Fletcher Allen Health Care, Inc. and Subsidiaries

Consolidated Financial Statements
September 30, 2010 and 2009

Fletcher Allen Health Care, Inc. and Subsidiaries
Index
September 30, 2010 and 2009

PRICEWATERHOUSECOOPERS

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Report of Independent Auditors

To the Board of Trustees of
Fletcher Allen Health Care, Inc:

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of operations, of changes in net assets, and cash flows present fairly, in all material respects, the financial position of Fletcher Allen Health Care, Inc. and its Subsidiaries ("the Organization") at September 30, 2010, and the results of their operations, their changes in net assets and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Organization's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion. The financial statements of the Organization as of September 30, 2009 and for the year then ended were audited by other auditors whose report dated December 10, 2009 expressed an unqualified opinion on those statements.

PricewaterhouseCoopers LLP

December 22, 2010

Fletcher Allen Health Care, Inc. and Subsidiaries
Consolidated Balance Sheets
September 30, 2010 and 2009

(In thousands)

	2010	2009
Assets		
Current assets		
Cash and cash equivalents	$ 78,632	$ 69,708
Patient and other trade accounts receivable - net of allowance for doubtful accounts of $15,891 and $15,761 in 2010 and 2009, respectively	106,391	104,108
Short-term investments	1,599	1,009
Inventories	16,883	13,493
Current portion of restricted assets	6,390	6,500
Estimated receivables from third-party payors	11,462	4,226
Prepaid and other current assets	22,503	27,185
Total current assets	243,860	226,229
Assets whose use is limited or restricted		
Board-designated assets	189,950	170,619
Assets held by trustee under bond indenture agreements	38,655	37,940
Restricted assets	39,916	35,606
Donor-restricted assets for specific purposes	12,416	11,233
Donor-restricted assets for permanent endowment	24,951	25,029
Total assets whose use is limited or restricted	305,888	280,427
Property and equipment, net	430,937	436,622
Other assets		
Deferred financing costs, net	16,106	16,904
Notes receivable and other assets	7,830	2,478
Investment in affiliated companies	4,714	4,476
Pledges receivable	1,130	1,376
Total other assets	29,780	25,234
	$ 1,010,465	$ 968,512

Fletcher Allen Health Care, Inc. and Subsidiaries
Consolidated Balance Sheets
September 30, 2010 and 2009

(In thousands)

	2010	2009
Liabilities and net assets		
Current liabilities		
Current installments of long-term debt	$ 8,706	$ 9,184
Accounts payable	19,428	14,575
Accrued expenses and other liabilities	38,328	45,552
Accrued payroll and related benefits	55,120	46,868
Estimated third-party payor settlements	15,418	15,237
Estimated amounts for incurred but not reported claims	26,150	24,845
Total current liabilities	163,150	156,261
Long-term liabilities		
Long-term debt - excluding current installments	400,934	409,298
Reserve for outstanding losses on malpractice and workers' compensation claims	20,206	22,103
Pension and other postretirement benefit obligations	31,762	30,337
Other long-term liabilities	15,833	9,365
Total long-term liabilities	468,735	471,103
Total liabilities	631,885	627,364
Commitments and contingent liabilities (note 11)		
Net assets		
Unrestricted	338,691	302,161
Temporarily restricted	14,938	13,958
Permanently restricted	24,951	25,029
Total net assets	378,580	341,148
	$ 1,010,465	$ 968,512

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

Fletcher Allen Health Care, Inc. and Subsidiaries
Consolidated Statements of Operations
Years Ended September 30, 2010 and 2009

(In thousands)

	2010	2009
Unrestricted revenue and other support		
Net patient service revenue	$ 803,931	$ 773,820
Premium revenue	79,967	78,102
Other revenue	29,024	22,744
Total unrestricted revenue and other support	912,922	874,666
Expenses		
Salaries, payroll taxes, and fringe benefits	530,861	494,144
Supplies and other	203,138	206,325
Purchased services	33,673	34,167
Depreciation and amortization	43,942	37,702
Interest expense	19,980	20,484
Provision for bad debts	24,516	20,476
Underwriting expenses	4,654	6,138
Medical claims	32,646	34,762
Total expenses	893,410	854,198
Income from operations	19,512	20,468
Nonoperating gains (losses)		
Investment income (losses)	27,301	(7,691)
Loss on interest rate swap contracts	(4,101)	(4,485)
Other	554	929
Total nonoperating gains (losses)	23,754	(11,247)
Excess of revenue over expenses	43,266	9,221
Net change in unrealized (losses) gains on investments	(3,475)	15,873
Assets released from restrictions for capital purchases	939	347
Pension related adjustments	(4,200)	(28,627)
Increase (decrease) in unrestricted net assets	$ 36,530	$ (3,186)

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

Fletcher Allen Health Care, Inc. and Subsidiaries
Consolidated Statements of Changes in Net Assets
For the Years Ended September 30, 2010 and 2009

(In thousands)

	2010	2009
Unrestricted net assets		
Excess of revenue over expenses	$ 43,266	$ 9,221
Net change in unrealized (losses) gains on investments	(3,475)	15,873
Assets released from restrictions for capital purchases	939	347
Pension related adjustments	(4,200)	(28,627)
Increase (decrease) in unrestricted net assets	36,530	(3,186)
Temporarily restricted net assets		
Gifts, grants, and bequests	1,655	2,810
Investment income	337	354
Net change in unrealized (losses) gains on investments	(841)	1,915
Net realized gains (losses) on investments	1,759	(1,464)
Net assets released from restrictions used in operations	(777)	(1,073)
Net assets released from restrictions used for nonoperating purposes	(191)	(405)
Net assets released from restrictions used for capital purchases	(939)	(347)
Transfer of net assets	(23)	698
Increase in temporarily restricted net assets	980	2,488
Permanently restricted net assets		
Gifts, grants, and bequests	59	48
Change in beneficial interest in perpetual trusts	(160)	(587)
Transfer of net assets	23	(698)
Decrease in permanently restricted net assets	(78)	(1,237)
Increase (decrease) in net assets	37,432	(1,935)
Net assets		
Beginning of year	341,148	343,083
End of year	$ 378,580	$ 341,148

