North Carolina Department of Health and Human Services
Division of Health Service Regulation

Pat McCrory
Governor

Aldona Z. Wos, M.D.
Ambassador (Ret.)
Secretary DHHS

Drexdal Pratt
Division Director

May 23, 2014

Tim Ludwig, VP Ancillary Services
CarolinaEast Medical Center
Post Office Box 12157
New Bern, North Carolina 28561

Exempt from Review

Facility:	CarolinaEast Medical Center
Project Description:	Renovate and expand space for women's and children's, emergency, surgical services, medical center entrance, administration and public access corridor
County:	Craven
FID #:	923126

Dear Mr. Ludwig:

In response to your letters dated October 25, 2013, March 31, 2014 and May 12, 2014, the above referenced proposal is exempt from certificate of need review in accordance with G.S 131E-184(g). Your certificate for Project ID P-10148-13 was received by the Certification of Need Section with your May 12, 2014 correspondence. Therefore, you may proceed to offer, develop or establish the above referenced project without a certificate of need.

However, you need to contact the Construction and Acute and Home Care Licensure and Certification Sections of the Division of Health Service Regulation to determine if they have any requirements for development of the proposed project.

It should be noted that this determination is binding only for the facts represented by you. Consequently, if changes are made in the project or in the facts provided in your correspondence referenced above, a new determination as to whether a certificate of need is required would need to be made by the Certificate of Need Section. Changes in a project include, but are not limited to: (1) increases in the capital cost; (2) acquisition of medical equipment not included in the original cost estimate; (3) modifications in the design of the project; (4) change in location; and (5) any increase in the number of square feet to be constructed.

If you have any questions concerning this matter, please feel free to contact this office.

Sincerely,

Jane Rhoe-Jones
Project Analyst

Martha J. Frisone, Interim Chief
Certificate of Need Section

cc: Construction Section, DHSR
Acute and Home Care Licensure and Certification Section, DHSR

CAROLINAEAST
HEALTH SYSTEM

CarolinaEast Medical Center
CarolinaEast Diagnostic Center
CarolinaEast Surgery Center
CarolinaEast Rehabilitation Hospital
CarolinaEast Heart Center
CarolinaEast Urology Center
CarolinaEast Internal Medicine
CarolinaEast Pediatrics
CarolinaEast Gastroenterology
CarolinaEast Cardiac Thoracic & Vascular Surgeons
CarolinaEast Physical Medicine & Rehabilitation
CarolinaEast Home Care
Crossroads Mental Health

May 12, 2014

Jane Rhoe-Jones, Project Analyst
North Carolina Department of Health and Human Services
Division of Health Services Regulation
Certificate of Need Section
2704 Mail Service Center
Raleigh, NC 27699-2704

Re: Certificate of Need FID #923126

Dear Ms. Rhoe-Jones,

Thank you for your letter dated May 8, 2014 regarding the above referenced project. As noted, CarolinaEast Medical Center was issued a Certificate of Need FID #923126 dated November 25, 2013 to expand and renovate existing space for women's and children's, emergency and surgical services.

Soon after the June 17, 2013 filing of the application Project I.D.#P-10148-13, the North Carolina General Assembly made changes to G.S. 131E-184(g) that I believe now makes our proposed project exempt from Certificate of Need law.

CarolinaEast has submitted correspondence with the Certificate of Need Section on October 25, 2013 and March 31, 2014 regarding our proposed project being exempt from Certificate of Need. Therefore please find enclosed with this letter the return of our Certificate of Need FID#923126. We ask that with its return, you grant us an exemption for this project pursuant to G.S.131E-184(g).

If you have any questions concerning this request, please do not hesitate to call me.

Respectfully,

Tim Ludwig, Vice President Ancillary Services
CarolinaEast Medical Center

Enclosure

cc: Martha J. Frisone, Interim Chief CON Section

STATE OF NORTH CAROLINA

Department of Health and Human Services
Division of Health Service Regulation

CERTIFICATE OF NEED

for
Project Identification Number #P-10148-13

FID #923126

ISSUED TO: **CarolinaEast Medical Center**
2000 Neuse Boulevard
New Bern, NC 28561

Pursuant to N.C. Gen. Stat. § 131E-175, et. seq., the North Carolina Department of Health and Human Services hereby authorizes the person or persons named above (the "certificate holder") to develop the certificate of need project identified above. The certificate holder shall develop the project in a manner consistent with the representations in the project application and with the conditions contained herein and shall make good faith efforts to meet the timetable contained herein. The certificate holder shall not exceed the maximum capital expenditure amount specified herein during the development of this project, except as provided by N.C. Gen. Stat. § 131E-176(16)e. The certificate holder shall not transfer or assign this certificate to any other person except as provided in N.C. Gen. Stat. § 131E-189(c). This certificate is valid only for the scope, physical location, and person(s) described herein. The Department may withdraw this certificate pursuant to N.C. Gen. Stat. § 131E-189 for any of the reasons provided in that law.

SCOPE: **Expand and renovate existing space for women's and children's, emergency and surgical services/ Craven County**

CONDITIONS: **See Reverse Side**

PHYSICAL LOCATION: **CarolinaEast Medical Center**
2000 Neuse Boulevard
New Bern, North Carolina 28561

MAXIMUM CAPITAL EXPENDITURE: **$3,466,021**

TIMETABLE: **See Reverse Side**

FIRST PROGRESS REPORT DUE: **April 15, 2014**

This certificate is effective as of the 25th day of November, 2013

Craig R. Smith

Chief, Certificate of Need Section
Division of Health Service Regulation

CONDITIONS:

1. **CarolinaEast Medical Center, Inc. shall materially comply with all representations made in its certificate of need application.**

2. **Upon completion of the project, CarolinaEast Medical Center, Inc. shall be licensed for no more than:**
   - **307 general acute care beds**
   - **20 inpatient rehabilitation beds**
   - **23 psychiatry beds, and**
   - **12 operating rooms; including 1 dedicated C-Section room on the campus involved in the proposed project; CarolinaEast Medical Center will maintain an additional six operating rooms at CarolinaEast Surgery Center, which are licensed as part of the hospital.**

3. **CarolinaEast Medical Center, Inc. shall develop and implement an Energy Efficiency and Sustainability Plan for the project that conforms to or exceeds energy efficiency and water conservation standards incorporated in the latest editions of the North Carolina State Building Codes. The plan must be consistent with the applicant's representations in the written statement as described in paragraph one of Policy GEN-4.**

4. **CarolinaEast Medical Center, Inc. shall not acquire, as part of this project, any equipment that is not included in the project's proposed capital expenditure in Section VIII of the application and which would otherwise require a certificate of need.**

5. **Prior to issuance of the certificate of need, CarolinaEast Medical Center, Inc. shall acknowledge acceptance of and agree to comply with all conditions stated herein in writing to the Certificate of Need Section.**

TIMETABLE:

Contract Award	**December 15, 2014**
50% Completion of Construction	**November 7, 2016**
Completion of Construction	**September 1, 2018**
Occupancy/Offering of Service(s)	**October 1, 2018**

North Carolina Department of Health and Human Services
Division of Health Service Regulation

Pat McCrory
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Division Director

May 8, 2014

Tim Ludwig, VP Ancillary Services
CarolinaEast Medical Center
Post Office Box 12157
New Bern, North Carolina 28561

Response to Request for Exemption Pursuant to G.S. 131E-184(g)

Facility:	CarolinaEast Medical Center
Project Description:	Renovate and expand space for women's and children's, emergency, surgical services, medical center entrance, administration and public access corridor
County:	Craven
FID #:	923126

Dear Mr. Ludwig:

The Certificate of Need (CON) Section received your letters dated October 25, 2013 and March 31, 2014 regarding the above referenced project.

CarolinaEast Medical Center submitted a certificate of need application (Project I.D. # P-10148-13) on June 17, 2013 proposing to renovate and expand space for women's and children's, emergency, and surgical services, medical center entrance, administration and the public access corridor. The certificate of need for Project I.D. # P-10148-13 was issued on November 25, 2013.

If you have any questions concerning this request, please do not hesitate to call me.

Sincerely,

Jane Rhoe-Jones, Project Analyst

Martha J. Frisone, Interim Chief
Certificate of Need Section

Certificate of Need Section
www.ncdhhs.gov
Telephone: 919-855-3873 • Fax: 919-733-8139
Location: Edgerton Building • 809 Ruggles Drive • Raleigh, NC 27603
Mailing Address: 2704 Mail Service Center •Raleigh, NC 27699-2704
An Equal Opportunity/ Affirmative Action Employer

CAROLINAEAST
HEALTH SYSTEM

CarolinaEast Medical Center
CarolinaEast Diagnostic Center
CarolinaEast Surgery Center
CarolinaEast Rehabilitation Hospital
CarolinaEast Heart Center
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CarolinaEast Cardiac Thoracic & Vascular Surgeons
CarolinaEast Physical Medicine & Rehabilitation
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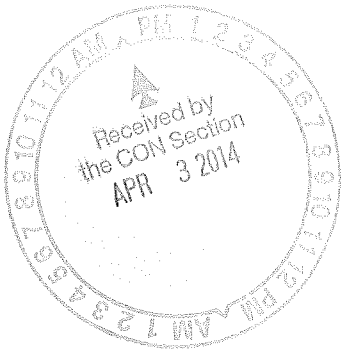
Crossroads Mental Health



March 31, 2014

Jane Rhoe-Jones, Project Analyst
Certificate of Need Section
NC Department of Health and Human Services
Division of Health Service Regulation

Re: FID#923126

Dear Ms. Rhoe-Jones,

CarolinaEast Medical Center has received your letter dated March 7, 2014 regarding additional information pertaining to our request for project exemption pursuant to G.S. 131E-184(g). This project is in regards to the renovation and expansion for women's and children's, emergency, surgical services, medical center entrance, administration, and public access corridor.

As per your request, included with this letter are:

1. A copy of our current license
2. Drawings and site plans that identify the proposed renovations and new construction
3. A brief description of each area affected

Please call me if I can supply additional information. As always, thank you for your assistance and consideration.

Respectfully,

Tim Ludwig
Vice President, Ancillary Service
CarolinaEast Health System
(252)633-8999
tludwig@carolinaeasthealth.com
New Bern, NC

State of North Carolina

Department of Health and Human Services
Division of Health Service Regulation

Effective January 01, 2014, this license is issued to

CarolinaEast Health System

to operate a hospital known as

CarolinaEast Medical Center

located in New Bern, North Carolina, Craven County.

This license is issued subject to the statutes of the State of North Carolina, is not transferable and shall remain in effect until amended by the issuing agency.

Facility ID: 923126

License Number: H0201

Bed Capacity: *350*

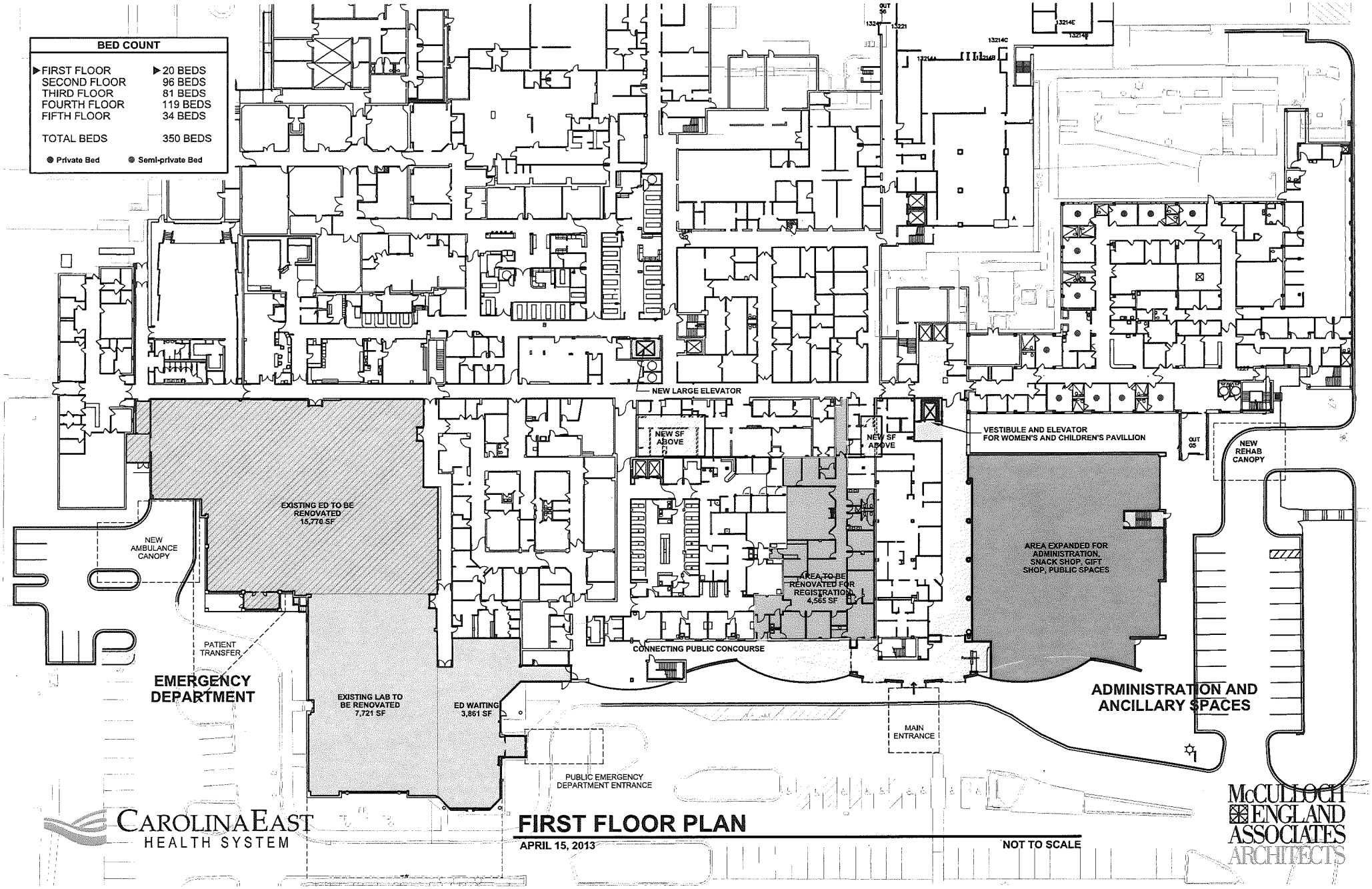
General Acute 307, Rehabilitation 20 , Psych 23,

Dedicated Inpatient Surgical Operating Rooms: 3
Dedicated Ambulatory Surgical Operating Rooms: 6
Shared Surgical Operating Rooms: 9
Dedicated Endoscopy Rooms: 2

Authorized by:

