

# Municipal Secondary Market Disclosure Information Cover Sheet

This cover sheet should be sent with all submissions made to the Municipal Securities Rulemaking Board, Nationally Recognized Municipal Securities Information Repositories, and any applicable State Information Depository, whether the filing is voluntary or made pursuant to Securities and Exchange Commission rule 15c2-12 or any analogous state statute.

See [www.sec.gov/info/municipal/nrmsir.htm](http://www.sec.gov/info/municipal/nrmsir.htm) for list of current NRMSIRs and SIDs

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**IF THIS FILING RELATES TO A SINGLE BOND ISSUE:**

Provide name of bond issue exactly as it appears on the cover of the Official Statement  
(please include name of state where issuer is located):

\$12,175,000

City of Hillsdale Hospital Finance Authority (Michigan)

Hospital Revenue Bonds, Series 1998

Hillsdale Community Health Center

Provide nine-digit CUSIP\* numbers if available, to which the information relates:

432492AF3

432492AG1

432492AH9

432492AJ5

432492AL0

432492AM8

432492AN6

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**IF THIS FILING RELATES TO ALL SECURITIES ISSUED BY THE ISSUER OR ALL SECURITIES OF A SPECIFIC CREDIT OR ISSUED UNDER A SINGLE INDENTURE:**

Issuer's Name (please include name of state where Issuer is located): \_\_\_\_\_

Other Obligated Person's Name (if any): \_\_\_\_\_  
(Exactly as it appears on the Official Statement Cover)

Provide six-digit CUSIP\* number(s), if available, of Issuer: \_\_\_\_\_

\*(Contact CUSIP's Municipal Disclosure Assistance Line at 212.438.6518 for assistance with obtaining the proper CUSIP numbers.)

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**TYPE OF FILING:**

Electronic (number of pages attached) 32  Paper (number of pages attached) \_\_\_\_\_

If information is also available on the Internet, give URL: www.firstriver.com

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**WHAT TYPE OF INFORMATION ARE YOU PROVIDING? (Check all that apply)**

A.  Annual Financial Information and Operating Data pursuant to Rule 15c2-12  
(Financial information and operating data should not be filed with the MSRB.)

Fiscal Period Covered: July 2005 – June 2006 (FY2006)

B.  Audited Financial Statements or CAFR pursuant to Rule 15c2-12

Fiscal Period Covered: July 2005 – June 2006 (FY2006)

C.  Notice of a Material Event pursuant to Rule 15c2-12 (Check as appropriate)

- |  |  |
|--|--|
| 1. <input type="checkbox"/> Principal and interest payment delinquencies                                 | 6. <input type="checkbox"/> Adverse tax opinions or events affecting the tax-exempt status of the security   |
| 2. <input type="checkbox"/> Non-payment related defaults   | 7. <input type="checkbox"/> Modifications to the rights of security holders                                  |
| 3. <input type="checkbox"/> Unscheduled draws on debt service reserves reflecting financial difficulties | 8. <input type="checkbox"/> Bond calls   |
| 4. <input type="checkbox"/> Unscheduled draws on credit enhancements reflecting financial difficulties   | 9. <input type="checkbox"/> Defeasances  |
| 5. <input type="checkbox"/> Substitution of credit or liquidity providers, or their failure to perform   | 10. <input type="checkbox"/> Release, substitution, or sale of property securing repayment of the securities |
|  | 11. <input type="checkbox"/> Rating changes  |

D.  Notice of Failure to Provide Annual Financial Information as Required

E.  Quarterly or Monthly Financial Information and Operating Data  
(Financial information and operating data should not be filed with the MSRB.)

Period Covered: \_\_\_\_\_

F.  Other Secondary Market Information (Specify): \_\_\_\_\_

I hereby represent that I am authorized by the issuer or obligor or its agent to distribute this information publicly:

**Issuer Contact:**

Name \_\_\_\_\_ Title \_\_\_\_\_  
Employer \_\_\_\_\_  
Address \_\_\_\_\_ City \_\_\_\_\_ State \_\_\_\_\_ Zip Code \_\_\_\_\_  
Telephone \_\_\_\_\_ Fax \_\_\_\_\_  
Email Address \_\_\_\_\_ Issuer Web Site Address \_\_\_\_\_

**Dissemination Agent Contact, if any:**

Name Shelley J. Aronson Title President  
Employer First River Advisory L.L.C.  
Address 2640 Override Drive City Ann Arbor State MI Zip Code 48104  
Telephone (734) 761-3624 Fax (734) 761-3614  
Email Address aronson@firstriver.com Relationship to Issuer Dissemination Agent

**Obligor Contact, if any:**

Name Valerie Fetters Title Chief Financial Officer  
Employer Hillsdale Community Health Center  
Address 168 South Howell Street City Hillsdale State MI Zip Code 49242  
Telephone (517) 437-5232 Fax (517) 437-0246  
Email Address vfetters@hchc.com Obligor Web Site Address www.hchc.com

**Investor Relations Contact, if any:**

Name \_\_\_\_\_ Title \_\_\_\_\_  
Telephone \_\_\_\_\_ Email Address \_\_\_\_\_

# HILLSDALE COMMUNITY HEALTH CENTER

168 South Howell Street

Hillsdale, MI 49242

## OFFICER'S CERTIFICATE

**DATED: OCTOBER 30, 2006**

Pursuant to Section 5.6(b)(i) of the Loan Agreement dated as of June 15, 1998 between the City of Hillsdale Hospital Finance Authority and Hillsdale Community Health Center, the undersigned hereby certifies that, to the best of my knowledge, no Event of Default under the Loan Agreement exists, nor has any event occurred which, with notice and/or passage of time, would constitute such an Event of Default. All capitalized terms used herein are defined in such Loan Agreement.

