

Central Michigan Community Hospital and Subsidiary

**Consolidated Financial Report
with Additional Information
September 30, 2003**

Central Michigan Community Hospital and Subsidiary

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Independent Auditor's Report

To the Board of Directors
Central Michigan Community Hospital

We have audited the accompanying consolidated balance sheet of Central Michigan Community Hospital and subsidiary as of September 30, 2003 and 2002, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Central Michigan Community Hospital and subsidiary at September 30, 2003 and 2002, and the consolidated results of their operations, changes in net assets, and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Plante & Moran, PLLC

November 14, 2003

Central Michigan Community Hospital and Subsidiary

Consolidated Balance Sheet

	September 30	
	2003	2002
		(Restated)
Assets		
Current Assets		
Cash	\$ 15,924,378	\$ 13,093,463
Patient accounts receivable - Net (Note 2)	5,095,833	3,592,366
Other accounts receivable	338,160	579,514
Inventories	1,146,622	1,133,913
Prepaid expenses and other	858,696	661,830
Assets held in trust to pay current liabilities (Note 5)	1,482,175	1,454,386
Total current assets	24,845,864	20,515,472
Other Assets (Note 5)	4,197,071	3,929,615
Restricted Assets (Note 5)	585,771	477,917
Property and Equipment - Net (Note 6)	24,989,135	26,179,938
Total assets	<u>\$ 54,617,841</u>	<u>\$ 51,102,942</u>
Liabilities and Net Assets		
Current Liabilities		
Current portion of long-term debt - Net of current portion (Note 8)	\$ 907,750	\$ 859,387
Accounts payable	2,369,608	1,426,931
Accrued liabilities (Note 7)	6,018,667	5,246,216
Cost report settlements payable (Note 4)	3,236,252	3,475,023
Total current liabilities	12,532,277	11,007,557
Long-term Debt - Net of current portion (Note 8)	19,918,566	20,785,821
Total liabilities	32,450,843	31,793,378
Net Assets		
Unrestricted	21,581,227	18,831,647
Temporarily restricted	535,286	427,484
Permanently restricted	50,485	50,433
Total net assets	22,166,998	19,309,564
Total liabilities and net assets	<u>\$ 54,617,841</u>	<u>\$ 51,102,942</u>

Central Michigan Community Hospital and Subsidiary

Consolidated Statement of Operations

	Year Ended September 30	
	2003	2002
		(Restated)
Unrestricted Revenue, Gains, and Other Support		
Net patient service revenue (Note 13)	\$ 53,119,355	\$ 48,650,009
Other operating revenue	2,724,470	2,850,357
	<u>55,843,825</u>	<u>51,500,366</u>
Operating Expenses		
Nursing services	13,355,465	11,487,694
Ancillary services	18,480,746	17,524,761
General services	4,767,661	4,451,214
Fiscal, administrative, and other services	11,168,917	8,879,829
Depreciation and amortization	2,583,438	2,893,058
Provision for bad debts	1,654,512	1,460,801
Interest	1,386,332	1,389,017
	<u>53,397,071</u>	<u>48,086,374</u>
Operating Income	2,446,754	3,413,992
Other Income (Expense) (Note 10)	<u>176,407</u>	<u>(909,839)</u>
Excess of Revenue Over Expenses	2,623,161	2,504,153
Assets Released From Restrictions	154,105	134,809
Change in Unrealized Gains and Losses on Investments (Note 5)	<u>(27,686)</u>	<u>(3,379)</u>
Increase in Unrestricted Net Assets	<u>\$ 2,749,580</u>	<u>\$ 2,635,583</u>