Secretary, N.C. Department of Health and Human Services

Director, Division of Health Service Regulation



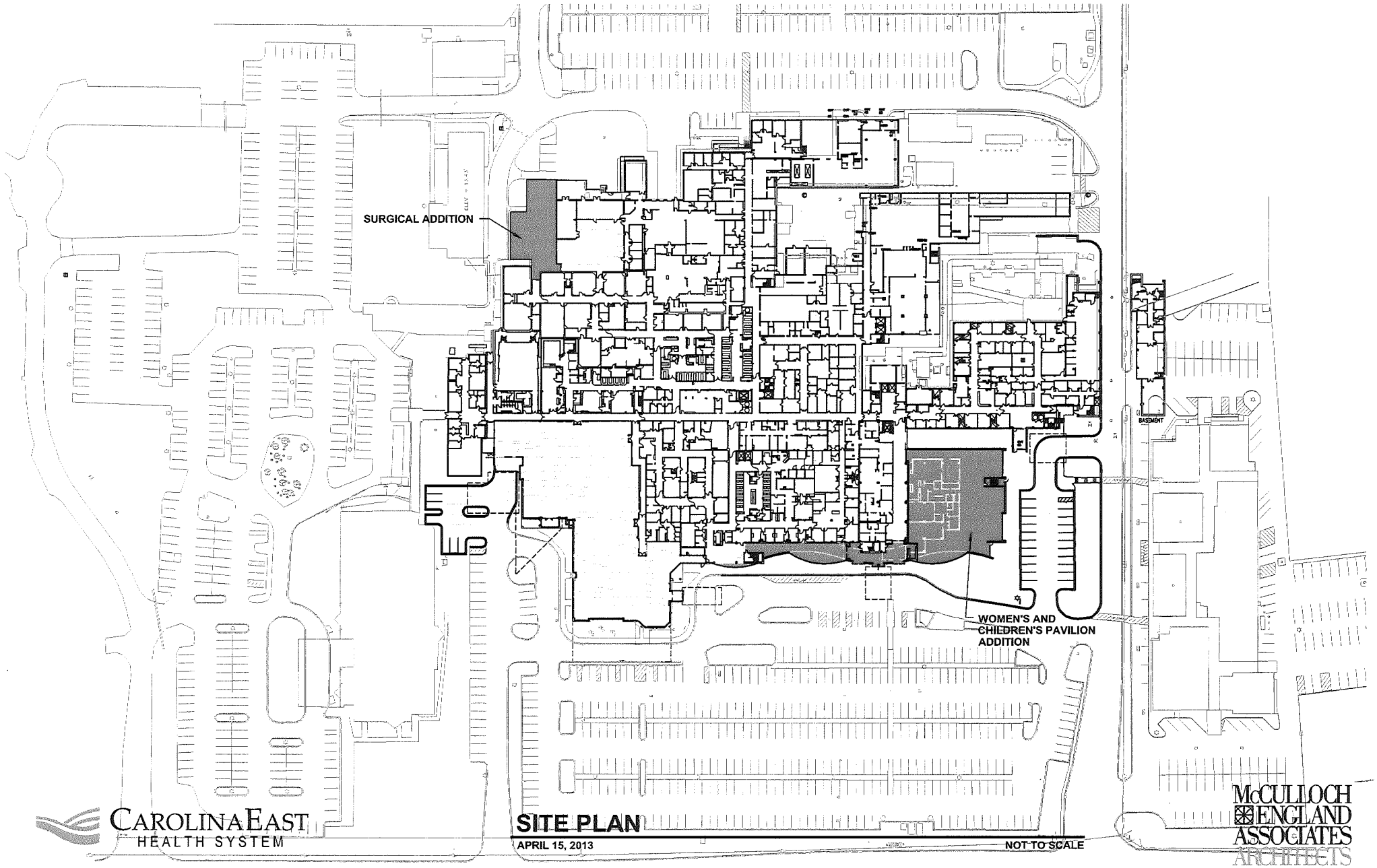
CAROLINAEAST HEALTH SYSTEM

FIRST FLOOR PLAN

APRIL 15, 2013

NOT TO SCALE

McCULLOCH ENGLAND ASSOCIATES ARCHITECTS



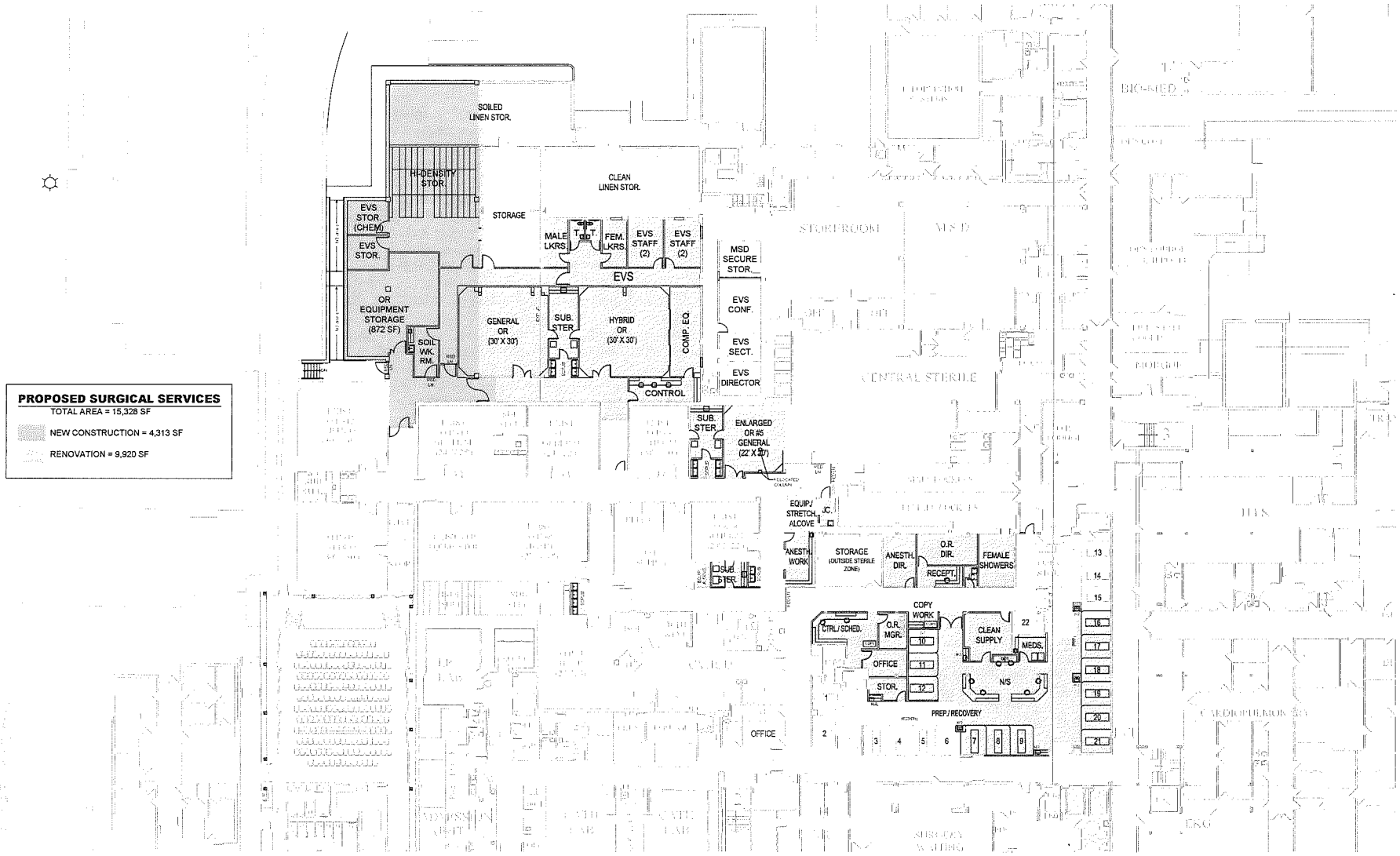
CAROLINAEAST HEALTH SYSTEM

SITE PLAN

APRIL 15, 2013

NOT TO SCALE

McCULLOCH ENGLAND ASSOCIATES ARCHITECTS



CAROLINAEAST
1ST FLOOR PLAN

Surgery Department Renovations

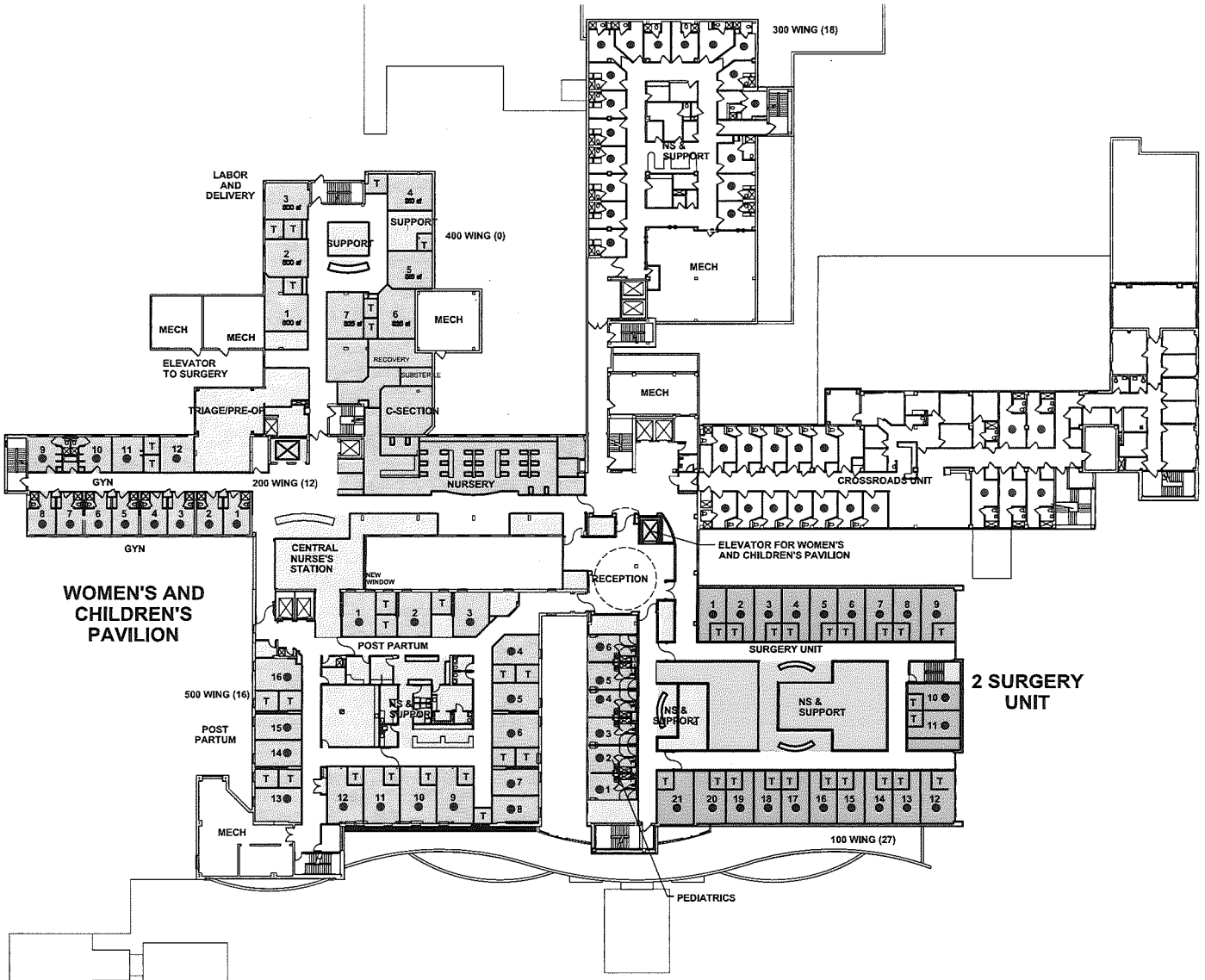
Proposed Plan - Option "J"

March 28, 2013

WILKERSON ASSOCS.
ARCHITECTS

BED COUNT	
FIRST FLOOR	20 BEDS
▶SECOND FLOOR	▶96 BEDS
THIRD FLOOR	81 BEDS
FOURTH FLOOR	119 BEDS
FIFTH FLOOR	34 BEDS
TOTAL BEDS	350 BEDS

● Private Bed ● Semi-private Bed



CAROLINAEAST HEALTH SYSTEM

SECOND FLOOR PLAN

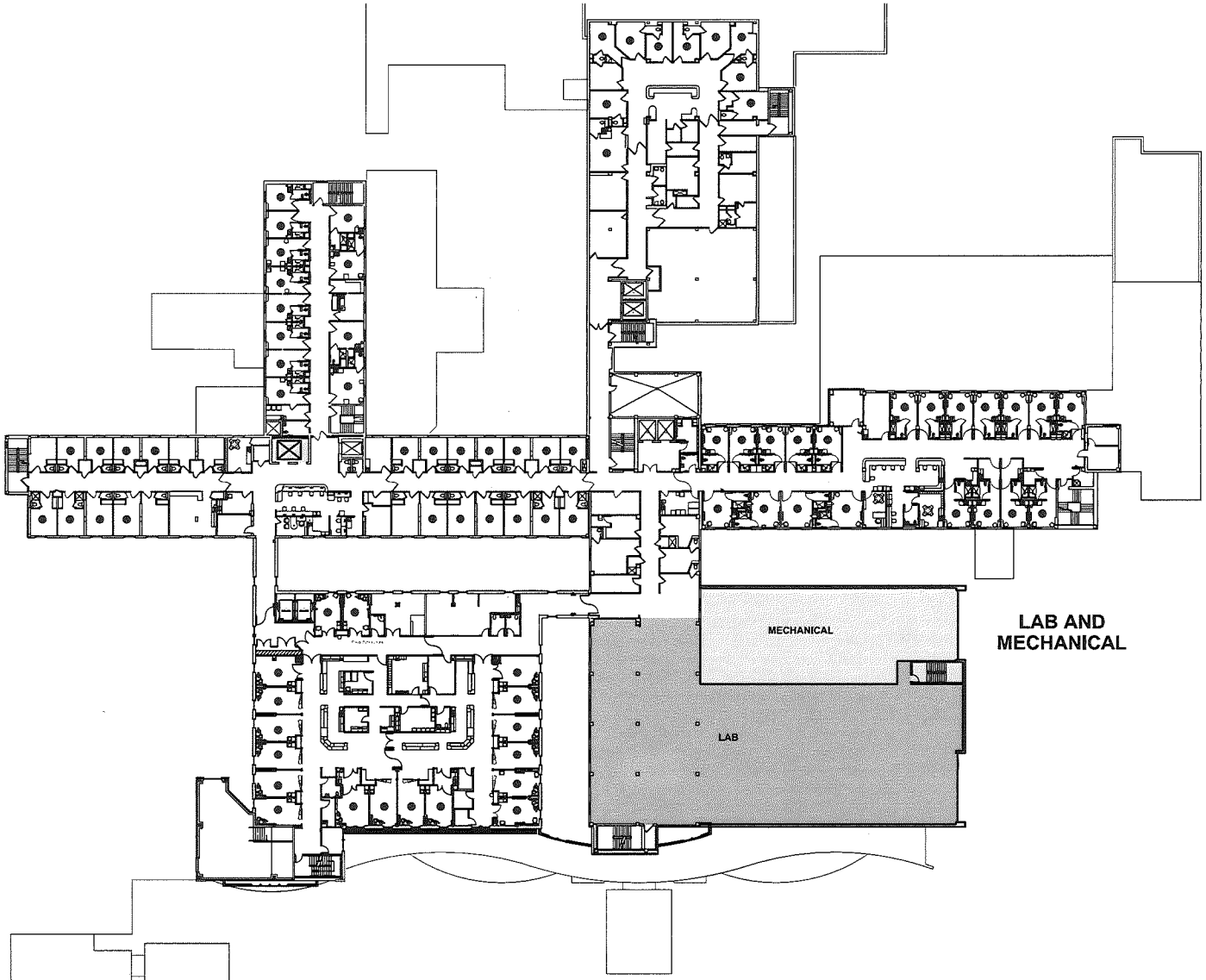
APRIL 15, 2013

NOT TO SCALE

McCULLOCH ENGLAND ASSOCIATES ARCHITECTS

BED COUNT	
FIRST FLOOR	20 BEDS
SECOND FLOOR	96 BEDS
▶ THIRD FLOOR	▶ 81 BEDS
FOURTH FLOOR	119 BEDS
FIFTH FLOOR	34 BEDS
TOTAL BEDS	350 BEDS

● Private Bed ● Semi-private Bed



LAB AND MECHANICAL

CAROLINAEAST HEALTH SYSTEM

THIRD FLOOR PLAN

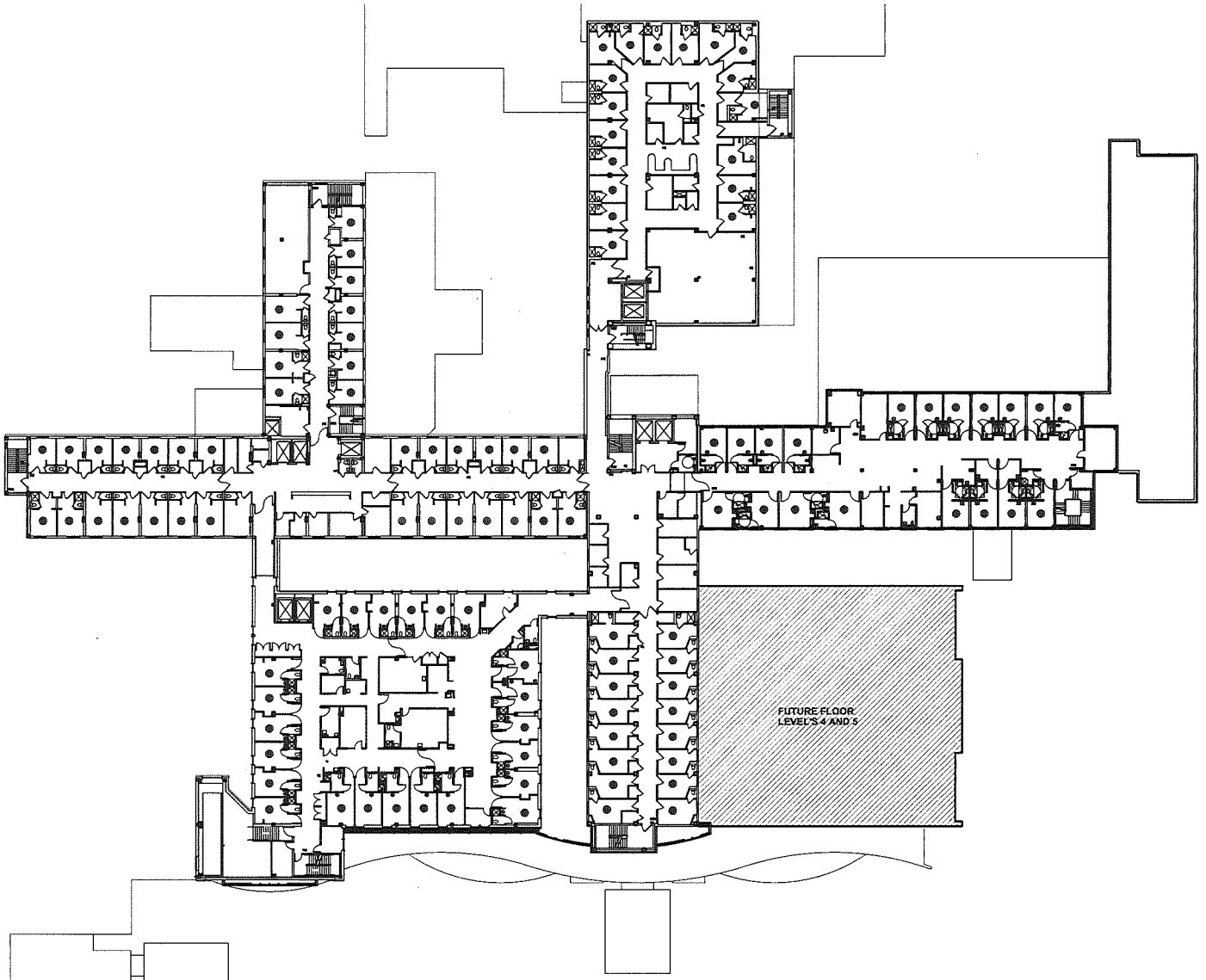
APRIL 15, 2013

NOT TO SCALE

McCULLOCH ENGLAND ASSOCIATES ARCHITECTS

BED COUNT	
FIRST FLOOR	20 BEDS
SECOND FLOOR	96 BEDS
THIRD FLOOR	81 BEDS
▶FOURTH FLOOR	▶119 BEDS
FIFTH FLOOR	34 BEDS
TOTAL BEDS	350 BEDS