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

Fletcher Allen Health Care, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
For the Years Ended September 30, 2010 and 2009

(In thousands)

	2010	2009
Cash flows from operating activities		
Increase (decrease) in net assets	$ 37,432	$ (1,935)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities		
Depreciation and amortization	43,942	37,702
Provision for bad debts	24,516	20,476
Contributions received restricted for long-term use	(2,050)	(3,212)
Pension related adjustments	4,200	28,627
Loss on disposal of property and equipment	51	-
Loss on interest rate swap contracts	4,101	4,485
Realized and unrealized gains on investments	(15,872)	(641)
Undistributed gains of affiliated companies	(239)	(117)
Change in beneficial interest in perpetual trusts	160	587
Changes in operating assets and liabilities		
Increase in patient and other accounts receivable	(26,707)	(22,351)
Increase in other current and noncurrent assets	(4,303)	(5,631)
Increase in estimated receivables from third-party payors	(7,236)	-
(Decrease) increase in accounts payable and accrued expenses	(893)	2,728
Increase in accrued payroll and related expenses	8,252	2,477
Increase in other current and non current liabilities	1,911	6,207
Decrease in pension and other postretirement benefit obligations	(2,775)	(3,909)
Net cash provided by operating activities	64,490	65,493
Cash flows from investing activities		
Acquisitions of property and equipment	(38,219)	(47,819)
Purchase of investments	(506,044)	(252,783)
Proceeds from sale of investments	495,814	243,597
Proceeds from sale of affiliated company	397	4,861
Net cash used in investing activities	(48,052)	(52,144)
Cash flows from financing activities		
Proceeds from contributions received restricted for long-term use	2,050	3,054
Repayment of long-term debt	(9,564)	(9,278)
Net cash used in financing activities	(7,514)	(6,224)
Net increase in cash and cash equivalents	8,924	7,125
Cash and cash equivalents		
Beginning of year	69,708	62,583
End of year	$ 78,632	$ 69,708
Supplemental cash flow information		
Cash paid during the year for interest	$ 21,062	$ 20,769
Capital expenditures included in accounts payable	1,028	2,506
Assets acquired under capital lease	761	1,820
Notes receivable acquired from sale of affiliated company (TVHP)	-	1,984
Notes receivable acquired from disposition of equity investee (NELC)	-	122

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

1. Organization

Fletcher Allen Health Care, Inc. (FAHC) is an academic and teaching health care center and regional referral center providing a full range of primary, secondary, and tertiary-level inpatient and outpatient health care services. FAHC is closely integrated with the University of Vermont College of Medicine (UVM) under an affiliation agreement for teaching and research.

FAHC is the sole member of the following subsidiaries: Fletcher Allen Health Ventures, Inc. (FAHV); Fletcher Allen Medical Group, PLLC (FAMG); University of Vermont Medical Group (UVM Medical Group); Fletcher Allen Coordinated Transport, LLC (FACT); Fletcher Allen Skilled Nursing Care, LLC (FASN); Fletcher Allen Health Care Foundation, Inc.; and VMC Indemnity Company Ltd. (VMCIC). Vermont Managed Care, Inc. (VMC) is a wholly owned subsidiary of FAHV.

In September 2010, Fletcher Allen Executive Services, LLC (FAES) was incorporated as a single member, Vermont based non-profit, limited liability corporation, with tax exempt status under FAHC. FAES is authorized to do business in New York State and currently provides limited executive and financial consulting services to Inter-Lakes Health, Inc. in Ticonderoga, New York.

2. Summary of Significant Accounting Policies

Principles of Consolidation

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

Use of Estimates

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

Cash and Cash Equivalents

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

Inventories

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

Prepaid and Other Current Assets

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

Contributions
Unconditional promises to give that are expected to be collected within one year are recorded at their estimated net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of estimated future cash flows. The discounts on those amounts are computed using a risk-free rate applicable to the year in which the promise is received. Amortization of the discount is included in contribution revenue. Conditional promises to give are not included as support until the conditions are substantially met.

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

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

Other-Than-Temporary Impairment of Investments
FAHC reviews its investments to identify those for which fair value is below cost. FAHC then makes a determination as to whether the investment should be considered other-than-temporarily impaired. FAHC recognized $0 and $39,274,000 in losses related to declines in value that were other-than-temporary in nature in the years ended September 30, 2010 and 2009, respectively.

Investment in Affiliates
Investments in 50%-owned affiliates are accounted for using the equity method of accounting and reported within investment in affiliated companies on the consolidated balance sheet. These include Vermont Clinical Resources, Inc.; Copley Woodlands, Inc.; The Vermont Health Plan (TVHP) (prior to its sale in fiscal year 2009); Starr Farm Partnership; and OB Net Services, LLC.

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

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

Depreciation is calculated using the following estimated useful lives, as recommended by the American Hospital Association:

Land improvements	15 - 20 years
Building and improvements	7 - 30 years
Fixed equipment	5 - 15 years
Major moveable equipment	2 - 15 years

Gifts of long-lived assets, such as land, buildings, or equipment, are reported as unrestricted support and are excluded from the excess of revenue over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long these long-lived assets must be maintained, expiration of donor restrictions is reported when the donated or acquired long-lived assets are placed in service.

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

Costs of Borrowing
Interest cost incurred on borrowed funds during the period of construction of capital assets, net of investment income on borrowed assets held by trustees, is capitalized as a component of the cost of acquiring those assets. Approximately $858,000 and $951,000 of interest was capitalized during the years ended September 30, 2010 and 2009, respectively. Net deferred financing costs totaled $16,106,000 and $16,904,000 at September 30, 2010 and 2009, respectively. Such amounts are reported within other assets and are amortized over the period the related obligations are outstanding using the effective interest method. Accumulated amortization of deferred financing costs totaled $5,723,000 and $4,925,000 at September 30, 2010 and 2009, respectively.