Included in this Municipal Secondary Market Disclosure filing are the following documents:

1. Audited financial statements prepared in accordance with GAAP by an Independent Public Accountant, in compliance with Section 5.6(a)(i) of the Loan Agreement; and
2. The Annual Report referred to in the Continuing Disclosure Agreement dated as of June 15, 1998, in accordance with Rule 15c2-12 of the Securities Exchange Commission.

The Corporation hereby appoints First River Advisory L.L.C. as the Dissemination Agent pursuant to Section 7 of the Continuing Disclosure Agreement.



Charles A. Bianchi, President

# HILLSDALE COMMUNITY HEALTH CENTER

## ANNUAL REPORT FOR THE FISCAL YEAR ENDED JUNE 30, 2006 (FY2006)

Unless otherwise noted, all data apply to the Fiscal Year Ended June 30, 2006, or are accurate as of June 30, 2006, as appropriate. OS pages refer to the Official Statement relating to the Securities, dated June 17, 1998.

### MEDICAL STAFF

<i>Active Staff Specialization [OS Page A-12]</i>					
<i>Internal Medicine</i>		<i>Surgery</i>		<i>Other</i>	
General	5	General Surgery	4	Family Practice	6
Cardiology	1	Ophthalmology	2	Obstetrics/Gynecology	2
Gastroenterology	1	Orthopedic Surgery	2	Pediatrics	2
Oncology	1	Otorhinolaryngology	1	Anesthesiology	1
Neurology	1	Podiatry	2	Emergency Medicine	2
Pulmonology	1	Urology	3	Pathology	1
Rheumatology	1	Vascular Surgery	2	Radiology	1
				Chiropractic	7
<b>Total Internal Medicine</b>	<b>11</b>	<b>Total Surgery</b>	<b>16</b>	<b>GRAND TOTAL</b>	<b>49</b>

<i>Age Distribution of the Active Staff [OS Page A-13]</i>		
<i>Age Range</i>	<i>Number of Physicians</i>	<i>Percent of Active Staff</i>
34 and under	7	14.3%
35 - 44	16	32.7%
45 - 54	21	42.9%
55 - 64	5	10.2%
65 and over	0	0.0%
TOTAL	49	
<small>Note: Column may not add to 100.0 due to rounding</small>		

<i>Active Staff Physicians, by Major Specialty [OS Page A-13]</i>				
	<i>Number</i>	<i>Median Age</i>	<i>Number Board-Certified</i>	<i>Number Board-Eligible</i>
Family Practice	6	40	6	0
Internal Medicine	11	47	10	1
Surgery	16	44	13	3
Obstetrics/Gynecology	2	52	1	1

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<i>Active Staff Physicians, by Practice Location</i> <i>[OS Page A-14]</i>	
Physicians' Office Building	11
Other City of Hillsdale Locations	21
Hospital-Based	5
<i>Subtotal, City of Hillsdale Locations</i>	37
Hudson	2
Jonesville	7
Litchfield	0
Quincy	0
Battle Creek	3
Jackson	0
Total	49
Note: During FY2002, physicians vacated the on-campus Medical Building and moved to a physician-owned Physicians' Office Building located elsewhere in Hillsdale, where they were joined by other physicians	

<i>Gross Revenue Attributable to Physician Referrals</i> <i>[OS Page A-14]</i>		
	<i>\$000 Omitted</i>	<i>Percentage</i>
Active Staff	66,979	79.9%
Physicians holding consulting or courtesy privileges, plus <i>locum tenens</i> physicians	10,230	12.2%
Unassigned Revenue	6,631	7.9%
Total Revenue	83,840	100.0%

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<i>Leading Referring Physicians</i> <i>[OS Page A-15]</i>						
<i>Rank</i>	<i>Specialty or Subspecialty</i>	<i>Age</i>	<i>Board-Certified / Eligible</i>	<i>Gross Revenue</i>	<i>Percent of Gross Revenue</i>	<i>Cumulative Percent</i>
1	Orthopedic Surgery	45	C	\$7,991,002	9.5%	9.5%
2	Orthopedic Surgery	38	C	\$6,419,723	7.7%	17.2%
3	Internal Medicine	51	C	\$5,033,300	6.0%	23.2%
4	Internal Medicine	38	C	\$3,571,639	4.3%	27.5%
5	Obstetrics/Gynecology	54	C	\$3,268,412	4.0%	31.5%
6	Gastroenterology	49	C	\$3,123,463	3.7%	35.2%
7	Family Practice	34	C	\$3,010,986	3.6%	38.8%
8	Family Practice	45	C	\$2,790,431	3.3%	42.1%
9	Family Practice	33	C	\$2,761,318	3.3%	45.4%
10	General Surgery	40	C	\$2,308,314	2.8%	48.1%
			C = Certified E = Eligible			