● Private Bed ● Semi-private Bed



CAROLINAEAST HEALTH SYSTEM

FOURTH FLOOR PLAN

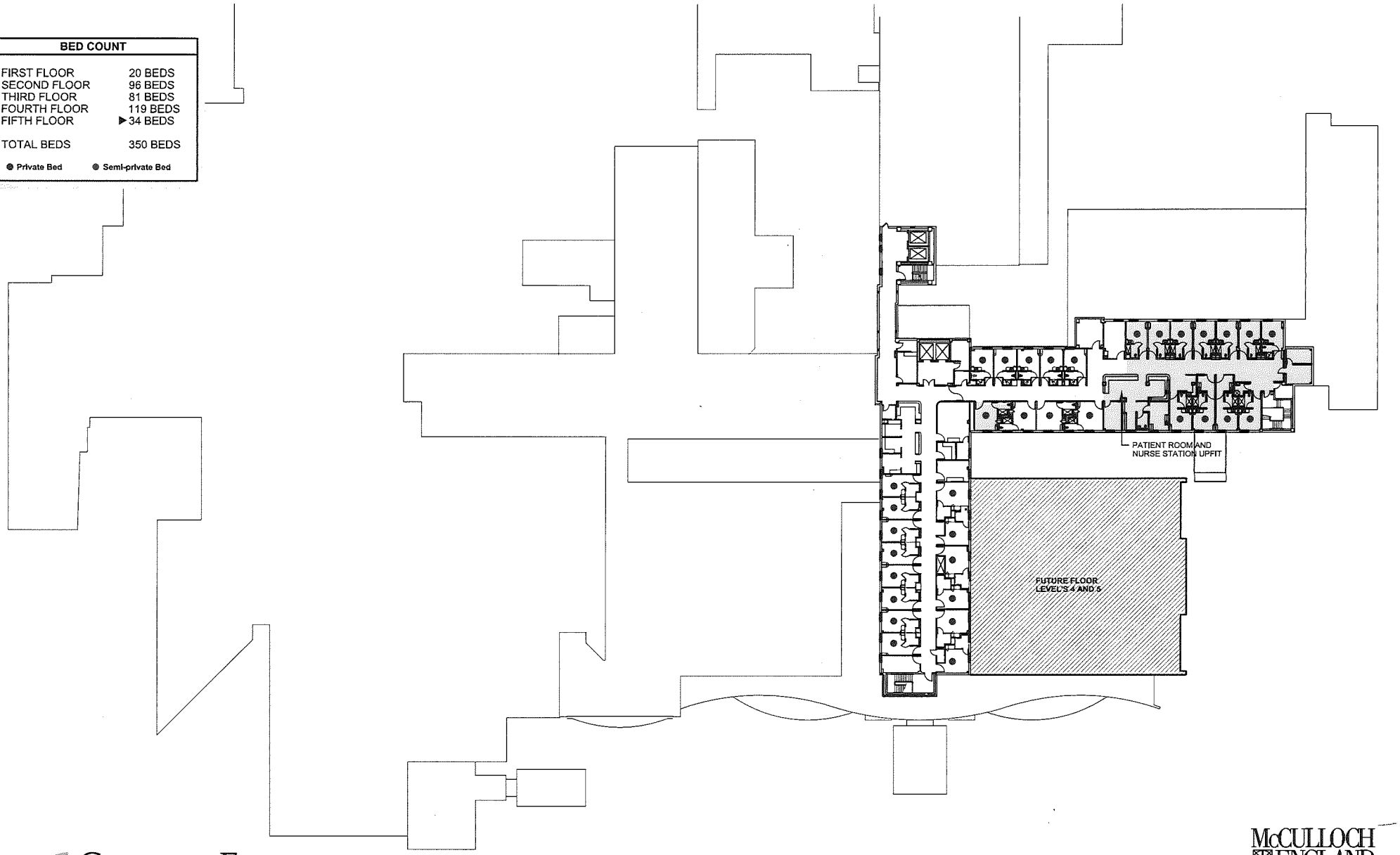
APRIL 15, 2013

NOT TO SCALE

McCULLOCH ENGLAND ASSOCIATES ARCHITECTS

BED COUNT	
FIRST FLOOR	20 BEDS
SECOND FLOOR	96 BEDS
THIRD FLOOR	81 BEDS
FOURTH FLOOR	119 BEDS
▶FIFTH FLOOR	▶34 BEDS
TOTAL BEDS	350 BEDS

● Private Bed ● Semi-private Bed



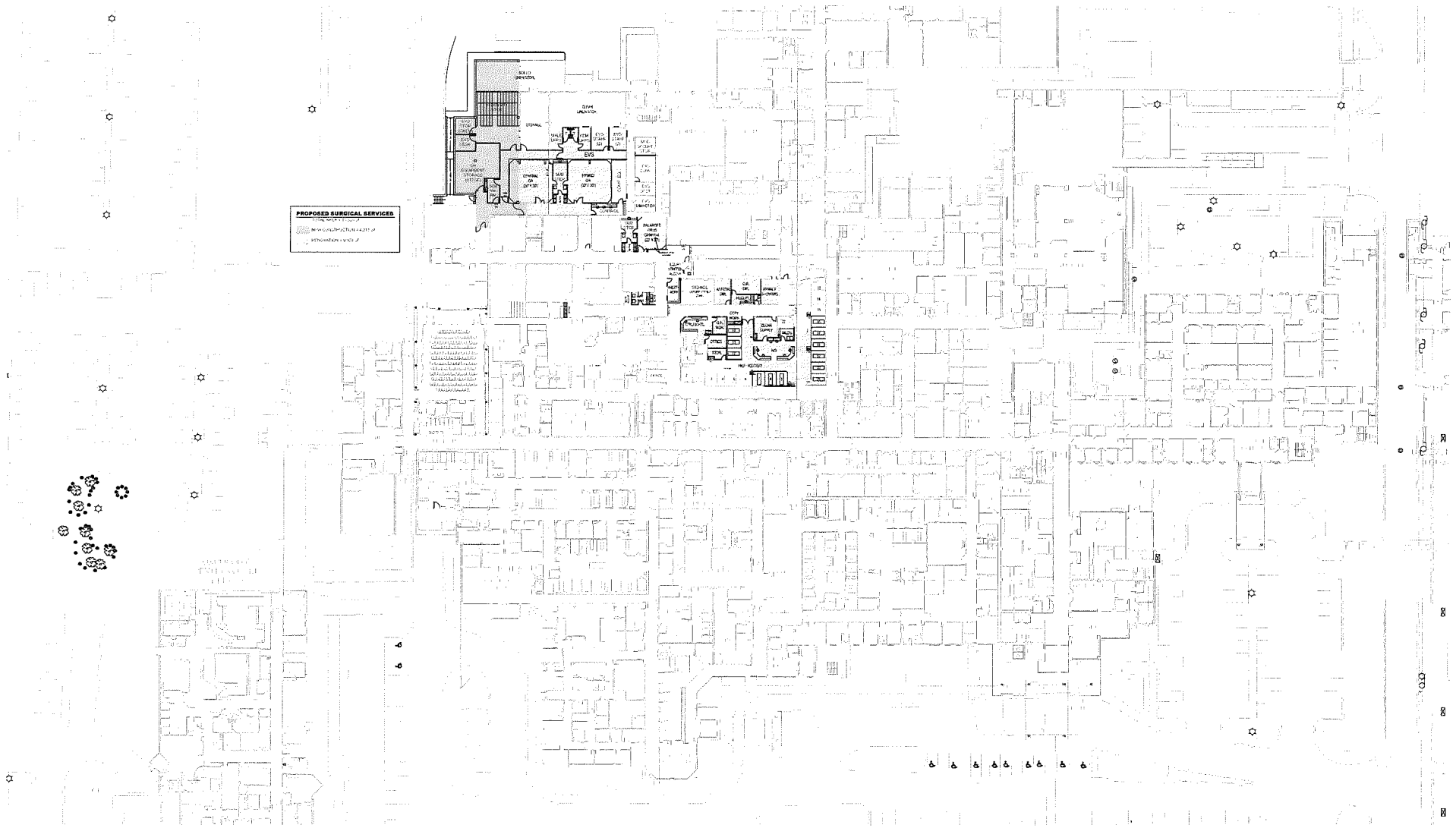
CAROLINAEAST
HEALTH SYSTEM

FIFTH FLOOR PLAN

APRIL 15, 2013

NOT TO SCALE

McCULLOCH
ENGLAND
ASSOCIATES
ARCHITECTS



CAROLINAEAST
1ST FLOOR PLAN

Surgery Department Renovations

Proposed Site Plan - Option "J"

March 28, 2013

WILKERSON ASSOCS.
ARCHITECTS

CarolinaEast Medical Center (CEMC) proposes to expand and renovate space at its main hospital campus related to the provision of women's and children's, emergency, and surgical services in order to remedy age-related facility deficiencies and increase efficiencies of these services. The proposed project is the largest renovation and expansion project in CEMCs 50 year history. In total, the project proposes to add approximately 45,470 square feet to the existing facility and to renovate approximately 96,029 square feet. The Significant renovation and expansion proposed in this project represents an unprecedented facility upgrade designed to meet the needs of Craven County and surrounding communities in the 21st century. In particular, the proposed project involves the following components:

- Women's and Children's Pavilion: CEMC proposes to expand, renovate, and consolidate women's and children's services, creating a Women's and Children's Pavilion. In order to accommodate the proposed renovation and consolidation, CEMC must relocate an existing general medical/surgical bed unit to the second floor of CEMCs proposed new construction.

- Emergency Department: CEMC proposes to renovate and expand its emergency department into existing laboratory and patient registration space. The laboratory will be relocated to the third floor of CEMCs proposed new construction while patient registration will be relocated to space vacated by administration on the first floor of the medical center.

- Surgery Department: CEMC proposes to replace and right-size three existing, outdated and undersized operating rooms by relocating one dedicated C-Section room to the proposed Women's and Children's Pavilion and developing two replacement operating rooms in existing space to be vacated by environmental services as well as new construction.

- Entrance, Administration, and Public Spaces: CEMC proposes to create a new main entrance and public access corridor, which will significantly improve wayfinding and access for patients, families and other visitors. Administration and public spaces will be relocated to the first floor of CEMC's proposed new construction.

Please note that given the scope of the proposed project, renovations and expansions must occur in phases in order to preserve CEMC's ability to care for patients while the project is ongoing. The proposed project will be developed over the course of five years in five phases noted below.

- Phase I: construct new three story addition[1] (relocate administration and public spaces to the first floor, relocate the post-surgical acute care bed unit to the second floor, relocate the laboratory to the third floor); upfit existing space on the second floor to accommodate six relocated pediatric beds; upfit existing space on the fifth floor to house 12 relocated acute care beds; and replace two operating rooms in space vacated by environmental services as well as new construction (to house a portion of the replaced operating rooms and support space as well as environmental services displaced by the operating room replacements)

- Phase II: renovate existing space on the second floor vacated by the post-surgical acute care bed unit to house 16 post-partum rooms; backfill vacated administration suite on the first floor with patient registration; and develop the public access corridor

- Phase III: renovate existing space on the second floor to house Labor & Delivery, gynecology beds, the C-Section suite, and the nursery

[1] The construction of the addition will require CEMC to reorient its existing rehab entrance in conjunction with the proposed project.

- Phase IV: renovate space vacated on the first floor by the laboratory and patient registration to house the expanded emergency department, including areas for waiting and registration
- Phase V: renovate existing emergency department space located on the first floor

As shown in the project schedule in Section XII, CEMC expects all five phases to be complete and the project to be operational by October 1, 2018. Please see Exhibits 2 and 3 for the existing and proposed line drawings[2].

Please note that although the proposed project involves the relocation of licensed acute care beds, CEMC's total licensed acute care bed complement will remain constant. Please see the table provided at the end of this section for a detailed summary of the bed movement associated with the proposed project. With this project CEMC does not propose any new services that it is not currently offering, but believes the proposed project will enable it to better deliver care in the services it currently offers. In particular, as discussed in Section III.I.(a), the proposed project will result in the modernization of the medical center with more appropriate allocation of space for increased patient safety, clinical quality, patient privacy, and staff and patient satisfaction. The specifics related to the various components of the proposed project are described below. The need for the project is discussed in Section III.1.

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[2] Please note that the existing and proposed line drawings of the first floor of the medical center show five intensive care unit beds in their current location in the catheterization lab. As explained in CEMC's previously approved application involving cardiac catheterization services, the medical center is in the process of relocating these acute care beds within the medical center.

FIRST FLOOR (EXISTING/RENOVATION)

Please see Exhibit 2 for a line drawing of the existing first floor layout which indicates the location of each of the service components located on this floor. As illustrated in the existing line drawings provided in Exhibit 2, the first floor currently houses the emergency, laboratory, surgery, administration, registration, and public (lobby, gift shop, and snack shop) areas.

Emergency Department

Emergency department (ED) services currently occupy approximately 15,770 square feet of space on the first floor of the medical center. CEMC operates a 34-room ED in the existing space. The 34-room ED is referred to as CEMC's main ED to distinguish it from CEMC's separate 15-room minor ED, which supports the main ED and typically provides care to lower acuity patients in order to accommodate lower turnaround times for patients. The proposed project involves the main ED and will not impact the number of treatment rooms in the minor ED. Please note that references throughout this application to CEMC's ED refer to CEMC's main ED unless otherwise noted.

As discussed in Section III.1, the existing space is well past its capacity limits based on national emergency care standards. The proposed project involves the renovation of 15,770 square feet in the existing ED. In addition, the proposed project will nearly double the size of the existing ED by expanding the department into 11,582 square feet of adjacent existing space to be vacated by the laboratory and patient registration in conjunction with the proposed project.[3] The proposed project will provide more appropriate, private space and increase the number of treatment rooms in the main ED from 34 to 45.

[3] With the completion of the new main entrance to the medical center, discussed below, CEMC plans to use the old patient registration entrance primarily for walk-in patients to the ED.

The expanded ED space will also allow the medical center to develop appropriate space to hold mental health/psychiatric patients until they can be transferred to a psychiatric facility (which can involve a two to three week waiting period for a space to open up). At present, there is no separate space for psychiatric patients that must wait in CEMC's ED in the event CEMC's adult psychiatric unit is full or the patient does not meet inpatient requirements (i.e., violent or pediatric patients). Given the violent nature of some of these patients, it is imperative that CEMC create space in the renovated ED to accommodate behavioral health patients in a more appropriate, safer space.

The expanded ED will include other areas that support emergency care. The expanded department will include ample space for waiting~ which will segregate public waiting from triage waiting to further speed the throughput of patients in the department. Clinical areas will include nursing stations, medication storage, physician work room and dictation station, an EMS work room and storage area, a family consult room, a viewing area and a body holding room. Staff offices, staff lounge/break room and equipment storage space will also provide support for the expanded department.

Surgery Department

Surgery department services currently occupy approximately 28,865 square feet of space on the first floor of the medical center. The department currently houses 12 operating rooms.[4] The proposed project involves the replacement of three operating rooms that were originally constructed in 1963 and are undersized by modern standards, each measuring approximately 370 square feet. As illustrated in the proposed line drawings provided in Exhibit 3, CEMC proposes to develop two replacement operating rooms in

[4] As documented on page 8b of CEMC's 2013 HLRA, Exhibit 4, the medical center is currently licensed for a total of 12 operating rooms (two dedicated open heart surgery operating rooms, one dedicated C-section room, and nine shared/inpatient/ambulatory operating rooms).

existing space vacated by envirorunental services as well as new construction (to accommodate the two right-sized operating rooms, necessary support space, as well as the displaced envirorunental services). As explained in Section 1II.1.(a), the replacement of two of CEMC's operating rooms on the first floor of the medical center will allow CEMC to create operating rooms that are properly sized to meet best practice guidelines and to perform the high technology surgical procedures that are the norm today. With appropriate sizing, these operating rooms can be used more efficiently. The pre and post-operative space will expand from eight pre-operative and 12 post-operative to a total of 22 pre/post-operative bays. In addition to increasing the number of bays, the size of the incremental bays will also be larger than the existing bays, improving privacy for patients.

The third operating room that CEMC proposes to replace is currently utilized as a dedicated C-Section room. As discussed below relative to the existing second floor, the proposed project involves the consolidation of women's and children's services in order to create a Women's and Children's Pavilion. One component of the proposed consolidation of women's and children's services involves the relocation of the medical center's dedicated C-Section room from the first floor surgical suite to the proposed Women's and Children's Pavilion.

As illustrated in the proposed line drawings included in Exhibit 3, the space vacated by the three operating rooms will be renovated to . house needed office space as well as female showers (which will be developed adjacent to the female lockers). In addition, while the renovation and expansion of these surgical services is underway, CEMC will utilize this opportunity to enlarge one of its existing operating rooms in its current location by relocating a support column.

Public Space (Lobby, Gift Shop, and Snack Shop)

The existing public space at CEMC is undersized and not easily negotiated by patients and families unfamiliar with the medical center. The existing public space, which encompasses approximately 4,918 square feet, will be demolished, making way for the development of a new three story tower, the first story of which will house administration and public space. The space vacated by administration on the existing first floor will be backfilled by registration.

FIRST FLOOR (PROPOSED NEW CONSTRUCTION)

Entrance

As illustrated in the proposed first floor drawings in Exhibit 3 as well as the site plan included in Exhibit 5, the proposed project involves the development of a new main entrance and public access corridor that will connect the new medical center lobby and the emergency department entrance.

Administration and Public Spaces

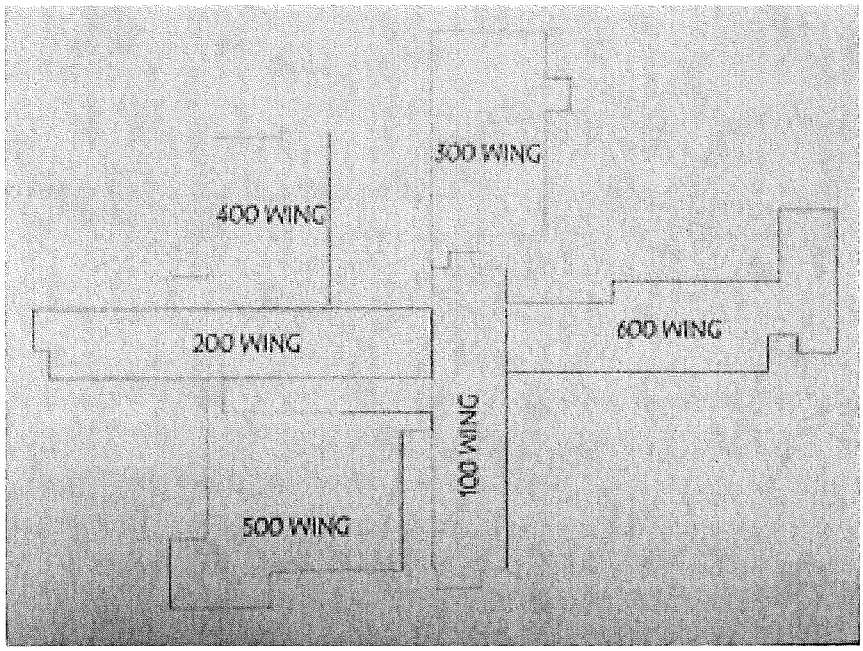
As noted previously, administration and public spaces will be relocated to the first floor of CEMC's proposed new construction (shown in pink on the proposed first floor plan in Exhibit 3). The first floor of the proposed new construction will congregate many public functions at the medical center, including the information desk, lobby, gift shop, and snack shop. The centralized placement of these services that are highly utilized by the public will improve access and optimize wayfinding.

SECOND FLOOR (EXISTING/RENOVATION)

Please see Exhibit 2 for a line drawing of the existing second floor layout which indicates the location of each of the service components located on this floor. As illustrated in the existing line drawings provided in Exhibit 2, the second floor currently houses women's services and a 23-bed general medical/surgical unit (also referred to as the post-surgical acute care bed unit or 2 Surg).

