Pinnacle Health Hospitals

Financial Statement

June 30, 2014

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June 30, 2014

REINSEL KUNTZ LESHER
certified public accountants & consultants

Independent Auditor's Report

To the Board of Directors
Pinnacle Health Hospitals
Harrisburg, Pennsylvania

Report on the Schedule of Expenditures of Federal Awards

We have audited the accompanying schedule of expenditures of federal awards of Pinnacle Health Hospitals for the year ended June 30, 2014, and the related notes to the schedule of expenditures of federal awards.

Management's Responsibility for the Schedule of Expenditures of Federal Awards

Management is responsible for the preparation and fair presentation of this schedule of expenditures of federal awards 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 a schedule of expenditures of federal awards that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the schedule of expenditures of federal awards based on our audit.

We conducted our audit 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 the schedule of expenditures of federal awards is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statement. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the schedule of expenditures of federal awards, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the schedule of expenditures of federal awards in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the schedule of expenditures of federal awards.

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

Opinion

In our opinion, the schedule of expenditures of federal awards referred to above presents fairly, in all material respects, the expenditures of federal awards of Pinnacle Health Hospitals for the year ended June 30, 2014, in accordance with accounting principles generally accepted in the United States of America.

Reinsel Kuntz Lesher LLP

March 24, 2015
York, Pennsylvania

Federal Grantor/Pass-Through Grantor/Program or Cluster	Federal CFDA	Pass-Through Entity Identifying Number	Year Ended June 30, 2014 Federal Expenditures
Department of Justice			
Pass-Through Programs from			
Pennsylvania State Chapter of Children's Advocacy Centers and Multidisciplinary Teams			
Improving the Investigation and Prosecution of Child Abuse and the Regional and Local Children's Advocacy Centers	16.758	5-HARR-PA-SA13	$ 4,865
Pennsylvania Commission on Crime and Delinquency			
Crime Victim Assistance	16.575	24261	47,169
Crime Victim Assistance	16.575	24263	3,821
Crime Victim Assistance	16.575	24265	1,542
Crime Victim Assistance	16.575	24267	5,923
Total Department of Justice			63,320
Department of Education			
Pass-Through Programs from			
Cumberland/Perry County			
Special Education - Grants for Infants and Families	84.181	Pinnacle Health	180,122
Dauphin County			
Special Education - Grants for Infants and Families	84.181	Pinnacle Health	100,000
Total Department of Education			280,122
Department of Health and Human Services			
Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	93.918	H76HA00617E0	288,705
Pass-Through Programs from			
The University of Pittsburgh Office of Research			
National Network of Libraries of Medicine: Mid-Atlantic Region	93.000	0020808-408495-Y2001	959
National Network of Libraries of Medicine: Mid-Atlantic Region	93.000	0020808-408495-Y2037	1,500
Pennsylvania Department of Public Welfare			
Affordable Care Act (ACA) Maternal, Infant, and Early Childhood Home Visiting Program	93.505	4100056834	106,115
Affordable Care Act (ACA) Maternal, Infant, and Early Childhood Home Visiting Program	93.505	4100061356	315,980
Pennsylvania Department of Health			
Hospital Preparedness Program (HPP) and Public Health Emergency Preparedness (PHEP) Aligned Cooperative Agreements	93.074	4100062677	72,256
State Partnership Grant Program to Improve Minority Health	93.296	6 STTMP101040-03-01	4,027
Maternal and Child Health Services Block Grant to the States	93.994	4100063801	719,770
Family Health Council of Central Pennsylvania			
HIV Care Formula Grants	93.917	Pinnacle Health	28,263
Jewish Health Federation			
HIV Care Formula Grants	93.917	Pinnacle Health	1,150
Total Department of Health and Human Services			1,538,725
Total Expenditures of Federal Awards			$ 1,882,167

See accompanying notes.

Note 1 - Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards (SEFA) includes only the federal grant activity of Pinnacle Health Hospitals (Organization) and is presented on the accrual basis of accounting. The SEFA is not intended to present fairly all of the expenses of the Organization taken as a whole in accordance with accounting principles generally accepted in the United States of America. 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*.

Note 2 - Grant Awards Reconciliation to Schedule of Expenditures of Federal Awards

The Organization was awarded grant contracts from various funding sources where the amounts reported on the SEFA do not agree with the amounts received in total funding during the year ended June 30, 2014 due to an overlap of the grant years and the fiscal year of the Organization, as well as the inclusion of some state funding within the total award. Reconciliations of the SEFA to the contract awards, segregated by funding source, are presented below.

Pennsylvania State Chapter of Children's Advocacy Centers and Multidisciplinary Teams

The contracts with the Pennsylvania Chapter of Children's Advocacy Centers and Multidisciplinary Teams for the Children's Resource Center includes federal funding through Improving the Investigation and Prosecution of Child Abuse and the Regional and Local Children's Advocacy Centers, CFDA 16.758. The reconciliation of the award amount to the amount reported on the SEFA consists of the following for the year ended:

	June 30, 2014
Contract 5-HARR-PA-SA13	
Total grant award - January 1, 2013 - December 31, 2013	$ 9,000
Expenditures incurred July 1, 2012 - June 30, 2013	(4,135)
Schedule of Expenditures of Federal Awards - CFDA 16.758	$ 4,865

Note 2 - Grant Awards Reconciliation to Schedule of Expenditures of Federal Awards (continued)

Pennsylvania Commission on Crime and Delinquency

The contracts with the Pennsylvania Commission on Crime and Delinquency (PCCD) for the Children's Resource Center include multi-year grant contracts comprised of federal funding through Crime Victim Assistance, CFDA 16.575. The reconciliation of the amounts reported on the SEFA to the award amounts consists of the following for the year ended:

	June 30, 2014
Contract 24261	
Total grant award - July 1, 2013 - June 30, 2015	$ 113,334
Funding carried forward to fiscal year ending June 30, 2015	(66,165)
Schedule of Expenditures of Federal Awards - CFDA 16.575	$ 47,169
Contract 24263	
Total grant award - July 1, 2013 - June 30, 2015	$ 6,970
Funding carried forward to fiscal year ending June 30, 2015	(3,149)
Schedule of Expenditures of Federal Awards - CFDA 16.575	$ 3,821
Contract 24265	
Total grant award - July 1, 2013 - June 30, 2015	$ 18,989
Funding carried forward to fiscal year ending June 30, 2015	(17,447)
Schedule of Expenditures of Federal Awards - CFDA 16.575	$ 1,542
Contract 24267	
Total grant award - July 1, 2013 - June 30, 2015	$ 11,305
Funding carried forward to fiscal year ending June 30, 2015	(5,382)
Schedule of Expenditures of Federal Awards - CFDA 16.575	$ 5,923

Note 2 - Grant Awards Reconciliation to Schedule of Expenditures of Federal Awards (continued)

Commonwealth of Pennsylvania Department of Public Welfare

The contracts with the Commonwealth of Pennsylvania Department of Public Welfare include federal funding through the Affordable Care Act (ACA) Maternal, Infant, and Early Childhood Home Visiting Program, CFDA 93.505. The reconciliation of the amounts reported on the SEFA to the award amounts consists of the following for the year ended:

	June 30, 2014
Contract 4100056834	
Total grant awards - July 1, 2013 - June 30, 2014	$ 112,804
Unspent funds	(6,689)
Schedule of Expenditures of Federal Awards - CFDA 93.505	$ 106,115
Contract 4100061356	
Total grant award - July 1, 2013 - June 30, 2014	$ 340,500
Unspent funds	(24,520)
Schedule of Expenditures of Federal Awards - CFDA 93.505	$ 315,980

Note 2 - Grant Awards Reconciliation to Schedule of Expenditures of Federal Awards (continued)

Commonwealth of Pennsylvania Department of Health

The contract for the Pennsylvania Lead and Healthy Homes Program is a grant comprised of federal funding through Maternal and Child Health Services Block Grant to the States, CFDA 93.994. The reconciliation of the amounts reported on the SEFA to the award amount consists of the following for the year ended:

	June 30, 2014
Contract 4100063801	
Total grant award - July 1, 2013 - June 30, 2014	$ 1,144,203
Unspent funds	(424,433)
Schedule of Expenditures of Federal Awards - CFDA 93.994	$ 719,770

The contract for the Minority Health Program is a grant comprised of federal funding through State Partnership Grant Program to Improve Minority Health, CFDA 93.296. The reconciliation of the amounts reported on the SEFA to the award amount consists of the following for the year ended:

	June 30, 2014
Contract 7/1/13-6/30/14	
Total grant award - July 1, 2013 - June 30, 2014	$ 4,150
Unspent funds	(123)
Schedule of Expenditures of Federal Awards - CFDA 93.296	$ 4,027

Family Health Council of Central Pennsylvania

The contract with the Family Health Council of Central Pennsylvania includes a grant comprised of federal funding through the HIV Care Formula Grants, CFDA 93.917. The reconciliation of the award amount to the amount reported on the SEFA consists of the following for the year ended:

	June 30, 2014
Contract 7/1/13-6/30/14	
Total grant award - July 1, 2013 - June 30, 2014	$ 163,080
Non-federal funds	(106,602)
Unspent funds	(28,215)
Schedule of Expenditures of Federal Awards - CFDA 93.917	$ 28,263

Note 2 - Grant Awards Reconciliation to Schedule of Expenditures of Federal Awards (continued)

Jewish Health Federation

The contract with the Jewish Health Federation includes a grant comprised of federal funding through the HIV Care Formula Grants, CFDA 93.917. The reconciliation of the award amount to the amount reported on the SEFA consists of the following for the year ended:

	June 30, 2014
Contract 7/1/13-6/30/14	
Total grant award - July 1, 2013 - June 30, 2014	$ 30,000
Non-federal funds	(4,600)
Unspent funds	(24,250)
Schedule of Expenditures of Federal Awards - CFDA 93.917	$ 1,150

Section I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued:	Unmodified
Internal control over financial reporting:	
Material weakness(es) identified?	☐ yes ☒ no
Significant deficiency(ies) identified?	☐ yes ☒ none reported
Noncompliance material to financial statements noted?	☐ yes ☒ no

Federal Awards

Internal control over major federal programs:	
Material weakness(es) identified?	☐ yes ☒ no
Significant deficiency(ies) identified?	☐ yes ☒ none reported
Type of auditor's report issued on compliance for major federal programs:	Unmodified
Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133?	☐ yes ☒ no

Identification of Major Programs:

CFDA Number(s)	Name of Federal Program or Cluster
93.505	Affordable Care Act - Maternal, Infant, and Early Childhood Home Visiting Program
93.994	Maternal and Child Health Services Block Grant to the States

Dollar threshold used to distinguish between Type A and Type B programs:	$300,000
Auditee qualified as low-risk auditee?	☒ yes ☐ no

REINSEL KUNTZ LESHER
certified public accountants & consultants

Independent Auditor's Report on Compliance for Each Major Federal Program; and Report on Internal Control Over Compliance Required by OMB Circular A-133

To the Board of Directors
Pinnacle Health Hospitals
Harrisburg, Pennsylvania

Report on Compliance for Each Major Federal Program

We have audited Pinnacle Health Hospitals' (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 June 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.

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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 June 30, 2014.

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.

