credit that exists with a maximum borrowing of $2,000,000 at September 30, 2014. The line matured on May 31, 2014, and bears interest at the Wall Street Journal prime rate adjusted daily with a floor of 3.25%, with advances collateralized by a portion of board designated funds. There was no outstanding balance drawn on this line of credit at September 30, 2014.

CPI has an uncollateralized line of credit in the amount of $1,000,000 at September 30, 2014. The interest rate is set at a floating rate equal to LIBOR plus 150 basis points (1.63% at September 30, 2014). At September 30, 2014 CPI had borrowings under the line of credit of $1,000,000. This revolving line of credit is interest only payments with accrued interest and principal due upon maturity. The maturity date for the line of credit is July 31, 2015.

CVPH has an available uncollateralized line of credit in the amount of $4,885,000 at September 30, 2014. The interest rate is set at a floating rate equal to LIBOR plus 150 basis points (2.00% at September 30, 2014). At September 30, 2014, CVPH had borrowings under the line of credit of $4,885,000. The maturity date for the line of credit is July 31, 2015.

***Long-Term Debt***

The estimated fair value of FAP's long-term debt is based on the recently traded value for debt for which a public market exists, and an estimate of the exit price for debt in which no public market exists. The estimate of the exit price includes the observable inputs related to the interest rates of comparable U.S. Treasury securities. Such amounts at September 30, 2014 and 2013, are approximately $482,351,000 and $501,679,000, respectively. The fair value of debt is considered a level 2 measurement.

## 7. Interest Rate Swap Agreements

For certain variable rate debt, interest rate swap agreements are used to manage interest rate risk and hedge the risk of cash flow volatility. The table below details FAP's swap agreements. None of the swap agreements require collateral posting. Both FAP 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. In addition, each agreement may be terminated following the occurrence of certain events, at which time FAP or the counterparty may be required to make a termination payment to the other.

| Swap | Bond Series | Notional Amount 09/30/2014 ($ in 000's) | Notional Amount 09/30/2013 ($ in 000's) | Counterparty | Expiration Date | Pay Fixed | Receive Floating |
|---|---|---|---|---|---|---|---|
| LIBOR Swap (Series B-1) | 2008A | $ 27,595 | $ 27,595 | Citibank, NA | December 1, 2034 | 3.76% | 66.5% of LIBOR + 32bps |
| LIBOR Swap (Series B-2) | 2008A | $ 27,595 | $ 27,595 | Citibank, NA | December 1, 2034 | 3.76% | 66.5% of LIBOR + 32bps |
| LIBOR Swap | Holly Court Loan | $ 9,446 | $ 9,902 | Peoples United Bank | September 30, 2028 | 2.67% | LIBOR + Swap Rate |
| LIBOR Swap | Series 2006A | $ 4,115 | $ 5,375 | Key Bank | July 1, 2017 | 3.50% | 69.0% of LIBOR |
| LIBOR Swap | Series 2007B | $ 11,395 | $ 11,595 | Key Bank | July 1, 2042 | 4.06% | 68.0% of LIBOR |
| LIBOR Swap | Series 2007A | $ 17,895 | $ 18,195 | Key Bank | July 1, 2042 | 4.00% | 65.0% of LIBOR |
| SIFMA Swap | Series 2011 | $ 5,120 | $ 5,205 | Key Bank | December 1, 2021 | 3.24% | 65.0% of LIBOR |

The fair value of interest rate swap agreements, all of which are recorded as other long-term liabilities at September 30, is as of follows:

| *(in thousands)* | Balance Sheet Location | Fair Value 2014 | Fair Value 2013 |
|---|---|---|---|
| 2008A Swaps | Other long-term liabilities | $ (9,914) | $ (8,566) |
| Holly Court Loan | Other long-term liabilities | (230) | (155) |
| 2006A Swap | Other long-term liabilities | (224) | (385) |
| 2007B Swap | Other long-term liabilities | (3,130) | (2,789) |
| 2007A Swaps | Other long-term liabilities | (5,016) | (4,499) |
| 2011 Swap | Other long-term liabilities | (606) | (668) |
| | | $ (19,120) | $ (17,062) |

The effect of interest rate swap agreements on the consolidated statement of operations and changes in net assets for 2014 and 2013 are as follows:

| *(in thousands)* | Location of Gain/(Loss) Recognized in Statement of Operations | Amount of Gain/Loss Recognized in Statement of Operations 2014 | Amount of Gain/Loss Recognized in Statement of Operations 2013 |
|---|---|---|---|
| 1994 Swap | Gain/(Loss) on interest rate swap contracts | $ - | $ 128 |
| 2008A Swaps | Gain/(Loss) on interest rate swap contracts | (1,348) | 5,648 |
| Holly Swap | Gain/(Loss) on interest rate swap contracts | (75) | (155) |
| 2006A Swap | Gain/(Loss) on interest rate swap contracts | 161 | 166 |
| 2007B Swap | Gain/(Loss) on interest rate swap contracts | (341) | 1,335 |
| 2007A Swaps | Gain/(Loss) on interest rate swap contracts | (517) | 2,051 |
| 2011 Swap | Gain/(Loss) on interest rate swap contracts | 62 | 277 |
| | | $ (2,058) | $ 9,450 |

## 8. 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 $16,239,000 and $15,840,000 for the year ended September 30, 2014 and 2013, respectively.

