QUINCY UNITED METHODIST HOME

Financial Statements
and Schedule

December 31, 2006

(With Independent Auditor's Report Thereon)

QUINCY UNITED METHODIST HOME

Table of Contents

Certification of Chief Executive and Chief Financial Officers	1
Independent Auditor's Report	2
Financial Statements:	
Statement of Financial Position	3
Statement of Activities and Changes in Net Assets	5
Statement of Cash Flows	6
Notes to Financial Statements	7
Independent Auditor's Report on Supplementary Information	24
Schedule:	
1 Statutory Minimum Liquid Reserves	25

RETIREMENT AND SENIOR
CARE SERVICES

1217 Slate Hill Road • Camp Hill, Pennsylvania 17011

Certification of Chief Executive and Chief Financial Officers

We are responsible for the financial statements and supporting information of Quincy United Methodist Home, as of December 31, 2006, and attest that they are accurate, complete and fairly presented.

The accuracy and completeness of financial information depends on our systems, process, and most importantly our integrity. Our commitment to integrity is reflected in the code of conduct that the leadership of PHI has established as the standard for the entire organization. We believe that this commitment, our processes and internal controls produce financial information that can be trusted.

Financial statements report our financial position and results using numbers and prescribed rules. They also include a significant amount of information that is required by financial reporting standards. We believe these financial statements disclose information that is important to create a complete picture of our stewardship of financial resources.

Financial statements alone can never reflect the breadth and depth of our stewardship of this ministry. They do not report on our most significant assets, our employees and volunteers. They also do not reflect our most important stewardship role; our commitment to provide Christian understanding and compassion to those seniors entrusted to our care. We believe that we continue to successfully fulfill the financial and non-financial aspects of our mission, extending a proud tradition of ministry that has served older persons in the name of Christ for the past 103 years.

Finally, we believe in openly and honestly sharing information. Please feel free to contact either of us if you have questions on any part of this report, or if we can be of further assistance in understanding PHI's mission.

Stephen E. Proctor
Chief Executive Officer
PHI

Jeffrey J. Davis
Chief Financial Officer
PHI

bmc

Independent Auditor's Report

The Board of Directors
Quincy United Methodist Home:

We have audited the accompanying statement of financial position of Quincy United Methodist Home (an affiliate of PHI) as of December 31, 2006, and the related statement of activities and changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides 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 Quincy United Methodist Home as of December 31, 2006, and the changes in its net assets, and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Beard Miller Company LLP

Beard Miller Company LLP
Lancaster, PA
March 9, 2007

QUINCY UNITED METHODIST HOME

Statement of Financial Position

December 31, 2006

Assets		**December 31, 2006**
Current assets:		
Cash and cash equivalents	$	588,661
Investments		646,565
Accounts receivable, net		1,736,844
Assets whose use is limited – required for current liabilities		344,938
Pledges receivable		7,395
Interest receivable		16,290
Inventory		27,507
Prepaid expenses and other current assets		200,568
Total current assets		3,568,768
Assets whose use is limited, net of current portion		713,738
Property and equipment (net of accumulated depreciation of $23,637,657)		15,870,858
Assets under capital leases (net of accumulated depreciation of $0)		21,111
Funds held in trust by others		5,224,727
Other assets:		
Deferred financing costs (net of accumulated amortization of $370,393)		76,545
Total assets	$	25,475,747

See accompanying notes to financial statements.

QUINCY UNITED METHODIST HOME

Statement of Financial Position

December 31, 2006

Liabilities and Net Assets		**December 31, 2006**
Current liabilities:		
Accounts payable	$	823,293
Accrued expenses		473,404
Current portion:		
Obligations under capital leases		6,449
Long-term debt		2,011,047
Total current liabilities		3,314,193
Resident deposits		31,000
Deferred revenue – entrance fees		7,396,679
Deferred revenue – other		22,083
Due to affiliates		450,019
Accrued pension		302,676
Long-term debt, net of current portion:		
Obligations under capital leases		14,151
Long-term debt		3,784,852
Total liabilities		15,315,653
Net assets:		
Unrestricted		4,527,475
Temporarily restricted		34,447
Permanently restricted		5,598,172
Total net assets		10,160,094
Total liabilities and net assets	$	25,475,747

See accompanying notes to financial statements.