Women's Services

As noted above, the project proposes to expand and consolidate women's services. At present, the majority of women's services are located on the second floor of the medical center. As illustrated in the existing line drawings included in Exhibit 2, the second floor currently houses five labor & delivery (L&D) rooms (one of which is semi-private, for a total of six L&D beds), three women's triage rooms, a nursery with 22 Level I bassinets, and 22 obstetrical/gynecological *(OB/GYN)* beds. The L&D rooms, women's triage rooms, and nursery are located on the 400 wing depicted in the graphic below while the *OB/GYN* beds are located on the 200 wing.



As discussed below relative to women's services, the purpose of the project is to increase the size of patient rooms, improve the flow of nursing support space, and to improve the overall ambiance of the services.

Labor & Delivery (L&D)

As noted previously, the existing L&D is located in the 400 wing on the second floor. L&D moved to its current location in 1985 and has undergone minimal renovations since that time. CEMC currently operates five L&D rooms, one of which operates as a semi-private room, for a total of six L&D beds. Upon completion of the proposed project, all of the L&D rooms will be private. As discussed in Section IIIJ, with the growing number of births, the number of L&D rooms is not sufficient to properly care for these patients. As such, CEMC proposes to add one unlicensed L&D room for a total of seven private L&D rooms upon project completion.

Nursery (Level I Bassinets)

The existing nursery is located in the 400 wing on the second floor. The nursery moved to its current location in 1985 and has undergone minimal renovations since that time. At present the nursery, which houses 22 bassinets, is undersized and outdated. As illustrated in the proposed line drawings included in Exhibit 3, the nursery will be relocated to space on the 200 wing of the second floor. While the proposed nursery will house the same number of bassinets, 22, it will occupy a larger footprint than the existing space. The proposed renovation and expansion will bring the nursery space up to current code requirements.

OB/GYN Beds

As noted previously, the existing OB/GYN beds are located in the 200 wing on the second floor. The OB/GYN beds moved to their current location in 1985 and have undergone minimal renovations since that time. CEMC currently operates 22 licensed OB/GYN beds.

Upon completion of the proposed project, the medical center will operate a total of 28 licensed OB/GYN beds.[5] The same need for L&D, discussed in detail in Section 111.1, produces a need for six additional OB/GYN rooms. As illustrated in the proposed line drawings included in Exhibit 3, CEMC proposes to develop 16 postpartum beds in space located on the 500 wing vacated by an existing post-surgical acute care bed unit in conjunction with the proposed project as discussed below. The remaining 12 OB/GYN beds will be located in existing space to be renovated on the 200 wing of the second floor.

Women's Triage Rooms

CEMC currently operates three women's triage rooms in one space (the rooms are separated by a curtain). In order to improve patient privacy and provide adequate capacity, CEMC proposes to renovate existing space on the 400 wing to house separate physical space for each of the triage rooms as well as add one additional triage room, increasing its triage room count from three to four.

The extensive renovations proposed in this application will create a more pleasing environment for women being cared for at CEMC.

Post-Surgical Acute Care Bed Unit/2 Surg

The 500 wing on the second floor of the existing medical center currently houses a 23-bed general medical/surgical unit (also referred to as the post-surgical acute care bed unit or *1/2* Surg"). In conjunction with the proposed project, this unit will relocate to the second floor of the proposed new construction. As noted below, a small portion of the space which will house this relocated unit consists of existing space located on the 100 wing to be vacated in conjunction with the proposed project.

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5 As noted previously, CEMC's total licensed acute care bed complement will remain constant upon completion of the proposed project.

100 Wing

The 100 wing on the second floor currently houses a 14-bed general medical/surgical unit. The 100 wing located on the second floor of the medical center will be vacated in conjunction with the proposed project. A portion of the space vacated by the 14-bed unit will be renovated to house the pediatric unit relocated from its current location on the third floor of the medical center. Upon completion of the proposed project, the pediatric unit will house six beds.[6] The renovated patient rooms will accommodate any equipment and staff required; will include all technology required in the headwalls by current standards of care; and, will provide amenities for visitors and overnight family members. The remaining space vacated by the 14-bed unit will be renovated to house a portion of the relocated post-surgical acute care bed unit.

SECOND FLOOR (PROPOSED NEW CONSTRUCTION)

Post-Surgical Acute Care Bed Unit/2 Surg

As noted above, the project proposes to expand and consolidate women's and children's services. In order to allow the consolidation to occur, CEMC's existing post-surgical acute care bed unit will be relocated to the second floor of new construction to be developed in conjunction with the proposed project (shown in green on the proposed second floor plan in Exhibit 3). Upon completion of the proposed project, the unit will house 21 beds.[7]

As noted previously, CEMC's total licensed acute care bed complement will remain constant upon completion of the proposed project.

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6 As noted previously, CEMC's total licensed acute care bed complement will remain constant upon completion of the proposed project.

7 Of the 21 beds to be replaced, 20 will be housed in new construction, while one (labeled as "21" in the proposed Second Floor Plan in the line drawings) will be developed in existing space on the 100 wing.

The patient rooms in the new construction will accommodate any equipment and staff required; will include all technology required in the headwalls by current standards of care; and, will provide amenities for visitors and overnight family members.

THIRD FLOOR (EXISTING/RENOVATION)

Please see Exhibit 2 for a line drawing of the existing third floor layout which indicates the location of the service component located on this floor. As illustrated in the existing line drawings provided in Exhibit 2, the third floor currently houses an 8-bed pediatric unit.

Pediatric

The 100 wing on the third floor of the existing medical center currently houses an 8-bed pediatric unit. As noted previously, in conjunction with the proposed project, this unit will relocate to space vacated in conjunction with the proposed project located on the 100 wing on the second floor of the medical center. The space vacated by the 8-bed unit is contiguous to the portion of the proposed new tower to house the relocated laboratory services; thus, the vacated unit will be renovated to be part of the new laboratory space.

THIRD FLOOR (PROPOSED NEW CONSTRUCTION)

Laboratory

Laboratory services currently occupy approximately 7,721 square feet of space adjacent to the emergency department on the first floor of the medical center. The laboratory includes microbiology, hematology, pathology, blood bank, and chemistry departments as well as support space for laboratory equipment and testing. Since most of the activity of the laboratory involves testing which is done within the confines of the department, the laboratory can be located anywhere in the medical center. For these reasons, CEMC proposes to relocate laboratory services to new construction on the third floor of the medical center (shown in orange on the proposed third floor plan in Exhibit 3).

Upon completion of the proposed project, the only component of laboratory services remaining on the first floor of the medical center will be a blood draw station.

Mechanical Space

The third floor of the new construction will also include mechanical space (shown in blue on the proposed third floor plan in Exhibit 3) that will support not only the new construction but also a portion of the existing medical center.

FIFTH FLOOR (EXISTING/RENOVATION)

Please see Exhibit 2 for a line drawing of the existing fifth floor layout.

Acute Care Bed Unit

The proposed renovation/expansion summarized to this point will result in the displacement of 12 of CEMC's acute care beds (general medical/surgical beds). Please refer to the table provided at the end of this section for a detailed account of the bed movement associated with the proposed project. Given the need to maintain its existing acute care bed complement of 307 beds as discussed in detail in Section III.I, CEMC proposes to renovate existing space[8] located on the fifth floor of the medical center to house 12 licensed acute care beds. The patient rooms will accommodate any equipment and staff required; will include all technology required in the headwalls by current standards of care; and, will provide amenities for visitors and overnight family members.

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[8] The existing space currently houses storage, office and conference room space. This space will not be replaced in conjunction with the proposed project.

SUMMARY

With this project CEMC does not propose any new services that it is not currently offering, but believes the proposed project will enable it to better deliver care in the services it currently offers. Further, as noted previously and as detailed in the table below, CEMC's total licensed acute care bed complement will remain constant.

Licensed Acute Care Beds	*Existing*	*Proposed*	*Net Change*
Involved in Scope of Proposed Project			
Medical/Surgical (Med/Surg)			
OB/GYN	22 (9+13)	28	+6
Pediatric	8	6	-2
General Med/Surg	37	33	-4
Post-Surgical Unit, "2 Surg" (current location: 2nd f/oor, 500 Wing; proposed location: 2nd floor of new addition)	23	21	
Second Floor Unit (current location: 100 Wing)	14		
Fifth Floor Unit (current and proposed location: 600 Wing)	0	12	
Total Med/Surg Involved in Scope of Proposed Project	67	67"	o
Not Involved in Scope of Proposed Project			
	240	240	o
Total	*307*	*307*	o

*With the exception of 20 of the 21 beds on the post-surgical acute care unit, all of the proposed beds will be located in renovated, not newly constructed space.

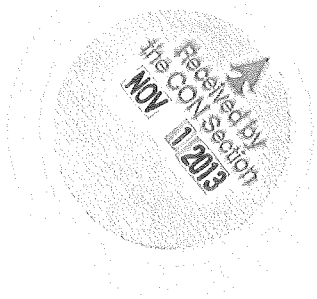
As discussed in Section III.I(a), the proposed project will result in the modernization of the medical center with more appropriate allocation of space for increased patient safety, clinical quality, patient privacy, and staff and patient satisfaction.

Given all of the moving parts of the proposed project, CEMC has provided the summary table below which indicates the location of the existing service components, where the service components will be relocated and whether the relocation involves new construction.

Current Location of Service Components	*Proposed Location (Renovated Space and/or New Construction)*		
	Renovated Space	*New Construction*	*Floor*
First Floor			
Laboratory		Relocated to 3rd floor of new tower	3rd
Emergency Department	Renovation of existing space & expansion into vacated laboratory/patient registration space		1st
Operating Rooms	Replacement of two existing ORs involving renovation/expansion of existing space to right-size the two ORs		1st
Environmental Services		Displaced by OR replacement and relocated to new construction adjacent to replacement ORs	1st
Dedicated C-Section Room	Replacement of one existing C-Section OR involving the relocation of the existing C-section OR to existing space in the proposed Women's and Children's		2nd
Public Space (lobby, gift shop, snack shop,) and Administrative Suite		Expansion becomes part of new main entrance and public access corridor (part of 1st floor of new tower)	1st
Patient Registration	Renovation of existing space vacated by the Administrative Suite		1st

Current Location of Service Components	*Proposed Location (Renovated Space and/or New Construction)*		
	Renovated Space	*New Construction*	*Floor*
Second Floor			
OB/GYN	Renovation of existing space & expansion into vacated general medical/surgical space on the second floor 500 wing		2nd
Labor and Delivery	Renovation of existing space & expansion into vacated nursery space		2nd
Nursery	Renovation of existing space vacated by OB/GYN		2nd
General Medical/Surgical beds (Second floor, 500 Wing, Post-Surgical Acute Care Bed Unit, "2 Surg")		Relocated to 2nd floor of new tower	2nd
General Medical/Surgical beds (Second floor, 100 Wing)	12 beds will be relocated to existing space on the fifth floor		5th
Third Floor			
Pediatric Unit	Relocated to existing space (vacated by the general medical/surgical beds on the second floor 100 wing)		2nd

CarolinaEast Medical Center
CarolinaEast Diagnostic Center
CarolinaEast Surgery Center
CarolinaEast Rehabilitation Hospital
CarolinaEast Heart Center
CarolinaEast Urology Center
CarolinaEast Internal Medicine
CarolinaEast Pediatrics
CarolinaEast Gastroenterology
CarolinaEast Cardiac Thoracic & Vascular Surgeons
CarolinaEast Physical Medicine & Rehabilitation
CarolinaEast Home Care
Crossroads Mental Health



October 25, 2013

Mr. Craig R. Smith, Chief
Certificate of Need Section
Division of Health Service Regulation
2704 Mail Service Center
Raleigh, NC 27699-2704

RE: CarolinaEast Medical Center's Renovation/Expansion Exemption Request

Dear Mr. Smith:

CarolinaEast Medical Center (CEMC), a hospital in New Bern, North Carolina intends to expand and renovate space at its main hospital campus related to the provision of existing women's and children's, emergency, and surgical services in order to remedy age-related facility deficiencies and increase efficiencies of these services. The purpose of this letter is to request a determination that CEMC's project is exempt from Certificate of Need (CON) review under the renovation and expansion exemption as stated under N.C. GEN. STAT. § 131E-184(g). The aforementioned project just received CON approval last week (Project ID # P-10148-13); however, given the recent expansion of the statutory language regarding projects exempt from CON review, CEMC believes that its project fully meets the current statutory exemptions identified under N.C. GEN. STAT. § 131E-184, which include renovation and expansion. If the project is confirmed as exempt, the hospital may consider turning in the Certificate of Need, assuming that one is ultimately issued following CEMC's confirmation of acceptance of the conditions in the Agency Findings for that project.

CEMC believes that its renovation and expansion project meets the criteria for an exemption outlined in N.C. GEN. STAT. § 131E-184(g), as demonstrated below.

1. **The sole purpose of the capital expenditure is to renovate, replace on the same site or expand the entirety or a portion of an existing health service facility that is located on the main campus.**

   The proposed project, described in detail below, involves only the main campus of CEMC, the address of which is 2000 Neuse Boulevard in New Bern. CEMC is part of CarolinaEast Health System, a comprehensive healthcare system, which includes two off-campus freestanding outpatient centers (a diagnostic center and an ambulatory surgical facility) and multiple physician offices throughout the region. The majority of outpatient care and

P.O. BOX 12157 2000 NEUSE BOULEVARD NEW BERN, NC 28561 252 / 633 8111 CAROLINAEASTHEALTH.COM

all inpatient services are provided at CEMC' hospital facility on the main campus at 2000 Neuse Boulevard, the site of the proposed project. In addition to housing all 307 of CEMC's acute care beds, the facility also includes inpatient rehabilitation and inpatient psychiatric beds, as well as an emergency department and multiple outpatient departments. As noted on its 2013 Hospital License Renewal Application, page 2, CEMC considers 2000 Neuse Boulevard to be the "main hospital" campus. CEMC, through its parent, CarolinaEast Health System, has financial and administrative control of the campus, as it owns the buildings and their contents and leases the land through a long-term lease with Craven County, of which CarolinaEast Health System is a component unit. CEMC operates the facility, receives all revenue for the services performed therein and pays expenses associated with the services. The buildings, fixtures and equipment used for these services are all held as capital assets of CarolinaEast Health System, as shown on its audited financial statements in Attachment 1. The hospital facility at 2000 Neuse Boulevard houses the administration of CarolinaEast Health System and CEMC in its entirety. Thus, CEMC maintains full administrative and financial control of the main campus at 2000 Neuse Boulevard.

CEMC proposes to **expand and renovate** space at its main hospital campus related to the provision of women's and children's, emergency, and surgical services in order to remedy age-related facility deficiencies and increase efficiencies of these services. In total, the project proposes to add approximately 45,470 square feet to the existing facility and to renovate approximately 96,029 square feet. **All of the services impacted by the project currently exist and are in operation at the existing facility.** In particular, the proposed project involves the following components:

- Women's and Children's Pavilion: CEMC proposes to **expand and renovate** women's and children's services in existing space, creating a Women's and Children's Pavilion. In order to accommodate the proposed **renovation and expansion**, CEMC must **replace** an existing general medical/surgical bed unit by relocating it to the second floor of CEMC's proposed new construction.
- Emergency Department: CEMC proposes to **renovate and expand** its emergency department into existing laboratory and patient registration space. The laboratory will be **replaced** through relocation to the third floor of CEMC's proposed new construction while patient registration will be **replaced** through relocation to space vacated by administration on the first floor of the medical center.
- Surgery Department: CEMC proposes to **replace and expand** three existing, outdated and undersized operating rooms by relocating one existing dedicated C-Section room to the proposed Women's and Children's Pavilion and developing two **replacement** operating rooms in existing space to be vacated by environmental services as well as new construction.

- Entrance, Administration, and Public Spaces: CEMC proposes to create a **replacement** main entrance and public access corridor, which will significantly improve wayfinding and access for patients, families and other visitors. Administration and public spaces will be **replaced** through relocation to the first floor of CEMC's proposed new construction.

Please note that although the proposed project involves the relocation of licensed acute care beds, CEMC's total licensed acute care bed complement will remain constant. Please see the table provided below for a detailed summary of the bed movement associated with the proposed project. With this project CEMC does **not propose any new services that it is not currently offering.**

Licensed Acute Care Beds	***Existing***	***Proposed***	***Net Change***
Involved in Scope of Proposed Project			
Medical/Surgical (Med/Surg)			
OB/GYN	22	28	+6
Pediatric	8	6	-2
General Med/Surg	37	33	-4
Post-Surgical Unit, "2 Surg" (current location: 2nd floor, 500 Wing; proposed location: 2nd floor of new addition)	*23*	*21*	
Second Floor Unit (current location: 100 Wing)	*14*	*0*	
Fifth Floor Unit (current and proposed location: 600 Wing)	*0*	*12*	
Total Med/Surg Involved in Scope of Proposed Project	***67***	***67****	***0***
Not Involved in Scope of Proposed Project			
	240	240	0
Total	***307***	***307***	***0***

*With the exception of 20 of the 21 beds on the post-surgical acute care unit, all of the proposed beds will be located in renovated, not newly constructed space.

Each service involved in the project currently exists at CEMC. As shown in the table on the following page, although the services will be renovated or expanded through relocation into existing space or new construction, all of the services currently exist.

Current Location of Service Components	*Proposed Location (Renovated Space and/or New Construction)*		
	Renovated Space	*New Construction*	*Floo*
First Floor			
Laboratory		Relocated to 3rd floor of new tower	3rd
Emergency Department	Renovation of existing space & expansion into vacated laboratory/patient registration space		1st
Operating Rooms	Replacement of two existing ORs involving renovation/expansion of existing space to right-size the two ORs		1st
Environmental Services (EVS)		Partially displaced by OR replacement and relocated to new construction adjacent to replacement ORs	1st
Dedicated C-Section Room	Replacement of one existing C-Section OR involving the relocation of the existing C-Section OR to existing space in the proposed Women's and Children's Pavilion		2nd
Public space (lobby, gift shop, snack shop) and Administrative Suite		Expansion becomes part of new main entrance and public access corridor (part of 1st floor of new tower)	1st
Patient Registration	Renovation of existing space vacated by the Administrative Suite		1st
Second Floor			
OB/GYN	Renovation of existing space and expansion into vacated general medical/surgical space on the second floor 500 wing		2nd
Labor and Delivery	Renovation of existing space and expansion into vacated nursery space		2nd
Nursery	Renovation of existing space vacated by OB/GYN		2nd
General Medical/Surgical Beds (Second Floor, 500 Wing, Post-Surgical Acute Care Bed Unit, "2 Surg")		Relocated to 2nd floor of new tower	2nd
General Medical/Surgical Beds (Second Floor, 100 Wing)	12 beds will be relocated to existing space on the fifth floor		5th
Third Floor			
Pediatric Unit	Relocated to existing space (vacated by the general medical/surgical beds on the second floor 100 wing)		2nd

2. **The capital expenditure does not result in a change in bed capacity or the addition of a health service facility or any other new institutional health service.**

The capital expenditure **does not result in a change in bed capacity.** Following completion of the project proposed in this application, the number of wards, private and semi-private rooms in the facility will be as follows:

	Number of Beds
Acute Care	307
Rehabilitation	20
Psychiatric	23
Total	**350**

This number is the same as the total shown on CEMC's 2013 Hospital License Renewal Application; therefore, no change in bed capacity will result from the project. Please see the table under number 1 above for further clarification regarding the beds involved in the project.