Central Michigan Community Hospital and Subsidiary

Consolidated Statement of Changes in Net Assets

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Net Assets - September 20, 2001 - As previously stated (Note I)	\$ 16,434,717	\$ 376,591	\$ 50,351	\$ 16,861,659
Restatement for the combination of Central Michigan Healthcare System	<u>(238,653)</u>	<u>-</u>	<u>-</u>	<u>(238,653)</u>
Net Assets - September 30, 2001 - As restated	16,196,064	376,591	50,351	16,623,006
Excess of revenue over expenses	2,504,153	-	-	2,504,153
Change in unrealized gains and losses on investments	(3,379)	-	-	(3,379)
Investment earnings on restricted assets	-	14,338	-	14,338
Restricted contributions	-	171,364	82	171,446
Assets released from restrictions	<u>134,809</u>	<u>(134,809)</u>	<u>-</u>	<u>-</u>
Increase in net assets	<u>2,635,583</u>	<u>50,893</u>	<u>82</u>	<u>2,686,558</u>
Net Assets - September 30, 2002 - As restated	18,831,647	427,484	50,433	19,309,564
Excess of revenue over expenses	2,623,161	-	-	2,623,161
Change in unrealized gains and losses on investments	(27,686)	-	-	(27,686)
Investment earnings on restricted assets	-	10,087	-	10,087
Restricted contributions	-	251,820	52	251,872
Assets released from restrictions	<u>154,105</u>	<u>(154,105)</u>	<u>-</u>	<u>-</u>
Increase in net assets	<u>2,749,580</u>	<u>107,802</u>	<u>52</u>	<u>2,857,434</u>
Net Assets - September 30, 2003	<u>\$21,581,227</u>	<u>\$ 535,286</u>	<u>\$ 50,485</u>	<u>\$22,166,998</u>

Central Michigan Community Hospital and Subsidiary

Consolidated Statement of Cash Flows

	Year Ended September 30	
	2003	2002 (Restated)
Cash Flows From Operating Activities		
Cash received from patients and third-party payors	\$ 52,857,513	\$ 52,113,177
Cash paid to suppliers and employees	(46,566,207)	(43,161,400)
Interest received	347,343	390,321
Donations received	16,819	20,741
Interest paid	(1,408,543)	(1,409,462)
Net cash provided by operating activities (Note 12)	5,246,925	7,953,377
Cash Flows From Investing Activities		
Purchase of property and equipment	(2,018,407)	(3,367,662)
Proceeds from property disposals	640,881	161,997
Net change in assets limited as to use by the Board and restricted cash	(592,306)	(376,492)
Net cash used in investing activities	(1,969,832)	(3,582,157)
Cash Flows From Financing Activities		
Principal payments on long-term debt	(859,387)	(799,896)
Proceeds from issuance of long-term debt	-	426,469
Net (increase) decrease in funds held by trustee under bond indenture	151,250	(90,164)
Restricted contributions and interest	261,959	185,784
Net cash used in financing activities	(446,178)	(277,807)
Net Increase in Cash	2,830,915	4,093,413
Cash - Beginning of year	13,093,463	9,000,050
Cash - End of year	\$ 15,924,378	\$ 13,093,463

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 1 - Nature of Business and Significant Accounting Policies

Reporting Entity - Central Michigan Community Hospital (the "Hospital"), a Michigan nonprofit corporation, operates a short-term, acute-care facility offering inpatient and outpatient health care, and home health services primarily to citizens of the Isabella County, Michigan area. Meridian Ventures, Inc. (MV), a taxable corporation, is a wholly owned subsidiary of the Hospital. MV has had minimal operations to date.

As of October 1, 2002, Central Michigan Healthcare System, Inc. (CMHS), a non-profit organization, which was related to the Hospital through common board governance, was dissolved and its operations were merged into the Hospital. Assets and liabilities of CMHS were absorbed by the Hospital. The operations of CMHS are reported as departments of the Hospital as of October 1, 2002. The transaction is accounted for in a manner consistent with a pooling of interests.

The comparative financial statements for 2002 have been restated to include the financial results of CMHS. As a result, October 1, 2001 net assets were restated to reflect the combination of CMHS. The result of the restatement was a decrease in total net assets of \$238,653. Cash as of October 1, 2001 was also restated in the amount of \$179,962.

Prior to October 1, 2002, Central Michigan Home Care, Inc. (CMHC), a nonprofit corporation, was a wholly owned subsidiary of the Hospital. As of October 1, 2002, CMHC was also merged into the Hospital, and the operations are now reported as a department of the Hospital.

Principles of Consolidation - The accompanying consolidated financial statements include the accounts of Central Michigan Community Hospital and its wholly owned subsidiary, Meridian Ventures, Inc. Intercompany transactions and balances have been eliminated in consolidation.

Temporarily and Permanently Restricted Net Assets - Temporarily and permanently restricted net assets are those whose use by the Hospital has been limited by donors to a specific time period or purpose.

Temporarily restricted net assets and the income earned on the assets are restricted by donors for the purchase of equipment and facility renovations. Interest earned on permanently restricted net assets is restricted by donors for the purchase of radiology equipment.