QUINCY UNITED METHODIST HOME

Statement of Activities and Changes in Net Assets

Year ended December 31, 2006

		2006		
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains and other support:				
Resident services, including amortization of entrance fees of $762,065	$ 12,753,343	—	—	12,753,343
Interest and dividend income	293,053	—	—	293,053
Realized gains on investments	17,957	—	—	17,957
Loss on disposal of assets	(7,151)	—	—	(7,151)
Gifts and bequests	295,433	7,395	136,194	439,022
Total revenues, gains and other support	13,352,635	7,395	136,194	13,496,224
Expenses:				
Nursing services	4,665,572	—	—	4,665,572
Rehabilitation	804,520	—	—	804,520
Recreation and special services	196,955	—	—	196,955
Pharmacy	421,211	—	—	421,211
Social services	71,255	—	—	71,255
Physician services	17,692	—	—	17,692
Food services	1,220,600	—	—	1,220,600
Building operations and maintenance	2,030,152	—	—	2,030,152
Housekeeping	337,619	—	—	337,619
Laundry and linen	162,839	—	—	162,839
General and administrative	1,697,096	—	—	1,697,096
Employee benefits	217,972	—	—	217,972
Interest	372,075	—	—	372,075
Depreciation	1,272,007	—	—	1,272,007
Amortization	7,750	—	—	7,750
Total expenses	13,495,315	—	—	13,495,315
Change in net assets before loss on abandoned projects and unrealized gains on investments and assets held in trust by others	(142,680)	7,395	136,194	909
Loss on abandoned projects	(924,050)	—		(924,050)
Unrealized gains on investments and assets held in trust by others	20,260	—	319,234	339,494
Change in net assets	(1,046,470)	7,395	455,428	(583,647)
Net assets, beginning of year	5,573,945	27,052	5,142,744	10,743,741
Net assets, end of year	$ 4,527,475	34,447	5,598,172	10,160,094

See accompanying notes to financial statements.

QUINCY UNITED METHODIST HOME

Statement of Cash Flows

Year ended December 31, 2006

		December 31, 2006
Cash flows from operating activities:		
Change in net assets	$	(583,647)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation		1,272,007
Proceeds from entrance fees and deposits		652,540
Amortization of entrance fees		(762,065)
Unrealized gains on investments and assets held in trust by others		(339,494)
Realized gain on investments		(17,957)
Loss on disposal of assets		7,151
Change in funds held in trust by others		(277,192)
Amortization		7,750
Loss on abandoned projects		924,050
Change in assets and liabilities:		
Accounts receivable		(369,174)
Pledges receivable		(7,395)
Other assets		190,960
Accounts payable		1,979
Accrued pension		(327,868)
Accrued expenses and deferred revenue other		(502,624)
Net cash used in operating activities		(130,979)
Cash flows used in investing activities:		
Acquisition of property and equipment		(270,749)
Proceeds from sale of investments		831,062
Purchases of investments		(727,537)
Net cash used in investing activities		(167,224)
Cash flows from financing activities:		
Refunds of entrance fees and deposits		(57,861)
Principal payments on long-term debt		(384,524)
Borrowings through capital leases		20,600
Due from affiliated entity		450,019
Net cash provided by financing activities		28,234
Net decrease in cash and cash equivalents		(269,969)
Cash and cash equivalents, beginning of year		858,630
Cash and cash equivalents, end of year	$	588,661

See accompanying notes to financial statements.

(1) General Information

Quincy United Methodist Home (the Corporation) is a not-for-profit corporation, which provides services in the south central region of Pennsylvania. The Corporation owns, operates and manages a continuing care retirement community and a personal care home. In total, the Corporation includes 184 independent living units, 31 assisted living units, 133 nursing beds.

As of October 1, 2006, the Corporation affiliated with PHI. The Corporation became a fully controlled affiliate of PHI. The Corporation is governed by a Board of Directors, all of whom are elected by the board of Trustees of PHI, the Corporation's parent organization.