Reinsel Kuntz Lesher LLP

March 24, 2015
York, Pennsylvania

Pinnacle Health System

(And controlled entities and subsidiaries)

Consolidated Financial Statements and Supplemental Data

June 30, 2014 and 2013

Pinnacle Health System
(And controlled entities and subsidiaries)
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June 30, 2014 and 2013

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Independent Auditor's Report

To the Board of Directors of Pinnacle Health System:

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Pinnacle Health System (and controlled entities and its subsidiaries), which comprise the consolidated balance sheets as of June 30,2014 and June 30, 2013, and the related consolidated statements of operations, changes in net assets, and its 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

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 entity'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 entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the 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, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Pinnacle Health Systems (and controlled entities and subsidiaries) as of June 30, 2014 and June 30, 2013, and the consolidated statements of operations, changes in net assets, and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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Other Matters

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 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 September 10, 2014 on our consideration of Pinnacle Health System'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 Pinnacle Health System's internal control over financial reporting and compliance.

PricewaterhouseCoopers LLP

Harrisburg, PA
September 10, 2014

Pinnacle Health System
(And controlled entities and subsidiaries)
Consolidated Statements of Financial Position
June 30, 2014 and 2013

(in thousands of dollars)	**2014**	**2013**
Assets		
Current		
Cash and cash equivalents	$ 23,152	$ 34,446
Accounts receivable - Patient, less allowance for doubtful accounts of approximately $37,092 in 2014 and $28,378 in 2013	120,370	84,476
Accounts receivable - Other	14,235	12,646
Investments	206,686	203,373
Inventories	14,816	12,282
Prepaid expenses	14,662	13,440
Trustee held funds for capital projects	738	89,285
Current portion of self-insurance trust funds	-	1,227
Total current assets	394,659	451,175
Assets limited as to use		
Self-insurance trust funds, net of current portion	-	3,450
Board-designated funds	65,153	54,602
Board-designated funds for capital acquisition	170,495	154,380
Funds held by trustee for debt service fund	14,591	14,588
Total assets limited as to use	250,239	227,020
Investments temporarily restricted as to use	15,724	13,474
Investments permanently restricted as to use	21,296	19,624
Property, plant and equipment, net	517,006	399,802
Pledges receivable	10,651	6,927
Goodwill	43,086	43,891
Other assets	20,914	21,071
Total assets	$ 1,273,575	$ 1,182,984

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

Pinnacle Health System
(And controlled entities and subsidiaries)
Consolidated Statements of Financial Position
June 30, 2014 and 2013

(in thousands of dollars)	**2014**	**2013**
Liabilities and Net Assets		
Current		
Current portion of long-term debt	$ 12,495	$ 11,273
Accounts payable and accrued expenses	62,694	51,605
Accrued salaries, wages and fees	33,546	27,772
Accrued vacation	20,752	19,671
Accrued insurance costs	22,689	26,705
Accrued retirement costs	499	460
Due to third-party payors	1,637	1,837
Advances from third-party payors	3,809	3,809
Total current liabilities	158,121	143,132
Long-term liabilities		
Accrued insurance costs, net of current portion	4,888	5,597
Accrued retirement costs, net of current portion	43,802	51,095
Interest rate swap agreement	5,522	5,741
Long-term debt, net of current portion	410,704	411,802
Total long-term liabilities	464,916	474,235
Net assets		
Unrestricted net assets		
Unrestricted net assets Pinnacle Health System	594,715	524,080
Noncontrolling interests in consolidated subsidiary company	1,435	1,512
Total unrestricted net assets	596,150	525,592
Temporarily restricted net assets	33,090	20,401
Permanently restricted net assets	21,298	19,624
Total net assets	650,538	565,617
Total liabilities and net assets	$ 1,273,575	$ 1,182,984

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

Pinnacle Health System
(And controlled entities and subsidiaries)
Consolidated Statements of Operations
Years Ended June 30, 2014 and 2013

(in thousands of dollars)	2014	2013
Unrestricted revenues		
Net patient service revenues (net of contractual allowances and discounts)	$ 882,429	$ 849,717
Provision for bad debts	(49,081)	(42,625)
Net patient service revenue less provision for bad debts	833,348	807,092
Other revenues	22,451	20,066
Net assets released from restrictions used for operations	3,446	3,393
Total unrestricted revenues	859,245	830,551
Expenses		
Salaries and wages	362,441	333,663
Fringe benefits	80,163	83,397
Professional fees	25,674	24,204
Supplies	136,040	128,978
Purchased services	145,570	138,340
Interest	15,768	17,582
Depreciation and amortization	56,821	51,287
Total expenses	822,477	777,451
Income from operations before pension settlement loss	36,768	53,100
Pension settlement loss	(44,913)	-
(Loss) income from operations after pension settlement loss	(8,145)	53,100
Nonoperating gains (losses)		
Investment income	37,495	23,500
(Loss) gain on disposal of assets	(225)	336
Loss on goodwill impairment	(1,525)	(1,584)
Realized and unrealized (losses) gains on interest rate swap	(1,235)	1,375
Nonoperating gain, net	34,510	23,627
Revenues and gains over expenses and losses	$ 26,365	$ 76,727

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

Pinnacle Health System
(And controlled entities and subsidiaries)
Consolidated Statements of Changes in Net Assets
Years Ended June 30, 2014 and 2013

(in thousands of dollars)	**2014**	**2013**
Unrestricted net assets		
Revenues and gains over expenses and losses	$ 26,365	$ 76,727
Change in post-retirement liability	43,913	34,440
Net assets released from restrictions for purchases of property, plant and equipment	36	2,413
Income (loss) attributable to and other changes in noncontrolling interests	245	(1,272)
Increase in unrestricted net assets	70,559	112,308
Temporarily restricted net assets		
Contributions	9,167	8,165
Net realized and unrealized gains on investments	7,032	4,156
Net assets released from restrictions	(3,511)	(5,729)
Increase in temporarily restricted net assets	12,688	6,592
Permanently restricted net assets		
Contributions	3	1
Net realized and unrealized gains on investments and changes in interests in beneficial trusts	2,225	1,937
Appropriation of endowment assets for spending	(554)	(511)
Increase in permanently restricted net assets	1,674	1,427
Increase in net assets	84,921	120,327
Net assets		
Beginning of year	565,617	445,290
End of year	$ 650,538	$ 565,617

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

Pinnacle Health System
(And controlled entities and subsidiaries)
Consolidated Statements of Cash Flows
Years Ended June 30, 2014 and 2013

(in thousands of dollars)	**2014**	**2013**
Cash flows from operating activities		
Change in net assets	$ 84,921	$ 120,327
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Net realized and unrealized gains on investments	(43,178)	(19,273)
Provision for bad debts	49,081	42,625
Depreciation and amortization	56,821	51,287
Loss (gain) on disposal of assets	225	(336)
Change in pension liability	(43,913)	(34,440)
Equity in (gains) losses of joint ventures and affiliates	699	(1,823)
Changes in noncontrolling interest in consolidated subsidiary company	(245)	1,272
Loss on goodwill impairment	1,525	1,584
Loss on pension settlement accounting	44,913	-
Restricted contributions and investment gain income	739	807
Change in current assets and liabilities		
Increase in accounts receivable	(86,564)	(50,143)
Increase in pledges receivable	(6,567)	(6,381)
Increase in inventories, goodwill, and other assets	(3,296)	(2,719)
Increase in prepaid expenses	(1,222)	(2,285)
Increase in accounts payable and accrued expenses	10,870	10,660
Increase in accrued salaries, wages and fees and accrued vacation	6,855	5,125
Decrease in accrued insurance and retirement costs	(12,979)	(90)
Decrease in advances from and amounts due to third-party payors	(200)	(4,058)
Net cash provided by operating activities	58,485	112,139
Cash flows from investing activities		
Purchase of property, plant and equipment	(169,450)	(102,287)
Net (contributions) distributions to joint ventures and affiliates	(454)	689
Sale (purchase) of investments, including assets limited as to use, net	102,499	(111,593)
Proceeds from sale of assets	195	276
Net cash used in investing activities	(67,210)	(212,915)
Cash flows from financing activities		
Cash paid for financing costs	-	(1,501)
Repayments of long-term debt	(5,719)	(30,224)
Proceeds from long-term debt	801	135,250
Cash receipts from pledges	2,843	1,901
Distributions (contributions) to noncontrolling interests in in consolidated subsidiary	245	(1,272)
Restricted contributions and investment income	(739)	(807)
Net cash (used) provided by financing activities	(2,569)	103,347
Net (decrease) increase in cash and cash equivalents	(11,294)	2,571
Cash and cash equivalents		
Beginning of year	34,446	31,875
End of year	$ 23,152	$ 34,446

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

1. Description of Organization

Pinnacle Health System ("Parent"), located in Harrisburg, Pennsylvania, consists of the following controlled entities and subsidiaries (collectively the "System").

Pinnacle Health Foundation ("Foundation"), is a tax-exempt, nonprofit corporation, engaged in fund raising activities for the benefit of the controlled entities of the System.

Pinnacle Health Hospitals ("Hospital"), is a tax-exempt, nonprofit, multi-facility acute care hospital.

Pinnacle Health Emergency Department Services, LLC ("PHEDS"), is a tax-exempt, nonprofit corporation engaged in providing professional services in the Pinnacle Health Emergency Department.

Pinnacle Health Hospitalist Services, LLC ("Hospitalists"), is a tax-exempt, nonprofit company that provides physician services to Pinnacle Health Hospital's inpatients and observation patients.

Community Life Team ("CLT"), is a tax-exempt, nonprofit entity that provides both emergency and nonemergency ambulance services to citizens in the Harrisburg, PA area and surrounding counties.

Pinnacle Health Medical Services ("PHMS"), is a tax-exempt, nonprofit entity engaged in the operation of both primary care and specialty physician practices and providing mental health services.

Pinnacle Health Cardiovascular Institute ("PHCVI") and its wholly-owned subsidiary, Cardiology Practice Inc. ("CPI"), are 100% owned for profit corporations engaged in providing comprehensive cardiac care. CPI ceased operations on December 31, 2012 and all assets and liabilities merged into PHCVI.

Pinnacle Health Medical Group ("PHMG") is a wholly-owned, for profit corporation engaged in the operation of primary care physician practices. PHMG ceased operations on December 31, 2013 and all assets and liabilities were transferred into PHMS.

Pinnacle Health Ventures Inc. (PHVI) and Pinnacle Health Imaging Inc. (PHI) were formed as a result of the acquisition of 100% of the stock of Tristan Associates on March 1, 2012. PHVI is the stock holding company and sole shareholder of PHI. PHI owns and/or leases radiology and imaging equipment and services at four office locations. PHI leases equipment and services to Hospital.

River Health ACO, LLC ("RHACO") was formed on April 15, 2013 and was approved by CMS to become recognized as an Accountable Care Organization (ACO) dedicated to improving the cost, quality, access and patient experience to care for residents of Central Pennsylvania. The ACO is comprised of two founding partners: Pinnacle Health System and Susquehanna Health System, Inc., and two independent primary care practice partners, Family Practice Centers, P.C. and Annville Family Medicine, P.C.

United Health Risk, Ltd. ("UHR") is a wholly-owned, for profit, offshore captive insurance company.

United Central Pennsylvania Reciprocal Risk Retention Group ("RRG") is a wholly-owned, for profit, Vermont captive insurance company.