Minimum future lease payments required under noncancelable operating leases at September 30, 2014, were as follows:

| *(in thousands)* | |
|---|---|
| **Years Ending September 30,** | |
| 2015 | $ 9,268 |
| 2016 | 8,116 |
| 2017 | 5,995 |
| 2018 | 3,470 |
| 2019 | 1,649 |
| Thereafter | 3,317 |
| | $ 31,815 |

## 9. Net Assets

**Temporarily Restricted Net Assets**
At September 30, 2014 and 2013, temporarily restricted net assets are available for the following purposes:

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| Indigent care | $ 1,179 | $ 1,037 |
| Education and research | 13,178 | 11,791 |
| Children's programs | 3,581 | 3,141 |
| Capital projects | 1,951 | 2,047 |
| Other health care services | 17,459 | 12,604 |
| Long-term care services at Woodridge | 1,525 | 1,880 |
| | $ 38,873 | $ 32,500 |

At September 30, 2014 and 2013, temporarily restricted net assets include approximately $19,573,000 and $17,656,000, respectively, 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, 2014 and 2013, income earned on permanently restricted net assets is restricted to:

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| Indigent care | $ 4,802 | $ 4,705 |
| Education and research | 7,243 | 7,094 |
| Other health care services | 19,975 | 18,804 |
| Long-term care services | 974 | 729 |
| | $ 32,994 | $ 31,332 |

**Endowment Funds**

FAP's endowment consists of approximately 92 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 relevant state laws for the states in which it operates 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. These state laws allow 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 years ended September 30, 2014 and 2013, $630,000 and $1,116,000, respectively, 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, 2014 and 2013, and the changes therein for the years then ended:

**Endowment Net Asset Composition by Type of Fund**

| | 2014 | | |
|---|---|---|---|
| *(in thousands)* | Temporarily Restricted | Permanently Restricted | Total |
| **September 30, 2014** | | | |
| Donor-restricted endowment funds | $ 19,573 | $ 21,367 | $ 40,940 |
| Total | $ 19,573 | $ 21,367 | $ 40,940 |

| (in thousands) | 2013 Temporarily Restricted | 2013 Permanently Restricted | 2013 Total |
|---|---|---|---|
| **September 30, 2013** | | | |
| Donor-restricted endowment funds | $ 17,656 | $ 20,733 | $ 38,389 |
| Total | $ 17,656 | $ 20,733 | $ 38,389 |

**Changes in Endowment Net Assets**

| (in thousands) | 2014 Temporarily Restricted | 2014 Permanently Restricted | 2014 Total |
|---|---|---|---|
| **Endowment net assets at September 30, 2013** | $ 17,656 | $ 20,733 | $ 38,389 |
| Investment return | | | |
| Investment income | 697 | - | 697 |
| Net appreciation | 2,480 | - | 2,480 |
| Total investment return | 3,177 | - | 3,177 |
| Appropriations of endowment assets for expenditure | (630) | - | (630) |
| Other | (630) | 634 | 4 |
| **Endowment net assets at September 30, 2014** | $ 19,573 | $ 21,367 | $ 40,940 |

| (in thousands) | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---|---|---|---|
| **Endowment net assets at September 30, 2012** | $ (44) | $ 16,170 | $ 19,072 | $ 35,198 |
| Acquired endowment net assets at October 1, 2012 | - | 14 | 1,557 | 1,571 |
| Investment return | | | | |
| Investment income | - | 298 | - | 298 |
| Net appreciation | - | 2,422 | - | 2,422 |
| Total investment return | - | 2,720 | - | 2,720 |
| Appropriations of endowment assets for expenditure | - | (1,116) | - | (1,116) |
| Adjustment for funds with deficiencies | 44 | (44) | - | - |
| Other | - | (88) | 104 | 16 |
| **Endowment net assets at September 30, 2013** | $ - | $ 17,656 | $ 20,733 | $ 38,389 |

***Beneficial Interest in Perpetual Trusts***

The above amounts exclude FAHC's beneficial interest in perpetual trusts, which are not within management's investment control. Such beneficial interests totaled $11,627,000 and $10,599,000 at September 30, 2014 and 2013, respectively.

***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. There were no deficiencies at September 30, 2014 and 2013.

***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.

## 10. Malpractice and Other Contingencies

**Malpractice and Workers' Compensation**
FAHC and CVMC are 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 for Professional Liability and $2,000,000 per claim for Commercial General Liability, with a $20,000,000 aggregate for Professional Liability and $10,000,000 for Commercial General Liability, with limits on such reinsurance. VMCIC provides claims-made coverage to certain affiliates of FAHC for periods prior to the merger that created FAHC.

CVPH self-insures for professional and general liability claims. A revocable trust has been established for the purpose of setting aside assets based on actuarial funding recommendations. The self-insurance liability reserves and the corresponding charges to operating expenses are based on estimates of asserted and currently identifiable unasserted claims, if any, and related legal expenses, and a provision for unknown incidents. The professional and general liability reserves are reported at their estimated undiscounted value. CVPH maintains excess commercial professional liability insurance policies which provide for self-insured retention limits of $2,000,000 per claim and $4,000,000 in the aggregate per policy year.

ECH is insured for malpractice claims under a claims-made policy. Coverage under this plan is limited to $2,000,000 per incident and $6,000,000 in the aggregate.

FAP, excluding ECH (discussed below), is also self-insured for workers' compensation claims, and maintains an excess insurance policy to limit its exposure on claims up to $1,000,000 per occurrence in the year ended September 30, 2014, with a $25,000,000 aggregate limit.