The Corporation has received a Certificate of Authority from the Pennsylvania Insurance Department as required by the Continuing Care Provider Registration and Disclosure Act of 1984, (the Act).

(2) Summary of Significant Accounting Policies

(a) Basis of Accounting

These financial statements, which are presented on the accrual basis of accounting, have been prepared to focus on the Corporation as a whole and to present balances and transactions according to the existence or absence of donor-imposed restrictions.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law.

(b) Tax Status

The Corporation and its subsidiaries are tax exempt under Section 501(c)(3) of the Internal Revenue Code

(c) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(continued)

(d) Cash and Cash Equivalents

The Corporation considers all liquid investments with a maturity of three months or less when purchased to be cash equivalents for the purposes of the statements of financial position and cash flows, except for those included in investments or assets whose use is limited. At times during the year ended December 31, 2006, cash balances may have exceeded the federally insured limit of $100,000.

(e) Investments

Investments in marketable equity securities with readily determinable fair values and all investments in debt securities are measured at fair value, as determined by a national exchange in the statements of financial position. A decline in market value of any investment below cost that is deemed to be other than temporary results in a reduction in carrying amount to fair value. The impairment is charged to realized loss and a new cost basis for the investment is established. For the year ended December 31, 2006, no amounts were charged to realized loss as management believes the decline in value is temporary due to the general economic conditions and not a permanent decline in value.

Investment income consisted of the following:

	2006
Interest and dividends	$ 293,053
Realized gains on investments	17,957
Unrealized gains on investments and assets held in trust by others	339,494
	$ 650,504

Investment expenses of $4,226 for the year ended December 31, 2006 has been included in general and administrative expenses.

(f) Accounts Receivable

Accounts receivable are shown net of an estimated allowance for doubtful accounts, as follows:

	2006
Total accounts receivable	$ 1,986,269
Less: allowance for doubtful accounts	(249,425)
Net accounts receivable	$ 1,736,844

The allowance for doubtful accounts is established based on management's assessment of the collectability of specific resident accounts and the aging of the accounts receivable.

(continued)

(g) ***Assets Whose Use is Limited***

Assets whose use is limited primarily include assets held by a trustee under the terms of various bond indentures and permanently restricted investments. Amounts required to meet current obligations of the Corporation have been reclassified in the statement of financial position as current assets.

(h) ***Pledges Receivable***

During 2006, a pledge was received for $19,985. As of December 31, 2006, the organization has received $12,590 of the gift and the remaining balance will be paid over the next year. The Corporation recorded this pledge at full value since it is due in the current year.

(i) ***Inventories***

Inventories consist of medical and dietary supplies. Inventory is valued at the lower of cost or market using the first-in, first-out method of inventory costing.

(j) ***Property and Equipment***

Property and equipment are stated at cost or, if donated, at fair market value on the date of donation. Depreciation is being provided on the straight-line method over the estimated useful lives of the assets. The Corporation's policy is to capitalize items in excess of $2,000 or for a group of items totaling $2,000 or more.

Depreciable lives are determined as follows:

Land improvements	3-35 years
Buildings and improvements	5-75 years
Departmental equipment, furniture and fixtures	1-40 years
Furniture	5-25 years
Vehicles	4 years

(k) ***Funds Held in Trust by Others***

The Corporation has been named as a beneficiary of several trusts which are administered and controlled by independent trustees. The trusts are recorded as contribution revenue when the Corporation is notified of the trust's existence. The Corporation receives the earnings from these trusts whose principal is to be held in perpetuity. The earnings from the trust are reported as investment income, increasing unrestricted net assets.

Assets held in trust by others are valued at the estimated fair value of the underlying investments. The change in the fair value of assets held in trust by others is reported as permanently restricted unrealized gains or losses on investments.

(continued)

(l) ***Deferred Financing Costs***

The Corporation has deferred the costs incurred for obtaining the proceeds of its long-term debt arrangements. These costs are being amortized over the term of the related financings using the straight-line method which approximates the effective interest method. Amortization expense is expected to be approximately $4,250 for each of the next five years.

(m) ***Workers' Compensation***

Accrued expenses include a provision for estimated self-insured workers' compensation claims for both reported claims not yet paid and claims incurred but not reported.