West Shore Surgery Center, LLP ("WSSC") is a limited liability partnership owned 2% by PHMS, the general partner, 49% by the Hospital and 49% by physicians.

Pinnacle Health System Obligated Group ("Obligated Group"), consists of the Parent, Hospital, and PHMS.

2. Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the Parent and its controlled entities and subsidiaries. The accounts of the controlled entities have been included in the consolidated financial statements to reflect the results of operations of entities under common control. All significant intercompany transactions have been eliminated.

Basis of Financial Reporting

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 and the reported amounts of revenues and expenses during the reporting period. These significant estimates include the accounts receivable allowance for doubtful accounts, contractual allowances, due to third party payors, accrued pension liabilities, accrued retirement costs and accrued insurance costs. Actual results could differ from those estimates as they are prepared based on certain assumptions which are subject to change.

Reclassification of Prior Year Balances

Certain 2013 balances have been reclassified to conform to the 2014 presentation.

Net Patient Service Revenues

The hospital has agreements with third party payors that provide for payments to the hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenues are reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods for tentative and final settlements.

Allowance for Doubtful Accounts

Accounts receivable are recorded at their estimated net realizable value. The allowance for doubtful accounts is estimated based upon historical collection rates.

Revenues and Gains Over Expenses and Losses

The consolidated statements of operations include revenues and gains over expenses and losses. Changes in unrestricted net assets which are excluded from revenues and gains over expenses and losses, consistent with industry practice, include changes in the post-retirement liability, noncontrolling interests and net assets released from donor restrictions to be used for purchases of property, plant and equipment.

Cash and Cash Equivalents

Cash and cash equivalents include cash management funds with original maturities of three months or less, excluding amounts whose use is limited by Board-designation or other arrangements under trust agreements. The System maintains cash and cash equivalents in local banks.

Investments

The System follows standards issued by the Financial Accounting Standards Board ("FASB") related to fair value accounting. The standards define fair value, establish a framework for measuring fair value and expand disclosures about fair value measurements. The standards also provide an option to report selected financial assets and liabilities at fair value and establish presentation and disclosure requirements. The fair value option permits the System to elect to measure eligible items at fair value on an instrument-by-instrument basis and then report the unrealized gains and losses for those items in the System's revenues and gains over expenses and losses. The System has chosen to record all of its investments under the fair value option permitted under these standards.

Under these fair value standards, the System is required to categorize and disclose certain assets and liabilities, including investments, at fair value, according to three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not always active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

The following is a description of the System's valuation methodologies for investments carried at fair value. These methods may produce a fair value calculation that may not be reflective of future fair values. Furthermore, while the System believes that its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of investments could result in a different estimate of fair value at the reporting date.

Where quoted prices are available in an active market, investments are classified in Level 1 of the valuation hierarchy. Investments in Level 1 include cash management funds, US Treasury Obligations, exchange-traded equity securities and mutual funds with a published daily net asset value or its equivalent ("NAV"). Investments in Level 2 include financial instruments valued based on quoted market prices for identical securities in markets that are not always active, quoted prices for similar securities in markets that are active, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. If quoted prices are not available, other accepted valuation methodologies, such as interest rates, observable yield curves and spreads may be used to determine fair value. This level includes investments in marketable corporate debt securities, U.S. agency debt securities, and other debt securities.

Level 2 also includes investments in certain mutual funds that permit daily redemptions but whose NAV is not published and investments in certain private entities that calculate NAV per share, or its equivalent, if the System has the ability to redeem its investment with the investee at the stated NAV at the measurement date or shortly thereafter. Such investments are considered "alternative investments" and are recorded at fair value based on the NAV as a practical expedient, as provided by the respective general partner or fund administrator of the individual alternative investment funds. There are no unfunded commitments for these investments.

The System believes the fair value of alternative investments in the consolidated balance sheets is a reasonable estimate of its ownership interest in the alternative investment funds. As part of the System's overall valuation process, management evaluates these third-party methodologies to ensure that they are representative of exit prices in the security's principal markets.

These valuation methods may produce a fair value estimate that may not be reflective of future fair values. Furthermore, while the System believes that its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine fair value could result in a materially different estimate of fair value at the reporting date. See Note 6 for additional details related to the System's investments.

Derivative Instruments

The System accounts for derivative financial instruments in accordance with standards issued by the FASB. These standards require that all derivative instruments be recorded on the balance sheet at fair value as either assets or liabilities. Since the derivatives entered into by the System do not qualify for hedge accounting, changes in fair value of the derivative are recognized in nonoperating gains/(losses). The use of derivative instruments by the System is currently limited to interest rate swaps.

Inventories

Inventories are stated at lower of cost (first-in, first-out method) or market.

Assets Limited as to Use

Assets limited as to use include Board-designated funds, Board-designated funds for capital acquisition and the portion of self-insurance funds and funds held by trustee that have not been reflected as current assets to meet the current portion of self-insured liabilities and long-term debt. Insurance collateral funds represent monies that are designated as collateral for a letter of credit that is designated to fund current and future liabilities for payment of professional liability and workers' compensation claims. Board-designated funds and Board-designated funds for capital acquisition represent funds designated by the Board of Directors for capital acquisition and replacement and to support System initiatives.

Property, Plant and Equipment

Property, plant and equipment is stated at cost, net of accumulated depreciation and amortization. Depreciation is computed on the straight-line method over the estimated useful lives of the assets. Gains and losses resulting from the sale or disposal of property, plant and equipment are included in nonoperating gains (losses). Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the financial statements.

Investments in and Advances to Joint Ventures and Affiliates
The System, through its controlled entities and subsidiaries, maintains an ownership interest in several joint ventures which provide various clinical and nonclinical services. These investments, with the exception of Affilia, are accounted for under the equity method since the ownership interest is between 20.0% and 50.0% and control is not exercised. The System maintains an 11.8% ownership interest in Affilia. and accounts for it on the cost method. Under the terms of the agreements, the System may be required from time to time to make additional cash contributions and provide working capital advances to the joint ventures.

Pledges Receivable
The System records its pledges receivable at the estimated net realizable value, discounted at a rate of 4% at June 30, 2014 and 2013. Pledges receivable in the amounts of $2,361, $2,233, $2,162, $1,021 and $72 are due in fiscal years 2015, 2016, 2017, 2018 and 2019, respectively.

Deferred Financing Costs
Deferred financing costs are amortized over the life of the bonds using the effective interest method.

During 2013, the System capitalized financing costs of $1,501, incurred as a result of the issuance of the Series 2012A Health System Revenue Bond. During 2014, the System capitalized financing costs of $0.

Amortization expense was $165 and $161 for the years ended June 30, 2014 and 2013, respectively.

Accrued Insurance Costs
Accrued insurance costs consist of estimated liabilities for reported and incurred but not reported claims related to professional liability, workers' compensation and employee health care. The System discounts its liabilities for professional liability and workers' compensation claims. As of June 30, 2014 and 2013, the discount rate was 3.50%.

Temporarily and Permanently Restricted Net Assets
Temporarily restricted net assets are those whose use by the System has been limited by donors to a specific time period or purpose. Permanently restricted net assets, excluding interest and dividend income earned on such assets which is unrestricted, have been restricted by donors to be maintained by the System or outside beneficial trusts in perpetuity.

Donor Restricted Gifts
Unconditional promises to give cash and other assets to the System are reported at estimated fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at estimated fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose or restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

Income Taxes
The majority of the System is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. On such basis, the exempt entities will not incur any liability for federal income taxes, except for possible unrelated business income.

The System evaluates uncertain tax positions using a two-step approach for recognizing and measuring tax benefits taken or expected to be taken in an unrelated business activity tax return and disclosures regarding uncertainties in tax positions. No adjustments to the consolidated financial statements were required as a result of this evaluation.

The following entities are not exempt from federal income tax: PHCVI, PHMG, PHVI, RRG, RHACO and WSSC, and therefore, may incur liabilities for federal and state income taxes.

Fair Value of Financial Instruments
Financial instruments include cash and cash equivalents, accounts receivable, investments, and interest rate swap agreement. The carrying amount reported in the consolidated balance sheets for cash and cash equivalents, accounts receivable, approximates fair value and investments and interest rate swap agreement equal fair value as of June 30, 2014 and 2013.

The undiscounted carrying value of the System's 2009A, 2011A, and 2012A revenue bonds was $398,235 and $403,825 at June 30, 2014 and 2013, respectively. The undiscounted fair value of the System's 2009A, 2011A, and 2012A revenue bonds was $419,829 and $415,968 at June 30, 2014 and 2013, respectively. The fair value of the System's revenue bonds was based on quoted market prices. The System considers the inputs in the valuation process of its long-term debt to be Level 2 in the fair value hierarchy.

Supplemental Disclosure of Cash Flow Information
Interest paid for the years ended June 30, 2014 and 2013 was $18,411 and $18,800, respectively.

There were no income taxes paid in fiscal 2014 and 2013.

During 2014 and 2013, capital lease obligations of $1,745 and $0, respectively, were incurred when the System entered into lease agreements to provide imaging equipment. These obligations are considered to be a noncash financing activity.

During 2014 and 2013, property, plant and equipment of $18,341 and $14,240 were included in accounts payable and accrued expenses.

Accounting for Defined Benefit and Other Postretirement Benefits
The System follows FASB standards over employer's accounting for defined benefit pension and other postretirement plans. Included in these standards is a requirement for an entity to recognize in its balance sheet, the overfunded or underfunded status of its defined benefit postretirement plans measured as the difference between the fair value of the plan assets and the benefit obligation. For a pension plan, this would be the projected benefit obligation; for any other postretirement plan, the benefit obligation would be the accumulated postretirement benefit obligation. These standards also require measurement dates for the pension plan obligation to be measured as of the date of the entity's balance sheet.

Goodwill
In accordance with Accounting Standards Update No. 2011-08 (“ASU 2011-08”), Testing Goodwill for Impairment, the System performs its annual goodwill impairment test as of March 31. Under ASU 2011-08, the Company assessed certain qualitative factors to determine if it was more likely than not that the fair value of certain segments within Pinnacle Health Medical Services, Pinnacle Health Hospitals, Pinnacle Health Ventures, and Pinnacle Health Cardiovascular Institute were less than their carrying amount.

3. Acquisitions

During fiscal year ended June 30, 2013 Pinnacle Health System acquired the building and assets of Greater Harrisburg Cancer Center for a total cost of $4,600 which included goodwill totaling $3,050. The building was located on land owned by Pinnacle Health System adjacent to the Pinnacle Health System Cancer Center and was used to accommodate the increased demand in the area for cancer treatment services. It was later decided to build a new Cancer Center near the new West Shore Hospital and the total goodwill of $3,050 was written off over FY13 and 14.

4. Net Patient Service Revenues

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

- **Medicare**: Inpatient acute care and rehabilitation 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. Medical education and transplant costs related to Medicare beneficiaries are paid based on a cost reimbursement methodology. Outpatient services are paid based on the ambulatory payment classification system. The System is paid for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicare fiscal intermediary.

- **Medicaid**: Inpatient services are rendered to Medicaid program beneficiaries based on a patient classification system similar to Medicare. Outpatient services are paid on a predetermined fee schedule.