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

**SERVICE VOLUMES AND UTILIZATION**

<i>Historical Adult Medical/Surgical (Including CCU) Utilization (excludes newborns) [OS Page A-17]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Days in Period	365	365	366	365	365
Licensed Beds	47	47	47	47	47
Available Beds	40	40	40	40	40
Admissions	2,413	2,761	2,795	2,545	2,546
Patient Days	8,204	8,721	8,844	8,349	8,760
Average Daily Census	22.5	23.9	24.2	22.9	24.0
Average LOS	3.4	3.2	3.2	3.3	3.4
Occupancy Rate (%)*	56.2	59.7	60.4	57.2	60.0
* Based on Available Beds rather than Licensed Beds					

<i>Historical Pediatrics Utilization (excludes newborns) [OS Page A-17]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Days in Period	365	365	366	365	365
Licensed Beds	9	9	9	9	9
Available Beds	4	4	4	4	4
Admissions	86	106	144	105	123
Patient Days	176	222	312	212	262
Average Daily Census	0.5	0.6	0.9	0.6	0.7
Average LOS	2.0	2.1	2.2	2.0	2.1
Occupancy Rate (%)*	12.1	15.2	21.3	14.5	17.9
* Based on Available Beds rather than Licensed Beds					

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<b>Historical Obstetrics Utilization</b> <i>(excludes newborns)</i> <i>[OS Page A-18]</i>					
	<b>Fiscal Years Ended June 30</b>				
	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>2002</b>
Days in Period	365	365	366	365	365
Licensed Beds	9	9	9	9	9
Available Beds	8	8	8	8	8
Admissions	464	466	458	464	469
Patient Days	948	989	923	837	923
Average Daily Census	2.6	2.7	2.5	2.3	2.5
Average LOS	2.0	2.1	2.0	1.8	2.0
Occupancy Rate (%)*	32.5	33.9	31.5	28.7	31.6
* Based on Available Beds rather than Licensed Beds					

<b>Historical Acute Care Utilization</b> <i>(excludes newborns)</i> <i>[OS Page A-19]</i>					
	<b>Fiscal Years Ended June 30</b>				
	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>2002</b>
Days in Period	365	365	366	365	365
Licensed Beds	65	65	65	65	65
Available Beds	52	52	52	52	52
Admissions	2,963	3,333	3,397	3,114	3,137
Adjusted Admissions <sup>1,2</sup>	7,386	7,827	8,037	7,459	7,097
Patient Days	9,328	9,932	10,079	9,398	9,949
Average Daily Census	25.6	27.2	27.5	25.7	27.3
Average LOS	3.1	3.0	3.0	3.0	3.2
Occupancy Rate (%) <sup>3</sup>	49.1	52.3	53.0	49.5	52.4
Net Patient Revenue per Adjusted Admission <sup>1,4</sup>	\$6,157	\$5,601	\$5,139	\$5,118	\$5,019
Gross Outpatient Revenue per Adjusted Admission <sup>1,4</sup>	\$6,797	\$5,713	\$5,416	\$4,795	\$4,774
<sup>1</sup> The FY2003 figure reported in the report relating to FY2003 was erroneous; this is the correct figure <sup>2</sup> Admissions are adjusted by the percentage gross revenue attributable to outpatient services <sup>3</sup> Based on Available Beds rather than Licensed Beds <sup>4</sup> Calculated by management from the Corporation's audited financial statements and other records, using definitions published by Standard & Poor's Corporation in <i>CreditWeek Municipal</i> , October 20, 1997 and in <i>CreditWeek</i> , October 1994					

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<i>McGuire Unit Utilization</i> <i>[OS Page A-20]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Days in Period*	365	365	366	365	365
Licensed Beds	21	21	21	21	21
Patient Days	7,165	7,042	7,212	6,773	6,516
Average Daily Census	19.6	19.3	19.7	18.6	17.9
Occupancy Rate (%)	93.5	91.9	93.8	88.4	85.0

<i>Surgical Procedures</i> <i>[OS Page A-20]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Inpatient	942	1,030	966	951	933
Outpatient	2,994	2,816	2,843	2,967	2,781
Total	3,936	3,846	3,809	3,918	3,714
Percent Outpatient (%)	76.1	73.2	74.6	75.7	74.9

<i>Emergency Department Volumes</i> <i>[OS Page A-21]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Visits	30,138	29,925	30,209	27,813	29,178
Change over Previous Period (%)	0.7	(0.9)	8.6	(4.7)	6.1
Transfers to Other Hospitals	167	151	141	135	133
Transfers per Thousand ED Visits	5.5	5.0	4.7	4.9	4.6

<i>Outpatient Service Volumes</i> <i>[OS Page A-21]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Scheduled Registrations	119,136	123,236	119,130	115,381	108,673
Change over Previous Period (%)	(3.3)	3.4	3.2	6.2	4.1