As shown by the scope of the project under number 1 above, **the capital expenditure will not result in the addition of a health service facility,** as defined in N.C. GEN. STAT. § 131E-176(9b).

The capital expenditure will not result in the addition of any other new institutional health service. Specifically, with the exception of the expenditure of more than $2 million for the project, **the project does not involve any other new institutional health service** as defined in N.C. GEN. STAT. § 131E-176(16)(a) and (c through v).

3. **The licensed health service facility proposing to incur the capital expenditure shall provide prior written notice to the Department along with supporting documentation to demonstrate that it meets the exemption criteria.**

This letter is intended to serve as the required notification. CEMC has not incurred a capital cost for the project prior to July 26, 2013. In fact, CEMC only recently received CON approval for this project, and is awaiting the issuance of the CON or the confirmation of the project's exemption before incurring capital expense for the project.

In addition, this project will comply with the **Policy GEN-4: Energy Efficiency and Sustainability for Health Service Facilities** requirement as it relates to exempt

projects. As with all CEMC's services, engineering management constantly seeks ways to improve and conserve energy and more efficiently utilize hospital resources. This project will be no different. See Attachment 2 for the energy efficiency and sustainability statement provided by CEMC as related to this project.

In accordance with N.C. Gen. Stat. § 131E-184, this letter provides written notice and demonstrates the exempt nature of the renovation and expansion project. Based on the information provided above, please confirm that CEMC's proposal is exempt from CON review. Please let us know as soon as possible if you need additional information to assist you in your consideration of this request. Thank you for your prompt attention to this request.

Sincerely,

Tim Ludwig
Vice President of Ancillary Services
CarolinaEast Health System

Attachments

Attachment 1

CAROLINAEAST HEALTH SYSTEM

(A Component Unit of Craven County, North Carolina)

Financial Statements

September 30, 2012 and 2011

(with Independent Auditors' Report thereon)

CAROLINAEAST HEALTH SYSTEM

BOARD OF DIRECTORS

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ROBERT "DELL" IPOCK
Vice-Chairman

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G. RAYMOND LEGGETT, III
President/CEO

CAROLINAEAST HEALTH SYSTEM

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September 30, 2012 and 2011

DIXON HUGHES GOODMAN LLP
Certified Public Accountants and Advisors

Independent Auditors' Report

To the Board of Directors
CarolinaEast Health System
New Bern, North Carolina

We have audited the accompanying balance sheets of CarolinaEast Health System (the "System") as of September 30, 2012 and 2011, and the related statement of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the CarolinaEast Medical Center Money Purchase Pension Plan or the CarolinaEast Medical Center Employee Benefit Trust fiduciary fund information, which statements reflect total assets of $56,580,345 and 5,266,563, respectively as of December 31, 2011 and increase in net assets of $1,081,341 and $498,064, respectively for the year then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for CarolinaEast Medical Center Money Purchase Pension Plan and the CarolinaEast Medical Center Employee Benefit Trust fiduciary fund information, is based solely on the report of the other auditors

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 audits provide a reasonable basis for our opinion.

In our opinion, the financial statements present fairly, in all material respects, the financial position of the System as of September 30, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and the Other Postemployment Benefits' Schedule of Funding Progress and Schedule of Employer Contributions on pages 3 through 10 and 42 and 43, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have

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applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Dixon Hughes Goodman LLP

January 29, 2013

CAROLINAEAST HEALTH SYSTEM

Management's Discussion and Analysis

September 30, 2012, 2011, and 2010

Management's discussion and analysis ("MD&A") of CarolinaEast Health System's ("System") financial performance provides an overall review of the System's activities for the fiscal year ended September 30, 2012. The intent of this discussion and analysis is to look at the System's performance as a whole. The primary government is defined as CarolinaEast Health System and its blended component unit. A review of the notes to the financial statements and financial statements will enhance an understanding of the System's performance.

Financial Highlights

- The assets of CarolinaEast Health System exceeded its liabilities at the close of the fiscal year by $376,499,372 (net assets).
- The System's total net assets increased by $31,428,869 during the year.
- Net assets invested in capital assets, net of related debt decreased by $1,090,077 at the end of the fiscal year.
- At the end of the current fiscal year, the unrestricted net assets show a balance of $259,653,952, an increase of $32,518,946.

SUMMARY OF CAROLINAEAST HEALTH SYSTEM:

CarolinaEast Health System is a premier multi-facility health care provider located in the heart of eastern North Carolina that provides comprehensive health care services to the people of Craven, Jones, Pamlico and surrounding counties. Previously known as Craven Regional Medical Authority, the System is comprised of two organizations, CarolinaEast Medical Center and CarolinaEast Physicians. The System is a health care provider that recognizes and accepts the responsibility for stewardship that comes with being a sole community provider. The System aims to fulfill this responsibility through a conscientious investment in human resources, technology, and the infrastructure necessary to provide high-quality health care services. The System has been able to fulfill this responsibility with superior performance and outcomes while exceeding its budgeted operating margins.

USING THIS ANNUAL REPORT:

The Annual Financial Report includes the financial statements and notes to the financial statements. In using the statements, please refer to note 1 of the basic financial statements for additional information regarding the definition of the reporting entity and the blended component unit. The financial statements report information about the System using full accrual accounting methods as utilized by similar business activities in the private sector. The financial statements include a balance sheet; a statement of revenues, expenses and changes in net assets; a statement of cash flows; fiduciary fund information; and notes to the financial statements.

The Statement of Revenues, Expenses, and Changes in Net Assets and Balance Sheet:

The balance sheet presents the financial position of the System on a full accrual, historical cost basis. While the balance sheet provides information about the nature and amount of resources and obligations at year-end, the statement of revenues, expenses and changes in net assets presents the results of the business activities over the course of the fiscal year and information as to how net assets changed during the fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows.

The Statement of Cash Flows:

The statement of cash flows presents changes in cash and cash equivalents, resulting from operational, capital financing, non-capital financing and investing activities. This statement presents cash receipts and cash disbursements information, without consideration of the earnings event, when an obligation arises, or depreciation of capital assets.

Fiduciary Fund Information:

Fiduciary fund information is included as a result of the System's fiduciary responsibility for a defined contribution pension plan and another postemployment benefit plan it sponsors.

Notes to the Financial Statements:

The notes to the financial statements provide required disclosures and other information essential to a full understanding of the material data provided in the financial statements. The notes present information about the System's accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies, and subsequent events, if any. The financial statements were prepared by the System's staff from the detailed books and records of the System.

OPERATING RESULTS AND CHANGES IN THE SYSTEM'S NET ASSETS

	Year Ended September 30,		
	2012	2011	2010
		(In thousands)	
Operating revenues:			
Net patient service revenue	$ 284,168	$ 272,948	$ 236,525
Other revenue	4,723	3,139	2,959
Total operating revenue	288,891	276,087	239,484
Operating expenses:			
Nursing and other professional services	203,665	191,187	162,378
General, administrative and support services	56,682	54,989	52,681
Depreciation and amortization	19,982	19,620	18,497
Interest	-	15	14
Total operating expense	280,329	265,811	233,570
Operating income	8,562	10,276	5,914
Non-operating revenues (expenses):			
Unrestricted contributions	76	91	39
Investment income	3,710	5,016	4,254
Realized and unrealized gains (losses)	20,928	(7,040)	10,062
Rental income	29	48	76
Other non-operating expense	(1,877)	(644)	(106)
Total non-operating revenue (expenses)	22,866	(2,529)	14,325
Change in net assets	31,428	7,747	20,239
Net assets beginning of year	345,071	337,324	317,085
Net assets end of year	$ 376,499	$ 345,071	$ 337,324

Operating Income

Operating income reflects income earned from operations before consideration of any income from investments or other non-operating income. In each of the past three years the System has reported positive operating income. For 2012 and 2011, operating income was down approximately $1.7 million and up $4.4 million, respectively, from prior years. The primary components that comprise operating income for 2012 and 2011 and the changes in income as compared to the prior year are discussed below.

Total operating revenue in 2012 increased approximately $12.8 million with the entire increase being realized from net patient service revenue. The change in net patient service revenue was primarily the result of an increase in inpatient/outpatient revenue and an increase in patient

chargeable rates implemented for 2012. The System acquired the Cardiac Thoracic and Vascular Associates of Eastern North Carolina and Coastal Physical Medicine, which also contributed to the increase in net patient revenue. The System has seen adjustments for third party payers such as Medicare and Medicaid as a percentage of gross patient revenue, excluding bad debt and charity care adjustments, increase slightly at 54.2% for 2012 and 52.3% for 2011.

The System continues to see changes in patient mix with Medicare, Medicaid and self pay comprising a higher percentage of the overall volume. As a result of such changes in patient mix, for 2012, the System wrote off $38.0 million in bad debt and charity care. One of the significant pressures facing the System and health care in general is the reduction of third party commercial payers and a corresponding shift to self-pay for healthcare bills. The System began writing off 40% for all new self-pay accounts in 2011. That amount totaled $10.6 million for 2012.

Total operating revenue in 2011 increased approximately $36.6 million with the entire increase being realized from net patient service volume. The change in net patient service revenue was primarily the result of an increase in inpatient/outpatient revenue and an increase in patient chargeable rates implemented for 2011. The System acquired the New Bern Urology Center and East Carolina Internal Medicine, which also contributed to the increase in net patient revenue. The System has seen adjustments for third party payers such as Medicare and Medicaid as a percentage of gross patient revenue, excluding bad debt and charity care adjustments, increase slightly at 52.3% for 2011 and 49.5% for 2010.

The System continues to see changes in patient mix with Medicare, Medicaid, and self-pay comprising a higher percentage of the overall volume. As a result of such changes in patient mix, for 2011, the System wrote off $32.9 million in bad debt and charity care. One of the significant pressures facing the System and health care in general is the reduction of third party commercial payers and a corresponding shift to self-pay for healthcare bills. The System began writing off 40% for all new self-pay accounts in 2011. That amount totaled $11.7 million for 2011.

For 2012, total operating expense increased approximately $14.5 million from 2011. In 2012, the System incurred eight months of operating expenses associated with the acquisition of Cardiac Thoracic and Vascular Associates of Eastern North Carolina and two months of operating expenses associated with the acquisition of Coastal Physical Medicine. The total additional expenditures for these acquisitions were $1.4 million. Neither entity was owned by the System in 2011. Physician salaries increased $5.3 million due to hiring additional physicians as well as fulfilling contractual obligations.

For 2011, total operating expense increased approximately $32 million from 2010. In 2011, the System incurred nine months of operating expenses associated with the acquisition of East Carolina Internal Medicine (ECIM) and twelve months of expenses associated with the acquisition of New Bern Urology. The total additional expenditures for these acquisitions were $25.6 million. Neither entity was owned by the System in 2010. The System also contracted with physician organizations to provide professional services to patients which have caused operating expenses to increase by approximately $2.1 million for 2011.

Non-Operating Revenues and Expenses:

Non-operating revenues and expenses consist primarily of interest and dividend income as well as both realized and unrealized gains on investments. Investment income totaled $3.7 million for 2012, which was a decrease of approximately $1.3 million from 2011. For 2012, the net unrealized and realized gains on investments totaled approximately $21.0 million, an increase of approximately $28.0 million from 2011. Both are the result of significant market fluctuations during the year.

Investment income totaled $5.0 million for 2011, which was an increase of approximately $762 thousand from 2010. For 2011, the decrease in the fair value of investments totaled approximately $7.0 million, a decrease of approximately $17.1 million from 2010. Both are the result of significant market fluctuations during the year.

SUMMARY OF SYSTEM NET ASSETS

	September 30,		
	2012	**2011**	**2010**
		(In thousands)	
Assets			
Current assets	$ 125,117	$ 110,864	$ 125,090
Assets limited as to use	186,180	163,692	138,209
Other assets (includes intangible capital assets and other non-current assets)	5,979	6,497	6,991
Capital assets, tangible net	112,680	114,003	112,723
Total assets	429,956	395,056	383,013
Liabilities			
Current liabilities	52,674	48,440	43,392
Long-term liabilities	782	1,545	2,297
Total liabilities	53,456	49,985	45,689
Net Assets			
Invested in capital assets, net of related debt	116,845	117,936	116,431
Unrestricted net assets	259,654	227,135	220,893
Total net assets	$ 376,499	$ 345,071	$ 337,324

For 2012, the System's net assets increased approximately $31.4 million from 2011. Along with a strong operational performance in 2012, the increase in total net assets is reflective of significant fluctuations in the market for non-operating investments. The following components comprise the change in net assets:

Assets:

For 2012, the System's total assets increased approximately $34.9 million from 2011. The net increase is largely from an increase in current and limited use assets.

- Current assets increased in total by $14.3 million in 2012 due primarily to a $2.8 million increase in cash, $6.1 million increase in short term investments, $3.2 million increase in patient receivables, and $1.7 million increase in prepaid expenses as compared to 2011.
- Limited use assets increased $22.5 million due to good market performance as well as the addition of $1.5 million to the System's investment portfolio in 2012.
- Capital assets decreased $1.3 million in 2012.

Liabilities:

The System's total liabilities increased approximately $3.5 million for 2012 over 2011. The following components comprised the net increase in liabilities:

- Trade accounts payable decreased by $335 thousand.
- Estimated third-party liabilities increased $4.5 million in 2012 due to potential audit impact.
- Accrued salaries increased $120 thousand due to bonuses being paid out in November 2012.

For 2011, the System's net assets increased approximately $7.7 million from 2010. Along with a strong operational performance in 2011, the increase in total net assets is reflective of significant fluctuations in the market for non-operating investments. The following components comprise the change in net assets:

Assets:

For 2011, the System's total assets increased approximately $12.0 million from 2010. The net increase is largely from an increase in limited use assets.

- Current assets decreased in total by $14.2 million in 2011 due primarily to a $6.6 million decrease in cash, an $18 million decrease in short term investments and a $10 million increase in receivables as compared to 2010.
- Limited use assets increased $25.5 million due to the addition of $15 million to the investment portfolio as well as transferring $17.6 million in securities to funded depreciation.
- Capital assets increased $1.3 million in 2011 due to the acquisition of physician practices.

Liabilities:

The System's total liabilities increased approximately $4.3 million for 2011 over 2010. The following components comprised the net increase in liabilities:

- Accounts payable and other liabilities increased approximately $3.7 million in 2011.
- Trade accounts payable increased by $1.1 million due to increased volume from the physician practices.
- Estimated third-party liabilities increased $2.6 million in 2011 due to potential audit impact.
- Accrued salaries increased $1.3 million due to bonuses paid out in November 2011.

CAPITAL ASSET AND DEBT ADMINISTRATION:

Capital Assets:

At the end of 2012, the System had approximately $118.4 million invested in tangible and intangible capital assets, net of accumulated depreciation and amortization as detailed in Note 6 to the financial statements. The System invested approximately $18.2 million in equipment and building additions, building refurbishments, construction in progress and land improvements during 2012. During 2012, the System completed various renovations including Employee Pharmacy, Crossroads, Cardiac Intensive Care Unit, Data Center, and Materiel Management. The purchase of a replacement MRI at the hospital, computer servers, the Cerner SurgiNet system, CT simulator for Radiation Oncology, patient monitoring system and the acquisition of the Cardio, Thoracic and Vascular Surgeons were all completed in 2012. Various other additions, refurbishments, and renovations were completed during 2012 in order to expand and preserve the infrastructure needed to provide continued quality health care services.

At the end of 2011, the System had approximately $120.2 million invested in tangible and intangible capital assets, net of accumulated depreciation as detailed in Note 6 to the financial statements. The System invested approximately $20.4 million in equipment and building additions, building refurbishments, construction in progress and land improvements during 2011. During 2011, the System completed various renovations including Radiation Oncology, various nursing units, Clinical Education and Construction Management office. The purchase of the DaVinci robot, acquisition of New Bern Urology Center, acquisition of East Carolina Internal Medicine and the purchase of a new ambulance were all completed in 2011. Various other additions, refurbishments, and renovations were completed during 2011 in order to expand and preserve the infrastructure needed to provide continued quality health care services.

Notes Payable:

The Notes Payable activity consisted solely of principal and interest payments on revenue notes. There were no changes to the System's credit rating. The reader may refer to note 8 of the financial statements for a summary of note payable activity.

ECONOMIC FACTORS:

CarolinaEast Health System continues to adjust its operations for reductions in reimbursement. The reductions in both federal and state funding have a direct impact on the operations of the System given that Medicare and Medicaid comprise approximately 64% and 65% for years ended 2012 and 2011, respectively, of the combined inpatient and outpatient volume for services provided to patients. With federal regulations such as the Patient Protection and Affordable Care Act and the Health Information Technology for Economic and Clinical Health Act, the System must prepare itself for significant reimbursement changes in the future.

CarolinaEast Health System serves as an economic stimulus in the community. Given the uncertainties that currently characterize the state and local economy, it is expected that the System will be faced with absorbing more uninsured patients, and more uncompensated care. The System receives no local taxpayer support to assist with this care.

The health care industry continues to be a dynamic environment characterized by continual change. With the economic fluctuations seen in the past year, the health care industry has not been immune to its impact with decrease in patient volume. As the demand for new technology and quality services continues to grow, so too does the cost to provide such services. The costs for Health supplies and drugs continue to increase as well as technological and professional costs. The System is challenged more than ever to improve health care quality, safety and efficiency as reimbursement reductions for services provided continue to impact the industry.

NEXT YEAR'S BUDGET AND RATES:

Budgetary Highlights

During the current year, the operating budget was prepared for the upcoming fiscal year. Budgeted operating expenses increased approximately $9.70 million from the actual current fiscal year's expenses, with the majority of the increase coming from labor and benefit expenses as well as data processing fees. The System's net patient service revenue increased 4.07% for the new budget year when compared to the current fiscal year. An overall rate increase of 6.00% was approved by the Board for the System's charges for services. With this approved rate increase, the System's operating margin is budgeted at 3.00%.