- **Capital Blue Cross and Highmark Blue Shield**: Inpatient acute care services and certain outpatient procedures rendered to Blue Cross and Blue Shield program beneficiaries are paid at prospectively determined rates per discharge or per procedure. Other outpatient services are paid at a discount from established rates.

- **Other Payors**: The System has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the System under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Notes to Consolidated Financial Statements (in thousands of dollars)

In accordance with ASU 2011-07, the following schedule represents the System's estimated net patient service revenue, before provision for bad debt expense, aggregated between self-pay and all other third-party payors for the fiscal years ended June 30, 2014 and 2013.

	June 30, 2014		
	Third-Party Payors	Self-Pay	Total All Payors
Patient service revenue (net of contractual allowances and discounts)	$ 838,375	$ 44,055	$ 882,430

	June 30, 2013		
	Third-Party Payors	Self-Pay	Total All Payors
Patient service revenue (net of contractual allowances and discounts)	$ 806,669	$ 43,048	$ 849,717

Revenue received under agreements with several third-party payors is subject to audit and retroactive adjustment. Adjustments related to settlements with third-party payors are included in the determination of revenues and gains over expenses and losses in the year in which such adjustments become known. Such adjustments resulted in an increase in revenue of approximately $2,284 and $2,730 in 2014 and 2013, respectively, due to the receipt of tobacco settlement payments, Medicare budget neutrality appeal payment and changes in general reserve estimates and other miscellaneous estimates.

5. Charity Care and Community Service

The System provides services to patients who meet the criteria of its charity care policy without charge or at amounts less than the established rates. Criteria for charity care consider family income levels, household size and ability to pay. Federal poverty guidelines are used as a means to determine the patient's ability to pay. Individuals who qualify for charity care are either uninsured or are extremely indigent and cannot afford their deductibles or coinsurance amounts.

The System maintains records to identify and monitor the level of charity care and community service it provides. These records include the amount of charges foregone based on established rates for services and the estimated cost of those services furnished under its charity care policy. The System provides community service programs to the community at large. A report is issued annually to inventory community benefits in furtherance of its exempt purpose.

Charges foregone associated with charity care service to individuals were approximately $30,749 and $26,597 for 2014 and 2013, respectively. The charity care amounts have been excluded from net patient service revenues. The cost incurred to provide such care was approximately $10,500 and $8,498 for 2014 and 2013, respectively.

Notes to Consolidated Financial Statements (in thousands of dollars)

6. Investments

Investments at June 30, 2014 and 2013, consist of:

	2014	2013
Investments		
Cash management funds	$ 12,326	$ 24,807
U.S. Government obligations	10,699	9,770
U.S. Treasuries	22,453	22,693
Corporate obligations	94,274	88,147
Fixed income investments	13,308	12,451
Domestic common stock	18,025	17,260
Other domestic equity investments and pooled trusts	20,254	15,543
Foreign equity investments	14,390	11,735
Accrued income	957	967
	$ 206,686	$ 203,373
Investments designated for capital projects		
Cash management funds	$ 738	$ 89,285
	$ 738	$ 89,285
Assets whose use is limited		
Self-Insurance Trust Funds		
Cash management funds	$ -	$ 140
U.S. Government obligations	-	200
U.S. Treasuries	-	2,356
Corporate obligations	-	1,956
Accrued income	-	25
	-	4,677
Less: Current portion	-	1,227
	$ -	$ 3,450
Board-designated funds		
Cash management funds	$ 387	$ 176
Fixed income investments	21,489	17,075
Domestic common stock	16,208	15,264
Other domestic equity investments and pooled trusts	16,120	13,165
Foreign equity investments	10,943	8,909
Accrued income	6	13
	$ 65,153	$ 54,602

Notes to Consolidated Financial Statements (in thousands of dollars)

	2014	2013
Board designated for capital acquisition		
Cash management funds	$ 1,154	$ 1,493
U.S. Government obligations	8,814	7,900
U.S. Treasuries	13,627	14,414
Corporate obligations	75,778	69,887
Fixed income investments	10,063	9,031
Domestic common stock	23,114	21,676
Other domestic equity investments and pooled trusts	22,936	17,684
Foreign equity investments	14,280	11,555
Accrued income	729	740
	$ 170,495	$ 154,380
Funds held by trustee		
Cash management funds	$ 14,591	$ 14,588
	$ 14,591	$ 14,588
Investments temporarily restricted as to use		
Cash management funds	$ 120	$ 1,191
U.S. Government obligations	124	30
U.S. Treasuries	21	16
Corporate obligations	590	232
Fixed income investments	4,922	3,977
Domestic common stock	3,702	2,846
Other domestic equity investments and pooled trusts	3,601	3,184
Foreign equity investments	2,639	1,994
Accrued income	5	4
	$ 15,724	$ 13,474
Investments permanently restricted as to use		
Cash management funds	$ 62	$ 35
Fixed income investments	4,394	3,568
Domestic common stock	3,379	3,656
Other domestic equity investments and pooled trusts	3,427	2,563
Foreign equity investments	2,152	1,900
Interests in beneficial trust	7,882	7,898
Accrued income	-	4
	$ 21,296	$ 19,624

Alternative investments, which are non-readily marketable investments, included in cash management funds, fixed income investments, other domestic equity and pooled trusts and foreign equity investments in the above totaled $106,939 and $92,201, respectively, at June 30, 2014 and 2013.

Investments designated for capital projects represent unspent proceeds from the 2012A Revenue Bonds for June 30, 2014 and June 30, 2013, respectively, which are required to be expended on capital projects.

Notes to Consolidated Financial Statements (in thousands of dollars)

In FY13, assets whose use is limited included investments pledged as collateral for a letter of credit to satisfy the requirements of the State of Pennsylvania to fund current and future payments of worker's compensation claims. In FY14 the letter of credit was replaced with a surety bond.

At the time of issuance of the 2009A bonds, the System was required to deposit an amount equal to $14,584 into a Debt Service Reserve Fund. These funds are invested in cash management funds and are classified as "Funds held by trustee for debt service fund" on the System's balance sheet. There was no Debt Service Fund requirement associated with the issuance of the 2012A bonds.

Investment income, on the consolidated statements of operations, including interest and dividend income, realized gains or losses on sales of securities, unrealized gains and losses from certain wholly owned insurance captives, investment partnerships, and unrestricted income from temporarily restricted funds and investments permanently restricted as to use, is comprised of the following for the years ended June 30, 2014 and 2013.

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The System's investments are managed by investment managers and bank trust departments. Because the System's investments include a variety of financial instruments, the related values as presented in the consolidated financial statements are subject to various market fluctuations which include changes in the equity markets, interest rate environment and general economic conditions.

The following table represents the fair value measurement levels for all assets and liabilities, which the System has recorded at fair value:

		Fair Value Measurement Using		
	June 30, 2014	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Assets				
Cash management funds (1)	$ 29,387	$ 29,339	$ 48	$ -
U.S. Government obligations (2)	19,597	-	19,597	-
U.S. Treasuries (2)	36,100	36,100	-	-
Corporate obligations (3)	170,642	-	170,642	-
Fixed income investments (3)	54,211	25,967	28,244	-
Domestic common stock (4)	64,427	64,427	-	-
Other domestic equity investments and pooled trusts (5)	66,339	9,725	56,614	-
Foreign equity investments (5)	44,405	22,378	22,027	-
Funds held in trust by others (6)	7,883	-	7,883	-
Accrued income	1,692	1,692	-	-
	$ 494,683	$ 189,628	$ 305,055	$ -
Liabilities				
Interest rate swap	$ 5,522	$ -	$ 5,522	$ -

Notes to Consolidated Financial Statements (in thousands of dollars)

		Fair Value Measurement Using		
	June 30, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Assets				
Cash management funds (1)	$ 131,943	131,877	$ 66	$ -
U.S. Government obligations (2)	17,522	-	17,522	-
U.S. Treasuries (2)	39,628	39,628	-	-
Corporate obligations (3)	160,223	-	160,223	-
Fixed income investments (3)	46,103	22,114	23,989	-
Domestic common stock (4)	60,702	60,702	-	-
Other domestic equity investments and pooled trusts (5)	52,140	1,938	50,202	-
Foreign equity investments (5)	36,094	18,140	17,954	-
Funds held in trust by others (6)	7,898	-	7,898	-
Accrued income	1,750	1,750	-	-
	$ 554,003	$ 276,149	$ 277,854	$ -
Liabilities				
Interest rate swap	$ 5,741	$ -	$ 5,741	$ -

(1) Cash management funds include investments with original maturities of three months or less, including cash, money market funds, overnight investments and commercial paper. Cash management funds are carried at market value.

(2) U.S. Treasuries, are individually owned and held through the System's investment portfolio are readily marketable securities and traded on an active market, therefore, they are considered Level 1. U.S. Government obligations are not always traded on an active market, therefore they are considered level 2.

(3) Corporate obligations and fixed income securities are direct investments in mutual funds and investment partnerships whose underlying investments include corporate bonds, mortgage backed securities, collateralized mortgage obligations and other fixed income securities. The mutual funds investments are considered Level 1. The direct investments in corporate obligations are considered Level 2.

(4) Domestic common stock includes individual exchange traded equities held. All individual equities are considered Level 1.

(5) Other domestic equity investments and foreign equity investments are investments in mutual funds and investment partnerships whose underlying investments are individual equity securities. Mutual fund investments are considered Level 1. The investment partnership holdings are valued periodically using NAV per unit and are considered Level 2.

(6) Funds held in trust are investments held in trust instruments that have been either donated or received as a testamentary trust from the grantors will where the System is the beneficiary of the trust instrument. The underlying securities in each trust are typically individually owned fixed income or equity securities or mutual funds which are invested in fixed income or equity securities. The trustee of each trust is responsible for managing and investing the assets in accordance with the trust arrangement. The funds held in trust are classified as Level 2.

Notes to Consolidated Financial Statements (in thousands of dollars)

As of June 30, 2014 and 2013, certain cash management funds, fixed income securities, other domestic equity investments and pooled trusts and foreign equity investments are considered Level 2 due to being included in investment funds whose NAV is not published or investment partnerships where the partners determine the fair value of the investment.

The System applies the valuation standard guidance related to investment funds that do not have a readily determinable fair value. The guidance allows the fair value measurements for these funds to be based on reported NAV if certain criteria are met, and establishes additional disclosures related to these investment funds. Accordingly, the fair values of the following investment funds have been estimated using reported NAV:

	2014		
Category of Investment	**Fair Value**	**Redemption Frequency (if Currently Eligible)**	**Redemption Notice Period**
Equity - Global	$ 22,026	Monthly	15 days
Equity - Domestic	56,614	Daily	same day
Fixed income	21,521	Daily	same day
Fixed income	6,730	Daily	3 to 5 days
Cash Management	48	Daily	same day
	$ 106,939		

	2013		
Category of Investment	**Fair Value**	**Redemption Frequency (if Currently Eligible)**	**Redemption Notice Period**
Equity - Global	$ 17,944	Monthly	15 days
Equity - Domestic	50,202	Daily	3 to 5 days
Fixed income	23,989	Daily/Weekly	3 to 5 days
Cash Management	66	Daily	same day
	$ 92,201		

7. Goodwill

Accounting standards do not allow goodwill to be amortized but requires that it be tested for impairment annually or more frequently when events or circumstances indicates that the carrying value of a reporting unit more likely than not either exceeds or is less than its fair value.