Prior to 2010, ECH provided for workers' compensation insurance through participation in the Healthcare of New York Workers Compensation Trust ("Trust"); a group self-insured trust regulated by the New York State Workers' Compensation Board ("WCB"). Participation in the Trust subjects ECH to joint and several liability. Should the Trust's assets be insufficient to cover its debts, each Trust member would be subject to a proportional premium assessment to fund the shortage. The Trust uses reinsurance agreements to reduce its exposure to large losses on both an individual and aggregate claim basis. On December 31, 2011, the Trust was voluntarily terminated. ECH has not been notified of any assessment resulting from participation in the Trust. In addition, management of ECH monitors the financial stability of the Trust on an ongoing basis in order to mitigate the risk of joint and several liability. Effective January 2010, ECH terminated the agreement with the self-insured trust and is covered under an indemnity plan with an insurance company. However, ECH remains liable for any claims during the period they were participating in the Trust, including any future assessments of the Trust.

The reserves for outstanding losses at FAHC and CVMC have been discounted at a rate of 2.7% and 2.9% at September 30, 2014 and 2013, resulting in a reduction in the reserve for professional liability of approximately $857,000 and $870,000 at September 30, 2014 and 2013, respectively, and a reduction in the reserve for workers' compensation of approximately $471,000 and $437,000 at September 30, 2014 and 2013, respectively. CVPH does not discount their reserve for professional liability, they are booked at nominal value.

As a result of changes in estimates of incurred events in prior years, primarily professional liability, the estimate of incurred losses increased by approximately $3,273,000 and $7,394,000 for the years ended September 30, 2014 and 2013, respectively.

**Employee Health and Dental Insurance**

FAHC 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, FAHC is responsible for paying claims and third party administrator costs. FAHC maintained a stop-loss insurance policy for its medical plan to limit its exposure on non-domestic claims above $550,000 per member per plan year ending December 31, 2014. FAHC and CVMC maintain a self-insured plan for employee dental.

Effective January 1, 2013, CVPH became self-insured for employee health insurance. Under the terms of the plan, employees and their dependents are eligible for participation and, as such, CVPH is responsible for the administration of the plan and any resultant liability incurred. CVPH maintained a specific stop-loss insurance policy to limit its exposure on cumulative claims exceeding $250,000 per member per year during the year ended September 30, 2014. Included in accounts payable and accrued expenses is a health insurance claims reserve of $1,275,000 related to claims incurred but not paid as of September 30, 2014.

**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.

## 11. 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, 2014 and 2013, was $15,601,000 and $14,372,000, respectively. The required minimum statutory capital at September 30, 2014 and 2013 was $2,599,000 and $2,332,000, respectively. In addition, a minimum liquidity ratio must be maintained whereby liquid assets, as defined by the Act, must exceed 75% of defined liabilities. The required minimum level of liquid assets was $19,529,000 and $17,511,000 at September 30, 2014 and 2013, respectively. The measurement of the required minimum level of liquid assets at September 30, 2014 and 2013 is $40,927,000 and $37,213,000, respectively. FAP reports all of VMCIC's investments in marketable securities as restricted assets in the accompanying consolidated balance sheets.

## 12. Pension Plans

Substantially all employees of FAP are covered under various noncontributory defined benefit pension plans, various defined contribution pension plans, or combinations thereof. Total expense for these plans consists of the following:

| | For the Years Ending September 30, | |
|---|---|---|
| *(in thousands)* | **2014** | **2013** |
| Defined benefit plans | $ 2,230 | $ 7,282 |
| Defined contribution plans | 31,161 | 29,803 |
| | $ 33,391 | $ 37,085 |

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.

Information regarding FAP benefit obligations, plan assets, funded status, expected cash flows and net periodic benefit cost follows within this footnote.

**Benefit Obligations**

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| **Changes in benefit obligations** | | |
| Projected benefit obligations - beginning of year | $ (377,958) | $ (278,923) |
| Effect of affiliation with CPI | - | (139,177) |
| Service cost | (4,495) | (4,999) |
| Interest cost | (18,824) | (15,503) |
| Benefits paid | 15,282 | 13,118 |
| Actuarial loss | (32,509) | 46,512 |
| Administrative expenses paid | 875 | 1,014 |
| Projected benefit obligation - end of year | (417,629) | (377,958) |
| Accumulated benefit obligation | (412,279) | (372,332) |
| **Changes in plan assets** | | |
| Fair value of plan assets - beginning of year | 311,658 | 197,341 |
| Effect of affiliation with CPI | - | 91,319 |
| Actual gain on plan assets | 34,355 | 22,970 |
| Contributions | 17,110 | 14,160 |
| Benefits paid | (15,282) | (13,118) |
| Administrative expenses paid | (875) | (1,014) |
| Fair value of plan assets - end of year | 346,966 | 311,658 |
| Funded status of the plan (long-term) | $ (70,663) | $ (66,300) |

Unrestricted net assets at September 30, 2014 and 2013 include unrecognized actuarial losses of $46,482,000 and $27,244,000, respectively, related to the defined benefit plan. Of this amount, $1,312,000 and $2,112,000 was recognized in net periodic pension costs in the years ended September 30, 2014 and 2013, respectively. The expected amortization of the unrecognized losses to be recognized in net periodic pension costs in the year ended September 30, 2015, is $1,770,000. The reconciliation of the unrecognized actuarial losses for the years ended September 30, 2014 and 2013 is as follows:

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| Unrecognized actuarial losses - beginning of year | $ 27,244 | $ 105,271 |
| Effect of affiliation with CPI | - | (25,459) |
| Net loss amortized during year | (1,312) | (2,112) |
| Net Net prior service cost amortized during year | - | - |
| Net loss during year | 20,550 | (50,456) |
| Unrecognized actuarial losses - end of year | $ 46,482 | $ 27,244 |

The cost components of the net periodic benefit cost for the years ended September 30, 2014 and 2013 are as follows:

| *(in thousands)* | | **2014** | | **2013** |
|---|---|---|---|---|
| Service cost | $ | 4,495 | $ | 4,999 |
| Interest cost | | 18,824 | | 15,503 |
| Expected return on plan assets | | (22,401) | | (19,026) |
| Amortization of unrecognized net loss | | 1,312 | | 2,112 |
| Net periodic benefit cost | $ | 2,230 | $ | 3,588 |

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

| | **2014** | **2013** |
|---|---|---|
| Weighted-average assumptions used to determine the benefit liability | | |
| Discount rates | 4.4% - 4.5% | 5.0% - 5.2% |
| Rates of increase in future compensation levels | 3.0% - 3.5% | 3.0% - 3.5% |
| Weighted-average assumptions used to determine expense | | |
| Discount rates | 5.0% - 5.2% | 4.0% - 4.2% |
| Rates of increase in future compensation levels | 3.0% - 3.5% | 3.5% - 3.8% |
| Expected long-term rate of return on plan assets | 6.5% - 7.5% | 6.5% - 8.0% |

The expected long-term rate of return for the FAP 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, FAP 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**

FAP's pension plans weighted-average asset allocations as of September 30, 2014 and 2013, by asset category, are as follows:

| | **2014** | **2013** |
|---|---|---|
| **Asset Category** | | |
| Money market | - % | - % |
| Bonds | 17 | 17 |
| Equities | 24 | 24 |
| Real estate | 2 | 2 |
| Mutual funds | 16 | 16 |
| Common collective trusts | 41 | 41 |
| | 100 % | 100 % |

The following table presents information, as of September 30, 2014 and 2013, about FAHC's pension assets that are measured at fair value on a recurring basis:

| | 2014 | | | |
|---|---|---|---|---|
| *(in thousands)* | **Quoted Prices in Active Markets (Level 1)** | **Other Observable Inputs (Level 2)** | **Unobservable Inputs (Level 3)** | **Fair Value** |
| Money market | $ 949 | $ - | $ - | $ 949 |
| Bonds | 46,797 | 12,027 | - | 58,824 |
| Equities | 78,839 | 5,377 | - | 84,216 |
| Mutual funds | 61,748 | - | - | 61,748 |
| Common collective trusts | - | 141,229 | - | 141,229 |
| Total | $ 188,333 | $ 158,633 | $ - | $ 346,966 |

| | 2013 | | | |
|---|---|---|---|---|
| *(in thousands)* | **Quoted Prices in Active Markets (Level 1)** | **Other Observable Inputs (Level 2)** | **Unobservable Inputs (Level 3)** | **Fair Value** |
| Money market | $ 1,112 | $ - | $ - | $ 1,112 |
| Bonds | 39,665 | 13,031 | - | 52,696 |
| Equities | 70,130 | 4,375 | - | 74,505 |
| Mutual funds | 56,579 | - | - | 56,579 |
| Common collective trusts | - | 126,766 | - | 126,766 |
| Total | $ 167,486 | $ 144,172 | $ - | $ 311,658 |

The investment strategy established 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, 2014 and 2013.

**Cash Flows - Contributions**
FAP expects to contribute $15,610,000 to its pension plans in the year ending September 30, 2015.

**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,** | | |
|---|---|---|
| 2015 | $ | 17,648 |
| 2016 | | 18,986 |
| 2017 | | 20,555 |
| 2018 | | 21,923 |
| 2019 | | 23,275 |
| 2020–2023 | | 132,902 |

***Multiemployer Defined Benefit Plan***

CVPH contributes to a multiemployer defined benefit pension plan under the terms of their collective-bargaining agreement that covers its SEIU 1199 union-represented employees. Pension expense for the years ended September 30, 2014 and 2013 were approximately $4,886,000 and $3,694,000, respectively, and reflects increased funding requirements as a result of pension underfunding issues. CVPH may be liable for its share of unfunded vested benefits, if any, related to the union plan. Information from the union plan's administrator is not available to permit CVPH to estimate its share, if any, of unfunded vested benefits.

The risk of participating in this multiemployer plan is different from single-employer plans in the following aspects:

a. Assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers.

b. If a participating employer stops contributing to the plan, the unfunded obligations of the Plan may be borne by the remaining participating employers.

c. If CVPH chooses to stop participating in the multiemployer plan, CVPH may be required to pay the plan an amount based on the underfunded status of the plan, referred to as a withdrawal liability.