Cash Equivalents - The Hospital considers all liquid investments purchased with an original maturity of three months or less to be cash equivalents, except for amounts included in restricted assets and other assets (see Note 5).

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Investments - Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the balance sheet. Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in excess of revenue over expenses unless the income or loss is restricted by donor or law. Changes in unrealized gains and losses on investments are excluded from excess of revenue over expenses.

Accounts Receivable - Accounts receivable for patients, insurance companies, and governmental agencies are based on gross charges. An allowance for uncollectible accounts is established on an aggregate basis by using historical loss rate factors applied to unpaid accounts based on aging. Loss rate factors are based on historical loss experience and adjusted for economic conditions and other trends affecting the Hospital's ability to collect outstanding amounts. Uncollectible amounts are written off against the allowance for uncollectible accounts in the period they are deemed to be uncollectible. The allowance for contractual adjustments and interim payment advances is based on expected payment rates from payors based on current reimbursement methodologies. This amount also includes amounts received as interim payments against unpaid claims by certain payors.

Inventories - Inventories are stated at the lower of cost, determined on a first-in, first-out basis, or market.

Assets Limited as to Use - Assets limited as to use primarily include assets held by trustees under indenture agreements and designated assets set aside by the Board of Directors for future capital improvements over which the Board retains control and may at its discretion subsequently use for other purposes. Amounts required to meet current liabilities of the Hospital have been reclassified in the balance sheet as current assets (see Note 5).

Property and Equipment - Property and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful lives of each class of depreciable asset and is computed using the straight-line method. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Excess of Revenue Over Expenses - The statement of operations includes excess of revenue over expenses. Changes in unrestricted net assets that are excluded from excess of revenue over expenses, consistent with industry practice, include changes in unrealized gains and losses on investments, permanent transfers of assets to and from affiliates for other than goods and services, and contributions of long-lived assets (including assets acquired using contributions, which by donor restriction were to be used for the purposes of acquiring such assets).

Net Patient Service Revenue - The Hospital and subsidiary have agreements with third-party payors that provide for payments at amounts different from established rates. Payment arrangements include prospectively determined rates per discharge and episode of care, reimbursed costs, fee-for-service arrangements, discounted charges, and per-diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Management believes that it is in compliance with all applicable laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

Bond Discount and Issue Costs - Bond discount and issue costs are amortized on the interest method over the life of the related debt issue.

Retirement Plan - The Hospital has defined contribution plans covering substantially all employees. Pension expense for the defined contribution plans is based on the amount of contribution approved by the Board of Directors. Required contributions to the plans for the years ended September 30, 2003 and 2002 were approximately \$443,000 and \$270,000, respectively.

Professional Liability Insurance - The provision for estimated medical malpractice claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported.

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Charity Care - The Hospital 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 Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as operating revenue (see Note 3).

Donor-Restricted Gifts - Contributions are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statement of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying financial statements.

Tax Status - Central Michigan Community Hospital is a nonprofit 501(c)(3), tax-exempt organization; accordingly, no tax provision is reflected in the consolidated financial statements. Meridian Ventures, Inc. is subject to income tax but had minimal operations in 2003 and 2002.

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 reported amounts and disclosures in the financial statements. Actual results could differ from those estimates.

Note 2 - Accounts Receivable

A summary of accounts receivable is as follows:

	2003	2002
		(Restated)
Patient accounts receivable	\$ 16,560,805	\$ 15,172,557
Less:		
Allowance for doubtful accounts	(2,789,101)	(2,459,864)
Allowance for contractual adjustments	(8,675,871)	(9,120,327)
Total patient accounts receivable	<u>\$ 5,095,833</u>	<u>\$ 3,592,366</u>

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 2 - Accounts Receivable (Continued)

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The composition of accounts receivable from patients and third-party payors is as follows:

	2003 Percent	2002 Percent (Restated)
Medicare	17.0	25.3
Medicaid	15.1	9.3
Blue Cross/Blue Shield of Michigan	17.8	20.4
Commercial insurance	17.1	16.3
Patients	<u>33.0</u>	<u>28.7</u>
Total	<u>100.0</u>	<u>100.0</u>

Note 3 - Charity Care

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies rendered under its charity care policy. The following information measures the level of charity care provided:

	<u>2003</u>	<u>2002</u>
Charges forgone, based on established rates	<u>\$ 255,258</u>	<u>\$ 245,572</u>

In addition, under arrangements with various governmental insurance programs, the Hospital provides significant care to the local indigent population for which reimbursement for services rendered is generally less than the cost of providing such services. As part of its obligation to the local communities, the Hospital also provides numerous other services that benefit the communities, which are generally performed at no charge.