(n) ***Resident Deposits***

Entrance fees and waiting list deposits received from prospective residents prior to occupancy under Residence and Care Agreements are included in resident deposits in the statement of financial position. These deposits are transferred to deferred revenue upon occupancy of the related units, except in the case of lifetime lease contracts. The portion refundable on these contracts is kept in resident deposits.

(o) ***Deferred Revenue – Entrance Fees***

Entrance fees are collected from residents at move-in pursuant to a Residence and Care Agreement. Under the full payment lease, only 10% is refundable after the fifth year and under the partial payment lease no amount is refundable after the third year. The entrance fee is amortized to income over the estimated remaining life expectancy of each resident. The agreements provide for potential death or termination refunds of the non-refundable portion if reoccupancy occurs before the contractual amortization is completed in accordance with the terms of the agreements. The remaining amount of unamortized, nonrefundable entrance fees is recorded as revenue upon a resident's death or termination of the contract.

The amount of entrance fees refundable to residents at December 31, 2006 under contractual refund provisions was approximately $3,923,000.

(continued)

(p) ***Recently Issued Accounting Pronouncements***

On September 29, 2006, the Financial Accounting Standards Board , "FASB" issued FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* ("SFAS 158"), which amends FASB Statement No. 87 and FASB Statement No. 106 to require recognition of the overfunded or underfunded status of pensions and other postretirement benefit plans on the employer's balance sheet. Under FASB Statement No. 158, gains and losses, prior service costs and credits, and any remaining transition amounts under FASB Statement No. 87 and FASB Statement No. 106 that have not yet been recognized through net periodic benefit cost will be recognized in accumulated other comprehensive income, net of tax effects, until they are amortized as a component of net periodic cost. The measurement date – the date at which the benefit obligation and plan assets are measured-is required to be the Corporation's fiscal year end. FASB Statement No. 158 is effective for employers without publicly traded equity securities for fiscal years ending after June 15, 2007, except for measurement date provisions, which are effective for fiscal years ending after December 15, 2008. The Corporation is currently analyzing the effects of FASB Statement No. 158 on its financial condition, results of operations and cash flows. The Corporation has not yet quantified the financial impact of implementing FASB Statement No. 158.

(q) ***Statutory Liquid Reserve***

The Continuing Care Provider Registration and Disclosure Act requires a working capital reserve equivalent to the greater of the total debt service payments due during the next 12 months on account of any loan or long-term financing, or 10% of the projected annual operating expenses of the Corporation exclusive of depreciation. The reserve is computed on only the proportional share of financing or operating expenses that are applicable to Residence and Care Agreements. The reserve requirement is considered to be fulfilled by the Corporation's unrestricted cash and investments.

(r) ***Temporarily and Permanently Restricted Net Assets***

Temporarily restricted net assets are those whose use by the Corporation has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Corporation in perpetuity. The interest and dividend income from these restricted assets is used for the charitable purpose.

(s) ***Donor Restrictions***

The Corporation reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or the purpose to which the donation is restricted is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities and changes in net assets as net assets released from restrictions. Donor restricted contributions whose restrictions are met within the same year as received are reflected as unrestricted contributions in the accompanying financial statements.

(continued)

(s) Donor Restrictions (continued)

The Corporation reports non-cash gifts as unrestricted support 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 those long-lived assets must be maintained, the Corporation reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

Contributions, including unconditional promises to give, are recognized as revenues when the promise to give is first made. Conditional promises to give are not recognized until they become unconditional, that is when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value as of the date of contribution.

(t) Resident Service Revenue and Business Concentration

Resident service revenue is reported at the estimated net realizable amount to be received from patients and others including Medicare, Pennsylvania Medicaid and other third-party payors for services rendered. The Corporation derives a portion of its revenues from federal and state reimbursement programs with a significant majority of state reimbursement from Pennsylvania Medicaid. The Corporation is certified to receive benefits under Medicare and Medicaid.