As a result of the annual goodwill impairment testing, an impairment loss of $1,525 and $1,584 was needed to be recognized in the year ended June 30, 2014 and 2013, respectively. The factors that management considered in determining that it was not more likely than not that the fair value of the segments containing goodwill was less than its carrying amount included industry and market conditions, overall financial performance compared to projected results, and volume growth.

Goodwill recorded on the Consolidated Balance Sheets at June 30, 2014 and 2013 amounted to $43,086 and $43,891, respectively.

Notes to Consolidated Financial Statements (in thousands of dollars)

The changes in the carrying amount of goodwill for the System for the years ended June 30, 2014 and 2013 are as follows:

Balance as of July 1, 2012	$ 42,425
Goodwill acquired during the year	3,050
Goodwill impaired during the year	(1,584)
Balance as of June 30, 2013	43,891
Goodwill acquired during the year	720
Goodwill impaired during the year	(1,525)
Balance as of June 30, 2014	$ 43,086

8. Net Assets

A summary of changes in consolidated unrestricted net assets attributable to Pinnacle Health System and transfers (to) from the noncontrolling interest in West Shore Surgery Center and River Health ACO for the years ended June 30, 2014 and 2013 are as follows:

	Total	Pinnacle Health System	Noncontrolling Interest in Partnerships
Balance June 30, 2012	$ 413,284	$ 411,809	$ 1,475
Revenues and gains over expenses and losses	76,727	75,420	1,307
Change in post-retirement liability	34,440	34,440	-
Net assets released from restrictions for purchase of property, plant, and equipment	2,411	2,411	-
Distributions to noncontrolling interests	(1,272)	-	(1,272)
Change in net assets	112,306	112,271	35
Balance June 30, 2013	525,590	524,080	1,510
Revenues and gains over expenses and losses	26,365	26,687	(322)
Change in post-retirement liability	43,913	43,913	-
Net assets released from restrictions for purchase of property, plant, and equipment	38	38	-
Contributions from noncontrolling interests	1,314	-	1,314
Distributions to noncontrolling interests	(1,070)	-	(1,070)
Change in net assets	70,560	70,638	(78)
Balance June 30, 2014	$ 596,150	$ 594,718	$ 1,432

Notes to Consolidated Financial Statements (in thousands of dollars)

Temporarily restricted net assets are available for the following purposes at June 30, 2014 and 2013:

	2014	2013
Health care services		
Purchase of equipment	$ 21,849	$ 12,425
Health education	9,465	6,409
Research and development	442	351
Indigent care	1,334	1,216
	$ 33,090	$ 20,401

In August 2008, FASB updated ASC 958-205, which requires enhanced disclosures about an organization's endowment funds. Although the state of Pennsylvania did not enact the Uniform Prudent Management of Institutional Funds "UPMIFA" Act, the System has disclosed its changes in net asset composition in accordance with ASC 958-205.

Changes to the reported amount of the System's endowments as of June 30th are as follows:

	Permanently Restricted
Net assets, June 30, 2012	$ 10,653
Investment return	
Investment income	879
Net appreciation (realized and unrealized)	704
Total investment return	1,583
New gifts	1
Appropriation of endowment assets for spending	(511)
Net assets, June 30, 2013	$ 11,726
Investment return	
Investment income	736
Net appreciation (realized and unrealized)	1,504
Total investment return	2,240
New gifts	3
Appropriation of endowment assets for spending	(554)
Net assets, June 30, 2014	$ 13,415

Permanently restricted net assets include investments held in perpetuity by others for the benefit of the Hospital of $7,883 and $7,898 and investments to be held in perpetuity by the Foundation for the benefit of the Hospital of $13,415 and $11,726, respectively, at June 30, 2014 and 2013. The income from these investments is expendable to support health care services and is reported as either a temporary restricted fund balance or as non-operating income in the consolidated statements of operations depending upon the donor instructions.

Notes to Consolidated Financial Statements (in thousands of dollars)

9. Property, Plant and Equipment

Property, plant and equipment at June 30, 2014 and 2013 consists of:

	2014	2013
Land	$ 12,858	$ 12,905
Land improvements	11,463	10,522
Leasehold Improvements	28,317	24,947
Building and building improvements	576,105	474,367
Equipment	370,682	302,551
	999,425	825,292
Accumulated depreciation and amortization	(522,186)	(489,762)
Construction in progress	39,767	64,272
	$ 517,006	$ 399,802

Depreciation expense was $56,253 and $50,785 for the years ended June 30, 2014 and 2013, respectively. Accumulated amortization for equipment under capital lease obligations was $20,966 and $16,542 at June 30, 2014 and 2013, respectively. Construction purchase commitments at June 30, 2014 and 2013 have been disclosed in Note 16.

10. Long-Term Debt

Long-term debt at June 30, 2014 and 2013 consists of:

	2014	2013
Dauphin County General Authority, Health System Revenue Bonds, Series 2009A, due at various dates through 2036 with a fixed interest rate that varies at intervals specified in the bond document between 3.00% to 6.00% and an average rate of 5.92% to 5.89% at June 30, 2014 and 2013, respectively	$ 167,897	$ 171,936
Dauphin County General Authority, Health System Revenue Bond, Series 2011A, due at various dates through 2041 with interest at 70% of a variable monthly interest rate plus 80 basis points. The rate was 0.91% and 0.94% at June 30, 2014 and 2013, respectively.	95,825	97,330
Dauphin County General Authority, Health System Revenue Bond, Series 2012A, due at various dates through 2042 with a fixed interest rate that varies at intervals specified in the bond document between 3.75% to 5.00% and an average rate of 4.0% at June 30, 2014 and 2013.	135,250	135,250
Various capital leases and loans at various interest rates	24,227	18,559
	423,199	423,075
Less: Current portion	12,495	11,273
	$ 410,704	$ 411,802

Notes to Consolidated Financial Statements (in thousands of dollars)

Lines of Credit
At June 30, 2014 and 2013, the System had an unused line of credit of $5,000 and $0, which bears interest at variable rates (Daily One Month Libor plus 75 basis points). At June 30, 2014, the variable rate line in the amount of $5,000 had a rate of .90%.

Letters of Credit
The System was contingently liable for outstanding letters of credit in the amounts of approximately $2,190 and $8,158 for the years ended June 30, 2014 and 2013, respectively, to satisfy the requirements of professional liability insurance policies, future worker's compensation claims, current construction site work and security deposits on certain real estate leases as applicable.

Bank Note
On March 1, 2012, the System secured a $26,000 taxable five year term bank loan through PNC Bank, N. A. which was primarily used to finance certain acquisitions. The interest rate was reset monthly and equals the 1 month LIBOR Index plus a margin of 58 basis points. The interest rate will not exceed the maximum rate permitted by law. All transaction related fees were paid directly from Pinnacle Health System operating funds. The loan was paid in full on March 1, 2013.

Revenue Bonds
The Series 2009A, 2011A and 2012A Bonds were issued under Master Trust Indentures which contains certain covenants of the Obligated Group, including, but not limited to, covenants regarding the payment of debt service on all the Master Notes and Master Guarantees issued there under, rates and charges, liquidity, indebtedness, transfers of assets, the incurrence of additional indebtedness and the granting of security interests in property and a pledge of gross receipts to collateralize such indebtedness.

A summary of scheduled principal repayments on long-term debt is as follows:

Fiscal Year	Debt	Capital Leases and Loans	Total
2015	$ 5,860	$ 6,635	$ 12,495
2016	6,170	4,714	10,884
2017	6,500	3,638	10,138
2018	6,850	2,950	9,800
2019	7,245	2,725	9,970
Thereafter	366,347	3,565	369,912
	$ 398,972	$ 24,227	$ 423,199

11. Interest Rate Swaps

The System has used derivative instruments, such as interest rate swaps, to manage certain interest rate exposures. Derivative instruments are viewed as risk management tools by the System and are not used for trading and speculative purposes.

When quoted market prices are not available, the valuation of derivative instruments is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including interest rate curves and implied volatilities. The estimates of fair value are made by an independent third-party valuation service using a standardized methodology based on observable market inputs. As part of the System's overall valuation process, management evaluates this third-party methodology to ensure that it is representative of exit prices in the principal markets. These future net cash flows, however, are susceptible to change primarily due to fluctuations in interest rates. As a result, the estimated values of these derivatives will change over time as cash is received and paid and also as market conditions change. As these changes take place, they may have a positive or negative impact on estimated valuations. Based on the nature and limited purposes of the derivatives that the System employs, fluctuation in interest rates have had only a modest effect on its results of operations. As such, fluctuations are generally expected to be countered by offsetting changes in income, expense, and/or values of assets and liabilities.

Notes to Consolidated Financial Statements (in thousands of dollars)

As of July 14, 2005, in conjunction with the Series 2005 Bond, the Hospital entered into an interest rate swap agreement with an initial notional amount of $55,000. Under the agreement the Hospital paid the counterparty, Citigroup, a fixed rate of 3.36% and in exchange Citigroup pays the Hospital 61.80% of LIBOR plus 0.32%. Due to the redemption of the Series 2005 Bonds, the interest rate swap agreement was amended and restated on June 24, 2009 in conjunction with the Series 2009A Bond. As of June 30, 2014, the Hospital recorded a liability of $5,522 and a related loss of $1,235, which was recorded in gain on interest rate swaps in the consolidated statement of operations. As of June 30, 2013, the Hospital recorded a liability of $5,741 and a related gain of $1,375, which was recorded in gain on interest rate swaps in the consolidated statement of operations.

The System has classified its interest rate swap in Level 2 of the fair value hierarchy, as the significant inputs to the overall valuations are based on market-observable data or information derived from or corroborated by market-observable data. For over-the-counter derivatives that trade in liquid markets, such as interest rate swaps, model inputs (i.e. contractual terms, market prices, yield curves, credit curves, and measures of volatility) can generally be verified, and model selection does not involve significant management judgment.

A summary of the related liabilities and income statement impact of the swaps at June 30, 2014 and 2013 is as follows:

	Balance Sheets		Statements of Operations	
Interest Rate Swap	**2014**	**2013**	**2014**	**2013**
Series 2005/2009A swap	$ 5,522	$ 5,741	$ (1,235)	$ 1,375
	$ 5,522	$ 5,741	$ (1,235)	$ 1,375

12. Funds Held by Trustee and Other

Certain funds are required to be established and controlled by the trustee during the periods certain bonds are outstanding.

Proceeds of $135,250 from the 2012A Revenue Bonds received on August 7, 2012 were used to undertake a project consisting of equipping, and development of a new approximately 200,000 square foot, 108 bed acute care hospital on the Fredricksen Campus located in Cumberland County, Pennsylvania; renovations and improvements to the Harrisburg Hospital facilities located in the City of Harrisburg, Pennsylvania; renovations and improvements to the Community General Hospital facilities located in Dauphin County, Pennsylvania; and payment of the costs of issuing the Bonds. During the fiscal year 2014 and 2013, respectively, $88,551 and $46,064 of the proceeds were released to pay for approved invoices, underwriters discount and issuance fees related to the projects. The amount remaining is included in investments designated for capital projects until such time as approved invoices are paid to satisfy the requirements of the Bond agreement.