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 4 - Cost Report Settlements

Approximately 70 percent of the Hospital's net patient service revenue is received from Medicare, Medicaid, and Blue Cross/Blue Shield of Michigan programs. The Hospital has agreements with these payors that provide for reimbursement to the Hospital at amounts different from its established rates. A summary of the basis of reimbursement is as follows:

- **Medicare** - Inpatient, acute-care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Outpatient and home care services related to Medicare beneficiaries are paid based on a prospectively determined amount per episode.
- **Medicaid** - Inpatient, acute-care services rendered to Medicaid program beneficiaries are also paid at prospectively determined rates per discharge. Capital costs relating to Medicaid patients are paid on a cost-reimbursement method. The Hospital is reimbursed for outpatient and home care services on an established fee-for-service methodology.
- **Blue Cross/Blue Shield of Michigan** - Inpatient, acute-care services are reimbursed at prospectively determined rates per discharge. These rates are based on a Medicare patient classification system and on Hospital-specific costs limited by a cap specified in the agreement with Blue Cross/Blue Shield of Michigan. Outpatient services are reimbursed based primarily on a fee-for-service methodology.

Cost report settlements result from the adjustment of interim payments to final reimbursement under these programs, which is subject to audit by fiscal intermediaries. Cost report settlements increased net patient service revenue by approximately \$1,000,000 and \$2,800,000 for the years ended September 30, 2003 and 2002, respectively, reflecting amounts received in excess of recorded amounts.

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 5 - Other Assets

The details of other assets are given below:

	<u>2003</u>	<u>2002</u>
		(Restated)
Assets limited as to use - At market value:		
Investments held by trustee under bond indenture	\$ 3,634,698	\$ 3,785,948
By Board of Directors for future capital		
improvements	<u>1,711,992</u>	<u>1,255,226</u>
Subtotal	5,346,690	5,041,174
Less amounts for payment of current liabilities	<u>(1,482,175)</u>	<u>(1,454,386)</u>
Total assets limited as to use	3,864,515	3,586,788
Bond issue costs and other - Net	<u>332,556</u>	<u>342,827</u>
Total other assets	<u>\$ 4,197,071</u>	<u>\$ 3,929,615</u>

The amounts for payment of current liabilities represents amounts held by the trustee for the principal portion and accrued interest to be paid during the subsequent year.

Investments, including restricted assets, consist of the following:

	<u>2003</u>	<u>2002</u>
		(Restated)
Money market investments	\$ 4,811,639	\$ 3,423,601
U.S. government obligations	<u>1,120,822</u>	<u>2,095,490</u>
Total	<u>\$ 5,932,461</u>	<u>\$ 5,519,091</u>

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 5 - Other Assets (Continued)

Investment income on assets limited as to use, cash equivalents, and other investments are comprised of the following for the years ended September 30, 2003 and 2002:

	2003	2002 (Restated)
Interest income in other revenue	\$ 61,267	\$ 69,931
Interest income in other income	286,076	320,390
Change in unrealized gains and losses on investments	<u>(27,686)</u>	<u>(3,379)</u>
Total investment income	<u>\$ 319,657</u>	<u>\$ 386,942</u>

Note 6 - Property and Equipment

The cost of property and equipment and depreciable lives are summarized as follows:

	2003	2002 (Restated)	Depreciable Life-Years
Land and land improvements	\$ 2,682,123	\$ 2,797,060	20
Buildings and building improvements	29,563,575	30,531,518	10-40
Equipment and fixtures	19,403,593	19,349,298	3-10
Construction-in-progress	<u>1,230,403</u>	<u>46,542</u>	-
Total cost	52,879,694	52,724,418	
Less accumulated depreciation	<u>(27,890,559)</u>	<u>(26,544,480)</u>	
Net carrying amount	<u>\$ 24,989,135</u>	<u>\$ 26,179,938</u>	

Depreciation expense for the years ended September 30, 2003 and 2002 amounted to approximately \$2,560,000 and \$2,825,000, respectively.