The reimbursement methodology for a variety of health care providers has changed significantly as a result of provisions contained in the Balanced Budget Act of 1997 ("Budget Act"). The Budget Act provides for a prospective payment system ("PPS") for Medicare reimbursement for skilled nursing services (rather than the retrospective cost-based methodology in place prior to July 1, 1998). Skilled nursing facilities are paid a federal per diem rate for covered services, which include routine and ancillary services and capital-related costs. In conjunction with PPS, billing for Medicare Part A Services is required for skilled nursing facilities. Under billing for Medicare Part A Services, facilities must bill Medicare for all of the services residents receive, with several exceptions, including all therapy services. The Corporation's skilled nursing facilities began utilizing this new rate methodology in January 1999.

Nursing services provided to Medicaid beneficiaries are paid at prospectively determined rates per day. These rates vary according to a resident classification system that is based on clinical diagnostic and other factors and the reimbursement methodology is subject to various limitations and adjustments. The Corporation's current concentration of skilled nursing facilities in Pennsylvania exposes it to the risk of changes in Medicaid reimbursement in this state.

Revenues from Medicare and Medicaid represent approximately 56% of revenues for 2006. Medicare and Medicaid receivables represent approximately 45% of accounts receivable at December 31, 2006.

(t) *Resident Service Revenue and Business Concentration (continued)*

The Commonwealth of Pennsylvania (the State) received approval from the Federal Center for Medicare Services (CMS), to retroactively assess a nursing bed assessment. For the periods July 1, 2005 to June 30, 2006, the Nursing Facility Assessment Program provided for a \$1.54 assessment per day for continuing care retirement community non-Medicare occupied beds, and \$15.95 a day for stand alone nursing facility non-Medicare occupied beds. As a part of this, nursing home providers received an additional supplement of \$5.17 a day, based on a number of factors, including their Medicaid utilization.

The supplemental and assessment amounts per day have not yet been finalized for the period 7/1-12/31/06. The State has published proposed amounts but no amount has been included on the Corporation's financial statements for this period.

For the year ended December 31, 2006 the Corporation received approximately \$62,364 additional revenue for the net effect of this assessment and supplement.

(u) *Charity Care*

The Corporation provides care to residents, who meet certain criteria under its charity care policy, at amounts less than its established rates. Charity care is recorded as a reduction of revenue.

(v) *Donated Services*

Donated services are reflected in the financial statements at the fair value of the service donated. The Corporation pays for most services requiring specific expertise.

(w) *Advertising*

Advertising costs are expensed in the year incurred. Total advertising expense for the year ended December 31, 2006, was \$44,124.

(x) *Classification of Expenses*

		2006
Program activities	$	11,798,219
General and administrative		1,682,462
Fundraising		14,634
	$	13,495,315

(y) ***Fundraising Expense***

Fundraising expenses incurred by the Corporation are included in general and administrative on the statement of activities and changes in net assets.

(z) ***Performance Indicator***

The Corporation measures the performance of its operations using the statement of activities, which includes a performance indicator of operations labeled as "changes in net assets before loss on impairment of assets and unrealized gains on investments and assets held in trust by others". Changes in unrestricted net assets which are excluded from this measure are: loss on impairment of assets and unrealized gains on investments and assets held in trust by others, and other significant adjustments which do not directly indicate operational performance.

(aa) Statement of Cash Flows

Interest paid during the year ended December 31, 2006 was $405,726.

(3) Investments

The cost and fair value of investments at December 31 is as follows:

	2006	
	Cost	**Fair value**
Money market funds	$ 493,891	493,891
Certificates of deposit	681,331	685,232
Marketable equity securities	266,259	324,264
Municipal debt securities	108,133	98,149
Corporate debt securities	100,680	103,705
Totals	$ 1,650,294	1,705,241
Less assets whose use is limited (note 5)		(1,058,676)
Total investments		$ 646,565

The Corporation invests in a wide variety of individual fixed income and equity investments including bonds issued by municipalities, corporate bonds, and common stock. The Corporation has approximately forty one of such individual holdings.

(3) Investments (continued)

As of December 31, 2006, five individual holdings have a market value that has been below cost for less than a year. These are all common stocks, and in total, their market value is less than six percent below cost.

Five individual holdings have a market value that has been below cost for more than a year. These are both municipal bonds and common stocks, and in total, their market value is less than twelve percent below cost.