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<i>Ancillary Services Provided to <u>Inpatients</u></i>					
<i>[OS Page A-22]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Laboratory <sup>1</sup>	80,544	82,045	77,155	67,126	62,754
MRI Scanning <sup>2</sup>	218	238	228	173	111
CT Scanning <sup>2</sup>	1,507	1,266	1,218	1,132	1,121
Ultrasonography <sup>2</sup>	2,388	2,617	2,536	2,327	2,429
Other Radiology <sup>2</sup>	4,801	5,171	5,110	4,944	4,802
Nuclear Medicine <sup>2</sup>	235	308	258	278	343
Electrocardiography <sup>1</sup>	4,130	4,647	4,504	4,494	4,030
Electroencephalography <sup>1</sup>	43	40	27	27	47
Cardiovascular Lab <sup>3,4</sup>	47	79	118	51	56
Physical Therapy <sup>3</sup>	1,917	2,169	2,088	2,128	1,932
Respiratory Therapy <sup>3</sup>	39,463	34,777	31,557	30,504	27,062
<sup>1</sup> Tests	<sup>2</sup> Examinations	<sup>3</sup> Procedures	<sup>4</sup> Includes stress tests, Holter monitors, vascular studies and cardiac rehabilitation		

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<i>Ancillary Services Provided to <u>Outpatients</u></i> <i>(includes ED, Home Care and McGuire Unit patients)</i> <i>[OS Page A-23]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Laboratory <sup>1</sup>	259,597	249,935	235,038	226,445	212,245
MRI Scanning <sup>2</sup>	366,646	2,370	2,127	1,866	1,757
CT Scanning <sup>2</sup>	5,365	4,246	4,230	4,034	4,064
Ultrasonography <sup>2</sup>	9,287	9,058	8,058	7,797	7,204
Other Radiology <sup>2</sup>	27,582	28,468	29,668	28,867	25,396
Nuclear Medicine <sup>2</sup>	4,677	4,303	4,449	5,959	4,946
Electrocardiography <sup>1</sup>	4,430	3,582	3,032	3,170	3,284
Electroencephalography <sup>1</sup>	128	106	108	127	94
Cardiovascular Lab <sup>3,4,5</sup>	5,078	3,921	3,910	3,772	3,679
Physical Therapy <sup>3</sup>	22,583	21,538	20,919	18,283	16,231
Respiratory Therapy <sup>3</sup>	17,172	14,981	13,138	12,367	6,903
Endoscopy <sup>3</sup>	2,461	2,391	2,273	1,651	2,052
Sleep Studies <sup>1</sup>	512	566	360	201	216
<sup>1</sup> Tests	<sup>2</sup> Examinations	<sup>3</sup> Procedures	<sup>4</sup> Includes stress tests, Holter monitors, vascular studies and cardiac rehabilitation		
<sup>5</sup> The FY2001 figure reported in the report relating to FY2001 was erroneous; this is the correct figure					
<sup>6</sup> The FY2003 and FY2002 figures reported in the report relating to those respective FYs were erroneous; these are the correct figures					

<i>Home Care Visits</i> <i>[OS Page A-23]</i>				
<i>Fiscal Years Ended June 30</i>				
<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
9,765	10,711	10,876	9,552	10,381

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

**FINANCIAL INFORMATION**

<i>McGuire Unit Payor Mix (expressed as percentages of patient-days) [OS Page A-32]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Medicare	63.5%	51.8%	50.3%	55.6%	63.3%
Medicaid	33.1%	37.8%	33.1%	16.9%	13.2%
Private Pay and Commercial Insurance	3.4%	10.4%	16.6%	27.5%	23.5%
TOTALS	100.0%	100.0%	100.0%	100.0%	100.0%

<i>Payor Mix [OS Page A-33]</i>										
	<i>Fiscal Years Ended June 30</i>									
	<i>By Gross Revenue</i>					<i>By Acute Care Patient-Days</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Medicare	45.0	43.0	40.1	42.7	41.9	60.2	56.4	55.7	57.0	58.1
Medicaid	12.0	11.0	12.0	9.2	9.0	12.1	11.4	11.9	8.5	8.8
Blue Cross	23.0	25.0	25.8	25.6	25.3	14.1	16.9	16.9	17.6	17.9
Commercial Insurance	16.0	17.0	18.4	19.0	20.5	10.2	11.7	12.2	13.6	12.5
Self-Pay	4.0	4.0	3.7	3.5	3.3	3.4	3.6	3.3	3.3	2.7
TOTALS	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

<i>Gross Patient Revenue by Service [OS Page A-33]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Inpatient	35.7%	38.5%	38.8%	38.8%	39.6%
Outpatient	58.2%	55.4%	54.1%	54.2%	53.3%
McGuire Unit	4.4%	4.0%	4.4%	4.4%	4.6%
Home Care	1.7%	2.1%	2.7%	2.6%	2.5%
TOTALS	100.0%	100.0%	100.0%	100.0%	100.0%

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<i>Summary of Statements of Operations – Unrestricted</i> ( <i>\$000s omitted</i> ) ( <i>OS Page A-34</i> )					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004<sup>1</sup></i>	<i>2003</i>	<i>2002</i>
Net Patient Service Revenue	45,477	42,876	41,300	38,178	35,038
Other Operating Revenue	1,016	<u>550</u>	<u>416</u>	<u>601</u>	<u>581</u>
Total Operating Revenue	46,493	43,426	41,717	38,779	35,619
Depreciation Expense	2,211	1,799	1,683	1,629	1,481
Interest Expense	720	648	614	632	635
Bad Debt Expense	2,545	2,209	3,384	2,612	2,354
Other Operating Expenses	<u>39,157</u>	<u>36,887</u>	<u>34,396</u>	<u>31,452</u>	<u>29,078</u>
Total Operating Expenses	44,634	41,543	40,077	36,324	33,548
Income from Operations	1,859	1,883	1,640	2,455	2,071
Net Nonoperating (Losses)	(695)	<u>(931)</u>	<u>(682)</u>	<u>(982)</u>	<u>(855)</u>
Revenue and Gains in Excess of Expenses	1,164	952	957	1,473	1,216
Depreciation included in Net Nonoperating (Losses)	0	0	0	0	26
Net Income Available for Debt Service (EBIDA) <sup>2</sup>	4,095	3,399	3,255	3,734	3,358
Capital Expenditures	2,367	3,578	4,399	1,607	1,483
<p>1 Certain FY2004 amounts have been changed to reflect statement of operations reclassifications reported in connection with the FY2005 audited financial statements</p> <p>2 Calculated by management from the Corporation's audited financial statements, using definitions published by Standard &amp; Poor's Corporation in <i>CreditWeek Municipal</i>, October 20, 1997</p>					