Construction-in-progress consists of costs incurred for various renovations throughout the Hospital. Total costs to complete the projects are approximately \$600,000.

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 7 - Accrued Liabilities

The details of accrued liabilities are given below:

	2003	2002
		(Restated)
Payroll and related items	\$ 980,233	\$ 626,415
Compensated absences	2,871,356	2,637,918
Other employee benefits	869,903	802,497
Professional liability claims (Note 11)	640,000	500,000
Accrued interest payable	657,175	679,386
	<u>6,018,667</u>	<u>5,246,216</u>
Total accrued liabilities	<u>\$ 6,018,667</u>	<u>\$ 5,246,216</u>

Note 8 - Long-term Debt

Long-term debt consists of the following:

	2003	2002
		(Restated)
Bonds payable, Series 1996	\$ 17,645,000	\$ 17,930,000
Bonds payable, Series 1993A	3,605,000	4,095,000
Less unamortized discount	(700,870)	(741,365)
Subtotal	20,549,130	21,283,635
Other	277,186	361,573
Subtotal	20,826,316	21,645,208
Less current portion	(907,750)	(859,387)
Long-term debt	<u>\$ 19,918,566</u>	<u>\$ 20,785,821</u>

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 8 - Long-term Debt (Continued)

Bonds payable, Series 1996, consist of Hospital Revenue Bonds that were issued by the Michigan State Hospital Finance Authority (the "Authority"). The bonds consist of serial bonds, payable in annual installments ranging from \$305,000 on October 1, 2003 to \$385,000 on October 1, 2007, at an interest rate ranging from 5.80 percent to 6.20 percent, and term bonds payable in annual installments ranging from \$410,000 on October 1, 2008 to \$1,350,000 on October 1, 2027, at an interest rate of 6.25 percent. The Hospital has pledged all future accounts, contract rights, chattel paper, instruments, documents, and general intangibles as described in the security agreement.

Bonds payable, Series 1993A, consist of Hospital Revenue Refunding Bonds that were issued by the Michigan State Hospital Finance Authority. The bonds consist of serial bonds, payable in annual installments ranging from \$520,000 on October 1, 2003 to \$550,000 on October 1, 2004, at an interest rate ranging from 5.875 percent to 6.00 percent, and term bonds payable in annual installments ranging from \$580,000 on October 1, 2005 to \$690,000 on October 1, 2008, at an interest rate of 6.00 percent. The Hospital has pledged substantially all deposits and investments and other assets for the payment of the bonds as described in the security agreement.

In connection with its loan agreement with the Authority, the Hospital has made a covenant relative to minimum debt service requirements and has agreed to maintain specified insurance coverage among other covenants. The Hospital is required to maintain certain deposits with a trustee. Such deposits are included in assets limited as to use (see Note 5).

Minimum principal payments on bonds payable and other long-term debt obligations to maturity as of September 30, 2003 are as follows:

2004	\$	907,750
2005		960,964
2006		1,014,319
2007		999,153
2008		1,035,000
Thereafter		<u>16,610,000</u>
Subtotal		21,527,186
Less unamortized discount		<u>(700,870)</u>
Total	\$	<u>20,826,316</u>

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 9 - Line of Credit

The Hospital has available a line of credit with a bank for \$2,000,000 at September 30, 2003 and \$1,500,000 at September 30, 2002, at a variable interest rate (4.00 percent and 4.75 percent at September 30, 2003 and 2002, respectively). As of September 30, 2003 and 2002, the Hospital did not have any outstanding borrowings on the line of credit.

Note 10 - Other Income (Expense)

The detail of other income (expense) is presented below:

	2003	2002
		(Restated)
Investment income:		
Funded depreciation	\$ 14,214	\$ 20,741
General	<u>271,862</u>	<u>299,649</u>
Total investment income	286,076	320,390
Expenses:		
Other expense	(109,669)	(1,091,045)
Restructuring costs	<u>-</u>	<u>(139,184)</u>
Total other income (expenses)	<u>\$ 176,407</u>	<u>\$ (909,839)</u>

Restructuring costs represent expenses incurred during by the Hospital for the merger of the Hospital and Central Michigan Healthcare System, Inc. (see Note 1) during 2002.

During 2002, the Hospital recognized losses on disposal of assets of approximately \$949,000 in connection with the write-off of various leasehold improvements, computer equipment, and property (included in other expenses).