The additional proceeds of $30,000 from the 2011A Revenue Bonds received June 28, 2011 were to be used to fund approved capital projects at both the Harrisburg Hospital and Community General Osteopathic Hospital, plus pay issuance costs. As of June 30, 2014, all of the proceeds were expended.

Nonoperating gains include $6 and $30 interest earned on the funds held by trustee and other for the years ended June 30, 2014 and 2013, respectively.

13. Retirement Plans

The System sponsors defined contribution plans covering substantially all of its employees and employees of certain wholly and partially owned subsidiaries. The plans allow participating employees to contribute a percentage of their annual salary subject to current Internal Revenue Service (“IRS”) limitations. Employee contributions are matched by the System at various percentages. The System’s contributions to the savings plans are $13,464 and $13,062 for 2014 and 2013, respectively.

The System sponsors a noncontributory defined benefit pension plan (the “Plan”) covering substantially all of its employees and employees of certain wholly owned subsidiaries employed prior to January 1, 2007. Effective December 31, 2006, the System amended the Plan by freezing benefits for all participants. Additional retirement benefits are provided through increased contributions to the defined contribution plans. The Parent also sponsors a supplemental noncontributory defined benefit pension plan covering certain executives of the controlled entities of the System. The supplemental plan is unfunded and the Hospital has recorded a liability of $3,280 and $3,287 at June 30, 2014 and 2013, respectively.

Pinnacle Health System began a process of de-risking the defined benefit retirement plan during the fiscal year ended June 30, 2014. The de-risking strategy included two risk transfer initiatives: 1)a series of offers to terminated vested participants for a lump sum payout of their benefit and 2)a buy out transaction with an insurance company which transferred the pension liability for retired participants receiving benefit payments from the Plan to the insurance company. The cumulative amount of lump sum distributions for the fiscal year ended June 30, 2014 was $37,148. A total of 1,214 participants accepted the lump sum offers. The buy out transaction resulted in the purchase of a single premium annuity contract covering all of the plan participants receiving pension payments at the effective date of the transaction. The combined lump sum payout and buy out annuity contract purchase resulted in the accelerated recognition of unrecognized loss ($44,913) prorated on the basis of the cash payout/annuity purchase relative to the plan total liability.

The System sponsors a nonqualified deferred compensation plan covering certain employees of PHCVI. The plan allows participating employees to defer a percentage of their compensation during the plan year as well as allowing company contributions subject to plan limitations. The System’s contributions to the plan are $469 and $559 for 2014 and 2013, respectively.

Notes to Consolidated Financial Statements (in thousands of dollars)

Pension costs are funded to the limits specified by the Employee Retirement Income Security Act of 1974, as amended. From time to time, the System may contribute additional amounts to the Plan as it deems appropriate, subject to funding limitations. During fiscal year 2015, the System expects to contribute approximately $24,000 to the Plan.

Other benefits provided by the System are a defined benefit postretirement health plan and a defined benefit postretirement life plan both covering employees of the former Capital Area Health Foundation who retired by December 31, 1996. The plan is unfunded and the Hospital has recorded a liability of $5,645 and $5,073 at June 30, 2014 and 2013, respectively.

The following is the status of the various employee benefit plans as of the measurement dates of June 30, 2014 and 2013.

	Pension Benefits		Other Postretirement Benefits	
	2014	2013	2014	2013
Change in benefit obligations				
Benefit obligation at beginning of year	$ 302,125	$ 319,645	$ 5,073	$ 5,162
Service cost	-	-	73	105
Interest cost	10,416	13,780	241	222
Participant contributions	-	-	25	20
Benefit payments from assets	-	-	(264)	(280)
Benefit payments from plan	(172,652)	(17,635)	-	-
Actuarial (gain) loss	22,387	(13,665)	496	(156)
Benefit obligation at end of year	162,276	302,125	5,644	5,073
Change in plan assets				
Fair value of plan assets at beginning of year	255,642	233,727	-	-
Actual return on plan assets	29,161	26,620	-	-
Participant contributions	-	-	25	21
Employer contributions	11,467	12,930	238	259
Benefit payments	(172,652)	(17,635)	(263)	(280)
Fair value of plan assets at end of year	123,618	255,642	-	-
Funded status	$ (38,658)	$ (46,483)	$ (5,644)	$ (5,073)
Amounts recognized in the balance sheet consist of				
Current accrued retirement costs	$ (217)	$ (216)	$ (282)	$ (244)
Long-term accrued retirement costs	(38,439)	(46,265)	(5,362)	(4,829)
	$ (38,656)	$ (46,481)	$ (5,644)	$ (5,073)
Amounts recognized in net assets consist of				
Unrecognized net actuarial loss (gain)	$ 46,639	$ 91,078	$ 390	$ (106)
Net prior service benefit	-	(29)	-	-
	$ 46,639	$ 91,049	$ 390	$ (106)

The accumulated benefit obligation for pension benefits at June 30, 2014 and 2013 is $162,276 and $302,125, respectively.

Notes to Consolidated Financial Statements (in thousands of dollars)

The assumptions used in the measurement of the System's net periodic benefit obligations are shown in the following table:

	Pension Benefits		Other Postretirement Benefits	
(benefit obligations)	2014	2013	2014	2013
Weighted-average assumptions at the years ending June 30				
Discount rate	4.22 %	4.63 %	4.22 %	4.63 %
Rate of compensation increase	N/A	N/A	2.50 %	2.50 %

The following table provides the components of net periodic benefit cost for the years ended June 30, 2014 and 2013:

	Pension Benefits		Other Postretirement Benefits	
	2014	2013	2014	2013
Net periodic benefit cost				
Service cost	$ -	$ -	$ 72	$ 106
Interest cost	10,416	13,780	241	222
Expected return on plan assets	(14,034)	(18,586)	-	-
Amortization of prior service cost	(29)	(30)	-	-
Amortization of net actuarial loss	6,785	12,613	-	-
Loss on pension settlement	44,914	-	-	-
Net periodic benefit cost	$ 48,052	$ 7,777	$ 313	$ 328
Other Changes in Plan Assets and Benefit Obligations recognized in unrestricted net assets				
Net (gain) loss	$ 7,260	$ (21,700)	$ 496	$ (156)
Amortization of net (gain) loss	(6,785)	(12,614)	-	-
Amortization of prior service cost	29	30	-	-
Total (gain) loss recognized in unrestricted net assets	504	(34,284)	496	(156)
Total recognized in net periodic benefit cost and unrestricted net assets	$ 48,556	$ (26,507)	$ 809	$ 172

The estimated net loss and prior service cost that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year are $4,947 and 10,242, respectively, for the Pension Plan and $0 and $0, respectively for the Other Postretirement Benefits Plan.

Notes to Consolidated Financial Statements (in thousands of dollars)

The assumptions used in the measurement of the System's benefit cost are shown in the following table:

	Pension Benefits		Other Postretirement Benefits	
(net periodic benefit cost)	**2014**	**2013**	**2014**	**2013**
Weighted-average assumptions at the years ending June 30				
Discount rate	4.72 %	4.40 %	4.63 %	4.40 %
Expected return on plan assets	7.41 %	8.00 %	N/A	N/A
Rate of compensation increase	N/A	N/A	2.50 %	2.50 %

A 9.00% annual rate of increase in the per capita costs of covered health care benefits was assumed for 2014 gradually decreasing to 5.00% by the year 2018.

Sensitivity Analysis, Postretirement Benefits
Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plan. At June 30, 2014, a one-percentage-point change in assumed health care cost trend rates would have the following effects:

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on total of service and interest cost components	$ 4	$ (4)
Effect on postretirement benefit obligation	126	(114)

Expected benefit payments for the years ended June 30 are as follows (for 2015 includes $4,281 of lump sum benefits paid to 90 individuals):

	Pension Benefits	Other Benefits
2015	$ 9,908	$ 282
2016	4,707	289
2017	5,656	294
2018	6,434	297
2019	7,182	299
2020 - 2024	45,082	1,477

Notes to Consolidated Financial Statements (in thousands of dollars)

The pension plan's asset allocation at June 30, 2014 and 2013, by asset category, is as follows:

	2014	2013
Pension plan assets		
Equity securities	27.30 %	56.40 %
Fixed income securities	51.80	32.20
Tactical allocation	8.50	9.90
Cash and cash equivalents	12.40	1.50
	100.00 %	100.00 %

The primary investment objective for the plan assets is to achieve maximum rates of return commensurate with safety of principal. Target asset allocation, credit quality and diversification guidelines and restrictions are approved by the Investment Committee of the Board of Directors of the Parent. The plan asset allocation is reviewed quarterly to determine whether the portfolio mix is within an acceptable range of the target allocation. Target asset allocations are based on asset and liability studies.

The target asset allocation for the portfolio is 23.00% equity, 44.00% fixed income securities, 7.00% tactical allocation and 26.00% cash equivalents.

The following table represents the fair value measurement levels for all pension assets, which the System has recorded at fair value:

		Fair Value Measurement Using		
	June 30, 2014	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Assets				
Cash management funds	$ 15,306	$ -	$ 15,306	$ -
Fixed income investments	64,038	-	64,038	-
Balanced Fund	10,471	10,471	-	-
Other domestic equity investments	27,993	27,993	-	-
Foreign equity investments	5,809	-	5,809	-
	$ 123,617	$ 38,464	$ 85,153	$ -

	June 30, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Assets				
Cash management funds	$ 3,784	$ -	$ 3,784	$ -
Fixed income investments	118,111	118,111	-	-
Other domestic equity investments	104,531	52,604	51,927	-
Foreign equity investments	29,216	18,894	10,322	-
	$ 255,642	$ 189,609	$ 66,033	$ -

Notes to Consolidated Financial Statements (in thousands of dollars)

As of June 30, 2014 and 2013, cash management funds of $15,306 and $3,784, fixed income securities of $64,038 and $0, respectively, other domestic equity investments and pooled trusts of $0 and $51,927, respectively and foreign equity investments of $5,809 and $10,322, respectively are considered Level 2 due to being included in investment funds whose NAV is not published or investment partnerships where the partners determine the fair value of the investment.

The System applies the valuation standard guidance related to investment funds that do not have a readily determinable fair value. The guidance allows the fair value measurements for these funds to be based on reported NAV if certain criteria are met, and establishes additional disclosures related to these investment funds. Accordingly, the fair values of the following investment funds have been estimated using reported NAV:

	2014		
Category of Investment	**Fair Value**	**Redemption Frequency (if Currently Eligible)**	**Redemption Notice Period**
Cash management funds	$ 15,306	Daily	1 day
Equity - Global	5,809	Daily	1 day
Fixed income	64,038	Daily	1 day
	$ 85,153		

	2013		
Category of Investment	**Fair Value**	**Redemption Frequency (if Currently Eligible)**	**Redemption Notice Period**
Cash management funds	$ 3,784	Daily	1 day
Equity - Global	10,322	Daily	1 day
Equity - Domestic	51,927	Daily	1 day
	$ 66,033		

14. Insurance Coverage

The System maintains self-insurance trust funds for professional liability claims that are not insured by captive insurance arrangements. The System's contributions to its self-insurance trust funds and the related self-insured liabilities are based on actuarial assumptions and methodologies, which are reviewed continuously with any adjustments reflected in current operations. Management believes that the accrual for self-insured liabilities is adequate as of June 30, 2014; however, it is reasonably possible the estimated reserve for self-insurance claims could change in the near term due to the inherent variability in determining such estimates.