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

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

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

Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts due from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Under the terms of various agreements, regulations, and statutes, certain elements of third-party reimbursement are subject to negotiation, audit, and/or final determination by the third-party payors. In addition, laws and regulations governing Medicare and Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Differences between amounts previously estimated for retroactive adjustments and amounts subsequently determined to be recoverable or payable are included in net patient service revenue in the year that such amounts become known. Changes in prior-year estimates increased net patient service revenue by approximately $3,713,000 and decreased net patient service revenue by approximately $2,000,000 in the years ended September 30, 2010 and 2009, respectively.

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

Medicare

Inpatient acute-care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient rehabilitation services are paid based on a prospective per discharge methodology. These rates vary according to a patient classification system based upon services provided, the patient’s level of functionality and other factors. Outpatient services are paid based upon a prospective standard rate for procedures performed or services rendered. FAHC is reimbursed for cost-reimbursable items at tentative rates, with final settlement determined after submission of annual cost reports by FAHC and audits thereof by the Medicare fiscal intermediary. Medicare reimbursement for professional billings is determined by a standard fee schedule that is determined by the Centers for Medicare and Medicaid Services of the U.S. Department of Health and Human Services. The percentage of net patient service revenue and premium revenue derived from the Medicare program was approximately 30% in the years ended September 30, 2010 and 2009.

Medicaid

Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. As with Medicare, reimbursement is based on a diagnosis-related group (DRG) system that is based on clinical, diagnostic, and other factors. For inpatient rehabilitation and neonatal cases, additional reimbursement is paid through a per diem add-on. For inpatient psychiatric cases, reimbursement is based on a per diem rate calculation, including adjustments for diagnostic factors and length of stay. Outpatient services rendered to Medicaid beneficiaries are paid based upon a prospective standard rate. Certain laboratory, mammography, therapy, and dialysis services are paid on a fee schedule. Medicaid reimbursement for professional services is determined by a standard fee schedule that is determined by the State of Vermont. The Medicaid program accounts for approximately 8% of FAHC's net revenue in the years ended September 30, 2010 and 2009.

Managed Care and Commercial Insurers
Services rendered to patients with commercial insurance are generally reimbursed at standard charges, less a negotiated discount or according to DRG or negotiated fee schedules. Approximately 46% and 47% of FAHC's net revenues were derived from contracted insurers in the years ended September 30, 2010 and 2009, respectively.

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

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

Other Revenue
Other revenue consists primarily of research revenue, sales of pharmaceuticals and related products, cafeteria sales, parking garage income, net assets released from restrictions used for operations, and rental income.

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

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

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

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

For tax years beginning after December 15, 2008, non-public companies adopted guidance under ASC740, Income Taxes, that prescribe a model for the recognition and measurement of uncertain tax benefits. This guidance did not have an impact on Fletcher Allen Health Care and its subsidiaries.

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

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

The estimated future undiscounted value of the asset retirement obligation is approximately $1,329,000 at September 30, 2010, substantially all of which relates to the estimated costs to remove asbestos that is contained within FAHC’s facilities. The initial asset retirement obligation was calculated using a discount rate of 4.5%. The asset retirement obligation at September 30, 2010 and 2009 was approximately $1,043,000 and $996,000 respectively. The adjustments to the carrying amount of the asset retirement obligation in the years ended September 30, 2010 and 2009 were primarily attributable to amortization expense and were not significant.

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

Recently Issued Accounting Pronouncements
In 2009, the FASB issued a statement that changes the accounting for combinations involving two or more not-for-profit entities and combinations in which a not-for-profit entity acquires a for-profit business or a nonprofit activity. This statement will be effective for fiscal years beginning after December 15, 2009.

Reclassifications
Certain amounts for the year ended September 30, 2009 have been reclassified to conform to the current year presentation.

Subsequent Events
FAHC has evaluated subsequent events through December 22, 2010, which is the date the financial statements were issued and has concluded that aside from the following item, there were no such events that require adjustments to the audited financial statements or disclosure in the notes to the audited financial statements.

On December 14, 2010, FAHC approved an affiliation agreement between FAHC and Central Vermont Medical Center, Inc. ("CVMC"). Under the terms of this agreement, FAHC and CVMC will jointly organize a new nonprofit, tax-exempt Vermont corporation, to be known as Fletcher Allen Partners, Inc, to act as the sole corporate member of both FAHC and CVMC, and with the purpose of establishing an integrated regional health care system under the common control of Fletcher Allen Partners, Inc. This agreement is subject to due diligence and regulatory approval that will take several months to complete.

3. Charity Care and Community Service

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

The amount of charges foregone for services and supplies furnished under FAHC’s charity care policy aggregated approximately $19,513,000 and $18,538,000 in 2010 and 2009, respectively.

4. Assets Whose Use is Limited or Restricted

Assets whose use is limited or restricted at September 30, 2010 and 2009 consisted of the following:

(in thousands)	**2010**	**2009**
Cash and cash investments	$ -	$ 202
Money market funds	14,117	7,130
Bonds and notes	24,538	30,810
Mutual funds	24,030	1,102
Common collective trusts	240,364	238,294
Beneficial interest in perpetual trusts	9,229	9,389
	312,278	286,927
Less: Current portion	(6,390)	(6,500)
	$ 305,888	$ 280,427

Investment income and gains (losses) for the years ended September 30, 2010 and 2009 consisted of the following:

(in thousands)	2010	2009
Nonoperating revenue and expenses		
Investment income	$ 8,873	$ 7,992
Net realized gains (losses)	18,428	(15,683)
	27,301	(7,691)
Other changes in unrestricted net assets–net change in unrealized gains (losses) on investments	(3,475)	15,873
Changes in temporarily restricted net assets		
Investment income	337	354
Net change in unrealized gains (losses) on investments	(841)	1,915
Net realized gains (losses) on investments	1,759	(1,464)
	1,255	805
Changes in permanently restricted net assets–change in beneficial interest in perpetual trusts	(160)	(587)
	$ 24,921	$ 8,400

As a result of the recognition of losses related to declines in value that were other-than-temporary in nature during the year ended September 30, 2009, there were no investments with a fair value less than their cost at September 30, 2010 and 2009.