CVPH's participation in the plan for the year ended September 30, 2014, is outlined in the table below. The "EIN/Pension Plan Number" column provides the Employee Identification Number ("EIN") and the three digit plan number, if applicable. Unless otherwise noted, the most recent Pension Protection Act ("PPA") zone status available in 2014 is for the plan's year-end at December 31, 2013. The zone status is based on information that CVPH received from the Plan and is certified by the plan's actuary. Among other factors, plans in the red zone are generally less than 65 percent funded, plans in the yellow zone are less than 80 percent funded, and plans in the green zone are at least 80 percent funded. The "FIP/RP Status Pending/Implemented" column indicates plans for which a financial improvement plan ("FIP") or a rehabilitation plan ("RP") is either pending or has been implemented. The last column lists the expiration date(s) of the collective-bargaining agreement to which the plan is subject.

| Pension Fund | EIN/Pension Plan Number | Zone Status Pension Protection Act 9/30/2014 | Zone Status Pension Protection Act 12/31/2013 | FIP/RP Status Pending/ Implemented | Surcharge Imposed | Expiration Date of Collective-Bargaining Agreement |
|---|---|---|---|---|---|---|
| 1199 SEIU Health Care Employees Pension Fund | 13-3604862-001 | not available | Green | June 26, 2009 | No | April 30, 2016 |

CVPH was not listed on the Plans' Forms 5500 as providing more than 5 percent of the total contributions. At the date the consolidated FAP financial statements were issued, Form 5500 was not available.

## 13. 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 net receivables from patients and third-party payers at September 30, 2014 and 2013 is as follows:

| | 2014 | 2013 |
|---|---|---|
| Medicare | 27 % | 27 % |
| Medicaid | 8 | 10 |
| Blue cross | 19 | 17 |
| Other third-party payers | 26 | 25 |
| Patients | 20 | 21 |
| | 100 % | 100 % |

## 14. Transactions With UVM

FAHC's Affiliation Agreement with UVM was renewed as of June 19, 2014, for 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. The current Affiliation Agreement provides for three components of financial support to UVM: (1) payments by FAHC, known as the "commitment," to fund two costs: (a) 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 and, (b) a portion of the cost of UVM facilities, utilities and other campus operating expenses that are not paid or reimbursed by any form of federal funding; (2) an academic support payment paid by FAHC and, (3) a Dean's Tax paid by UVM Medical Group. The amounts of the commitment approximated $36,528,000 and $54,389,000 in the years ended September 30, 2014 and 2013, respectively. In addition, FAHC reimburses UVM for equipment rental, research, and certain other administrative expenses through the commitment. In addition to the commitment, FAHC made academic support payments to UVM in monthly installments. The amount of the academic support payment was $4,972,000 and $4,935,000 in the years ended September 30, 2014 and 2013, respectively. Under the Affiliation Agreement, the Dean's Tax is paid to UVM by FAHC in an amount equal to 2.3% of the Medical Group's net patient service revenues exclusive of all Medicaid revenues for that fiscal year. The amount of the Dean's Tax approximated $5,146,000 and $4,717,000 in the years ended September 30, 2014 and 2013, respectively.

Under the current affiliation agreement, the base payments for the academic support payments increase to $7,500,000 in fiscal year 2015, with an inflationary increase in the years thereafter.

## 15. Functional Expenses

FAP provides general health care services to residents within its geographic location. Expenses related to providing these services for the years ended September 30, 2014 and 2013, are as follows:

| *(in thousands)* | **2014** | **2013** |
|---|---|---|
| Education and research | $ 1,951 | $ 2,786 |
| Health care services | 1,235,262 | 1,131,565 |
| Management and general | 272,042 | 327,045 |
| Total functional expenses | 1,509,255 | 1,461,396 |
| Less: Nonoperating expenses | 1,725 | 2,547 |
| Total operating expenses | $ 1,507,530 | $ 1,458,849 |

## 16. 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.

Accounts receivable, prior to adjustment for doubtful accounts, is summarized as follows at September 30, 2014 and 2013:

| *(in thousands)* | 2014 | 2013 |
|---|---|---|
| **Receivables** | | |
| Patients | $ 61,974 | $ 55,188 |
| Third-party payers | 178,508 | 154,754 |
| | $ 240,482 | $ 209,942 |

The allowance for doubtful accounts is summarized as follows at September 30, 2014 and 2013:

| *(in thousands)* | 2014 | 2013 |
|---|---|---|
| **Allowance for doubtful accounts** | | |
| Patients | $ 25,765 | $ 24,638 |
| Third-party payers | 12,535 | 9,512 |
| | $ 38,300 | $ 34,150 |

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

Net patient service revenue before the provision for bad debts and enhanced Medicaid graduate medical education revenues for the years ended September 30, 2014 and 2013, is summarized as follows:

| *(in thousands)* | 2014 | 2013 |
|---|---|---|
| **Net patient service revenue** | | |
| Patients | $ 33,913 | $ 58,851 |
| Third-party payers | 1,421,240 | 1,226,816 |
| | $ 1,455,153 | $ 1,285,667 |

## 17. Subsequent Events

FAP has evaluated subsequent events through December 23, 2014, which is the date the consolidated financial statements were issued and has concluded that, there were no such events that require adjustments to the consolidated financial statements or disclosure in the notes to the consolidated financial statements.