Effective December 31, 2002, primary professional and general liability insurance is provided through the System's wholly owned for profit captive insurance company, RRG. Professional liability is provided on a claims-made basis meeting statutory limit requirements of $500 per claim subject to a $2,500 annual aggregate for the Hospital, and a $1,500 annual aggregate for physician and skilled nursing claims. Additional coverage of $500 per claim and $1,500 in the aggregate is provided by the Mcare Fund (formerly the Medical Professional Liability Catastrophic Fund – "CAT Fund") established under the Medical Care Availability and Reduction of Error Act ("Mcare Act").

Coverage for general liability is on an occurrence basis providing $1,000 per claim subject to a $2,000 aggregate.

Prior to December 31, 2002, malpractice coverage was provided by commercial carriers on a claims-made basis with statutory/primary limits of $500 per claim and $2,500 for hospital claims and $1,500 for physician and skilled nursing claims in the aggregate with additional coverage of $700 per claim and $2,100 in the aggregate by the Mcare Fund. Coverage for general liability was on an occurrence basis providing $1,000 per claim subject to a $1,000 aggregate.

Effective January 1, 2013, the System purchased $30,000 in excess liability limits with separate limits established for professional liability exposure and general liability and other underlying coverage. For the period January 1, 2012 to December 31, 2012, excess limits were $25,000 with separate limits for Professional and General Liability. A $4,000 self-insured retention layer for professional and general liability exposure is underwritten by the System's wholly owned captive, UHR. For period January 1, 2010 to December 31, 2011, excess limits were $20,000 with separate limits for Professional and General Liability. For period January 1, 2007 to December 31, 2009, excess limits were $10,000 with separate limits for Professional and General Liability. At January 1, 2006, coverage included a $2,000 self-insured retention with an $8,000 annual aggregate limit for professional and general liability exposure. Effective January 1, 2004 through December 31, 2005, a shared $8,000 excess layer over a $1,000 self-insured retention layer. Claims in the $8,000 excess layer are shared 50% by a commercial insurance carrier and 50% self-insured. Self insured exposure is re-insured through the Parent's wholly owned captive, UHR. Effective January 1, 2003 through December 31, 2003, the System maintained excess liability coverage of $4,000 per claim and in the aggregate provided through UHR, with an additional $5,000 per claim and in the aggregate provided by a commercial insurance carrier. Prior to January 1, 2003, the System maintained excess liability coverage with a commercial carrier in the amount of $25,000 over the above limits.

At June 30, 2014 and 2013, the System also maintained Directors and Officers liability coverage with limits of $20,000 and Excess Workers' Compensation coverage over a self-insured retention of $750.

The actuarially computed liability to all health care providers (hospitals, physicians, and others) participating in the Mcare Fund at June 30, 2014 is expected to be substantially in excess of the amount the Mcare Fund has available to pay these claims. The Commonwealth of Pennsylvania has indicated that the unfunded liability will be funded exclusively through surcharge assessments in future years as claims are settled and paid. No provision has been made for any future Mcare Fund assessments in the accompanying June 30, 2014 and 2013 consolidated financial statements as the System's portion of the Mcare Fund unfunded liability could not be reasonably estimated.

15. Significant Concentrations of Credit Risk

The System's operations are located in Harrisburg, Pennsylvania. Its primary service area includes Harrisburg, Pennsylvania and the surrounding Greater Harrisburg Metropolitan Area. Financial instruments which subject the System to concentrations of credit risk consist primarily of cash and cash equivalents, investments, and accounts receivable.

The System typically maintains cash and cash equivalents and temporary investments in local banks. As of July 21, 2010, cash and cash equivalents and temporary investments are insured by the FDIC up to a limit of $250.

Notes to Consolidated Financial Statements (in thousands of dollars)

The System grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at June 30, 2014 and 2013 was as follows:

	2014	2013
Medicare	28.00 %	27.00 %
Medicaid	16.00	18.00
Capital Blue Cross/Highmark Blue Shield	23.00	24.00
HMO	3.00	5.00
Other third-party payors	10.00	10.00
Patients	20.00	16.00
	100.00 %	100.00 %

16. Commitments and Contingencies

Operating Leases

The System has entered into various lease arrangements for equipment, office space, and storage. Lease expense was $14,318 and $13,577 for the years ended June 30, 2014 and 2013, respectively. As of June 30, 2014, the System's lease commitments for the years ended June 30, 2015, 2016, 2017, 2018 and 2019 are $11,279, $10,158, $9,271, $8,995 and $8,865, respectively, and $39,797 in the aggregate for the years thereafter.

Loan Commitment and Debt Guarantees

As of June 30, 2014 and 2013 there was no outstanding debt guaranteed.

Purchase Commitments

The System has outstanding purchase commitments related to various projects of approximately $33,500 and $103,597 at June 30, 2014 and 2013, respectively.

Equity Contribution Commitments

The System is committed to provide equity contributions to PPI to fund any losses. During 2014 and 2013, the System provided equity contributions of $1,750 and $2,250, respectively.

Regulatory Compliance

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The System believes that it is in compliance with all applicable laws and regulations through the years ended June 30, 2014 and 2013. Compliance with such laws and regulations can be subject to government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid program.

Notes to Consolidated Financial Statements (in thousands of dollars)

17. Functional Expenses

The System provides general health care services to residents within its geographical area. Expenses related to providing these services for the years ended June 30, 2014 and 2013 are approximately as follows:

	2014	2013
Health care services	$ 657,342	$ 616,540
General and administrative	165,135	160,911
	$ 822,477	$ 777,451

18. Subsequent Events

The System evaluated subsequent events through September 10, 2014, which is the date the financial statements are considered widely distributed. Management reviews for and identifies subsequent events through participation at Board of Director meetings and subcommittee meetings.

On August 7, 2014 Pinnacle Health Hospitals (PHH) signed a contribution agreement with RehabClinics, Inc. and Joyner Sportsmedicine Institute, Inc., both affiliates of Select Medical Corporation, to form Pinnacle Health Select Rehabilitation, LLC. On the same date, Pinnacle Health Select Rehabilitation, LLC signed a purchased services agreement and facility lease agreement with PHH.

Hospitals will contribute certain assets and operations specific to The Helen M. Simpson inpatient rehabilitation hospital and eight outpatient therapy clinics. PinnacleHealth will have a non-controlling interest in the new entity.

Report of Independent Auditors
on Accompanying Consolidating Information

To the Board of Directors of Pinnacle Health System:

We have audited the consolidated financial statements of Pinnacle Health System as of June 30, 2014 and for the year then ended and our report thereon appears on pages 35 – 38 of this document. That audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The consolidating information is presented for purposes of additional analysis and is not a required part of the financial statements. The consolidating information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated the financial statements taken as a whole.

PricewaterhouseCoopers LLP

Harrisburg, Pennsylvania
September 10, 2014

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Pinnacle Health System
(And controlled entities and subsidiaries)
Consolidating Statement of Financial Position
June 30, 2014

Schedule I

(in thousands of dollars)	Parent	Hospital	PHMS	Elimin-ations	Obligated Group	RRG & UHR Combined	Foundation	PHEDS	PHCVI	PHMG	PHVI	CLT	Riverhealth ACO	WSSC	Elimin-ations	Consolidated Balances
Assets																
Current																
Cash and cash equivalents	$ 15,004	$ 1,046	$ 512	$ -	$ 16,562	$ 3,497	$ 592	$ -	$ 298	$ -	$ 23	$ 330	$ 920	$ 930	$ -	$ 23,152
Accounts receivable, patient	-	108,067	5,739	-	113,806	-	-	1,469	2,537	-	-	1,773	-	785	-	120,370
Accounts receivable, other	170	10,263	952	-	11,385	2,569	118	-	18	-	166	63	39	-	(123)	14,235
Investments	136,902	41,586	-	-	178,488	28,153	-	-	-	-	-	45	-	-	-	206,686
Inventories	-	13,950	512	-	14,462	-	-	-	46	-	-	16	-	292	-	14,816
Prepaid expenses	3,759	8,712	1,038	-	13,509	57	26	187	456	-	168	76	29	154	-	14,662
Due from related parties	55,075	3,084	2,216	-	60,375	-	-	-	-	-	-	204	-	-	(60,579)	-
Current portion of investments designed for capital projects	-	738	-	-	738	-	-	-	-	-	-	-	-	-	-	738
Total current assets	210,910	187,446	10,969	-	409,325	34,276	736	1,656	3,355	-	357	2,507	988	2,161	(60,702)	394,659
Assets limited as to use																
Board-designated funds	-	18,630	-	-	18,630	-	46,523	-	-	-	-	-	-	-	-	65,153
Funded Depreciation	-	170,495	-	-	170,495	-	-	-	-	-	-	-	-	-	-	170,495
Funds held by trustee for debt service fund	-	14,591	-	-	14,591	-	-	-	-	-	-	-	-	-	-	14,591
Total assets limited as to use	-	203,716	-	-	203,716	-	46,523	-	-	-	-	-	-	-	-	250,239
Temporarily restricted funds	-	9,854	-	-	9,854	-	15,724	-	-	-	-	-	-	-	(9,854)	15,724
Investments permanently restricted as to use	-	21,298	-	-	21,298	-	13,413	-	-	-	-	-	-	-	(13,415)	21,296
Property, plant and equipment, net	2,321	491,717	11,280	-	505,318	-	-	-	2,891	-	6,456	954	163	1,224		517,006
Pledges receivable temporarily restricted as to use	-	10,651	-	-	10,651	-	10,651	-	-	-	-	-	-	-	(10,651)	10,651
Goodwill	-	315	6,156	-	6,471	-	-	-	5,605	-	30,985	25	-	-	-	43,086
Other assets	10,110	17,730	1,407	-	29,247	-	-	-	1,785	-	388	-	-	-	(10,506)	20,914
Total assets	$ 223,341	$ 942,727	$ 29,812	$ -	$ 1,195,880	$ 34,276	$ 87,047	$ 1,656	$ 13,636	$ -	$ 38,186	$ 3,486	$ 1,151	$ 3,385	$ (105,128)	$ 1,273,575

Pinnacle Health System
(And controlled entities and subsidiaries)
Consolidating Statement of Financial Position
June 30, 2014 — Schedule I