Note 11 - Professional Liability Insurance

The Hospital is insured against potential professional liability claims under a claims-made policy, whereby only the claims reported to the insurance carrier during the policy period are covered regardless of when the incident giving rise to the claim occurred. Under the terms of the policy, the Hospital must pay a deductible towards the cost of litigating or settling any asserted claim. In addition, the Hospital bears the risk of the ultimate costs of any individual claim exceeding the policy limits for claims asserted in the policy year.

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 11 - Professional Liability Insurance (Continued)

At September 30, 2003 and 2002, the Hospital has accrued \$640,000 and \$500,000, respectively, for estimated losses in connection with those professional liability claims for which an amount can be reasonably estimated (see Note 7).

Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during the claims-made term, but reported subsequently, will be uninsured.

Note 12 - Cash Flows

A reconciliation of the increase in net assets to net cash flows provided by operating activities is as follows:

	2003	2002
		(Restated)
Increase in net assets	\$ 2,857,434	\$ 2,686,558
Adjustments to reconcile increase in net assets to net cash from operating activities:		
Depreciation and amortization	2,583,438	2,893,058
Loss on disposal of equipment	45,538	1,088,173
Provision for bad debts	1,654,512	1,460,801
Change in net unrealized gains and losses on investments	27,686	3,379
Restricted contributions and investment earnings	(261,959)	(185,784)
(Increase) decrease in assets:		
Patient accounts receivable	(3,157,979)	(68,361)
Other accounts receivable	241,354	(325,444)
Cost report settlements receivable	-	118,089
Inventories	(12,709)	(132,049)
Prepaid expenses and other	(196,866)	(126,024)
Other assets	(9,881)	229,557
Increase (decrease) in liabilities:		
Accounts payable	942,677	405,311
Accrued liabilities	772,451	(867,155)
Cost report settlements payable	(238,771)	773,268
Net cash provided by operating activities	<u>\$ 5,246,925</u>	<u>\$ 7,953,377</u>

Central Michigan Community Hospital and Subsidiary

Notes to Consolidated Financial Statements September 30, 2003 and 2002

Note 12 - Cash Flows (Continued)

There were no significant noncash financing or investing activities for the years ended September 30, 2003 and 2002.

Note 13 - Net Patient Service Revenue

The detail of net patient service revenue is shown below:

	2003	2002 (Restated)
Patient service revenue:		
Routine and inpatient ancillary	\$ 37,946,953	\$ 32,177,039
Outpatient ancillary	85,192,919	69,656,985
Total patient service revenue	123,139,872	101,834,024
Revenue deductions:		
Current year	71,020,517	55,984,015
Prior year settlements	(1,000,000)	(2,800,000)
Total revenue deductions	70,020,517	53,184,015
Net patient service revenue	<u>\$ 53,119,355</u>	<u>\$ 48,650,009</u>

The reduction in revenue deductions for prior year settlements results from the reimbursement on final settlement of cost reports in excess of amounts estimated by the Hospital.

Note 14 - Functional Expenses

The Hospital and subsidiary provide general health care services to residents within their geographic locations. Expenses related to providing these services are as follows:

	2003	2002 (Restated)
Health care services	\$ 40,913,239	\$ 38,162,049
General and administrative	12,483,832	9,924,325
Total functional expenses	<u>\$ 53,397,071</u>	<u>\$ 48,086,374</u>

Additional Information



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To the Board of Directors
Central Michigan Community Hospital

We have audited the consolidated financial statements of Central Michigan Community Hospital and subsidiary for the years ended September 30, 2003 and 2002. Our audits were made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The following schedules, on pages 20-25, are presented for the purpose of additional analysis and are not a required part of the basic consolidated financial statements. Such information has been subjected to the procedures applied in the audits of the basic consolidated financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic consolidated financial statements taken as a whole.