The cost and estimated fair value of securities classified as available-for-sale by the organization as of September 30, 2010 and 2009 were as follows:

(in thousands)	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
2010				
Mutual funds	$ 22,719	$ 1,311	$ -	$ 24,030
Money market funds	15,716	-	-	15,716
Bonds and notes	24,333	205	-	24,538
Common collective trusts	229,317	11,047	-	240,364
	$ 292,085	$ 12,563	$ -	$ 304,648

	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
2009				
Mutual funds	$ 1,102	$ -	$ -	$ 1,102
Money market funds	8,139	-	-	8,139
Bonds and notes	29,543	1,267	-	30,810
Common collective trusts	222,682	15,612	-	238,294
	$ 261,466	$ 16,879	$ -	$ 278,345

5. Property and Equipment

A summary of property and equipment at September 30, 2010 and 2009 is as follows:

(in thousands)	2010	2009
Land	$ 8,016	$ 8,016
Land improvements	10,551	10,178
Leasehold improvements	35,707	35,120
Buildings	486,702	470,281
Equipment, furniture, and fixtures	195,932	179,281
	736,908	702,876
Less: Accumulated depreciation and amortization	(316,606)	(282,538)
	420,302	420,338
Construction–in–progress	10,635	16,284
	$ 430,937	$ 436,622

FAHC wrote off approximately $9,050,000 in fully depreciated assets in the year ended September 30, 2010. At September 30, 2010, FAHC had commitments to purchase approximately $6,211,000 of property and equipment.

6. Investment in Affiliated Companies

Investment in affiliated companies at September 30, 2010 and 2009 consisted of the following:

(in thousands)	2010	2009
Starr Farm Partnership	$ 4,522	$ 4,283
OB Net Services, LLC	192	193
	$ 4,714	$ 4,476

Distributions from these affiliated organizations totaled $500,000 and $750,000 for the years ended September 30, 2010 and 2009, respectively. FAHC's share of the income of these affiliates is reported as other nonoperating gains and totaled approximately $739,000 and $785,000 for the years ended September 30, 2010 and 2009, respectively.

Summarized financial information from the unaudited financial statements of the Starr Farm Partnership at September 30, 2010 and 2009, was as follows:

(in thousands of dollars)	Ownership Percentage	Total Assets	Net Assets	Change in Net Assets
2010				
Starr Farm Partnership	50%	$ 10,167	$ 9,044	$ 478
2009				
Starr Farm Partnership	50%	$ 10,213	$ 8,566	$ 71

7. Long-Term Debt

Long-term debt at September 30, 2010 and 2009 consisted of the following:

(in thousands)	2010	2009
Vermont Educational and Health Buildings Financing Agency Hospital Revenue Bonds		
Series 2008A Bonds, variable rate (0.23% and 0.22% at September 30, 2010 and 2009, respectively), payable through 2030	$ 54,705	$ 54,705
Series 2007A Bonds, fixed rate (4.00% to 4.75%), payable through 2037 (including unamortized premium of $101 and $105)	56,321	56,325
Series 2004B Bonds, fixed rate (4.00% to 5.50%), payable through 2035 (including unamortized premium of $142 and $148)	155,017	157,948
Series 2004A Bonds, fixed rate (2.75% to 5.00%), payable through 2025 (including unamortized premium of $1,391 and $1,488)	39,398	41,311
Series 2000A Bonds, fixed rate (5.38% to 6.25%), payable through 2028 (including unamortized discount of $566 and $599)	94,399	95,016
Select Auction Variable-Rate Securities (SAVRS) 1994 Bonds, variable rate (4.93% and 4.93% at September 30, 2010 and 2009, respectively), payable through 2013 (including unamortized discount of $106 and $141)	8,345	10,809
Capital leases and other notes payable	1,455	2,368
	409,640	418,482
Less: Current portion	(8,706)	(9,184)
Long–term debt	$ 400,934	$ 409,298

Revenue Bonds

On May 21, 2008, FAHC converted the Series 2004B auction rate bonds from 35-day variable-rate bonds to fixed-rate bonds through a mandatory tender of the bonds as provided for under the original bond agreement. The tender was financed through the reissuance of $160,525,000 of Series 2004B bonds as tax-exempt fixed-rate bonds, and a payment of $2,700,000 from FAHC's debt service reserve funds. The Series 2004B bonds require FAHC to maintain a debt service reserve fund. As of September 30, 2010 and 2009, the reserve fund balance was approximately $14,834,000 and $14,552,000, respectively, and complied with the requirement to maintain a debt service reserve fund.

Also on May 21, 2008, FAHC in connection with the Vermont Educational and Health Building Financing Agency (the "Agency"), issued $54,705,000 of tax-exempt variable-rate hospital revenue bonds ("Series 2008A"), the proceeds of which were used to refund its Series 2000B bonds in the amount of $50,000,000, pay an early termination payment in the amount of $3,128,000 on a related interest rate swap, and pay issuance costs in the amount of $1,602,000. The Series 2008A bonds are collateralized by an irrevocable letter of credit from a local bank in the amount of $55,334,000, which expires in 2014. The interest rate on the Series 2008A bonds is set weekly. Series 2008A bondholders have the option to put the bonds back to FAHC. Such bonds would be subject to remarketing efforts by FAHC's remarketing agent. To the extent that such remarketing efforts were unsuccessful, the nonmarketable bonds would be purchased from the proceeds of the letter of credit. Monthly payments of principal on the letter of credit borrowings would commence on the first calendar day of the first month that commences more than one year after the borrowing. Repayment in full of the letter of credit would be required by the earlier of four years from the date of the borrowing under the letter of credit or the stated expiration date (currently, April 30, 2014).