CONTACT THE FINANCIAL MANAGER:

This financial report is designed to provide our customers and creditors with a general overview of the finances of CarolinaEast Health System to demonstrate the accountability for the monies received and for services provided. If you have any questions or concerns about this report or need additional information, contact:

Tammy Sherron, V.P. Finance
CarolinaEast Health System
2000 Neuse Boulevard
New Bern, N.C. 28561

CAROLINAEAST HEALTH SYSTEM

Balance Sheets - Proprietary Fund

September 30, 2012 and 2011

Assets	2012	2011
Current assets:		
Cash and cash equivalents	$ 15,480,515	$ 12,644,637
Assets limited as to use, current portion	840,999	840,998
Short-term investments	52,010,978	45,922,270
Patient accounts receivable, net	40,234,274	37,045,922
Other receivables	4,858,292	4,411,209
Inventories	6,714,857	6,751,213
Prepaid expenses	4,977,393	3,247,464
Total current assets	125,117,308	110,863,713
Assets limited as to use, net of current portion	186,179,926	163,691,878
Other assets:		
Intangible capital assets, net of amortization	5,710,358	6,228,782
Other noncurrent assets	268,285	268,285
Total other assets	5,978,643	6,497,067
Capital assets – tangible:		
Land and construction in progress	11,962,537	9,109,376
Buildings and fixtures	143,437,478	141,872,221
Equipment	155,439,774	146,378,293
Land improvements	3,963,433	3,887,578
	314,803,222	301,247,468
Less accumulated depreciation	(202,123,070)	(187,244,373)
Capital assets - tangible, net	112,680,152	114,003,095
Total assets	$ 429,956,029	$ 395,055,753

CAROLINAEAST HEALTH SYSTEM

Balance Sheets - Proprietary Fund, Continued

September 30, 2012 and 2011

Liabilities and Net Assets	2012	2011
Current liabilities:		
Current maturities of note payable	$ 727,741	$ 676,968
Current maturities of capital lease obligation	35,027	74,322
Trade accounts payable	8,869,043	9,204,078
Accrued salaries, wages, and withholdings	15,629,052	15,509,235
Accrued interest payable	103,816	150,358
Estimated third party payor settlements	27,309,656	22,825,199
Total current liabilities	52,674,335	48,440,160
Long-term liabilities:		
Note payable, less current maturities	782,322	1,510,063
Capital lease obligation, less current maturities	-	35,027
Total long-term liabilities	782,322	1,545,090
Total liabilities	53,456,657	49,985,250
Net Assets:		
Invested in capital assets, net of related debt	116,845,420	117,935,497
Unrestricted	259,653,952	227,135,006
Total net assets	376,499,372	345,070,503
Total liabilities and net assets	$ 429,956,029	$ 395,055,753

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

CAROLINAEAST HEALTH SYSTEM

Statements of Revenues, Expenses, and Changes in Net Assets - Proprietary Fund

For the Years Ended September 30, 2012 and 2011

	2012	2011
Operating revenues:		
Net patient service revenue	$ 284,167,754	$ 272,947,938
Other revenue	4,723,082	3,138,698
Total operating revenues	288,890,836	276,086,636
Operating expenses:		
Nursing and other professional services	203,665,069	191,186,465
General, administrative, and support services	56,681,939	54,989,391
Depreciation and amortization	19,982,159	19,620,004
Interest	-	15,125
Total operating expenses	280,329,167	265,810,985
Operating income	8,561,669	10,275,651
Non-operating revenues (expenses):		
Unrestricted contributions	76,080	90,564
Net investment income	3,710,684	5,016,014
Realized gains on investments	7,768,592	7,641,242
Unrealized gains (losses) on investments	13,159,692	(14,681,647)
Rental income	28,630	48,435
Other non-operating expenses	(1,876,478)	(643,860)
Non-operating revenues (expenses), net	22,867,200	(2,529,252)
Change in net assets	31,428,869	7,746,399
Total net assets, beginning	345,070,503	337,324,104
Total net assets, ending	$ 376,499,372	$ 345,070,503

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

CAROLINAEAST HEALTH SYSTEM

Statements of Cash Flows - Proprietary Fund

Years Ended September 30, 2012 and 2011

	2012	2011
Cash flows from operating activities:		
Cash received from and on behalf of patients	$ 273,994,861	$ 260,733,500
Cash payments to suppliers for services and goods	(115,278,846)	(108,543,705
Cash payments to employees for services	(145,047,144)	(135,010,001)
Interest paid on long-term debt	(122,032)	(183,088)
Other operating cash receipts	13,890,675	7,445,864
Net cash provided by operating activities	27,437,514	24,442,570
Cash flows from noncapital financing activities:		
Unrestricted gifts	76,080	90,564
Donations	(1,841,694)	(540,377)
Rental income	28,630	48,435
Net cash used by noncapital financing activities	(1,736,984)	(401,378)
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(18,188,918)	(20,430,065)
Proceeds from disposition of capital assets	13,343	46,134
Principal payments on capital lease obligations	(74,322)	(113,205)
Principal payments on revenue notes	(676,968)	(629,738)
Net cash used in capital and related financing activities	(18,926,865)	(21,126,874)
Cash flows from investing activities		
Purchase of investments, net	(5,343,893)	(13,025,409)
Income on investments	3,710,684	5,016,014
Net cash used by investing activities	(1,633,209)	(8,009,395)
Net increase (decrease) in cash and cash equivalents	5,140,456	(5,095,077)
Cash and cash equivalents		
Beginning of year	30,566,182	35,661,259
End of year	$ 35,706,638	$ 30,566,182

CAROLINAEAST HEALTH SYSTEM

Statements of Cash Flows - Proprietary Fund, Continued

Years Ended September 30, 2012 and 2011

	2012	2011
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$ 8,561,669	$ 10,275,651
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	19,463,735	19,101,580
Amortization	518,424	518,424
Change in:		
Patient accounts receivables	(3,188,352)	(7,914,010)
Other receivables	(447,083)	(2,040,130)
Inventories	36,353	73,437
Prepaid expenses	(1,729,929)	(611,869)
Accounts payable and accrued expenses	4,222,697	5,039,487
Net cash provided by operating activities	$ 27,437,514	$ 24,442,570
Reconciliation of cash and cash equivalents to the balance sheet:		
Unrestricted cash and cash equivalents	$ 15,480,485	$ 12,644,637
Cash and cash equivalents:		
Held by bond/note paying agent	841,020	841,010
By Board for capital improvements	19,385,133	17,080,535
	20,226,153	17,921,545
Cash and cash equivalents, including limited-use assets, at end of year	$ 35,706,638	$ 30,566,182
Noncash capital and related financing activities		
Losses on disposal of capital assets	$ 34,783	$ 1,978
Noncash investing activities		
Unrealized gains (losses) on investments	$ 13,159,692	$ (14,681,647)
Realized gains on investments	$ 7,768,592	$ 7,641,242

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

CAROLINAEAST HEALTH SYSTEM

Statements of Fiduciary Net Assets - Fiduciary Funds

Year Ended December 31, 2011

Assets:	CarolinaEast Medical Center Money Purchase Pension Plan	CarolinaEast Medical Center Employee Benefit Trust
Investments	$ 56,580,345	$ 5,018,864
Contributions receivable	-	247,699
Net Assets Held in Trust for Fiduciary Plans	$ 56,580,345	$ 5,266,563

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

CAROLINAEAST HEALTH SYSTEM

Statements of Changes in Fiduciary Net Assets - Fiduciary Funds

Year Ended December 31, 2011

	CarolinaEast Medical Center Money Purchase Pension Plan	CarolinaEast Medical Center Employee Benefit Trust
Additions:		
Contributions	$ 4,550,840	$ 628,337
Investment income:		
Net appreciation in fair value of investments	-	136,209
Dividends and interest	1,067,317	124,853
Total additions	5,618,157	889,399
Deductions:		
Net depreciation in fair value of investments	1,377,200	-
Distributions to participants	2,958,919	328,967
Administrative expenses	200,697	62,368
Total deductions	4,536,816	391,335
Increase in net assets	1,081,341	498,064
Net assets held in trust for fiduciary plans		
Beginning of year	55,499,004	4,768,499
End of year	$ 56,580,345	$ 5,266,563

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

1. **Summary of Significant Accounting Policies**

Reporting Entity and Nature of Operations – The operations of CarolinaEast Health System ("System") consist primarily of providing health care services to patients in eastern North Carolina. Based on the financial accountability criteria established by the Governmental Accounting Standards Board, the System is considered to be a component unit of the Craven County ("County") reporting entity, and is included as a discretely presented component unit in the basic financial statements of Craven County, North Carolina. The Board of Commissioners of Craven County, North Carolina established the System to provide Health services to County residents. The Commissioners appoint the System's governing board and can remove System board members for cause as stated under North Carolina General Statutes Section 131 E-22. The System must also receive approval from the County Commissioners before issuing revenue bonds. The System was established under North Carolina General Statutes Section 131 E "Hospital Authorities Act". The System is financially accountable for CarolinaEast Medical Center, Inc., and CarolinaEast Physicians, Inc. Both are tax exempt under Internal Revenue Code section 501 (c)(3). Both organizations are considered a blended component unit of the System.

Basis of Presentation – The accompanying financial statements have been prepared in accordance with the principles contained in the Audit and Accounting Guide for Health Care Entities published by the American Institute of Certified Public Accountants ("AICPA") and all applicable governmental accounting standards. These statements present information about the System and include the financial activities of the overall entity, except for fiduciary activities. The statement of fiduciary net assets and statement of changes in fiduciary net assets present information about CarolinaEast Medical Center Money Purchase Pension Plan (see Note 10) and CarolinaEast Medical Center Employee Benefit Trust (see Note 11). The fiduciary fund information is included due to the System's fiduciary responsibility for the pension trust and employee benefit trust.

Basis of Accounting – The System utilizes the basis of accounting utilized by business activities and proprietary funds whereby revenue and expenses are recognized on the economic resources measurement focus and the accrual basis of accounting. As permitted by accounting principles generally accepted in the United States of America, the System has elected to apply only applicable FASB Statements and Interpretations issued before November 30, 1989 in accordance with Governmental Accounting Standards Board Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting.

The fiduciary funds separate, stand-alone financial statements are prepared in accordance with the Standards of the Governmental Accounting Standards Board for pension and other post employment benefit trust funds. The financial statements are prepared using the accrual basis of accounting. Employer contributions are recognized in accordance with each plan's funding policy. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

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 and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents – For the purpose of reporting cash flows, the System considers all short-term investments having a maturity at the date of purchase of three months or less to be cash equivalents. Throughout the year the System has bank balances which exceed federal depository limits.

Investments in Debt and Equity Securities – The System has investments in debt and marketable equity securities which are carried at fair value. Fair value of investments other than those of the North Carolina Capital Management Trust ("NCCMT") and the First American Prime Obligation Fund are determined by quoted market prices. Amounts in the NCCMT (an SEC registered 2a-7 money market fund) and the First American Prime Obligation Fund are valued at the fair values as determined by the share prices. Debt securities consist primarily of obligations of the U.S. government, commercial paper and corporate bonds. Marketable equity securities consist primarily of common stocks that are traded or listed on national exchanges. Gains and losses on debt and marketable equity securities, both realized and unrealized, are included in nonoperating revenues. Interest and dividends on investments in debt and equity securities are included in nonoperating revenues when earned.

Short-term Investments – Short-term investments include marketable securities representing the investment of cash available for current operations. They are not considered cash equivalents since the System considers them part of their investing activities.

Valuation of Investments in Fiduciary Funds – The Plan's investments are stated at fair value. Shares of registered investment companies (mutual funds) are reported at fair value based on the quoted market price of the fund which represents the net asset value of the shares held by the fund at year end. Shares held in common collective trust funds are reported at fair value based on the unit prices quoted by the fund, representing fair value of the underlying investments. Participant notes receivable are valued at cost which approximates fair value. Purchases and sales of securities are recorded on a trade date basis.

Patient Accounts Receivable – The System records receivables at billed amounts and provides for estimated unbilled amounts at fiscal year end. Management provides an estimate for potentially uncollectible accounts on a monthly basis based on a review of outstanding receivables, historical payment patterns and their knowledge of other specific factors effecting the collection of accounts.

Inventories – Inventories are valued at the lower of cost (first-in, first-out basis) or market.

Assets Whose Use is Limited – Noncurrent cash and investments are designated or restricted for long-term purposes. Designated assets include assets set aside by the Board for future capital improvements over which the Board retains control. Restricted assets include assets held by a trustee under note indenture agreements. The current portion of these assets represents the amounts which are required to be utilized for debt service during the next fiscal year and are being held by the note trustee.

Intangible Capital Assets – Intangible capital assets consist of goodwill associated with cost in excess of fair value of the net assets of entities acquired in purchase transactions. Goodwill is being amortized on a straight-line basis over five to thirty years. Estimated future amortization expense of intangible assets is as follows:

2013	$ 518,424
2014	518,424
2015	518,424
2016	518,424
2017	518,424
Thereafter	3,118,238
	$ 5,710,358

Tangible Capital Assets – Tangible capital assets are recorded at cost or at fair value at the date of donation, if donated. The System's policy is to generally capitalize assets with a cost of $1,000 or greater. The System provides for depreciation using the straight-line method for both financial reporting and cost reimbursement purposes over the estimated useful lives of the depreciable properties. The range of estimated useful lives of major categories of property and equipment are as follows:

Land improvements	5 - 25 years
Building and improvements	15 - 40 years
Equipment	3 - 20 years

The System evaluates prominent events or changes in circumstances affecting capital assets to determine whether impairment of a capital asset has occurred. A capital asset is generally considered impaired if both (a) the decline in service utility of a capital asset is large in magnitude and (b) the event or change in circumstance is outside the normal lifecycle of the capital asset. Impaired capital assets that will no longer be used by the System are reported at the lower of carrying value or fair value. Impairment losses on capital assets that will continue to be used by the government are measured using the method that best reflects the diminished service utility of the capital asset. Any insurance recoveries received as a result of impairment events or changes in circumstance resulting in the impairment of a capital asset are netted against the impairment loss.

Self-Insurance – The System acts as a partial self-insurer for health insurance programs. Estimated claims are accrued as incurred.

Net Assets – Net assets classifications are defined as follows, as applicable:

- Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including any restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
- Restricted – This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- Unrestricted net assets – This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt", above.

Operating Income – The System distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from the primary purpose of the System, which is to provide medical services to the region. Operating revenues consist of net patient services and other miscellaneous services. Operating expenses consist of salaries and benefits, medical supplies, depreciation of capital assets, interest expense, and other overhead costs. All revenues and expenses not meeting these criteria are considered non-operating.

Net Patient Service Revenue – Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others and includes estimated retroactive adjustments under reimbursement agreements with third-party payers. Estimated retroactive adjustments are accrued in the period the related services are rendered and adjusted in future periods, as final settlements are determined. It is possible that the amounts of final settlements could be materially different than those presented herein. Bad debts approximated $27,400,000 and $23,200,000 in 2012 and 2011, respectively.

Charity Care – The System provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The System, maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy, the estimated cost of those services and supplies, and equivalent service statistics. Amounts of charity care provided based on the cost to provide was approximately $4,200,000 and $4,000,000 for the years ended September 30, 2012 and 2011, respectively. The estimated costs of providing charity services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing charity to patients. The ratio of cost to charges is calculated based on the System's total expenses divided by gross patient service revenue.

Sales and Income Taxes – The System is a governmental unit exempt from income tax and CarolinaEast Health System, Inc. is exempt from income tax under Section 501 (c)(3) of the Internal Revenue Code. In addition, the System receives reimbursement from the State of North Carolina for sales taxes paid during the year. The accompanying financial statements do not reflect a provision or liability for federal and state income taxes. The System determined that they do not have any material unrecognized tax benefits or obligations as of September 30, 2012. The System believes they are no longer subject to income tax examinations for years prior to September 30, 2009.

Pension Plan – The System maintains a noncontributory primary retirement plan covering all permanent, full-time employees who have completed four consecutive full-time years of service. Employer contributions are based on a fixed percentage of base earnings for each employee and are recognized as the base earnings are recognized.

Other Postemployment Benefits ("OPEB") – The System sponsors and has fiduciary responsibility for CarolinaEast Medical Center Employee BenefitTrust, a single-employer, defined benefit OPEB. The plan covers retirees of CarolinaEast Medical Center who have at least 20 years of continuous full-time service, have attained the age of 55, and were employed prior to July 1, 1995. Employer contributions are based on actuarial calculations.

Subsequent Events – The System evaluated the effect subsequent events would have on the proprietary fund financial statements through January 29, 2013, which is the date the proprietary fund financial statements were available to be issued.

2. Net Patient Service Revenue

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

Medicare – Inpatient acute care, outpatient, psychiatric and rehabilitative services rendered to Medicare program beneficiaries are reimbursed at prospectively determined rates. The System is reimbursed at interim rates for cost reimbursable items with final settlement determined after submission of the annual cost reports and audits of these reports by the Medicare fiscal

intermediary. The difference between established billing rates and reimbursements are recorded as contractual adjustments to patient service revenue. The System's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization under contract with the fiscal intermediary. The System's Medicare services represent approximately 55% of total patient service revenue for the years ended September 30, 2012 and 2011, respectively. The System's Medicare cost reports have been audited by the Medicare fiscal intermediary through September 30, 2006. The 2007 and 2008 audits are in process. Any differences between the estimated cost report settlement amount recorded in the financial statements on an accrual basis and the amounts determined by the administrative agencies of the programs and subsequent revisions in estimated settlements are included in operations in the year in which the amount is determined.

Physician services are reimbursed based upon a physician fee schedule that is updated each January. The difference between established billing rates and reimbursements are considered contractual adjustments and are recorded separately from acute care adjustments.

Medicaid – Acute inpatient services rendered to patients are reimbursed at a prospectively determined rate per discharge. Inpatient psychiatric and rehabilitative services are reimbursed at a prospectively determined rate per patient day. Services to outpatients are reimbursed at a percentage of cost as defined in the Medicaid regulations, currently 80%. The System is reimbursed for Medicaid outpatient services at tentative rates with final settlement determined after submission of annual cost reports and audits thereof by the Medicaid fiscal intermediary. Medicaid services represent approximately 9% of total patient service revenue for the years ended September 30, 2012 and 2011, respectively. The System's Medicaid cost reports have been audited through September 30, 2008. Any differences between the estimated cost report settlement amount recorded in the financial statements on an accrual basis and the amounts determined by the administrative agencies of the programs and subsequent revisions in estimated settlements are included in operations in the year in which the amount is determined.