(in thousands of dollars)	Parent	Hospital	PHMS	Elimin-ations	Obligated Group	RRG & UHR Combined	Foundation	PHEDS	PHCVI	PHMG	PHVI	CLT	Riverhealth ACO	WSSC	Elimin-ations	Consolidated Balances
Liabilities and Net Assets																
Current																
Current portion of long-term debt	$ -	$ 11,880	$ 262	$ -	$ 12,142	$ -	$ -	$ -	$ -	$ -	$ 90	$ 123	$ -	$ 263	$ (123)	$ 12,495
Accounts payable and accrued expenses	2,607	51,685	4,235	-	58,527	43	135	319	209	-	1,962	307	800	385	7	62,694
Accrued salaries, wages and fees	4,583	17,547	6,931	-	29,061	-	-	1,076	3,089	-	-	269	41	10	-	33,546
Accrued vacation	1,920	14,336	2,303	-	18,559	-	-	783	1,145	-	-	227	38	-	-	20,752
Accrued insurance costs	-	9,024	-	-	9,024	13,665	-	-	-	-	-	-	-	-	-	22,689
Accrued retirement costs	-	499	-	-	499	-	-	-	-	-	-	-	-	-	-	499
Due to related parties	-	-	-	-	-	-	3,515	-	50,165	-	6,627	-	272	48	(60,627)	-
Due to third-party payors	-	1,637	-	-	1,637	-	-	-	-	-	-	-	-	-	-	1,637
Advances from third-party payors	-	3,809	-	-	3,809	-	-	-	-	-	-	-	-	-	-	3,809
Total current liabilities	9,110	110,417	13,731	-	133,258	13,708	3,650	2,178	54,608	-	8,679	926	1,151	706	(60,743)	158,121
Long-term																
Accrued insurance costs, net of current portion	-	4,888	-	-	4,888	-	-	-	-	-	-	-	-	-	-	4,888
Accrued retirement costs, net of current portion	-	43,802	-	-	43,802	-	-	-	-	-	-	-	-	-	-	43,802
Interest rate swap agreement	-	5,522	-	-	5,522	-	-	-	-	-	-	-	-	-	-	5,522
Long-term debt, net of current portion	-	405,825	4,419	-	410,244	-	-	-	-	-	52	385	-	408	(385)	410,704
Total long-term liabilities	-	460,037	4,419	-	464,456	-	-	-	-	-	52	385	-	408	(385)	464,916
Net assets																
Unrestricted net assets:																
Unrestricted net assets Pinnacle Health System	214,231	330,469	11,662	-	556,362	20,568	36,892	(522)	(40,972)	-	29,455	2,175	-	836	(10,079)	594,715
Noncontrolling interests in consolidated subsidiary company	-	-	-	-	-	-	-	-	-	-	-	-	-	1,435	-	1,435
Total unrestricted net assets	214,231	330,469	11,662	-	556,362	20,568	36,892	(522)	(40,972)	-	29,455	2,175	-	2,271	(10,079)	596,150
Temporarily restricted net assets	-	20,506	-	-	20,506	-	33,090	-	-	-	-	-	-	-	(20,506)	33,090
Permanently restricted net assets	-	21,298	-	-	21,298	-	13,415	-	-	-	-	-	-	-	(13,415)	21,298
Total net assets	214,231	372,273	11,662	-	598,166	20,568	83,397	(522)	(40,972)	-	29,455	2,175	-	2,271	(44,000)	650,538
Total liabilities and net assets	$ 223,341	$ 942,727	$ 29,812	$ -	$ 1,195,880	$ 34,276	$ 87,047	$ 1,656	$ 13,636	$ -	$ 38,186	$ 3,486	$ 1,151	$ 3,385	$ (105,128)	$ 1,273,575

Pinnacle Health System
(And controlled entities and subsidiaries)
Consolidating Statement of Operations
Year Ended June 30, 2014

Schedule II

(in thousands of dollars)	Parent	Hospital	PHMS	Elimin-ations	Obligated Group	RRG & UHR Combined	Foundation	PHEDS	PHCVI	PHMG	PHVI	CLT	Riverhealth ACO	WSSC	Elimin-ations	Consolidated Balances
Unrestricted revenues																
Net patient service revenues	$ -	$ 762,680	$ 62,283	$ -	$ 824,963	$ -	$ -	$ 17,478	$ 22,698	$ 1,815	$ 68	$ 7,207	$ -	$ 8,200	$ -	$ 882,429
Provision for bad debts	-	(35,541)	(3,037)	-	(38,578)	-	-	(6,430)	(1,260)	(20)	-	(2,813)	-	20	-	(49,081)
Net patient service revenue less provision for bad debts	-	727,139	59,246	-	786,385	-	-	11,048	21,438	1,795	68	4,394	-	8,220	-	833,348
Other revenues	53,903	15,938	15,097	(82,903)	2,035	6,678	180	-	3,268	255	7,013	1,157	-	2	1,863	22,451
Net assets released from restrictions used for operations	308	2,230	734	-	3,272	-	173	-	1	-	-	-	-	-	-	3,446
Total unrestricted revenues	54,211	745,307	75,077	(82,903)	791,692	6,678	353	11,048	24,707	2,050	7,081	5,551	-	8,222	1,863	859,245
Expenses																
Salaries and wages	26,737	224,705	60,542	-	311,984	-	-	13,071	28,811	1,556	-	4,395	642	1,982	-	362,441
Fringe benefits	19,496	43,207	9,692	(210)	72,185	-	-	1,842	4,694	292	-	808	152	318	(128)	80,163
Management and support	-	69,109	7,905	(69,784)	7,230	-	490	991	2,156	248	-	815	-	-	(11,930)	-
Professional fees	6,495	23,366	2,004	(10,676)	21,189	259	92	85	178	27	1,008	49	3,258	51	(522)	25,674
Supplies	1,277	126,194	5,312	-	132,783	-	38	17	1,029	105	1	224	15	2,024	(196)	136,040
Purchased services and other	20,852	105,516	9,760	(2,233)	133,895	4,300	250	1,433	3,463	333	5,016	1,063	307	1,412	(5,902)	145,570
Interest	-	15,435	274	-	15,709	-	-	-	-	-	15	40	-	11	(7)	15,768
Depreciation and amortization	938	50,182	2,128	-	53,248	-	-	-	1,253	77	1,426	430	5	382	-	56,821
Total expenses	75,795	657,714	97,617	(82,903)	748,223	4,559	870	17,439	41,584	2,638	7,466	7,824	4,379	6,180	(18,685)	822,477
Income (loss) from operations before pension settlement loss	(21,584)	87,593	(22,540)	-	43,469	2,119	(517)	(6,391)	(16,877)	(588)	(385)	(2,273)	(4,379)	2,042	20,548	36,768
Pension settlement loss	-	(44,913)	-	-	(44,913)	-	-	-	-	-	-	-	-	-	-	(44,913)
(Loss) income from operations after pension settlement loss	(21,584)	42,680	(22,540)	-	(1,444)	2,119	(517)	(6,391)	(16,877)	(588)	(385)	(2,273)	(4,379)	2,042	20,548	(8,145)
Nonoperating gains (losses)																
Investment income (loss)	15,518	20,743	(138)	-	36,123	1,696	3,543	(3)	(21)	(7)	(9)	(4)	-	(1)	(3,822)	37,495
Federal taxes	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Loss on disposal of assets	-	336	(19)	-	317	-	-	-	-		(528)	-	-	(14)	-	(225)
Loss on goodwill impairment	-	(1,525)	-	-	(1,525)	-	-	-	-	-	-	-	-	-	-	(1,525)
Realized and unrealized losses on interest rate swaps	-	(1,235)	-	-	(1,235)	-	-	-	-	-	-	-	-	-	-	(1,235)
Nonoperating gain (loss), net	15,518	18,319	(157)	-	33,680	1,696	3,543	(3)	(21)	(7)	(537)	(4)	-	(15)	(3,822)	34,510
Revenues and gains over (under) expenses and losses	$ (6,066)	$ 60,999	$ (22,697)	$ -	$ 32,236	$ 3,815	$ 3,026	$ (6,394)	$ (16,898)	$ (595)	$ (922)	$ (2,277)	$ (4,379)	$ 2,027	$ 16,726	$ 26,365

Pinnacle Health System
(And controlled entities and subsidiaries)
Consolidating Statement of Changes in Net Assets
Year Ended June 30, 2014

Schedule III

(in thousands of dollars)	Parent	Hospital	PHMS	Elimin-ations	Obligated Group	RRG & UHR Combined	Foundation	PHEDS	PHCVI	PHMG	PHVI	CLT	Riverhealth ACO	WSSC	Elimin-ations	Consolidated Balances
Unrestricted net assets																
Revenues and gains over (under) expenses and losses	$ (6,066)	$ 60,999	$ (22,697)	$ -	32,236	$ 3,815	$ 3,026	$ (6,394)	$ (16,898)	$ (595)	$ (922)	$ (2,277)	$ (4,379)	$ 2,027	$ 16,726	$ 26,365
Change in post-retirement liability	-	43,913	-	-	43,913	-	-	-	-	-	-	-	-	-	-	43,913
Capital contributions	(8,421)	(28,442)	28,778	-	(8,085)	-	-	5,939	37	407	-	2,214	3,064	-	(3,576)	-
Net assets released from restrictions for purchases of property, plant and equipment	-	13	13	-	26	-	-	(1)	1	-	-	10	-	-	-	36
Income attributable to noncontrolling interests	-	-	-	-	-	-	-	-	-	-	-	-	1,314	(2,183)	1,114	245
Increase (decrease) in unrestricted assets	(14,487)	76,483	6,094	-	68,090	3,815	3,026	(456)	(16,860)	(188)	(922)	(53)	(1)	(156)	14,264	70,559
Temporarily restricted net assets																
Contributions	-	9,530	-	-	9,530	-	9,167	-	-	-	-	-	-	-	(9,530)	9,167
Net realized and unrealized gains on investments	-	1,816	-	-	1,816	-	7,033	-	-	-	-	-	-	-	(1,817)	7,032
Net assets released from restrictions	-	(2,994)	-	-	(2,994)	-	(3,511)	-	-	-	-	-	-	-	2,994	(3,511)
Increase in temporarily restricted assets	-	8,352	-	-	8,352	-	12,689	-	-	-	-	-	-	-	(8,353)	12,688
Permanently restricted net assets																
Contributions	-	3	-	-	3	-	3	-	-	-	-	-	-	-	(3)	3
Income distributions	-	(554)	-	-	(554)	-	(554)	-	-	-	-	-	-	-	554	(554)
Net realized and unrealized gains on investments	-	2,225	-	-	2,225	-	2,240	-	-	-	-	-	-	-	(2,240)	2,225
Increase in permanently restricted assets	-	1,674	-	-	1,674	-	1,689	-	-	-	-	-	-	-	(1,689)	1,674
Increase (decrease) in net assets	(14,487)	86,509	6,094	-	78,116	3,815	17,404	(456)	(16,860)	(188)	(922)	(53)	(1)	(156)	4,222	84,921
Net assets																
Beginning of year	228,718	285,764	5,568	-	520,050	16,753	65,993	(66)	(24,112)	188	30,377	2,228	1	2,427	(48,222)	565,617
End of year	$ 214,231	$ 372,273	$ 11,662	$ -	$ 598,166	$ 20,568	$ 83,397	$ (522)	$ (40,972)	$ -	$ 29,455	$ 2,175	$ -	$ 2,271	$ (44,000)	$ 650,538

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Schedule III

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 Directors of Pinnacle Health System:

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 financial statements of Pinnacle Health System (and controlled entities and subsidiaries), which comprise Pinnacle Health System's financial statements as of June 30, 2014 and the related notes to the financial statements, and have issued our report thereon dated September 10, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Pinnacle Health System'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 financial statements, but not for the purpose of expressing an opinion on the effectiveness of Pinnacle Health System's internal control. Accordingly, we do not express an opinion on the effectiveness of Pinnacle Health System'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 entity's 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Pinnacle Health System's 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*.

Schedule III

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 entity'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

PricewaterhouseCoopers LLP
Harrisburg, PA
September 10, 2014