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

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

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

Scheduled Maturities of Long-Term Debt
Scheduled maturities of long-term debt, assuming the Series 2008A bonds are not put back to FAHC, and payments on capital lease obligations for the next five years and thereafter are as follows:

(in thousands)

Years Ending September 30		
2011	$	8,706
2012		9,073
2013		8,305
2014		6,260
2015		9,265
Thereafter		367,165
	$	408,774

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

Letter of Credit
If the 2008A letter of credit were fully drawn down, then the schedule of repayments of the 2008A letter of credit would be as follows: $21,176,000 in the year ending September 30, 2012, $21,176,000 in the year ending September 30, 2013, and $12,353,000 in the year ending September 30, 2014.

8. Interest Rate Swap Agreements

FAHC utilizes interest rate swap agreements to manage interest rate risk related to the variable rate Series 2008A Bonds and variable rate SAVRS 1994 Bonds. These agreements had aggregate notional amounts of approximately $55.2 million and $8.5 million, respectively, as of September 30, 2010. Pursuant to each agreement, FAHC is obligated to pay the applicable swap counterparty amounts based on a fixed interest rate and is to receive payment from such swap counterparty based on variable interest rates.

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

In connection with the issuance of the Series 2008A bonds, FAHC entered into two interest rate swap contracts in the notional principal amount of $27,595,000 each. Under these contracts, FAHC will pay a fixed rate of 3.76% on a notional amount equal to the outstanding amount of the Series 2008A bonds for the term of the Series 2008A bonds and receive an alternative floating rate derived from a LIBOR based formula, which may or may not equal the rate on the Series 2008A bonds. The termination date of these swap contracts is December 1, 2030.

FAHC and its counterparty under the 1994 swap agreement entered into a bilateral pledge agreement whereby, on a monthly basis, the counterparty calculates the aggregate exposure amount based on current market value of replacing the interest rate swap agreement with a like financial instrument should either party default. Depending upon the market price at the calculation date, FAHC or its counterparty is required to either collateralize or insure any aggregate exposure in excess of $1,000,000. The replacement of fair value of the interest rate swap agreement with a like instrument would cause FAHC to pay approximately $815,000 at September 30, 2010 and 2009, to the counterparty. The counterparty to the 1994 swap agreement has declared bankruptcy and FAHC has made payments to the trustee in the bankruptcy during the years ended September 30, 2010 and 2009. FAHC makes payments at a rate of 4.93% and receives payments at a variable rate. The termination date of the 1994 swap agreement is September 12, 2013.

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

	2010		2009	
(in thousands)	**Balance Sheet Location**	**Fair Value**	**Balance Sheet Location**	**Fair Value**
1994 Swap	Other long-term liabilities	$ (815)	Other long-term liabilities	$ (815)
2008A Swap	Other long-term liabilities	$ (11,405)	Other long-term liabilities	$ (7,304)

The effects of interest rate swap agreements on the consolidated statements of operations and changes in net assets for 2010 and 2009 are as follows:

		Amount of Gain (Loss) Recognized in Statement of Operations	
(in thousands)	**Location of Gain (Loss) Recognized in Statement of Operations**	**2010**	**2009**
2008A Swap	Loss on interest rate swap contracts	$ (4,101)	$ (4,485)

9. Operating Leases

FAHC has entered into certain operating lease agreements for the rental of building space and equipment. Rental expense amounted to $11,468,000 and $10,384,000 for the years ended September 30, 2010 and 2009, respectively.

Minimum future lease payments required under noncancelable operating leases at September 30, 2010, were as follows:

(in thousands)

Years Ending September 30	
2011	$ 7,104
2012	7,023
2013	4,792
2014	3,786
2015	3,512
Thereafter	5,418
	$ 31,635

10. Net Assets

Temporarily Restricted Net Assets
At September 30, 2010 and 2009, temporarily restricted net assets are available for the following purposes:

(in thousands)	**2010**	**2009**
Indigent care	$ 503	$ 451
Education and research	7,497	6,645
Children's programs	2,092	1,818
Capital projects	1,385	1,490
Other health case services	3,461	3,554
	$ 14,938	$ 13,958

At September 30, 2010 and 2009, temporarily restricted net assets include approximately $8,319,000 and $7,159,000, respectively, of accumulated gains on permanently restricted net assets, which are subject to board appropriation in accordance with state law.

Permanently Restricted Net Assets
At September 30, 2010 and 2009, permanently restricted net assets are restricted to:

(in thousands)	**2010**	**2009**
Investments to be held in perpetuity, income expendable to support		
Indigent care	$ 4,012	$ 4,066
Education and research	3,923	3,888
Other health care services	17,016	17,075
	$ 24,951	$ 25,029

Endowment Funds

FAHC's endowment consists of approximately 78 funds established for a variety of purposes. FAHC does not currently have any unrestricted funds designated by the Board of Trustees (the "Board") to function as endowment. Accordingly, for the purposes of this disclosure, endowment funds include only donor-restricted endowment funds. As required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law

FAHC has interpreted state law as requiring realized and unrealized gains of permanently restricted net assets to be retained in a temporarily restricted net asset classification until appropriated by the Board and expended. State law allows the Board to appropriate the net appreciation of permanently restricted net assets as is prudent considering FAHC's long-and short-term needs, present and anticipated financial requirements, and expected total return on its investments, price level trends, and general economic conditions. In the years ended September 30, 2010 and 2009, $72,000 and $475,000, respectively, was appropriated.

