



MIDDLESEX HEALTH SERVICES, INC.

Financial Statements

September 30, 2009 and 2008

(With Independent Auditors' Report Thereon)

MIDDLESEX HEALTH SERVICES, INC.

Financial Statements

September 30, 2009 and 2008

Table of Contents

	Page
Independent Auditors' Report	1
Balance Sheets	2
Statements of Operations and Changes in Net Assets	3
Statements of Cash Flows	4
Notes to Financial Statements	5



KPMG LLP
One Financial Plaza
Hartford, CT 06103-4103

Independent Auditors' Report

The Board of Directors
Middlesex Health Services, Inc.:

We have audited the accompanying balance sheets of Middlesex Health Services, Inc., a not-for-profit Connecticut corporation, (Services) as of September 30, 2009 and 2008, and the related statements of operations and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Services' management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Services' internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Middlesex Health Services, Inc. as of September 30, 2009 and 2008, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

KPMG LLP

December 23, 2009

MIDDLESEX HEALTH SERVICES, INC.

Balance Sheets

September 30, 2009 and 2008

Assets	2009	2008
Current assets:		
Cash and cash equivalents	\$ 1,139,651	954,607
Accounts receivable	54,505	24,335
Prepaid expenses and other current assets	2,702	4,268
Current portion of investments limited as to use	158,424	152,047
Total current assets	1,355,282	1,135,257
Investments limited as to use, net of current portion	573,928	594,997
Property and equipment, net	5,160,184	5,366,900
Deferred financing costs, net of accumulated amortization of \$127,629 in 2009 and \$118,639 in 2008	118,042	127,032
Total assets	\$ 7,207,436	7,224,186
Liabilities and Unrestricted Net Assets		
Current liabilities:		
Current portion – long-term debt	\$ 235,000	220,000
Accounts payable and accrued expenses	137,983	174,358
Due to related parties	5,247	7,678
Estimated self-insurance liability	118,574	103,120
Accrued interest payable	84,589	87,284
Deferred revenue	133,710	60,854
Total current liabilities	715,103	653,294
Long-term debt, net of current portion	6,252,624	6,477,463
Total liabilities	6,967,727	7,130,757
Commitments and contingencies (note 6)		
Unrestricted net assets	239,709	93,429
Total liabilities and unrestricted net assets	\$ 7,207,436	7,224,186

See accompanying notes to financial statements.

MIDDLESEX HEALTH SERVICES, INC.

Statements of Operations and Changes in Net Assets

Years ended September 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Revenues:		
Resident revenues	\$ 2,882,316	2,900,071
Ancillary revenues	37,294	39,197
Other revenues	3,600	3,600
Total revenues	<u>2,923,210</u>	<u>2,942,868</u>
Expenses:		
Salaries and wages	1,137,112	1,085,445
Payroll taxes and employee benefit	297,964	300,229
Purchased services	171,140	207,493
Maintenance	197,620	211,161
Management and professional fee	112,631	134,780
Advertising	28,265	26,141
Food and beverage	161,965	161,971
Depreciation and amortization	238,276	238,480
Interest, net	316,307	308,717
Other	115,650	114,251
Total expenses	<u>2,776,930</u>	<u>2,788,668</u>
Excess of revenues over expenses	146,280	154,200
Unrestricted net assets (deficit), beginning of year	<u>93,429</u>	<u>(60,771)</u>
Unrestricted net assets, end of year	<u>\$ 239,709</u>	<u>93,429</u>

See accompanying notes to financial statements.

MIDDLESEX HEALTH SERVICES, INC.