Plante & Moran, PLLC

November 14, 2003

Central Michigan Community Hospital and Subsidiary

Consolidated Schedule of Unrestricted Revenue, Gains, and Other Support

	Year Ended September 30		Increase (Decrease)
	2003	2002 (Restated)	
Routine Services			
Medical and surgical	\$ 5,249,053	\$ 5,318,884	\$ (69,831)
Intensive care	2,130,384	1,907,447	222,937
Obstetrics	2,579,023	2,643,078	(64,055)
Total routine services	9,958,460	9,869,409	89,051
Ancillary Services			
Inpatient:			
Operating rooms	7,071,384	5,269,626	1,801,758
Recovery rooms	731,858	501,150	230,708
Medical and surgical supplies	3,374,563	2,335,993	1,038,570
Emergency	1,899,366	1,692,371	206,995
Laboratory	3,393,590	2,906,820	486,770
Cardiopulmonary	42,228	46,793	(4,565)
Diagnostic imaging	2,479,977	1,980,301	499,676
Pharmacy	5,436,461	4,268,027	1,168,434
Dietician instruction	1,622	882	740
Rehabilitation services	253,090	287,223	(34,133)
Anesthesiology	745,449	593,988	151,461
Respiratory therapy	2,558,905	2,424,456	134,449
Total inpatient	27,988,493	22,307,630	5,680,863

Central Michigan Community Hospital and Subsidiary

Consolidated Schedule of Unrestricted Revenue, Gains, and Other Support (Continued)

	Year Ended September 30		Increase (Decrease)
	2003	2002 (Restated)	
Ancillary Services (Continued)			
Outpatient:			
Operating rooms	\$ 14,510,730	\$ 11,057,458	\$ 3,453,272
Recovery rooms	2,594,647	2,083,274	511,373
Emergency	8,586,563	7,474,119	1,112,444
Medical and surgical supplies	3,347,511	2,558,329	789,182
Anesthesiology	1,208,460	1,075,419	133,041
Laboratory	12,644,115	10,033,956	2,610,159
Treatment rooms	1,309,205	1,150,563	158,642
Cardiopulmonary	943,641	877,214	66,427
Diagnostic imaging	17,468,706	13,502,396	3,966,310
Urgent care	2,251,144	2,007,256	243,888
Clinics and physician offices	6,597,737	7,185,514	(587,777)
Home care	1,457,722	1,233,529	224,193
Sleep lab	1,102,047	1,161,973	(59,926)
Dietician instruction	8,017	975	7,042
Pharmacy	7,878,710	5,025,704	2,853,006
Respiratory therapy	773,959	688,324	85,635
Rehabilitation services	2,510,005	2,540,982	(30,977)
	<u>85,192,919</u>	<u>69,656,985</u>	<u>15,535,934</u>
Total outpatient			
	<u>113,181,412</u>	<u>91,964,615</u>	<u>21,216,797</u>
Total ancillary services			
Total patient service revenue	123,139,872	101,834,024	21,305,848

Central Michigan Community Hospital and Subsidiary

Consolidated Schedule of Unrestricted Revenue, Gains, and Other Support (Continued)

	Year Ended September 30		Increase (Decrease)
	2003	2002 (Restated)	
Revenue Deductions - Provision for adjustment of revenue to reimbursement			
Medicare	\$ 26,537,502	\$ 20,513,560	\$ 6,023,942
Medicaid	8,199,262	7,257,346	941,916
Blue Cross/Blue Shield of Michigan	26,611,232	17,487,979	9,123,253
Charity and free care	255,258	245,572	9,686
Domestic health claims	2,930,006	2,298,693	631,313
Clinics and physicians office	2,308,219	1,889,229	418,990
Other allowances and discounts	3,179,038	3,491,636	(312,598)
Total revenue deductions	<u>70,020,517</u>	<u>53,184,015</u>	<u>16,836,502</u>
Net patient service revenue	53,119,355	48,650,009	4,469,346
Other Operating Revenue			
Cafeteria	262,144	255,319	6,825
Drugs sold - Employees	732,218	687,050	45,168
Miscellaneous	937,877	1,090,992	(153,115)
Interest income - Bond and interest redemption fund	61,267	69,931	(8,664)
Shared service expense recovery from other institutions	438,727	422,435	16,292
Rentals	292,237	324,630	(32,393)
Total other operating revenue	<u>2,724,470</u>	<u>2,850,357</u>	<u>(125,887)</u>
Total unrestricted revenue, gains, and other support	<u>\$ 55,843,825</u>	<u>\$ 51,500,366</u>	<u>\$ 4,343,459</u>