A summary of investments with fair values below cost as of December 31, 2006 follows:

		Less than 12 Months		More than 12 Months		Total	
		Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Municipal bonds	$	—	—	98,149	(9,984)	98,149	(9,984)
Subtotal debt securities		—	—	98,149	(9,984)	98,149	(9,984)
Common stocks		26,553	(1,514)	37,361	(7,342)	63,914	(8,856)
Subtotal securities		26,553	(1,514)	37,361	(7,342)	63,914	(8,856)
Total temporarily impaired securites	$	26,553	(1,514)	135,510	(17,326)	162,063	(18,840)

(4) Related Party Transactions

The Corporation has a Development, Marketing and Management Agreement (Management Agreement) with its parent organization. Under the Management Agreement, PHI provides the Corporation with various management and administrative services. In 2006, there were no fees incurred under this agreement.

Amounts due to affiliates for various expenses as of December 31, 2006 are $450,019.

In addition, the Corporation purchases medications from Continuing Care Rx, Inc. As of December 29, 2004, PHI sold its majority interest in Continuing Care Rx Holdings, Inc. and remains a minority shareholder. Total purchases from Continuing Care Rx, Inc. for 2006 were approximately $237,039, of which $113,724 is included in accounts payable as of December 31, 2006.

(5) Assets Whose Use is Limited

At December 31 assets whose use is limited consisted of the following:

		2006
Permanently restricted investments	$	373,444
Community home trust reserve fund		344,938
Debt service reserve fund		340,294
		1,058,676
Less current portion		(344,938)
	$	713,738

(6) Property and Equipment

A summary of property and equipment and accumulated depreciation at December 31 is as follows:

		2006		
		Cost		Accumulated depreciation
Land	$	1,586,989		–
Land improvements		6,030,020		4,327,121
Buildings and improvements		18,346,740		9,210,420
Departmental equipment, furniture and fixtures		13,035,553		9,624,551
Furniture		131,282		114,008
Vehicles		368,377		361,557
Construction-in-progress		9,554		–
	$	39,508,515		23,637,657
Net book value			$	15,870,858

As the Corporation undertakes expansion and improvement projects, costs are included in construction-in-progress. As projects are completed, the costs are transferred to buildings and building improvements. Ongoing improvement and expansion is anticipated in the normal course of operations.

As of December 31, 2006, there were no commitments for future construction.

During 2006, it was determined that a planned renovation and construction project was not moving forward and $924,050 of assets were written off as costs associated with abandoned projects.

(7) Long-term Debt

Long-term debt as of December 31 consisted of the following:

		2006
Mortgage note payable, Community Program Loan Trust, payable in monthly installments of $28,126, due August 2014. The note bears an interest rate of 5%, and is collateralized by all property pland and equipment except the ILU assets.	$	1,393,746
Mortgage note payable, Waynesboro Borough Authority, payable in monthly installments of $18,255, due January 2025. The note bears an interest rate of 5.36% and is collateralized by all ILU assets and a second lien on all other property plant and equipment.		2,733,897
Mortgage note payable, M&T Bank, is payable on demand. If no demand is made, payable in monthly installments of of $9,090 and due July 2028. The note bears an interest rate of 7.50%. The note is collateralized by a second lien position on the ILU assets, and all other property plant and equipment.		1,182,446
Note payable, M&T Bank, is payable on demand. Unless called, payable in monthly installments of principal of $1,200 plus accrued interest, and due February 2039. The note bears a variable interest rate of prime plus one percent, 9.25% at December 31, 2006. The note is collateralized by all personal property, fixtures and receivables.		463,800
Note payable, John Deere Credit, payable in monthly installments of $374. The note bears an interest rate of 3.80%. The note is collateralized by equipment.		22,010
		5,795,899
Less current portion		(2,011,047)
	$	3,784,852

Under the terms of the Corporation's debt, the Corporation is required to maintain certain measures of financial performance as long as the notes are outstanding. These covenants have not been met as of December 31, 2006. A waiver has been obtained by the bank for this time period.