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

Endowment Net Asset Composition and Changes in Endowment Net Assets

The following is a summary of the endowment net asset composition by type of fund at September 30, 2010 and 2009, and the changes therein for the years then ended:

Endowment net asset composition by type of fund

(in thousands)	Temporarily Restricted	Permanently Restricted	Total
2010			
Donor-restricted endowment funds	$ 8,319	$ 15,722	$ 24,041
2009			
Donor-restricted endowment funds	$ 7,159	$ 15,640	$ 22,799

Changes in endowment net assets

(in thousands)	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets at September 30, 2008	$ 6,289	$ 16,290	$ 22,579
Investment return			
Investment income	354	-	354
Net appreciation	451	-	451
Total investment return	805	-	805
Appropriations of endowment assets for expenditure	(475)	-	(475)
Other	540	(650)	(110)
Endowment net assets at September 30, 2009	7,159	15,640	22,799
Investment return			
Investment income	337	-	337
Net appreciation	918	-	918
Total investment return	1,255	-	1,255
Appropriations of endowment assets for expenditure	(72)	-	(72)
Other	(23)	82	59
Endowment net assets at September 30, 2010	$ 8,319	$ 15,722	$ 24,041

Beneficial Interest in Perpetual Trusts

The above amounts exclude FAHC's beneficial interest in perpetual trusts, which are not within management's investment control. Such beneficial interests totaled $9,229,000 and $9,389,000 at September 30, 2010 and 2009, respectively.

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor requires FAHC to retain as a fund of perpetual duration. There were no such deficiencies at September 30, 2010 or 2009.

Investment Return Objectives and Spending Policy

FAHC has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to the programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity or for a donor-specified period(s). Under this policy, the endowment assets are invested in a manner to generate returns at least equal to and preferably greater than the consumer price index. To satisfy its long-term rate-of-return objectives, FAHC targets a diversified asset allocation that places a greater emphasis on equity-based investments within prudent risk constraints.

11. Malpractice and Other Contingencies

Malpractice and Workers' Compensation

FAHC is insured against malpractice losses under a claims-made insurance policy with VMCIC, its wholly owned subsidiary. VMCIC has reinsurance with commercial carriers for coverage above a self-insured retainage amount of $5,000,000 per claim with a $20,000,000 aggregate, with limits on such reinsurance. VMCIC provides claims-made coverage to certain affiliates of FAHC for periods prior to the merger that created FAHC.

FAHC is also self-insured for workers' compensation claims, and maintains an excess insurance policy to limit its exposure on claims to $600,000 per occurrence, with a $25,000,000 aggregate.

The reserves for outstanding losses have been discounted at a rate of 3% at September 30, 2010 and 2009, resulting in a reduction in the reserve of approximately $1,820,000 and $1,819,000 in the years ended September 30, 2010 and 2009, respectively, for professional liability and a reduction in the reserve of approximately $274,000 and $345,000 at September 30, 2010 and 2009, respectively, for worker's compensation.

Activity in the reserve for outstanding losses and loss-related expenses at VMCIC for malpractice and workers' compensation claims for the years ended September 30, 2010 and 2009 is summarized as follows:

(in thousands)	**2010**	**2009**
Balance at beginning of year	$ 35,850	$ 37,325
Less: Reinsurance receivables	(4,711)	(5,793)
Net balance - beginning of year	31,139	31,532
Losses incurred related to		
Current period	9,552	10,168
Prior acts and tail coverage assumed	(4,716)	(291)
Total incurred	4,836	9,877
Paid losses related to		
Current period	933	1,079
Prior period	5,834	9,191
Total paid	6,767	10,270
Net balance - end of year	29,208	31,139
Reinsurance recoverables	4,171	4,711
Balance at end of year	$ 33,379	$ 35,850

As a result of changes in estimates of incurred events in prior years, primarily professional liability, the estimate of incurred losses decreased by approximately $4,716,000 and $291,000 for the years ended September 30, 2010 and 2009, respectively.

The reserve for losses, which was determined with the assistance of an actuarial consultant, includes estimates of claims incurred but not reported. Approximately $7,850,000 and $6,500,000 of the reserve at September 30, 2010 and 2009, is included in current liabilities and the balance of the reserve is included in the noncurrent reserve for outstanding losses on malpractice and workers' compensation claims in the accompanying consolidated balance sheets at September 30, 2010 and 2009, respectively.

Employee Health and Dental Insurance

FAHC maintains a self-insurance plan for employee health and dental insurance. Under the terms of the plan, employees and their dependents are eligible for participation and, as such, FAHC is responsible for the administration of the plan and any resultant liability incurred. FAHC maintained a stop-loss insurance policy to limit its exposure on cumulative claims between $150,000 and $100,000 per member per year in the years ended September 30, 2010 and 2009, with a per-year benefit maximum equal to the amount of premiums paid under the policy. In addition to the self-insurance plan, FAHC maintained a commercial policy to limit its exposure on cumulative claims exceeding $175,000 per member per year.

New York State Medicaid Audit

FAHC received an audit report from the New York State Office of the Medicaid Inspector General (OMIG) that related to the period October 1, 2003 to September 30, 2008. The report claims that OMIG has identified between $7.1 million and $8.7 million in overpayments. Management believes that the report’s findings and demand for repayment are based upon an incorrect interpretation and application of applicable New York law, and on that basis, FAHC has declined to repay the amounts demanded and is vigorously pursuing an administrative appeal. Although management believes the positions asserted in its appeal are legally supported, there can be no assurance that FAHC will ultimately prevail in the appeal.

Other Contingencies

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

Collective Bargaining Agreements

The organization is subject to a collective bargaining agreement with respect to its Registered Nurse ("RN") and Licensed Practical Nurse ("LPN") nursing staff. The current agreement runs through July 9, 2012, and covered approximately 1,631 and 1,664 staff at September 30, 2010 and 2009, respectively. The organization is also subject to a new collective bargaining agreement with the technical bargaining unit. The current agreement runs from March 19, 2010 through March 1, 2013 and covers approximately 306 staff.