# Fletcher Allen Partners, Inc. and Subsidiaries
## Schedule of Expenditures of Federal Awards
## Year Ended September 30, 2014

| Federal Agency/Program | Federal CFDA No. | Pass-Through Awards Entity | Pass-Through Awards Number | Total Expenditures |
|---|---|---|---|---|
| **Medicaid Cluster** | | | | |
| U.S. Department of Health and Human Services ("DHHS") | | | | |
| Passed through other organizations | | | | |
| Children with Special Health Needs Child Development Clinic & Personal Care Services Program | 93.778 | VT Dept of Health | 03420-6377S | $ 5,784 |
| BluePrint Grant | 93.778 | Dept of Vt Health Access | 03410-6109 | 32,424 |
| Vermont Health Connect Navigation Grant | 93.778 | VT Dept of Health | 03410-1370-15 | 2,134 |
| Children with Special Needs FY14 Global HHS Portion | 93.778 | VT Dept of Health | 03420-6187S | 26,351 |
| | 93.778 Total | | | 66,693 |
| Total Medicaid Cluster | | | | 66,693 |
| **Highway Planning and Construction Cluster** | | | | |
| U.S. Department of Transportation ("DOT") | | | | |
| Passed through other organizations | | | | |
| Highway Planning and Construction | 20.205 | VT Dept of Public Safety | CA0278 | 1,530 |
| Total Highway Planning and Construction Cluster | | | | 1,530 |
| **Highway Safety Cluster** | | | | |
| U.S. Department of Transportation | | | | |
| Passed through other organizations | | | | |
| Governor's Highway Safety | 20.600 | VT Dept of Public Safety | 02140-1112-6000 | 15,329 |
| Governor's Highway Safety | 20.613 | VT Dept of Public Safety | 02140-1012-6219 | (15,329) |
| Total Highway Safety Cluster | | | | - |
| **Student Financial Assistance Cluster** | | | | |
| U.S. Department of Education ("DOE") | | | | |
| Direct Awards | | | | |
| Federal Pell Grant Program | 84.063 | N/A | N/A | 47,486 |
| Total Student Financial Assistance Cluster | | | | 47,486 |
| **Other Programs** | | | | |
| U.S. Department of Health and Human Services | | | | |
| Direct Awards | | | | |
| OP Early Intervention Services | 93.918 | N/A | N/A | $ 639,563 |
| Total DHHS Direct Programs | | | | 639,563 |
| Passed through other organizations | | | | |
| BIO Grant | 93.074 | Health Research Inc | 2023-10 | 27,044 |
| Hemophilia Treatment Centers (SPRANS) | 93.110 | Mount Sinai School of Medicine | 6 H30 MC24048-02-01 | 18,088 |
| Hemophilia Treatment Centers (SPRANS) | 93.110 | Mount Sinai School of Medicine | 5 H30 MC24048-03-00 | 6,029 |
| | 93.110 Total | | | 24,117 |
| Education Training Center FY14 | 93.145 | Univ. of Massachusetts Worcester | WA00120856 ETC-08 | 43,502 |
| Education Training Center FY15 | 93.145 | Univ. of Massachusetts Worcester | WA00218320/RFS2015023 | 13,881 |
| | 93.145 Total | | | 57,383 |
| Public Health Surveillance for the Prevention of Complications | 93.184 | Univ. of Massachusetts Worcester | ATHN2011001-1-3 | 21,400 |
| CD10-10011 Strengthening Public Health Infrastructure for Improved Health Outcomes | 93.211 | Univ. of Vermont | G22RH22699 9769-001 | 32,676 |
| Screening, Brief Intervention, and Referral to Treatment Substance Abuse & Mental Health Services | 93.243 | VT Dept of Health | 03420-A14096S | 185,286 |
| Universal Newborn Hearing Screening | 93.251 | VT Dept of Health | 03420-6183S | 150,157 |
| Universal Newborn Hearing Screening | 93.251 | VT Dept of Health | 03420-6405S | 46,902 |
| | 93.251 Total | | | 197,059 |

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

# Fletcher Allen Partners, Inc. and Subsidiaries
## Schedule of Expenditures of Federal Awards
## Year Ended September 30, 2014