<i>Profitability Ratios</i> ( <i>OS Page A-35</i> )					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Debt Service Coverage Ratio <sup>1,2</sup>	2.30	1.94	1.80	2.43	2.15
Excess Margin <sup>2</sup>	2.54%	2.09%	2.33%	3.90%	3.50%
Operating Margin <sup>2</sup>	4.00%	4.15%	3.93%	6.33%	5.81%
<p><sup>1</sup> Based on FY2006 Annual Debt Service on the Series 1998 Bonds and other Long-Term Debt of \$1,783,151. This figure includes \$516,948 of annual debt service that in the form of a Guaranty of the debt of a limited liability company (the LLC) that owns the Physicians' Office Building (the POB), which Guaranty is subordinate to the several, though not joint, guaranties of the physicians who are members of the LLC and who occupy the POB. If the annual debt service relating to this Guaranty were not included in the calculation of FY2006 Annual Debt Service, the Debt Service Coverage Ratio would have been 3.23 in FY2006.</p> <p><sup>2</sup> Calculated by management from the Corporation's audited financial statements, using definitions published by Standard &amp; Poor's Corporation in <i>CreditWeek Municipal</i>, October 20, 1997 and in <i>CreditWeek</i>, October 1994</p>					

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<i>Cost and Productivity Measures</i> <i>[OS Page A-35]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Total FTEs	295.0	296.2	292.4	287.6	285.0
FTEs per Adjusted Admission <sup>1</sup>	0.040	0.042	0.036	0.039	0.012
FTEs per Adjusted Occupied Bed <sup>1</sup>	4.3	4.9	4.4	4.4	4.5
Adjusted Acute Care Patient-Days <sup>1</sup>	24,960	24,720	24,361	24,159	23,327
Paid-hours per Adjusted Patient-Day <sup>1</sup>	25.7	24.9	25.0	25.5	25.1
McGuire Unit Paid Hours per Patient-Day <sup>1</sup>	4.8	5.0	4.7	6.0	6.0
Capital Expense / Total Expenses <sup>1</sup>	6.6%	5.8%	5.7%	6.2%	6.3%
Bad Debt Expense / Operating Revenue <sup>1</sup>	5.5%	7.2%	8.1%	6.7%	6.6%

<sup>1</sup> Calculated by management from the Corporation's audited financial statements and other records, using definitions published by Standard & Poor's Corporation in *CreditWeek Municipal*, October 20, 1997

<i>Balance Sheet Summary</i> <i>(\$000s omitted)</i> <i>[OS Page A-36]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Cash and Temporary Investments <sup>1</sup>	4,719	4,655	3,740	5,490	2,648
Net Patient Accounts Receivable	7,908	6,261	6,480	5,043	5,443
Other Current Assets	1,781	<u>2,067</u>	<u>1,694</u>	<u>1,422</u>	<u>1,985</u>
Total Current Assets	14,409	12,982	11,913	11,955	10,076
Non-Current Cash and Investments (unrestricted) <sup>1</sup>	8,973	7,752	7,419	5,708	5,658
Property and Equipment	16,154	16,246	14,355	12,273	12,213
Other Assets	4,266	<u>4,846</u>	<u>3,996</u>	<u>2,763</u>	<u>3,326</u>
Total Assets	43,801	41,827	37,683	32,700	31,273
Current Liabilities	9,964	9,237	8,244	5,423	5,412
Long-Term Debt	13,791	13,909	11,858	11,170	11,460
Net Assets	<u>20,045</u>	<u>18,681</u>	<u>17,582</u>	<u>16,106</u>	<u>14,401</u>
Total	43,801	41,827	37,683	32,700	31,273

<sup>1</sup> Used in Days' Cash on Hand, Cash-to-Debt and Quick Ratio calculations

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<i>Liquidity Ratios</i> <i>[OS Page A-37]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Current Ratio <sup>1</sup>	1.45	1.41	1.45	2.20	1.86
Quick Ratio <sup>1</sup>	2.17	2.02	2.14	2.99	2.54
Days in Patient Accounts Receivable <sup>1</sup>	63.5	52.1	57.3	48.2	56.7
Days Cash on Hand <sup>1</sup>	117.8	111.2	106.1	117.8	94.6
Cash-to-Debt <sup>1,2</sup>	94.2%	84.9%	90.8%	97.1%	70.5%