(continued)

(7) Long-term Debt (continued)

Maturities for the five years subsequent to December 31, 2006 are as follows:

Years ended December 31,		Aggregate maturities
2007	$	2,011,047
2008		388,955
2009		409,173
2010		430,444
2011		333,932
Thereafter		2,222,348
	$	5,795,899

(8) Leases

The Corporation is obligated under a capital lease for equipment that expires in 2009. At December 31, 2006, the gross amount of the equipment and related accumulated amortization recorded under capital leases was as follows:

		2006
Office equipment	$	21,111
Accumulated amortization		—
	$	21,111

A schedule of future minimum lease payments under the capital lease together with the present value of the net minimum lease payments as of December 31, 2006 follows:

2007	$	8,085
2008		8,085
2009		7,412
		23,582
Amounts representing interest		(2,982)
	$	20,600

Rental expense under operating leases was $3,228 for the year ended December 31, 2006. There are no future minimum operating lease payment commitments at December 31, 2006.

(continued)

(9) Temporarily Restricted Net Assets

Temporarily restricted net assets as of December 31 are available for the following purposes:

	2006
Nursing scholarships	$ 27,052
Contribution receivable	7,395
	$ 34,447

No net assets were released from restriction during 2006 in satisfaction of the above restrictions.

(10) Permanently Restricted Net Assets

Income from the following permanently restricted net assets as of December 31 is restricted for:

	2006
Investments to be held in perpetuity, the income from which is expendable to support the Corporation's operations	$ 5,224,727
Benevolent Care	373,445
	$ 5,598,172

(11) Charity Care

The Corporation provides care to residents who meet certain criteria under its charity care policy at amounts less than its established rates. Because the Corporation does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. In addition, the Corporation considers contractual allowances charity care. The total amount of charity care provided under these policies was $1,154,089 for the year ended December 31, 2006, of which the amount of charges foregone for services and supplies was approximately $192,741.

(continued)

(12) Retirement Plan

The Corporation has a defined benefit pension plan covering substantially all employees. This plans was curtailed and the benefits were frozen effective December 31, 2004. The benefits are based on years of service and the employee's average compensation during the last 10 years of employment. The Corporation's funding policy is to contribute annually the minimum amount required under statutory funding limitations. Contributions are intended to provide for benefits attributed to service through December 31, 2004.

A comparison of accumulated plan benefits and plan net assets for the Corporation's defined benefit plan consists of the following as of December 31, 2006:

Obligations and Funded Status:		
Change in Benefit Obligation:		
Project benefit obligation - beginning of year	$	(2,914,615)
Interest cost		(159,230)
Distributions		368,669
Change due to assumptions as of end of year		126,003
Experience loss as of beginning of year		(9,369)
Projected benefit obligation - end of year	$	(2,588,542)
Change in Plan Assets:		
Fair value of plan assets - beginning of year	$	2,275,816
Actual return on plan assets		249,414
Contributions		181,000
Benefits Paid		(420,364)
Projected benefit obligation - end of year	$	2,285,866
Funded Status		(302,676)
Unrecognized net transition asset	$	–
Unrecognized net loss		304,380
Unrecognized prior service cost		–
Minimum pension liability adjustment in equity		(304,380)
Accrued Pension Liability, Net	$	(302,676)
As Presented on Consolidated Balance Sheet:		
Intangible asset - pension plan	$	–
Minimum pension liability		(302,676)
Accrued Pension Liability, Net	$	(302,676)

(continued)

QUINCY UNITED METHODIST HOME

Notes to Financial Statements

December 31, 2006

(12) Retirement Plan (continued)

The accumulated benefit obligation amounted to $2,588,542 as of December 31, 2006.

Net periodic pension expense included in following components for the year ended December 31, 2006:

Service cost	$	51,695
Interest cost		159,230
Expected return on plan assets		(186,993)
Amortiztion of unrecognized net loss		21,857
Net Periodic Pension Expense	$	45,789

The plan's funded status as of any measurement date is based on prevailing market conditions as to discount rate and plan assets and, accordingly, is subject to volatility.

The following weighted average rates were used in determining the actuarial present value of the projected benefit obligations and the related net periodic pension cost as of December 31, 2006:

Discount rate	5.8%
Expected rate of return on plan asset:	8.0%
Rate of compensation increase	3.0%

The expected long-term rate of return on plan assets reflects the average rate of earnings expected on the funds invested or to be invested to provide for the benefits included in the projected benefit obligation. The selected rate considers the historical and expected future investment trends of the present and expected assets in the plan.