The System has received supplemental payments from the State of North Carolina under the State Medicaid plan. These payments are subject to adjustment and settlement based upon audited cost reports and the specifics of the State Medicaid plan, which provides for the possibility of settlements of any overpayments by Medicaid on an aggregate basis by participating hospitals. Any differences between the estimated settlement amount recorded in the financial statements on an accrual basis and the amounts determined by the State of North Carolina and subsequent revisions in estimated settlements are included in operations in the year in which the amount is determined. The System received $9,228,248 in supplemental payments for fiscal year ended September 30, 2012. Estimated third-party liabilities related to supplemental payments received by the System during fiscal years 2004 through 2012 were $16,588,542 and $13,410,529 at September 30, 2012 and 2011, respectively, and remain open to settlement. Estimated third-party liabilities is based on information received during fiscal year 2012 from the North Carolina Department of Medical Assistance and estimates from management concerning potential overpayments of Medicaid supplemental funds to participating hospitals during fiscal years 2004 through 2012. The Supplemental payments in years prior to 2004 have been settled.

In April 2012, the Center for Medicare and Medicaid Services approved a North Carolina Medicaid assessment plan to reduce the gap between Medicaid and uninsured costs and payments ("GAP Plan") retroactive to January 1, 2011. Under the GAP Plan, providers periodically pay an assessment to the State and periodically receive Medicaid payments from the State. In 2012, the State collected assessments and made payments for the three quarters ended September 30, 2011 and the four quarters ended September 30, 2012. During 2012, the System paid assessments of $4,199,169, which were recorded as operating expense, and received payments of $6,034,812, which were recorded as net patient revenue.

Laws and regulations governing the Medicare and Medicaid programs are extremely 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. The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Net patient service revenue increased approximately $513,000 and $296,000 for 2012 and 2011, respectively due to allowances previously estimated that are no longer necessary as a result of final settlements and years that are no longer subject to audits, reviews, and investigations.

Contractual adjustments totaled approximately $380,811,000 and $335,978,000 for the years ended September 30, 2012 and 2011, respectively.

Recovery Audit Contractors Program – In 2005, Centers for Medicare and Medicaid Services (CMS) announced a new demonstration project using recovery audit contractors (RACs) as part of CMS' further efforts to assure accurate payments. The project uses the RACs to search for potentially improper Medicare payments that may have been made to healthcare providers and that were not detected through existing CMS program integrity efforts. Once a RAC identifies a claim it believes improper, it makes a deduction from the provider's Medicare reimbursement in an amount estimated to equal the overpayment. The project completed operating under a pilot basis in multiple states in 2008. Section 302 of the Tax Relief and Health Care Act of 2006 makes the RAC program permanent in all 50 states by no later than 2010. The System has reserves of approximately $3,900,000 related to the RAC program included in estimated third party payor settlements at September 30, 2012 and 2011, respectively.

3. Cash and Cash Equivalents, Deposits, and Investments

Deposits - The deposits of the System are governed by North Carolina General Statutes. The System may establish official depositories with any bank or savings and loan whose principal office is located in North Carolina. The System may also establish time deposits in the form of NOW accounts, SuperNOW and money market accounts, and certificates of deposit. The System's policy and practice is for its depository relationships to conform to state law.

Generally, deposits of governmental units are either insured or collateralized by using one of two methods. Under the dedicated method, all deposits exceeding the federal depository insurance coverage level are collateralized with securities held by the unit's agents in the

System's name. Under the pooling method, a collateral pool, all uninsured deposits are collateralized with securities held by the State Treasurer's agent in the name of the State Treasurer. Since the State Treasurer is acting in a fiduciary capacity for the unit, these deposits are considered to be held by its agents in the unit's name. The amount of the pledged collateral is based on an approved averaging method for non-interest bearing deposits and the actual current balance for interest bearing deposits. Depositories using the pooling method report to the State Treasurer the adequacy of their pooled collateral covering uninsured deposits.

The State Treasurer does not confirm this information with the unit or the escrow agent. Because of the inability to measure the exact amount of collateral pledged for the units under the pooling method, the potential exists for under collateralization, and this risk may increase in periods of high cash flows. However, the State Treasurer of North Carolina enforces strict standards of financial stability for each depository that collateralizes public deposits under the pooling method.

All of the System's deposits are maintained with financial institutions which collateralize excess deposits by the pooling method; responsibility for sufficient collateralization of these excess deposits rests with the banks that have chosen the pooling method. The North Carolina State Treasurer monitors the pooling method for adequate collateralization. At September 30, 2012, the System's deposits had a carrying amount of $13,577,942 and a bank balance of $23,937,954. Of the bank balance, $500,000 was covered by federal depository insurance; $23,437,954 was covered by collateral held by the pooling method.

Cash and cash equivalents consist of the following at September 30:

	2012	2011
Cash on hand	$ 8,280	$ 7,280
Deposits	13,577,942	10,963,327
Mutual fund money markets	1,894,293	1,674,030
	$ 15,480,515	$ 12,644,637

Investments - North Carolina General Statutes (Local Government Budget and Fiscal Control Act and Hospital Authorities Act) authorize the System to invest in obligations of the U.S. Treasury; obligations of any agency of the United States of America, provided the payment of principal and interest of such obligations is fully guaranteed by the United States; certain quasi-federal agencies; obligations of the State of North Carolina or any subdivision thereof; commercial paper bearing the highest credit ratings available; bankers acceptances of accepting banks or holding companies either (i) incorporated in the State of North Carolina or (ii) bearing the highest available long term debt rating; the NCCMT; and in other property or securities in which trustees, guardians, executors, administrators, and others acting in a fiduciary capacity may legally invest funds under their control.

The System employs a blend of management styles to diversify its portfolio, reduce overall risk and create a superior opportunity for positive returns. Such approaches are intended to ensure the System has adequate reserves to hedge against unanticipated events, and allow the System to accomplish its short-term and long-term capital plan as well as to earn an acceptable return on available funds through a total return concept of managed assets, thereby supplementing capital and operational expenses.

By Policy, the System's investment portfolio should be comprised of approximately 35% fixed income, 43% equity and 20% alternative assets and 2% cash with fixed income and equity tolerable variability of +/- 2.5%. Alternative assets may vary from target by a low of 1.5% and a high of 5%

As of September 30, 2012 the System had the following investments and maturities. (Amounts are in thousands.)

Investment Type	Fair Value	< Than 1 Year	1 - 5 Years	6 - 10 Years	11 - 20 Years	> Than 20 Years
US Government Treasury Notes	$ 17,581	$ 10,604	$ 2,956	$ 4,021	$ -	$ -
US Government Agencies	16,828	180	4,207	5,465	6,870	106
Corporate Bonds	37,968	405	27,568	6,309	365	3,321
Templeton Global Bond Fund	5,938	N/A	5,938	N/A	N/A	N/A
Equity Securities	103,994	N/A	N/A	N/A	N/A	N/A
Hedge Funds	36,496	N/A	N/A	N/A	N/A	N/A
Short Term Cash Equivalents	7,322	N/A	N/A	N/A	N/A	N/A
NC Capital Management Trust	13,958	N/A	N/A	N/A	N/A	N/A
NC Capital Management Trust - Bank of New York Trustee	841	N/A	N/A	N/A	N/A	N/A
Total	$ 240,926	$ 11,189	$ 40,669	$ 15,795	$ 7,235	$ 3,427

The above table includes $1,894,293 of a mutual fund money market account which is included in unrestricted cash and cash equivalents.

Interest Rate Risk: As a means of limiting its exposure to fair value losses, the System investment policy dictates that mortgage backed securities or other asset backed securities will never comprise more than 30% of the fixed income portfolio and corporate debt securities will never comprise more than 50% of the fixed income portfolio. Additionally, the policy provides that the maximum maturity of any non-mortgage backed fixed income instrument will not exceed 10 years without the approval of The System's Board and investment managers should not exceed a 7-year expected weighted average maturity for investments in mortgage backed paper and government agencies including Ginnie Maes, Freddie Macs or Fannie Maes. The maturities in the Templeton Global Bond Fund have an average duration of approximately 2.8 years as shown in the preceding schedule.

Credit Risk: The System's investment policy requires corporate obligations to meet the commercial paper rating of A1 by Moody's or P1 by S&P and bond rating in the "BBB" category or better by S&P, Moody's, and Fitch. "BBB" securities will be limited to 10% of the fixed income portfolio. No single "BBB" issue will be greater than $500,000 face value at purchase. Obligations of the U.S. Government or explicitly guaranteed by the U.S. Government are generally not considered to have credit risk. The Templeton Global Bond Fund is unrated.

As of September 30, 2012, the total quality ratings for the above debt holdings were as follows:

Holdings	AAA	AA	A	BBB	BB	B	Total
US Government Agencies	100.00%						100.00%
Corporate Bonds	15.29%	14.48%	58.48%	11.75%			100.00%
Short Term Cash Equivalents	100.00%						100.00%
NC Capital Management Trust	100.00%						100.00%
NC Capital Management Trust - Bank of New York Trustee	100.00%						100.00%

Concentration of Credit Risk: The System's investment policy states individual cumulative debt instruments by anyone issuer shall be confined to a maximum of 5% of the fixed income portfolio. There is no concentration of credit risk.

Equity Investment Guidelines: Each equity holding will be limited to 6% of the equity portfolio determined at the time of investment.

Permissible types of equity investments include equities of U.S. and foreign companies listed on the NYSE, ASE and NASDAQ traded OTC securities to include common and preferred and convertible preferred stocks. Equity investments may also include publicly traded mutual funds, unit trusts and other common investment funds comprised of commingled securities listed on the NYSE, ASE and NASDAQ traded OTC securities.

Alternative Assets: A fund of funds hedge fund is employed to offer diversification as an investment alternative with low correlation to fixed income and equity securities. A fund of funds performance is measured against the performance of an appropriate hedge fund index.

Other Investment Guidelines: The primary portfolio shall contain no derivatives to enhance the overall yield of the stock or bond portfolio. The Alternative Asset class may use derivatives. Investment managers must maintain compliance with State of North Carolina laws and regulations, and all other applicable laws, rules and regulations.

As of December 31, 2011, CarolinaEast Medical Center Money Purchase Pension Plan held investments in a common collective trust totaling $14,904,536, cash and a money market account totaling $20,051, registered investment companies totaling $40,080,288 and participant loans totaling $1,575,470. The Plan is subject to State Statutes governing investments of pension plans, which generally provides for any type of investment subject to the "prudent man rule".

As of December 31, 2011, CarolinaEast Medical Center Employee Benefit Trust held investments in registered investment companies and a money market fund totaling $5,018,864. The Plan is subject to State Statutes governing investments of pension plans, which generally provides for any type of investment subject to the "prudent man rule".

The Plans have no formal policies associated with interest rate risk, credit risk, custodial credit risk or the concentration of credit risk. The interest rate risk and credit risk associated with bond mutual funds is not significant to the financial statements.

Due to the level of risks associated with investment securities, it is at least reasonably possible that changes in the value of investment securities will occur in the near future and such changes could materially affect the amounts reported in these financial statements.

4. Receivables

Receivables consist of the following at September 30:

	2012	2011
Gross patient accounts receivables	$ 54,939,361	$ 50,356,935
Less allowance for doubtful accounts	(14,705,087)	(13,311,013)
Total patient accounts receivable	$ 40,234,274	$ 37,045,922
Refundable North Carolina sales tax	$ 1,971,103	$ 2,019,801
Other receivables	2,887,189	2,391,408
Total other receivables	$ 4,858,292	$ 4,411,209

5. Assets Limited as to Use

The Board has designated funds for replacement of buildings and equipment.

Payments made in conjunction with the System's debt service under a revenue note order are held by a trustee until disbursed for payment of principal and interest to note holders (see Note 8).

The composition of assets limited as to use at September 30 is as follows:

	2012	2011
Internally designated for capital improvements	$ 185,889,146	$ 163,344,608
Under indenture agreements, held by trustee		
Interest fund	113,258	164,030
Principal fund	727,762	676,980
Total investments held by trustee	841,020	841,010
Accrued interest receivable	290,759	347,258
Total	187,020,925	164,532,876
Less amounts that are required for current liabilities	840,999	840,998
Assets limited as to use	$ 186,179,926	$ 163,691,878

6. Capital Asset Activity

Capital asset activity for the year ended September 30 was as follows:

	Year Ended September 30, 2012			
	Beginning Balance	Increases	Decreases	Ending Balance
Intangible Capital Assets				
Intangible assets	$ 15,727,713	$ -	$ -	$ 15,727,713
Less accumulated depreciation/amortization for Intangible assets	(9,498,931)	(518,424)	-	(10,017,355)
Total intangible capital assets being amortized, net	$ 6,228,782	$ (518,424)	$ -	$ 5,710,358
Tangible Capital Assets				
Capital assets, not being depreciated:				
Land	$ 6,779,352	$ 475,548	$ -	$ 7,254,900
Construction in progress	2,330,024	10,470,364	(8,092,751)	4,707,637
Total capital assets, not being depreciated	9,109,376	10,945,912	(8,092,751)	11,962,537
Capital assets, being depreciated:				
Building and fixtures	141,872,221	1,565,257	-	143,437,478
Equipment	146,378,293	13,694,646	(4,633,165)	155,439,774
Land improvements	3,887,578	75,855	-	3,963,433
Total capital assets being depreciated	292,138,092	15,335,758	(4,633,165)	302,840,685
Less accumulated depreciation for:				
Land improvements, buildings and fixtures, and equipment	(187,244,373)	(19,463,735)	4,585,038	(202,123,070)
Total tangible capital assets being depreciated, net	104,893,719	(4,127,977)	(48,127)	100,717,615
Total tangible capital assets	114,003,095	6,817,935	(8,140,878)	112,680,152
Total capital assets, net	$ 120,231,877	$ 6,299,511	$ (8,140,878)	$ 118,390,510

	Year Ended September 30, 2011			
	Beginning Balance	Increases	Decreases	Ending Balance
Intangible Capital Assets				
Intangible assets	$ 15,727,713	$ -	$ -	$ 15,727,713
Less accumulated depreciation/amortization for Intangible assets	(8,980,507)	(518,424)	-	(9,498,931)
Total intangible capital assets being amortized, net	$ 6,747,206	$ (518,424)	$ -	$ 6,228,782
Tangible Capital Assets				
Capital assets, not being depreciated:				
Land	$ 4,438,331	$ 2,341,021	$ -	$ 6,779,352
Construction in progress	5,401,255	3,801,809	(6,873,040)	2,330,024
Total capital assets, not being depreciated	9,839,586	6,142,830	(6,873,040)	9,109,376
Capital assets, being depreciated:				
Building and fixtures	132,619,295	9,371,102	(118,176)	141,872,221
Equipment	144,868,359	11,668,377	(10,158,443)	146,378,293
Land improvements	3,766,782	120,796	-	3,887,578
Total capital assets being depreciated	281,254,436	21,160,275	(10,276,619)	292,138,092
Less accumulated depreciation for:				
Land improvements, buildings and fixtures, and equipment	(178,371,299)	(19,101,580)	10,228,506	(187,244,373)
Total tangible capital assets being depreciated, net	102,883,137	2,058,695	(48,113)	104,893,719
Total tangible capital assets	112,722,723	8,201,525	(6,921,153)	114,003,095
Total capital assets, net	$ 119,469,929	$ 7,683,101	$ (6,921,153)	$ 120,231,877

All depreciation is directly or indirectly in relation to the provision of health care services. Depreciation expense was approximately $19,464,000 and $19,102,000 for the year ended September 30, 2012 and 2011, respectively. The System has various renovation projects in progress at September 30, 2012. The estimated cost to complete these projects is approximately $7,500,000.

Interest expense capitalized was $117,486 and $167,963 for the years ended September 30, 2012 and 2011, respectively.

Legal title to the System's property and equipment, except equipment purchased by the System from unrestricted funds, is held by Craven County. The facilities are leased to the System, under a lease agreement which expires in 2024, for an annual rental of one dollar. In the event of dissolution of the System or its failure to function as a hospital and to operate as required in the lease, all of its monies, properties and assets shall revert to Craven County.

Net assets invested in capital assets, net of related debt, as of September 30 are as follows:

	2012	2011
Capital assets, as above	$ 118,390,510	$ 120,231,877
Capital related debt (Note 8)	1,545,090	2,296,380
	$ 116,845,420	$ 117,935,497

7. Accrued Salaries, Wages, and Withholdings

Accrued salaries, wages, and employee withholdings consist of the following at September 30:

	2012	2011
Salaries and wages	$ 8,219,322	$ 8,443,861
Vacation pay	5,173,635	4,923,151
Employee withholdings and related accruals	2,236,095	2,142,223
	$ 15,629,052	$ 15,509,235

8. Note Payable

The Series 1993 revenue notes are limited obligations of the System and are collateralized by the net revenue of the System. Interest on the revenue notes is payable annually on November 1, through November 1, 2013.

Note payable activity for the year ended September 30, 2012 was as follows:

	Year Ended September 30, 2012				
	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Revenue notes	$ 2,187,031	$ -	$ (676,968)	$ 1,510,063	$ 727,741

Note principal outstanding at September 30 is as follows:

	2012	2011
Series 1993 Health Care Facilities revenue notes:		
7.50% interest payable annually on November 1, maturing through November 1, 2013	$ 1,510,063	$ 2,187,031
Current portion	(727,741)	(676,968)
Total revenue notes payable, long-term	$ 782,322	$ 1,510,063

Scheduled payments of note principal and interest are as follows:

Fiscal Year	Principal	Interest	Total Debt Service
2013	$ 727,741	$ 113,255	$ 840,996
2014	782,322	58,674	840,996
Total note and interest payable	$ 1,510,063	$ 171,929	$ 1,681,992

9. Other Revenue

Other revenue consists of the following for the year ended September 30:

	2012	2011
Cafeteria and snack shop sales	$ 1,505,662	$ 1,362,789
Other services and vendor rebates	1,015,276	505,816
Other	2,202,144	1,270,093
	$ 4,723,082	$ 3,138,698

Meaningful Use of Electronic Health Records (EHR) - The System recognizes revenues for incentives earned under the Medicare program in the period in which it is reasonably assured that it will comply with the applicable EHR meaningful use requirements and payment has been received. Incentive payments received under the Medicare program include a discharge-related portion, which is calculated by Centers for Medicare & Medicaid Services based on the System's most recently filed cost report. Such amounts are subject to adjustment at the time of settling the 12-month cost report for the System's fiscal year that begins after the beginning of the payment year. The System achieved compliance with the Year 1 meaningful use requirements under the Medicare program during 2012 and, accordingly, recognized other operating revenues of approximately $678,000 in the statements of revenues, expenses and changes in net assets for the year ended September, 2012. The payments are included within the "Other" category from the chart above.