| Federal Agency/Program | Federal CFDA No. | Pass-Through Awards Entity | Pass-Through Awards Number | Total Expenditures |
|---|---|---|---|---|
| Poison Control and Stabilization Program | 93.253 | Northern New England Poison Control Center | n/a | 46,054 |
| Poison Control and Stabilization Program | 93.253 | Northern New England Poison Control Center | n/a | 4,578 |
| | 93.253 Total | | | 50,632 |
| Universal Newborn Hearing Screening | 93.283 | VT Dept of Health | 03420-5957S | (18) |
| Universal Newborn Hearing Screening | 93.283 | VT Dept of Health | 03420-6182S | 64,295 |
| Universal Newborn Hearing Screening | 93.283 | VT Dept of Health | 03420-6406S | 29,151 |
| | 93.283 Total | | | 93,428 |
| Small Rural Hospital Improvement Grant | 93.301 | Health Research Inc | 15-3533-13 | 8,724 |
| Gynecologic Oncology Group | 93.395 | HRI Roswell Park Cancer Institute Division | 5U10CA027469-31 | 35,469 |
| Vermont Blueprint for Health Administration | 93.525 | VT Dept of Health | 03410-1205-14/ HBEIE120130 | 37,943 |
| Vermont Health Connect Navigation Grant | 93.525 | VT Dept of Health | 03410-1370-15 | 3,306 |
| | 93.525 Total | | | 41,249 |
| Mental Health Screening for Refugee Children FY14 | 93.576 | VT Dept of Health | 03420-6164S | 12,854 |
| SafeTiNet | 93.715 | Univ. of Colorado Denver | 1R01HS019908-01 | (18,163) |
| Hospital Preparedness Program | 93.889 | Health Research Inc | 2053-08 | 113,928 |
| BIO Grant | 93.889 | HRI, HRSA | 2023-09 | 17,709 |
| Emergency Training | 93.889 | VT Dept of Health | 03420-5979S | 18,406 |
| VT Bioterrorism Preparedness Program | 93.889 | VT Dept of Health | 03420-6180S | 60,151 |
| | 93.889 Total | | | 210,194 |
| Ryan White Title 2 69-170 | 93.917 | VT Dept of Health | 03420-5918P | (96) |
| Ryan White Title 2 69-170 | 93.917 | VT Dept of Health | 03420-5713P | (705) |
| Ryan White Title 2 69-170 | 93.917 | VT Dept of Health | 03420-6124S | 167,932 |
| Ryan White Title 2 | 93.917 | VT Dept of Health | 03420-6372S | 41,355 |
| | 93.917 Total | | | 208,486 |
| Office of Alcohol and Drug Abuse prevention Day One Program | 93.959 | VT Dept of Health | 03420-A14046P | 423 |
| Office of Alcohol and Drug Abuse prevention Day One Program | 93.959 | VT Dept of Health | 03420-A13050P | 2,000 |
| | 93.959 Total | | | 2,423 |
| SAFE Title II Grant | 93.940 | VT Dept of Health | 03420-5827P | 12,388 |
| MCH Services Title V Block Grant Program | 93.994 | VT Dept of Health | 03420-6363S | 10,000 |
| MCH Services Title V Block Grant Program | 93.994 | VT Dept of Health | 6B04MC21401-01 | 5,986 |
| MCH Services Title V Block Grant Program | 93.994 | VT Dept of Health | 03420-6137S | 30,000 |
| MCH Services Title V Block Grant Program | 93.994 | VT Dept of Health | 03420-6366S | 35,000 |
| MCH Services Title V Block Grant Program | 93.994 | VT Dept of Health | 03420-6139S | 85,871 |
| MCH Services Title V Block Grant Program | 93.994 | VT Dept of Health | 03420-6187S | 54,062 |
| MCH Services Title V Block Grant Program | 93.994 | VT Dept of Health | 03420-6377S | 11,742 |
| MCH Services Title V Block Grant Program | 93.994 | VT Dept of Health | 03420-6186S | 105,042 |
| MCH Services Title V Block Grant Program | 93.994 | VT Dept of Health | 03420-6361S | 27,184 |
| | 93.994 Total | | | 364,887 |
| Total DHHS passed through other organizations | | | | 1,567,536 |
| Total DHHS | | | | 2,207,099 |
| U.S. Department of Labor ("DOL") | | | | |
| Passed through other organizations | | | | |
| H1-B | 17.268 | NY Dept of Labor | C014610 | 31,695 |
| Total DOL | | | | 31,695 |
| Total Other Programs | | | | 31,695 |
| Total Federal Awards | | | | $ 2,354,503 |

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, 2014

### 1. Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards presents the federal grant expenditures of Fletcher Allen Partners, Inc. and Subsidiaries ("FAP") for the year ended September 30, 2014.

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 or credits to amounts reported as expenditures in prior years.

### 2. Subrecipients

During fiscal 2014, FAP provided $161,423 to subrecipients of the OP Early Intervention Services award (CFDA #93.918) and $7,500 to subrecipients of the Screening, Brief Intervention, and Referral to Treatment: Substance Abuse & Mental Health Services award (CFDA #93.243) as follows. These amounts are included in the accompanying Schedule of Expenditures of Federal Awards:

| | | |
|---|---|---|
| Brattleboro Memorial Hospital | $ | 77,623 |
| Northern Counties Health Care, Inc. | | 41,500 |
| Rutland Regional Medical Center | | 42,300 |
| Total 93.918 | | 161,423 |
| Washington County Mental Health Services, Inc. | | 7,500 |
| Total 93.243 | | 7,500 |
| Total Subrecipients | $ | 168,923 |

### 3. Federal Direct Loans

Federally-guaranteed loans distributed to students by the William D. Ford Federal Direct Loan Program during the year ended September 30, 2014 are summarized as follows:

| | Federal CFDA Number | | |
|---|---|---|---|
| Federal Direct Stafford Loan Program | 84.268 | $ | 69,454 |
| Federal Direct PLUS Loan Program | 84.268 | | 6,986 |
| Total William D. Ford Federal Direct Loans | | $ | 76,440 |

These distributions and related funding sources are not included in the Organization's general purpose financial statements.

# Part II

# Reports on Compliance and Internal Controls

**Independent Auditor's Report 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. and Subsidiaries:

We have audited, 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, the consolidated financial statements of Fletcher Allen Partners, Inc. and Subsidiaries (the "Organization"), which comprise the consolidated balance sheet as of September 30, 2014, and the related consolidated statement of operations, changes in net assets and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 23, 2014.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the consolidated financial statements, we considered the Organization's internal control over financial reporting ("internal control") to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control.

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 a 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. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Organization's consolidated financial statements are free from 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*.

## Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Organization's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

PricewaterhouseCoopers LLP

December 23, 2014

**Independent Auditor's Report 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. and Subsidiaries:

## Report on Compliance for Each Major Federal Program

We have audited Fletcher Allen Partners, Inc. and Subsidiaries' (the "Organization") compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Organization's major federal programs for the year ended September 30, 2014. 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.

### *Management's Responsibility*

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

### *Auditor's Responsibility*

Our responsibility is to express an opinion on compliance for each of the Organization's major federal programs based on our audit of the types of compliance requirements referred to above. 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 on compliance for each major federal program. However, our audit does not provide a legal determination of the Organization's compliance.

### *Opinion on Each Major Federal Program*

In our opinion, the Organization complied, in all material respects, with the types of compliance 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, 2014.