12. Statutory Capital and Surplus

VMCIC is registered under the Bermuda Insurance Act of 1978 and related regulations (the “Act”) and is obligated to comply with various provisions of the Act regarding minimum levels of solvency and liquidity. Statutory capital and surplus at September 30, 2010 and 2009, was $23,599,000 and $16,959,000, respectively, and the amount required to be maintained by VMCIC, and not available for distribution, was $2,570,000 and $2,571,000, respectively. In addition, a minimum liquidity ratio must be maintained whereby liquid assets, as defined by the Act, must exceed 75% of defined liabilities. The minimum required level of liquid assets was $19,295,000 and $19,311,000 at September 30, 2010 and 2009, respectively. FAHC reports all of VMCIC’s investments in marketable securities as restricted assets in the accompanying consolidated balance sheets.

13. Pension Plans and Other Postretirement Benefits

Fletcher Allen Health Care Defined Benefit Pension and Postretirement Health Care Plans
Employees of the former Medical Center Hospital of Vermont (MCHV) are covered by a pension plan (the "Plan"), formerly the Pension Plan for Employees of Vermont Health Foundation, Inc. The Plan is a defined benefit final average pay plan with benefit accruals based on an average of salary rates on each January 1. It is FAHC's policy to fund at least the required minimum contribution under Internal Revenue Code, Section 412.

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

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

The premiums paid by retirees participating in the FAHC postretirement health care plan exceed the cost covered by FAHC. Therefore, the projected benefit obligation has been reduced to zero. A reconciliation of the changes in the FAHC defined benefit plan projected benefit obligations and the fair value of assets for the years ended September 30, 2010 and 2009 is as follows:

(in thousands)	FAHC Defined Benefit Plan 2010	FAHC Defined Benefit Plan 2009
Changes in benefit obligations		
Projected benefit obligations - beginning of year	$ (123,701)	$ (111,222)
Service cost	(495)	(512)
Interest cost	(7,230)	(9,074)
Benefits paid	6,060	6,838
Actuarial loss	(8,591)	(10,211)
Administrative expenses paid	527	480
Projected benefit obligation - end of year	(133,430)	(123,701)
Accumulated benefit obligation	(132,495)	(122,606)
Changes in plan assets		
Fair value of plan assets - beginning of year	93,388	105,629
Actual gain (loss) on plan assets	9,696	(9,652)
Contributions	5,275	4,729
Benefits paid	(6,060)	(6,838)
Administrative expenses paid	(527)	(480)
Fair value of plan assets - end of year	101,772	93,388
Funded status of the plan	$ (31,658)	$ (30,313)

Unrestricted net assets at September 30, 2010, include unrecognized actuarial losses of $56,683,000 related to the defined benefit plan. Of this amount, $1,681,000 is expected to be recognized in net periodic pension costs in the year ending September 30, 2011.

Unrestricted net assets at September 30, 2009, include unrecognized actuarial losses of $52,515,000 related to the defined benefit plan. Of this amount, $1,518,000 was recognized in net periodic pension costs in the year ended September 30, 2010.

Amounts included in unrestricted net assets related to the postretirement health care plan are not significant.

The cost components of the net periodic benefit cost for the years ended September 30, 2010 and 2009 are as follows:

	FAHC Defined Benefit Plan	
(in thousands)	**2010**	**2009**
Service cost	$ 495	$ 410
Interest cost	7,230	7,259
Expected return on plan assets	(6,791)	(8,180)
Amortization of unrecognized net loss	1,518	1,319
Net periodic benefit cost	$ 2,452	$ 808

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

	FAHC Defined Benefit Plan	
	2010	**2009**
Weighted-average assumptions used to determine the benefit liability		
Discount rates	5.5%	6.0%
Rates of increase in future compensation levels	3.5	3.5
Weighted-average assumptions used to determine expense		
Discount rates	6.0	6.8
Rates of increase in future compensation levels	3.5	3.5
Expected long-term rate of return on plan assets	7.5	8.0

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

Plan Assets
FAHC's pension plan weighted-average asset allocations as of September 30, 2010 and 2009, by asset category, are as follows:

	2010	2009
Asset Category		
Equity securities	42%	61%
Debt securities	48	30
Real estate investment trusts	4	4
Other	6	5
	100%	100%

The following table presents information as of September 30, 2010 and 2009, about FAHC's pension assets that are measured at fair value on a recurring basis:

(in thousands)	Quoted Prices in Active Markets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Fair Value
2010				
Money market	$ -	$ 577	$ -	$ 577
Mutual fund	11,672	-	-	11,672
Common collective trusts	-	89,523	-	89,523
Total	$ 11,672	$ 90,100	$ -	$ 101,772
2009				
Money market	$ -	$ 665	$ -	$ 665
Common collective trusts	-	92,723	-	92,723
Total	$ -	$ 93,388	$ -	$ 93,388

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

There was no level 3 activity for the years ended September 30, 2009 and 2010.

Cash Flows - Contributions
FAHC expects to contribute $6,330,000 to its pension plan in the year ending September 30, 2011.

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

(in thousands)

Years Ending September 30		
2011	$	6,874
2012		7,628
2013		8,109
2014		8,550
2015		8,936
2016–2020		48,351

Medical Center of Vermont (MCHV) - Retirement Plan

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

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

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

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

In accordance with ERISA guidelines, FAHC provided a new retirement plan for employees of the former MCHV, FAH, and UHC, effective July 1, 1996. The new plan is described as follows:

Fletcher Allen Health Care, Inc. - Retirement Plan
FAHC maintains a tax-sheltered annuity benefit plan covering substantially all of its employees who have at least six months of continuous service. Contributions are determined based on a percentage of employees' salaries up to 10% of pay.

Benefit Plan Costs
FAHC generally funds the benefit costs related to the above retirement plans, including defined contribution plans and postretirement benefit plans, as incurred. Benefit plan costs amounted to $27,918,000 and $23,440,000 for the years ended September 30, 2010 and 2009, respectively. These amounts do not include the amounts paid to UVM as discussed in Note 15.