Central Michigan Community Hospital and Subsidiary

Consolidated Schedule of Expenses by Natural Classification

	Year Ended September 30		Increase (Decrease)
	2003	2002 (Restated)	
Salaries and wages	\$ 21,250,523	\$ 20,081,559	\$ 1,168,964
Vacation, sick, and holiday	2,737,104	2,247,182	489,922
Longevity	154,010	159,058	(5,048)
Payroll taxes	1,754,556	1,623,138	131,418
Employee benefits	1,810,470	1,340,773	469,697
Retirement	443,139	274,638	168,501
Professional services	4,441,330	4,073,832	367,498
Recruitment	448,173	126,509	321,664
Physician fees	278,990	264,757	14,233
Patient billable supplies	6,398,361	4,833,302	1,565,059
Supplies - Other	3,530,119	3,426,591	103,528
Insurance	875,706	527,389	348,317
Advertising	318,034	272,133	45,901
Utilities	889,364	862,541	26,823
Repairs and maintenance	1,152,362	1,296,349	(143,987)
Rent	398,800	426,252	(27,452)
Depreciation and amortization	2,583,438	2,893,058	(309,620)
Provision for bad debts	1,654,512	1,460,801	193,711
Interest	1,386,332	1,389,017	(2,685)
Miscellaneous	891,748	507,495	384,253
Total	\$ 53,397,071	\$ 48,086,374	\$ 5,310,697

Central Michigan Community Hospital and Subsidiary

Consolidated Schedule of Expenses Departmental Basis

	Year Ended September 30		Increase (Decrease)
	2003	2002 (Restated)	
Nursing Services			
Nursing administration	\$ 459,718	\$ 550,339	\$ (90,621)
Medical and surgical	2,700,853	2,364,917	335,936
Intensive care	997,196	866,163	131,033
Obstetrics	1,172,685	1,038,798	133,887
Mental health	-	83,332	(83,332)
Operating room	1,828,108	1,506,000	322,108
Recovery room	741,440	631,055	110,385
Emergency room	2,692,271	2,434,392	257,879
Medical supplies	2,763,194	2,012,698	750,496
Total nursing services	13,355,465	11,487,694	1,867,771
Ancillary Services			
Anesthesiology	967,429	784,093	183,336
Laboratory	3,421,440	2,961,983	459,457
Cardiopulmonary	169,023	164,743	4,280
Diagnostic imaging	3,303,768	2,839,828	463,940
Urgent care	871,399	836,607	34,792
Clinics and physician office practices	3,788,189	4,821,531	(1,033,342)
Oncology	107,767	112,814	(5,047)
Home care	778,463	475,794	302,669
Sleep lab	148,372	168,113	(19,741)
Pharmacy	3,779,985	3,159,320	620,665
Respiratory therapy	392,777	370,836	21,941
Rehabilitation services	752,134	829,099	(76,965)
Total ancillary services	18,480,746	17,524,761	955,985

Central Michigan Community Hospital and Subsidiary

Consolidated Schedule of Expenses Departmental Basis (Continued)

	Year Ended September 30		Increase (Decrease)
	2003	2002 (Restated)	
General Services			
Transcription	\$ 206,589	\$ 202,054	\$ 4,535
Medical records	532,712	444,030	88,682
Dietary	1,298,831	1,223,596	75,235
Plant operation	1,715,145	1,591,102	124,043
Housekeeping	780,720	786,683	(5,963)
Laundry	233,664	203,749	29,915
Total general services	4,767,661	4,451,214	316,447
Fiscal, Administrative, and Other Services			
Fiscal services	2,221,283	2,212,780	8,503
Information systems	1,218,350	1,063,263	155,087
Administration	2,158,603	2,046,441	112,162
Human resources	936,796	452,014	484,782
Materials management	198,991	186,910	12,081
Case management	207,016	87,863	119,153
Employee benefits	1,925,406	1,030,688	894,718
Health promotion	78,276	61,701	16,575
Fitness center	159,080	169,887	(10,807)
Communications and marketing	630,325	401,229	229,096
Quality and corporate compliance	1,434,791	1,167,053	267,738
Total fiscal, administrative, and other services	11,168,917	8,879,829	2,289,088
Depreciation and Amortization	2,583,438	2,893,058	(309,620)
Provision for Bad Debts	1,654,512	1,460,801	193,711
Interest	1,386,332	1,389,017	(2,685)
Total operating expenses	<u>\$ 53,397,071</u>	<u>\$ 48,086,374</u>	<u>\$ 5,310,697</u>