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*Other Matters*

The results of our auditing procedures disclosed an instance of noncompliance, which is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying schedule of findings and questioned costs as item 2014-001. Our opinion on each major federal program is not modified with respect to this matter.

The Organization's response to the noncompliance finding identified in our audit is described in the accompanying Management's Views and Corrective Action Plan. The Organization's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

**Report on Internal Control Over Compliance**

Management of the Organization is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Organization's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program 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. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

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 material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

PricewaterhouseCoopers LLP

June 4, 2015

# Part III

# Federal Award Findings and Questioned Costs

# Fletcher Allen Partners, Inc. and Subsidiaries
## Schedule of Findings and Questioned Costs
## Year Ended September 30, 2014

**I. Summary of Auditors' Results**

**Financial Statements**

| | | |
|---|---|---|
| Type of auditors' report issued: | Unmodified | |
| Internal control over financial reporting:<br>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:<br>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 auditors' report issued on compliance for major programs | Unmodified | |
| Any audit findings disclosed that are required to be reported in accordance with Section .51O (a) of OMB Circular A-133? | _x_ yes | ___ no |

***Identification of Major Programs***

| Name of Federal Program | CFDA No. |
|---|---|
| OP Early Intervention Services | 93.918 |
| Screening, Brief Intervention, and Referral to Treatment: Substance Abuse & Mental Health Services | 93.243 |

| | | |
|---|---|---|
| Dollar Threshold used to Distinguish Type A and Type B Programs: | | $300,000 |
| Qualification of Auditee 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

**2014-001 – Subrecipient Monitoring**
**Grantor:** U.S. Department of Health and Human Services
**Award Name:** OP Early Intervention Services
**Award Year:** 07/2013 – 06/2014
**Award Numbers:** N/A
**CFDA Numbers:** 93.918

**Condition**
The Organization has various policies and procedures in place to monitor subrecipients at the grant level including among others, review of invoices and frequent communication with subrecipients which allow the Organization to verify that the subrecipient expenditures are incurred in accordance with the requirements of the federal award. In addition, the Organization obtains and reviews reports issued pursuant to OMB Circular A-133 ("A-133 reports") filed on the Federal Audit Clearinghouse website, and discusses audit findings with the subrecipient, as well as their impact on the Organization's funds. Per review of the Organization's three subrecipients disclosed in Footnote 2 of the Schedule of Expenditures of Federal Awards, one subrecipient met the audit requirements of OMB Circular A-133 to have an audit conducted and completed within 9 months of their audit period end. However, due to an administrative error, this subrecipient's A-133 report was not obtained or reviewed in a timely manner by the Organization.

**Criteria**
OMB A-110, *Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations*, paragraph 51(a), states that a pass-through entity is responsible for managing and monitoring each project, program, subaward, function or activity supported by the award. OMB Circular A-133, Subpart D, Section 400(d) further indicates a pass-through entity is responsible for:

1. Ensuring that subrecipients expending $500,000 or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of OMB Circular A-133 and that the required audits are completed within 9 months of the end of the subrecipient's audit period.
2. Issuing a management decision on audit findings within 6 months after receipt of the subrecipient's audit report and ensuring that the subrecipient takes timely and appropriate corrective action.
3. Considering whether subrecipient audits necessitate adjustment of the pass-through entity's own records.

**Cause**
The Organization has policies in place including obtaining and reviewing A-133 reports filed on the Federal Audit Clearinghouse website, and discussing audit findings with the subrecipient, as well as their impact on the Organization's funds. However, one instance was identified where no A-133 report was obtained or reviewed in a timely manner for a subrecipient. This failure to obtain the A-133 report resulted from an administrative error and as such, no report was obtained.

**Effect**
Without the appropriate level of subrecipient monitoring, the Organization may not be aware of noncompliance issues that are directly related to the awards that are passed-through to subrecipients. In addition, the Organization has increased risk that federal funding disbursed to a subrecipient will not be effectively managed and expended in accordance with the terms and conditions of its agreement with the federal agency.

**Questioned Cost**
There are no questioned costs.

**Recommendation**
We recommend that the Organization further emphasize the receipt and review of subrecipient A-133 reports for all subrecipients requiring such audits. This will ensure that the review is executed timely, consistently, and accurately in accordance with the compliance requirements.

**Management's Views and Corrective Action Plan**
Management's views and corrective action plan is included at the end of this report after the summary schedule of prior audit findings and status.

# Fletcher Allen Partners, Inc. and Subsidiaries
## Summary of Status of Prior Audit Findings
## Year Ended September 30, 2014

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

**FLETCHER ALLEN PARTNERS**

**111 Colchester Avenue - 101PA3**
**Burlington, VT 05401**
**802-847-3968**

Management's View and Corrective Action Plan

June 4, 2015

The Fletcher Allen Partners Grants Management office will proactively review all of the Organization's subrecipients to ensure that they are meeting the requirements listed in the Criteria section of Finding 2014-001 included in the report, and that, where applicable, findings noted in the subrecipients' A-133 reports will be appropriately considered and discussed with the subrecipient. The Grants Management office will also assess the impact of subrecipients' findings on the Fletcher Allen Partners A-133 report. Additionally, Fletcher Allen Partners will update current policies and procedures to clarify the roles and responsibilities for individuals in the Grants Management office to ensure there are no administrative errors resulting in the lack of diligence around subrecipients.

Thank you,

Todd Keating
Network CFO
Fletcher Allen Partners