14. Concentrations of Credit Risk

FAHC grants credit without collateral to its patients, most of whom are local residents and are insured under third-party agreements. The mix of receivables from patients and third-party payors at September 30, 2010 and 2009 is as follows:

	2010	2009
Medicare	34%	32%
Medicaid	14	13
Blue cross	17	17
Other third-party payors	29	33
Patients	6	5
	100%	100%

15. Transactions With UVM

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

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

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

The commitment is an annual undertaking by FAHC to fund a portion of the salary, benefits and related expenses of physician-faculty paid through UVM's payroll process. The minimum commitment payment for each full-time faculty member is $30,000 for salary plus the cost of UVM benefits. The total amount of the commitment is subject to variation each year based upon the needs of FAHC and UVM for physician staffing; the availability of funding sources apart from FAHC to pay for such personnel; and the allocation of the time and effort of physician-faculty among clinical, teaching, research and administrative activities. The amounts of the commitment for physician-faculty salaries and fringe benefits approximated $13,069,000 and $12,334,000 in the years ended September 30, 2010 and 2009, respectively. In addition, FAHC reimburses UVM for equipment rental, research, and certain other administrative expenses through the commitment.

The base academic support payment is paid to UVM by FAHC in monthly installments. Under the prior Affiliation Agreement, the amount of the base payment was $4,011,000 and $4,167,000 in the years ended September 30, 2010 and 2009, respectively. Under the new Affiliation Agreement, the base payment increases to $4,750,000 for the year ending September 30, 2011 and includes a $434,000 payment to support UVM's Dana Medical Library. The base payment increases on each anniversary date of the Agreement by the percentage increase in FAHC's Medicare inpatient hospital reimbursement.

Under the prior Affiliation Agreement, the Dean's Tax was paid by FAHC and was a percentage of the base compensation of faculty physicians. The amount of the Dean's Tax was $4,940,000 and $3,914,000 in the years ended September 30, 2010 and 2009, respectively. Under the new Affiliation Agreement, the Dean's Tax is paid to UVM by UVM Medical Group in an amount equal to the greater of two percent (2.0%) of the Medical Group's net patient service revenues for that fiscal year or $4,600,000.

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

16. Functional Expenses

FAHC provides general health care services to residents within its geographic location. Expenses related to providing these services for the years ended September 30, 2010 and 2009 are as follows:

(in thousands)	**2010**	**2009**
Education and research	$ 1,332	$ 1,364
Health care services	781,646	734,593
Management and general	110,432	118,241
	$ 893,410	$ 854,198

17. Fair Value Measurements

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

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

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

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

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

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

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

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

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

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

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

Common Collective Trusts
The estimated fair values of common collective trusts are determined based upon the net asset value ("NAV") provided by the fund managers and assessed for reasonableness by management. Such information is generally based on the pro-rata interest in the net assets of the underlying investments. There are no unfunded commitments or liquidity restrictions related to these common collective trusts at September 30, 2010 and 2009.

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

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

Long-Term Debt
The estimated fair values of FAHC's long-term debt is based on current traded value. Such amounts at September 30, 2010 and 2009 are approximately $413,027,000 and $413,134,000, respectively.

The following table presents information as of September 30, 2010 and 2009, about FAHC's financial assets and liabilities that are measured at fair value on a recurring basis:

2010 *(in thousands)*	**Quoted Prices in Active Markets (Level 1)**	**Other Observable Inputs (Level 2)**	**Unobservable Inputs (Level 3)**	**Fair Value**
Mutual funds	$ 23,377	$ 653	$ -	$ 24,030
Money market funds	15,716	-	-	15,716
Bonds and notes	-	24,538	-	24,538
Common collective trusts	-	240,364	-	240,364
Beneficial interest in perpetual trusts	-	-	9,229	9,229
	$ 39,093	$ 265,555	$ 9,229	$ 313,877
Interest rate swap agreements	$ -	$ 12,220	$ -	$ 12,220

2009 *(in thousands)*	**Quoted Prices in Active Markets (Level 1)**	**Other Observable Inputs (Level 2)**	**Unobservable Inputs (Level 3)**	**Fair Value**
Mutual funds	$ -	$ 1,102	$ -	$ 1,102
Money market funds	8,341	-	-	8,341
Bonds and notes	-	30,810	-	30,810
Common collective trusts	-	238,294	-	238,294
Beneficial interest in perpetual trusts	-	9,389	-	9,389
	$ 8,341	$ 279,595	$ -	$ 287,936
Interest rate swap agreements	$ -	$ 8,119	$ -	$ 8,119

A roll forward of those marketable securities and investments whose use is limited that have been classified by FAHC as level 3 within the fair value hierarchy (defined above) for the years ended September 30, 2010 and 2009 is as follows:

(in thousands)	**2010**	**2009**
Beginning of year	$ -	$ -
Reclassification of beneficial interest in perpetual trusts from level 2 to level 3	9,389	-
Decrease in fair value of beneficial interest in perpetual trusts	(160)	-
End of year	$ 9,229	$ -
Decrease in fair value of level 3 investments held at September 30, included in the statement of changes in net assets	$ (160)	$ -

There was no level 3 activity in the year ended September 30, 2009.

18. Pledges Receivable

Pledges receivable represent unconditional promises to give and are net of allowances for uncollectible amounts. Pledges are recorded at the present value of their estimated future cash flows. The current yields for 1- to 10-year U.S. Treasury notes are used to discount contributions receivable. Pledges collectible within one year are classified as other current assets and total $894,000 and $848,000 as of September 30, 2010 and 2009, respectively. Estimated cash flows due after one year are discounted using the discounted rate of 5.14% and 4.53% for the years ended September 30, 2010 and 2009, respectively.

Pledges are expected to be collected as follows:

(in thousands)	**2010**	**2009**
Amounts due		
Within one year	$ 961	$ 919
In one to five years	819	1,073
In more than five years	1,248	1,317
	3,028	3,309
Less: Unamortized discount	797	803
	2,231	2,506
Less: Allowance for uncollectables	207	214
Net pledges receivables	$ 2,024	$ 2,292