10. Retirement Plans

The System provides pension benefits for all of its qualifying employees through three defined contribution pension plans.

CarolinaEast Medical Center Plan Description ("Primary Plan"): The System sponsors and has fiduciary responsibility for CarolinaEast Medical Center Money Purchase Pension Plan, a noncontributory defined contribution plan covering all employees of CarolinaEast Health System who meet the eligibility requirements. An employee is eligible to participate in the plan following four consecutive full-time Years of Service with the System. Full-time employees are those that customarily work at least 36 hours per week. Employer contributions are based on a fixed percentage of base earnings for each employee. The benefit to the employee under the plan is the System's contribution plus investment earnings. Employees are fully vested after 10 years of continuous employment.

The Plan issues a separate, stand-alone financial report which can be obtained by contacting Tammy Sherron, V.P. of Finance, 2000 Neuse Boulevard, New Bern, N.C. 28561. The Plan was created by act of the Trustees of CarolinaEast Medical Center, who have the ability to amend or terminate the Plan.

Funding Policy: The Systems' contributions were calculated using a covered payroll amount of $48,857,914 for the year ended September 30, 2012. Total contributions were $4,885,791 for the year ended September 30, 2012, which represents 10 percent of covered payroll.

Significant Accounting Policies of the Plan: The Plan prepares its financial statements on the accrual basis of accounting. Employer contributions are recognized when due and receivable. Distributions to participants are recognized when due and payable in accordance with the terms of the Plan. Investments are valued at fair value based on quoted market prices.

The Plan does not have formal policies regarding interest rate, credit, custodial credit or concentration of credit risks.

CarolinaEast Health System TSA Plans ("Supplementary Plan"): The System maintains supplementary retirement plans under IRS Code Sections 403(b) and 457(b) which are administered by the Lincoln National Life Insurance Company and The Variable Annuity Life Insurance Company (VALIC). The 403(b) plan is a contributory plan with the System matching a fixed percentage of base earnings for each eligible employee. To receive an employer contribution, eligible employees must contribute a minimum of 3 percent of their eligible salary, and have completed 1 year of continuous service. Contributions by eligible employees are matched by the System at a rate of 2% of the employee's eligible salary. Employees contributing a portion of their eligible salary to the 457(b) plan do not receive a matching employer contribution. All employees are eligible to participate in both plans at the date of hiring. The employee contributions are made on a tax-deferred basis. The benefit to the employee under each plan is the amount contributed plus investment earnings. Employees are fully vested after one year of continuous employment.

The System's 403(b) contributions were calculated using a covered payroll amount of $59,324,308 and $48,185,360 for the years ended September 30, 2012 and 2011, respectively. The System's contributions were $1,186,486 and $963,707, or 2 percent of covered payroll for the year ended September 30, 2012 and 2011, respectively. Employee contributions to the plan totaled $5,404,347 and $4,981,984 or 9.11% and 10.34% of covered payroll for the year ended September 30, 2012 and 2011, respectively. Employee contributions to the 457(b) plan totaled $881,387 and $864,255 for the years ended September 30, 2012 and 2011, respectively.

These plans are not included in the System's reporting entity and do not issue separate, stand-alone financial reports.

11. Other Postemployment Benefits

Plan Description: The System sponsors and has fiduciary responsibility for CarolinaEast Medical Center Employee Benefit Trust, a single-employer, defined benefit OPEB plan established and governed by the System's governing board. A trust was established on April 1, 2007 for this plan and the plan has a plan year of January 1 to December 31. As such, the Plan's first fiscal year end was December 31, 2007. The System provides other postemployment benefits (OPEB) comprised of health care and group life insurance benefits to retirees of CarolinaEast Medical Center who have at least 20 years of continuous full-time service, have attained the age of 55 and were employed prior to July 1, 1995. The System pays the full cost of coverage for these benefits until age 65. Also, retirees can purchase coverage for their spouse at the System's group rates. The System elected to discontinue the post-retirement benefit to individuals employed on or after July 1, 1995. The plan issues a stand-alone financial report. That report can be obtained by contacting Tammy Sherron, V.P. of Finance, 2000 Neuse Boulevard, New Bern, N.C. 28561.

As of the actuarial valuation report dated January 1, 2012 the System's membership consisted of:

Retirees eligible for benefits	50
Active plan members	230
Total	280

Funding Policy: Prior to April 1, 2007, the System funded these obligations on a pay-as-you-go basis. During 2007, the System funded the actuarially determined net OPEB obligation which was accrued at September 30, 2006 and made some interim pay-as-you-go benefit payments until the trust was funded and thereafter the annual required contributions determined in actuarial valuations.

Annual OPEB Cost and Net OPEB Obligation: The System's OPEB cost (expense) for the fiscal year ended September 30, 2011 was calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. Prior to 2009, the System used one year in their determination, however due to significant losses in plan assets during the plan year end December 31, 2008, the System revised the amortization period to 5 years. The most recent actuarial valuation is dated January 1, 2012.

The System's annual OPEB cost components, the percentage of annual OPEB cost contributed to the trust, and its net OPEB obligation for the years ended September 30, 2012, 2011 and 2010 were as follows:

Fiscal Year Ended	Annual OPEB Cost (APC)	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
09/30/2010	$ 514,055	100.00%	$0
09/30/2011	$ 497,939	95.00%	$0
09/30/2012	$ 628,337	100.00%	$0

Summary of Significant Accounting Policies: The plan's financial statements are prepared using the accrual basis of accounting. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

Funded Status and Funding Progress: The plan was fully funded on April 1, 2007, the date the trust was established.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether actuarial value of the plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions. Projections of benefits for financial reporting purposes are based on the substantive plan (the plan understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

Methods and assumptions as of the latest actuarial valuations follow.

Valuation date	January 1, 2012
Actuarial cost method	Projected unit credit
Amortization method	Level dollar
Remaining amortization period	4 years
Asset valuation method	Market value
Actuarial assumptions:	
Investment rate of return	7.0%
Health care cost trend rates	9.0% down to 5.0%
Includes inflation at	3.0%
Cost-of-living adjustments	None

12. Risk Management, Commitments and Contingencies

The System is exposed to various risks of loss related to torts, theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health benefits.

Health Benefits: Effective January 1, 2001, the System established a limited risk, self-insurance program to provide health benefits to the System's employees. The System is billed on a weekly basis for claims by Blue Cross Blue Shield, the plan administrator. The System carries stop-loss insurance through Blue Cross Blue Shield, which has stop loss for individual claims in excess of $200,000. The claims liability reported at year-end is based on the requirements of Governmental Accounting Standards Board Statement No. 10, which requires that a liability for claims be reported if information prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred at the statement of net assets date and the amount can be reasonably estimated.

Changes in the System's claims liability amount for retained risk for fiscal years 2012 and 2011 were:

	Beginning of Fiscal Year Liability	Current Year Claims and Changes in Estimates	Claim Payments	Balance at Fiscal Year End
2011-2012	$ 1,000,000	$ 15,052,244	$ 15,052,244	$ 1,000,000
2010-2011	$ 1,000,000	$ 15,384,063	$ 15,384,063	$ 1,000,000

Total claims expense is partially offset by employee contributions.

Contract Commitments: The System has several employment contracts with physicians requiring base annual salary payments for the years ended September 30 2012 and 2011 as follows, plus various incentive bonuses with bonuses based on various financial performance targets. The employment contracts range from one to three year commitments, with additional annual renewal period options after the initial contract period. The initial terms, including one year automatic renewals, expire at various dates ranging from November 2011 to December 2014. The contractual liability was approximately $3,098,000 and $1,696,000 for the years ended September 30, 2012 and 2011, respectively.

Workers' Compensation and Professional Liability: The System formerly had professional liability and/or workers' compensation insurance coverage with three insurance companies that are now in liquidation:

- PHICO Insurance Company ("PHICO"): Went into liquidation on February 1, 2002. Provided professional liability and workers' compensation coverage for System.

- Reliance Insurance Company ("Reliance"): Went into liquidation on October 31, 2001. Provided workers' compensation coverage for System.

- The Virginia Insurance Reciprocal ("ROA"): Went into liquidation on June 20, 2003. Provided workers' compensation coverage for System.

Following the start of liquidation of each of these companies, responsibility for further defense and/or payments relating to cases and claims formerly insured by the companies was assumed by the North Carolina Insurance Guaranty Association (the "Fund"). The Fund handled the cases and claims and paid all costs and expenses relating thereto with limited input from the System.

The Fund notified the System that it was requesting reimbursement for both indemnity payments and defense expenses relating to cases and claims pertaining to all three former insurers pursuant to N.C.G.S. §58-48-50 (a1)(1). Such reimbursement claim was based on the System's having a net worth that exceeded $50,000,000 on December 31 of the year in which each of the former insurers became insolvent.

The System notified the Fund that it disputed the Fund's legal position with regard to the Fund's right to reimbursement for all indemnity payments and defense expenses, including attorneys' fees, paid by the Fund in the subject cases and claims. Discussions continued between the Fund and System concerning this matter until the Fund initiated formal litigation by filing a declaratory judgment action on March 4, 2004.

Prior to the dispute between the Fund and the System, the System had established certain reserves to provide for payment of professional liability cases where the settlement or judgment would potentially exceed the statutory $300,000 indemnity payment limit provided by the Fund. The amount of the reserve relating to each pending case was based upon assessment of the System's potential financial exposure for settlements or judgments that exceeded the indemnity provided by the Fund. The System reassessed the nature and extent of its reserves once the System became aware of the Fund's claim for reimbursement and in anticipation of the System having to eventually reimburse the Fund for all indemnity payments and all or part of defense expenses relating to cases and claims.

On September 29, 2004, the Fund and System agreed upon a resolution of the declaratory judgment action and entered into a formal Settlement Agreement and Release of All Claims.

As part of the settlement, the System paid the Fund $13,679 during the fiscal year 2012.

The System continues to maintain reserves to cover reimbursement obligations relating to those cases and claims that remain pending. These include several professional liability matters that may involve substantial exposure for both indemnity and defense expenses as well as multiple workers' compensation matters involving continued periodic benefits payments or that are the subject of pending judicial appeals. The nature and extent of these reserves are periodically reviewed for adequacy and reasonableness by management.

Professional Liability: The System spent $1,024,824 for General, Professional and Umbrella coverage in fiscal year 2012. These premiums represent a transfer of risk and are not determined retrospectively. These policies are claims made basis policies, meaning claims are covered based on incidents arising on or after the policy retroactive date and which are reported during the term of the policy.

Other: The System carries commercial insurance coverage for all other risks of loss. There have been no significant reductions in insurance coverage from the prior year, and settled claims have not exceeded coverage in any of the past three fiscal years.

Asserted and Unasserted Claims: The System is aware of various asserted and unasserted claims. Management has been unable to reasonably estimate the amount of the loss, if any, since the ultimate resolution of these matters will be dependent upon future events. Management of the System and its legal counsel feel that these claims can be successfully defended and intend to resist the allegations of these matters in every way and do not plan to seek out-of-court settlements. In the event that judgments adverse to the interests of the System should be rendered, management and its legal counsel feel any liability will be fully covered under the System's existing insurance policies.

13. Pronouncements Issued Not Yet Implemented

In November 2010, The GASB issued Statement No. 61, The Financial Reporting Entity: Omnibus-an amendment of GASB Statements No. 14 and No. 34. The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. The requirements of Statement No. 14, The Financial Reporting Entity, and the related financial reporting requirements of Statement No. 34, Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments, were amended to better meet user needs and to address reporting entity issues that have arisen since the issuance of those Statements. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2012. Management has not currently determined what impact, if any, these statements may have on its financial statements.

In December 2010, The GASB issued Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements. The objective of this Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements:

1. Financial Accounting Standards Board (FASB) Statements and Interpretations
2. Accounting Principles Board Opinions
3. Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure.

This Statement also supersedes Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, thereby eliminating the election provided in paragraph 7 of that Statement for enterprise funds and business-type activities to apply post-November 30, 1989 FASB Statements and Interpretations that do not conflict with or contradict GASB pronouncements. However, those entities can continue to apply, as other accounting literature, post-November 30, 1989 FASB pronouncements that do not conflict with or contradict GASB pronouncements, including this Statement. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2011. Management has not currently determined what impact, if any, these statements may have on its financial statements.

In 2011, the GASB issued GASB Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position. This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources and amends the net asset reporting requirements in Statement No. 34, Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments. This Statement must be adopted no later than the year ending September 30, 2013. Management has not currently determined what impact, if any, this statement may have on its financial statements.

In 2012, the GASB issued GASB Statement No. 65, Items Previously Reported as Assets and Liabilities, which clarifies the appropriate reporting of deferred outflows of resources and

deferred inflows of resources to ensure consistency in financial reporting. This Statement specifically requires certain balances currently being reported as assets and liabilities to be reported as deferred outflows of resources and deferred inflows of resources on the Balance Sheet. Further, the pronouncement also requires certain items currently reported as assets and liabilities on the Balance Sheet to be reported as outflows of resources and inflows of resources on the Statement of Revenues, Expenses, and Changes in Net Assets. This Statement must be adopted no later than the year ending September 30, 2014. Management has not currently determined what impact, if any, this statement may have on its financial statements.

In 2012, the GASB issued GASB Statement No. 67, Financial Reporting for Pension Plans, and GASB Statement No. 68, Accounting and Financial Reporting for Pensions, which require enhanced note disclosure and required supplementary information for both defined benefit and defined contribution pension plans as well as provide standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expenses for pension plans. GASB Statement No. 67 also requires the presentation of new information about annual money-weighted rates of return in the notes to the financial statements and in 10-year required supplementary information schedules. GASB Statement No. 68 requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability in the Statement of Financial Position, and to more comprehensively and comparably measure the annual costs of pension benefits. The Statement also enhances accountability and transparency through revised and new note disclosures and required supplementary information. GASB Statement No. 67 must be adopted for pension plans no later than fiscal year 2014, while GASB Statement No. 68 must be adopted no later than the year ending September 30, 2015. The System has not yet determined the impact of these Statements on the financial statements.

SUPPLEMENTAL SCHEDULES

CAROLINAEAST HEALTH SYSTEM

Other Postemployment Benefits

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (AVA)	Actuarial Accrued Liabilities (AAL)	Unfunded AAL (UAAL)	AVA as percentage of AAL
04/01/2007	$ 4,134,467	$ 4,803,647	$ 669,180	86%
01/01/2008	$ 4,662,084	$ 4,994,563	$ 332,479	93%
01/01/2009	$ 3,704,730	$ 5,348,769	$ 1,644,039	69%
01/01/2010	$ 4,289,091	$ 5,607,624	$ 1,318,533	76%
01/01/2011	$ 4,768,499	$ 6,149,239	$ 1,380,740	78%
01/01/2012	$ 5,266,563	$ 6,145,115	$ 878,552	86%

CAROLINAEAST HEALTH SYSTEM

Other Postemployment Benefits

Schedule of Employer Contributions

Plan Year Ended	Annual Required Contribution	Percentage Contributed
December 31, 2009	$ 514,055	106%
December 31, 2010	497,939	95%
December 31, 2011	628,337	100%
December 31, 2012	574,181	NA

Attachment 2

CAROLINAEAST
HEALTH SYSTEM

April 12, 2013

CarolinaEast Medical Center

CarolinaEast Diagnostic Center

CarolinaEast Surgery Center

CarolinaEast Rehabilitation Hospital

CarolinaEast Heart Center

CarolinaEast Urology Center

CarolinaEast Internal Medicine

CarolinaEast Pediatrics

CarolinaEast Gastroenterology

CarolinaEast Home Care

Crossroads Mental Health

CarolinaEast Health System

Women's and Children's Pavilion, Emergency Department, and Surgery Department Expansion and Renovations Projects

Energy Conservation

Energy conservation measures will include, but are not limited to the following:

1. Use of occupancy sensors for lighting in offices and non-critical areas.
2. Use of 25 watt T-8 lamps or T-5 lamps for increased lighting efficiency. LED Fixtures will also be considered.
3. High efficiency transformers,
4. LED surgical lights
5. Full DDC building automation system with individual room thermostats.
6. Basic Commisioning.
7. Leakage test on all ductwork above 2" static pressure.
8. Use of variable speed drives on all fan motors over 5 hp.
9. Pressure independent two-way flow control valves on AHU chilled water coils.
10. New AHU's will be connected to the existing central plant which utilizes a flat plate heat exchanger for "free cooling" during cool weather periods.
11. Registration for EPA Energy Star Program.
12. Project will require additional chiller capacity. New chiller/chillers will be high efficiency units with environmentally friendly refrigerants. High efficiency magnetic bearing chillers will be considered.
13. Project will require additional boiler capacity. New boiler will be a high efficiency unit with oxygen trim controls and boiler stack gas economizer.
14. Use of air flow monitors to maintain accurate control of outside air.
15. Wall insulation to meet or exceed ASHRAE 90.1-2007 requirements,
16. Roof insulation to meet or exceed ASHRAE 90.1-2007 requirements,
17. Glazing with "U"-value and Shading Coefficient to meet or exceed ASHRAE 90.1-2007 requirements,
18. Glazing to be no more than 40 percent of the wall area per exposure,
19. Building shading

Water Conservation

Water Conservation measures will include, but will not be limited to the following:

1. Low flow water fixtures, will consider the use of dual flush (low/high) fixtures in public areas.
2. Will consider / evaluate recovery of AHU condensate for cooling tower makeup.
3. The use of automatic faucet sensor controls

Indoor Air Quality

Measures will include, but are not limited to:

1. High-efficiency air filtration is to be used to help maintain indoor air quality.
2. Low VOC paints and low VOC adhesives will be specified to promote good indoor air quality.

Sustainable Design

Where possible, specified construction materials will be selected for their sustainability features and their reduced impact on the environment. Several items meeting these requirements will include, but will not be limited to the following:

1. Regionally manufactured products such as masonry (block and brick) and flooring (sheet flooring and carpet) will be specified for the project.
2. High performance Low-E insulated glazing will be specified in all exterior windows.
3. Wall and roof insulation "R" value to meet or exceed NC State Building Code.
4. A program will be established with the general contractor to separate and direct recyclable materials such as copper, steel, and aluminum to collection facilities (for future recycling). Other demolished products will be reviewed for possible recycling / reuse such as cabinetry, furniture, and equipment to keep these materials out of the local landfill.
5. A reflective type roofing material will be specified to reduce the heat island effect and the amount of overall energy required to cool the building expansions.