The expected return on plan assets was determined based on capital market assumptions developed by the Home's independent investment advisors along with other factors such as asset allocation target, investment manager performance, and overall pension performance. The capital market assumptions were projected over a five, ten and 30-year time horizon. Specifically, investment returns for the pension fund were projected over a 10-year period using varying equity allocations.

The pension plan assets were invested and allocated in the following manner as of December 31, 2006:

Equity securities	46.4%
Debt securitieis	45.8%
Other	7.8%

(continued)

(12) Retirement Plan (continued)

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid during the years ending December 31:

2007	56,764
2008	63,327
2009	71,821
2010	82,340
2011	95,387
2012-2015	638,068

The Corporation is not required and therefore, does not expect to contribute to the pension plan during the year ending December 31, 2007.

Starting in 2007, the Corporation's plan will be merged into PHI's. This plan is a defined-contribution retirement plan covering all employees that have completed one year of service and have reached the age of 21. Vesting occurs after five years of service. Contributions to the plan are at the discretion of the Board of Trustees of PHI. No expense was incurred for the year ended December 31, 2006.

(13) Commitments and Contingencies

The Corporation is involved in several legal proceedings arising from its activities in the health care industry. Although it is not possible to presently determine the final outcome of these matters, management believes the aggregate liability, if any, resulting from such proceedings will not have a material adverse effect on the Corporation's assets, liabilities, net assets, operations or cash flows.

(14) Financial Instruments

(a) *Fair Values of Financial Instruments*

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and cash equivalents: The carrying amount approximates fair value because of the short term nature of those investments.

Investments: The fair values of municipal bonds, corporate bonds and equity securities are estimated based on quoted market prices for those or similar investments. Management has determined the fair value of other equity securities based on the stock prices and implied yields of similar publicly traded securities as of December 31, 2006.

(14) Financial Instruments (continued)

Long-term debt: The carrying amount included in long-term debt in the statement of financial position for bonds payable and mortgages payable approximate fair value.

The Corporation has a number of other financial instruments, none of which are held for investment purposes. The Corporation estimates that the fair value of all financial instruments at December 31, 2006 does not differ materially from the aggregate carrying values of its financial instruments recorded in the accompanying statements of financial position.

(b) Financial Instruments with Off-Balance-Sheet Risk

Financial instruments with off-balance-sheet risk to the Corporation, consist of certain financial guarantees of its affiliates and letters of credit obtained from various financial institutions. The Corporation's exposure to credit loss in the event of nonperformance by the other party to the financial instrument is represented by the contractual amount of those obligations.

Independent Auditor's Report on Supplementary Information

To the Board of Directors
Quincy United Methodist Home:

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The following supplementary information accompanying the financial statements is presented for purposes of additional analysis and is not required part of the basic financials statements. The supplementary information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and, accordingly, we express no opinion on such information.

Beard Miller Company LLP

Beard Miller Company LLP
Lancaster, PA
March 9, 2007

QUINCY UNITED METHODIST HOME

Statutory Minimum Liquid Reserves
(See Independent Auditor's Report on Supplementary Information)

As of December 31, 2006

2007 Budgeted Operating Expenses	$ 14,117,097	
Less: depreciation expense	(1,244,000)	
Expenses subject to minimum liquid assets requirement	12,873,097	
Percentage of continuing care residents at December 31, 2006	63%	
	8,110,051	
Statutory requirement	10%	
Statutory minimum liquid reserve requirement	$ 811,005	(a)
Next 12 months debt service payments:		
Principal payments on debt assuming no demand is made	$ 400,905	
Interest payments	280,500	
Total debt service for next 12 months	681,405	
Percentage of continuing care residents at December 31, 2006	63%	
Statutory minimum liquid reserve requirement	$ 429,285	(b)
Assets satisfying statutory minimum liquid reserve requirement		
Unrestricted cash and investments	$ 1,235,226	
Greater of (a) or (b)	811,005	
Assets in excess of statutory minimum liquid reserve requirement	$ 424,221	