Statements of Cash Flows

Years ended September 30, 2009 and 2008

	2009	2008
Cash flows from operating activities:		
Excess of revenues over expense:	\$ 146,280	154,200
Adjustments to reconcile excess of revenues over expense to net cash provided by operating activities		
Depreciation and amortization	238,276	238,480
Changes in operating assets and liabilities		
Accounts receivable, net	(30,170)	18,235
Prepaid expenses and other current assets	1,566	1,519
Accounts payable and accrued expenses and accrued interest payable	(39,070)	14,405
Estimated self-insurance liability	15,454	57,779
Due to related parties	(2,431)	(10,522)
Deferred revenue	72,856	(9,420)
Net cash provided by operating activities	402,761	464,676
Cash flows from investing activities:		
Purchases of property and equipment	(12,409)	(27,412)
Investments limited as to use	14,692	6,792
Net cash provided by (used in) investing activities	2,283	(20,620)
Cash flows from financing activities:		
Repayment of long-term deb	(220,000)	(210,000)
Net cash used in financing activities	(220,000)	(210,000)
Net increase in cash	185,044	234,056
Cash and cash equivalents, beginning of year	954,607	720,551
Cash and cash equivalents, end of year	\$ 1,139,651	954,607
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	\$ 349,137	360,688

See accompanying notes to financial statements.

MIDDLESEX HEALTH SERVICES, INC.

Notes to Financial Statements

September 30, 2009 and 2008

(1) Organization

Middlesex Health Services, Inc. (Services), is a wholly owned subsidiary of Middlesex Health System, Inc. (System). In addition to Services, System's subsidiaries include: Middlesex Hospital (the Hospital), Middlesex Health Resources, Inc. (Resources), and MHS Primary Care, Inc. (MHSPC).

Services operates a licensed assisted living facility, One MacDonough Place, located in Middletown, Connecticut. The facility has 70 residential units comprised of studios, one-bedroom, and two-bedroom apartments. Services provides assistance with activities of daily living, nursing services, client assessment, and supervision of and assistance with medication administration. Residents receive individualized assistance, designed to meet their needs 24 hours a day. Resident contracts are generally a year long and renewable, though there are some contracts for short-term respite care.

(2) Summary of Significant Accounting Policies

(a) Basis of Presentation

The financial statements have been prepared on the accrual basis of accounting in conformity with U.S. generally accepted accounting principles.

(b) Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization is being provided using the straight-line method over the estimated useful lives of the related assets.

Depreciation and amortization are computed using the straight-line method over the following estimated useful lives:

<u>Classifications</u>	<u>Life</u>
Building and improvements	5-35 years
Furniture and equipment	3-10 years

(c) Deferred Financing Costs

Deferred financing costs are amortized over the life of the related debt.

(d) Resident and Ancillary Revenues

Resident and ancillary revenues are recorded when earned for rental use and when services are performed, respectively. Rents received in advance are deferred until earned.

(e) Income Taxes

Services is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code and is generally exempt from Federal income taxes pursuant to Section 501(a) of the Internal Revenue Code.

MIDDLESEX HEALTH SERVICES, INC.

Notes to Financial Statements

September 30, 2009 and 2008

(f) *Investments Limited as to Use*

Services are required to maintain certain deposits with a trustee relating to its outstanding bonds (see note 4). Such deposits are included in investments limited as to use in the accompanying balance sheets and consist of \$573,928 and \$594,997 in the debt service reserve fund and \$158,424 and \$152,047 in the debt service fund as of September 30, 2009 and 2008, respectively.

(g) *Cash equivalents*

Services consider all highly liquid investments with a maturity of three months or less at the time of purchase to be cash equivalents.

(h) *Use of Estimates*

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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. Actual results could differ from those estimates.

(i) *Estimated Self-Insurance Liability*

Effective February 1, 2004, Services adopted a policy of self-insuring a portion of its workers' compensation insurance coverage through System's self-insurance program. The annual self-insured retention limit for the fiscal year was \$400,000 per occurrence (see note 6).

(j) *Fair value measurements*

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 and liability in an orderly transaction between market participants at the measurement date.

Services uses a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires Services to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

- Level 1 – Quoted prices in active markets for identical assets or liabilities
- Level 2 – Observable inputs other than quoted prices included in Level 1, such as quoted prices for markets that are not active or other inputs that are observable or can be corroborated by observable market data.
- 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. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

MIDDLESEX HEALTH SERVICES, INC.

Notes to Financial Statements

September 30, 2009 and 2008

The table below segregates all financial assets and liabilities that are measured at fair value on a recurring basis (at least annually) into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date.