<sup>1</sup> Calculated by management from the Corporation's audited financial statements and other records, using definitions published by Standard & Poor's Corporation in *CreditWeek Municipal*, October 20, 1997 and *CreditWeek*, October 1994, and by Moody's Investors Service in *Health Care Medians*, June 1996

<sup>2</sup> The denominator of this ratio includes the current portion of long-term debt

<i>Case-Mix Indices</i> <i>[OS Page A-38]</i>					
	<i>Fiscal Years Ended June 30</i>				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Medicare	1.3052	1.2807	1.2052	1.2650	1.1740
Medicaid	0.6213	0.6053	0.6472	0.7204	0.6171
Blue Cross	0.9104	0.8234	0.8028	0.7846	0.8598

**MUNICIPAL SECONDARY MARKET DISCLOSURE**  
**City of Hillsdale Hospital Finance Authority / Hillsdale Community Health Center**  
**Fiscal Year Ended June 30, 2006**

<i>Top Ten DRGs [OS Page A-39]</i>					
<i>DRG</i>	<i>Description</i>	<i>Discharges</i>	<i>Percent</i>	<i>Cumulative Percent</i>	<i>Average LOS</i>
391	Normal Newborn	342	11.6%	11.6%	1.7
373	Vaginal Delivery, without Complications	275	9.3%	20.9%	1.5
88	Chronic Obstructive Pulmonary Disease	138	4.7%	25.6%	4.0
89	Simple Pneumonia and Pleurisy, > Age 17, with Complications	128	4.3%	29.9%	4.3
544	Major Joint Replacement or Reattachment of Lower Extremity	123	4.2%	34.1%	3.3
127	Heart Failure and Shock	113	3.8%	37.9%	3.8
371	Cesarean Section, without Complications	82	2.8%	40.7%	3.3
132	Atherosclerosis with Complications	64	2.2%	42.9%	2.0
209	Major Joint and Limb Reattachment Procedures, Lower Extremity	54	1.8%	44.7%	3.0
174	Gastrointestinal Hemorrhage with Complications	53	1.8%	46.5%	2.8

# **Hillsdale Community Health Center**

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**Financial Report**  
**June 30, 2006**

# Hillsdale Community Health Center

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## Independent Auditor's Report

To the Board of Trustees  
Hillsdale Community Health Center

We have audited the accompanying balance sheet of Hillsdale Community Health Center (the "Hospital") as of June 30, 2006 and 2005 and the related statements of operations, changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits 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 referred to above present fairly, in all material respects, the financial position of Hillsdale Community Health Center at June 30, 2006 and 2005 and the results of its 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*

August 25, 2006

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# Hillsdale Community Health Center

## Balance Sheet

	<u>June 30, 2006</u>	<u>June 30, 2005</u>
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 4,719,436	\$ 4,654,679
Accounts receivable (Note 2)	7,907,763	6,261,166
Other current assets	1,781,401	2,066,569
Total current assets	14,408,600	12,982,414
Investments (Note 3)	10,702,200	9,423,963
Property and Equipment (Note 4)	16,153,703	16,246,221
Other Assets (Note 5)	2,536,221	3,174,065
Total assets	<u>\$ 43,800,724</u>	<u>\$ 41,826,663</u>
<b>Liabilities and Net Assets</b>		
<b>Current Liabilities</b>		
Current portion of long-term debt (Note 7)	\$ 742,687	\$ 698,530
Accounts payable	2,493,254	3,498,989
Estimated third-party payor settlements (Note 6)	2,650,000	1,790,000
Accrued liabilities and other	4,078,366	3,249,065
Total current liabilities	9,964,307	9,236,584
Long-term Debt (Note 7)	13,791,334	13,909,032
Total liabilities	23,755,641	23,145,616
<b>Net Assets</b>		
Unrestricted	19,933,565	18,599,045
Temporarily restricted (Note 9)	111,518	82,002
Total net assets	20,045,083	18,681,047
Total liabilities and net assets	<u>\$ 43,800,724</u>	<u>\$ 41,826,663</u>

# Hillsdale Community Health Center

## Statement of Operations

	Year Ended	
	June 30, 2006	June 30, 2005
<b>Unrestricted Revenue, Gains, and Other Support</b>		
Net patient service revenue	\$ 45,476,848	\$ 42,875,767
Other	1,015,832	550,081
Unrestricted revenue, gains, and other support	46,492,680	43,425,848
<b>Expenses</b>		
Salaries and wages	15,482,836	14,799,181
Employee benefits and payroll taxes	4,089,050	3,819,130
Operating supplies and expenses	19,585,585	18,269,313
Depreciation and amortization	2,210,938	1,799,329
Provision for bad debts	2,545,282	2,208,718
Interest expense	720,334	648,239
Total expenses	44,634,025	41,543,910
<b>Operating Income</b>	1,858,655	1,881,938
<b>Other Income (Expense)</b>		
Investment income (Note 3)	741,072	522,686
Contributions	27,727	90,100
Other expenses	-	(1,493)
Rent income	12,884	9,980
Physician recruitment expenses	(1,476,457)	(1,594,027)
Total other expense	(694,774)	(972,754)
<b>Excess of Revenue Over Expenses</b>	1,163,881	909,184
<b>Change in Unrealized Gains on Investments (Note 3)</b>	50,095	45,892
<b>Net Assets Released from Restriction</b>	120,544	160,342
<b>Increase in Unrestricted Net Assets</b>	<b>\$ 1,334,520</b>	<b>\$ 1,115,418</b>

# Hillsdale Community Health Center

## Statement of Changes in Net Assets

	Year Ended June 30	
	2006	2005
<b>Unrestricted Net Assets</b>		
Excess of revenue over expenses	\$ 1,163,881	\$ 909,184
Change in unrealized gains and losses on investments (Note 3)	50,095	45,892
Net assets released from restriction	<u>120,544</u>	<u>160,342</u>
<b>Increase in Unrestricted Net Assets</b>	1,334,520	1,115,418
<b>Temporarily Restricted Net Assets</b>		
Restricted contributions	150,060	144,200
Net assets released from restriction	<u>(120,544)</u>	<u>(160,342)</u>
<b>Increase (Decrease) in Temporarily Restricted Net Assets</b>	<u>29,516</u>	<u>(16,142)</u>
<b>Increase in Net Assets</b>	1,364,036	1,099,276
<b>Net Assets - Beginning of year</b>	<u>18,681,047</u>	<u>17,581,771</u>
<b>Net Assets - End of year</b>	<u><b>\$ 20,045,083</b></u>	<u><b>\$ 18,681,047</b></u>

# Hillsdale Community Health Center

## Statement of Cash Flows

	Year Ended	
	June 30, 2006	June 30, 2005
<b>Cash Flows from Operating Activities</b>		
Cash received from patients and third-party payors	\$ 45,922,777	\$ 43,998,539
Cash paid to suppliers and employees	(42,998,979)	(39,787,844)
Investment income received	489,707	377,684
Interest paid	(720,334)	(648,239)
Cash received from other operating income	1,018,345	648,668
Net cash provided by operating activities	3,711,516	4,588,808
<b>Cash Flows from Investing Activities</b>		
Purchase of property and equipment	(2,366,871)	(3,577,725)
Proceeds from sale of property and equipment	42,500	-
Purchase of investments	(976,777)	(541,840)
Proceeds from sale of joint ventures	167,972	-
Cash proceeds to assets limited as to use	-	(82,186)
Advances to physicians	(596,517)	(2,308,286)
Proceeds from land contracts	6,415	479,417
Net cash used in investing activities	(3,723,278)	(6,030,620)
<b>Cash Flows from Financing Activities</b>		
Proceeds from issuance of debt obligations	659,388	2,753,686
Principal payments of debt obligations	(732,929)	(541,250)
Proceeds from restricted contributions	150,060	144,200
Net cash provided by financing activities	76,519	2,356,636
<b>Net Increase in Cash and Cash Equivalents</b>	64,757	914,824
<b>Cash and Cash Equivalents - Beginning of year</b>	4,654,679	3,739,855
<b>Cash and Cash Equivalents - End of year</b>	<b>\$ 4,719,436</b>	<b>\$ 4,654,679</b>

# Hillsdale Community Health Center

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## Notes to Financial Statements June 30, 2006 and 2005

### **Note I - Nature of Business and Significant Accounting Policies**

Hillsdale Community Health Center (the "Hospital") operates a short-term, acute care facility including a skilled-nursing unit providing inpatient and outpatient health care services to the Hillsdale, Michigan area.

**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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

**Patient Accounts Receivable** - Accounts receivable for patients are stated at net amounts. An allowance for uncollectible accounts is established on an aggregate basis by using historical write-off rate factors applied to unpaid accounts stratified by payor and number of days the accounts are outstanding. Uncollectible amounts are written off against the allowance for doubtful accounts in the period they are determined to be uncollectible. An allowance for contractual adjustments is also established on an aggregate basis and is computed based on agreements with third-party payors that provide payment to the Hospital at amounts different than the established charges. Contractual adjustments are written off against the allowance for contractual adjustments in the period payment is received.

**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 income from operations unless the income or loss is restricted by donor or law. Unrealized gains or losses on investments are excluded from income from operations.

**Joint Affiliations** - A joint affiliation was established with Borgess Hospital of Kalamazoo. The Hospital was engaged in a joint venture with Borgess Hospital as 50-50 owners of Jonesville Clinic. Jonesville Clinic was sold during the year ended June 30, 2006.

**Property and Equipment** - Property and equipment amounts are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method.

**Bond Issue Costs** - Bond issue costs are included in other assets (see Note 5). These costs are being amortized over the life of the debt. Amortization expense was \$15,269 for the years ended June 30, 2006 and 2005.

# Hillsdale Community Health Center

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## Notes to Financial Statements June 30, 2006 and 2005

### **Note I - Nature of Business and Significant Accounting Policies (Continued)**

**Self-insurance** - The Hospital acts as a self-insurer for the health insurance benefits up to limits as provided for an agreement with its insurance plan administrator. The cost of claims, including an estimate for unprocessed claims, is recognized as an operating expense in the year of the incident. A cost-to-charge ratio of approximately .50 is applied to all domestic claims and recorded as health care benefits along with foreign claims paid. The balance was adjusted to net patient revenue.

**Net Patient Service Revenue** - The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, 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. Retroactively calculated adjustments arising under reimbursement agreements with third-party payors 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. Final determination of compliance of such laws and regulations is subject to future government review and interpretation. Violations may result in significant regulatory action including fines, penalties, and exclusions from the Medicare and Medicaid programs.