	Total carrying value at September 30, 2009	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant other unobservable inputs (Level 3)
Investments limited as to use	\$ 732,352	\$ 732,352	\$ —	\$ —

Services' investments limited as to use are limited to U.S. treasury bills, U.S. treasury bonds and money market funds that are measured at the price reported on the active market on which they are traded. Based on these inputs, the investments limited as to use are classified within Level 1 of the valuation hierarchy at September 30, 2009.

(k) Recent Accounting Standards

In May 2009, the FASB issued guidance which established principles and requirements for recognition and disclosure of subsequent events. In particular, it sets forth the period after the balance sheet date during which management of a reporting entity shall evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, the circumstances under which an entity shall recognize events or transactions occurring after the balance sheet date in its financial statements and the disclosures that an entity shall make about events or transactions that occurred after the balance sheet date. This guidance is to be applied to the accounting for and disclosure of subsequent events not addressed in other applicable GAAP and was effective for the year ended September 30, 2009. In accordance with the guidance, management has evaluated events subsequent to September 30, 2009 and through December 23, 2009.

(3) Property and Equipment

Property and equipment as of September 30, 2009 and 2008 consist of the following:

	2009	2008
Land	\$ 894,611	894,611
Building and improvements	6,137,250	6,129,883
Furniture and equipment	555,599	550,557
	7,587,460	7,575,051
Less accumulated depreciation	(2,427,276)	(2,208,151)
Property and equipment, net	\$ 5,160,184	5,366,900

MIDDLESEX HEALTH SERVICES, INC.

Notes to Financial Statements

September 30, 2009 and 2008

(4) Long-Term Debt

In October 1997, the Connecticut Health and Educational Facilities Authority (CHEFA) issued \$8,450,000 of Revenue Bonds, Middlesex Health Services Issue, Series I for the construction of One MacDonough Place (the Project). Services is obligated to provide amounts, which will be sufficient to enable CHEFA to pay the principal and interest on the bonds. The proceeds of the bonds, together with certain investment income and an equity contribution by Services, were used to finance the land acquisition, construction, and equipment as well as to pay for certain start-up expenses, to pay a portion of the interest on the bonds through January 1, 2000, to fund the debt service reserve fund and to pay certain costs related to the issuances of the bonds.

The bonds mature from July 1, 2007 through July 1, 2027 at interest rates between 4.700% and 5.125%. The Hospital issued a guaranty note to secure the CHEFA obligations of Services.

The fair value of Services' CHEFA bonds, based on market prices, was approximately \$6,331,000 and \$6,723,000 at September 30, 2009 and 2008, respectively.

Aggregate scheduled principal repayments on long-term debt are as follows:

	<u>Long-term debt</u>
Year ending September 30:	
2010	\$ 235,000
2011	245,000
2012	255,000
2013	270,000
2014	285,000
Thereafter	<u>5,330,000</u>
	6,620,000
Less bond discount	132,376
Less current portion	<u>235,000</u>
	<u>\$ 6,252,624</u>

(5) Retirement Savings Plan

Services sponsors a 403(b) retirement savings plan (the Plan) for its employees. The Plan allows participants to contribute up to 10% of their annual compensation, not to exceed certain limitations. There is no matching contribution from Services.

MIDDLESEX HEALTH SERVICES, INC.

Notes to Financial Statements

September 30, 2009 and 2008

(6) Estimated Self-Insurance Liability for Workers' Compensation Insurance

The costs of certain workers' compensation claims falling within Services' retention limits have been estimated by management and reflected in the accompanying financial statements. These estimates are subject to change, however, in the opinion of Services' management, the ultimate resolution of these claims will not have a material impact on Services' results of operations or financial position.

(7) Management Contract

Services had a management contract with Genesis Health Ventures, Inc. (Genesis) to manage and provide oversight of the day-to-day operations of One MacDonough Place. In consideration for performing these services Genesis is paid a monthly management fee and an incentive fee as defined by the management contract. Total management fees for the years ended September 30, 2009 and 2008 were \$87,696 and \$88,286, respectively. The contract was terminated effective October 1, 2009.