**Charity Care** - The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Services provided on a charity basis during 2006 and 2005 amounted to \$396,047 and \$258,013, respectively.

**Excess of Revenue Over Expenses** - The statement of operations includes excess of revenue over expenses. Changes in unrestricted net assets, which are excluded from excess of revenue over expenses, consistent with industry practice, include net assets released from restrictions for the acquisition of long-lived assets, permanent transfers of assets to and from affiliates for other than goods and services, minimum pension liability adjustment, and changes in unrealized gains and losses on investments.

# Hillsdale Community Health Center

## Notes to Financial Statements June 30, 2006 and 2005

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

**Contributions** - The Hospital reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of changes in net assets as net assets released from restrictions.

The Hospital reports gifts of property and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Hospital reports the expiration of donor restrictions when the assets are placed in service.

**Tax Status** - The Hospital and its subsidiaries are nonprofit, tax-exempt organizations and, accordingly, no tax provision is reflected in the financial statements.

**Reclassifications** - Certain amounts in the Hospital's 2005 financial statements have been reclassified to conform with the presentation in the Hospital's 2006 financial statements.

### Note 2 - Patient Accounts Receivable

The details of patient accounts receivable are as follows:

	<u>2006</u>	<u>2005</u>
Patient accounts receivable	\$ 18,155,763	\$ 16,320,166
Less:		
Allowance for uncollectible accounts	(2,334,000)	(2,100,000)
Allowance for contractual adjustments and interim payment advances	<u>(7,914,000)</u>	<u>(7,959,000)</u>
Net patient accounts receivable	<u>\$ 7,907,763</u>	<u>\$ 6,261,166</u>

# Hillsdale Community Health Center

## Notes to Financial Statements June 30, 2006 and 2005

### Note 2 - Patient Accounts Receivable (Continued)

The Hospital is located in Hillsdale, Michigan. The Hospital grants credit without collateral to patients, most of whom are local residents and are insured under third-party payor agreements. The composition of receivables from patients and third-party payors was as follows:

	Percentage	
	2006	2005
Medicare	31	34
Blue Cross/Blue Shield of Michigan	21	21
Medicaid	7	8
Commercial insurance and HMOs	17	22
Self-pay	24	15
Total	100	100

### Note 3 - Investments

The details of investments are as follows:

	2006	2005
Assets limited as to use:		
Professional and general liability self insurance	\$ 559,783	\$ 571,000
Debt service reserve and payment funds	957,714	957,714
Donor-restricted assets	111,518	82,002
Deferred compensation	100,545	60,839
Other investments	8,972,640	7,752,408
Total	\$ 10,702,200	\$ 9,423,963
Cash and cash equivalents	\$ 2,613,476	\$ 2,178,893
Corporate bonds	1,052,227	1,039,169
Mutual funds - Equity	1,403,319	60,839
Governmental bonds	1,588,848	1,482,789
Corporate stocks	4,044,330	4,662,273
Total	\$ 10,702,200	\$ 9,423,963

# Hillsdale Community Health Center

## Notes to Financial Statements June 30, 2006 and 2005

### Note 3 - Investments (Continued)

The details of investment income are as follows:

	<u>2006</u>	<u>2005</u>
Interest and dividend income	\$ 489,707	\$ 377,684
Net realized gains on investments	<u>251,365</u>	<u>145,002</u>
Subtotal	741,072	522,686
Net unrealized gains and losses on investments	<u>50,095</u>	<u>45,892</u>
Total	<u>\$ 791,167</u>	<u>\$ 568,578</u>

### Note 4 - Property and Equipment

Cost of property, plant, and equipment and depreciable lives are summarized as follows:

	<u>2006</u>	<u>2005</u>	<u>Depreciable Life - Years</u>
Land	\$ 103,162	\$ 103,162	-
Land improvements	272,885	272,885	5
Buildings	21,433,331	20,599,131	5-50
Equipment	13,720,433	12,175,904	5-10
Capital leases	827,797	827,797	5-10
Construction in progress	<u>233,067</u>	<u>1,168,746</u>	
Total cost	36,590,675	35,147,625	
Accumulated depreciation	<u>(20,436,972)</u>	<u>(18,901,404)</u>	
Total property and equipment	<u>\$ 16,153,703</u>	<u>\$ 16,246,221</u>	

At June 30, 2006, the Hospital had commitments related to the construction of a 10-bed mental health addition. The mental health addition has a projected cost to complete of approximately \$2,300,000. The project will be completed utilizing funds from a capital campaign and issuance of a HELP loan.

# Hillsdale Community Health Center

## Notes to Financial Statements June 30, 2006 and 2005

### Note 5 - Other Assets

The details of other assets are as follows:

	<u>2006</u>	<u>2005</u>
Physician advances - Net of current portion of \$1,000,000 and \$1,300,000 for the years ended June 30, 2006 and 2005, respectively	\$ 1,701,219	\$ 2,393,458
Land contract receivables	494,596	256,961
Jonesville joint venture	-	167,972
Bond issuance costs	260,714	275,982
Deposits	<u>79,692</u>	<u>79,692</u>
Total other assets	<u>\$ 2,536,221</u>	<u>\$ 3,174,065</u>

### Note 6 - Cost Report Settlements

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Approximately 65 percent of the Hospital's net patient service revenue is received from the Medicare, Medicaid, and Blue Cross/Blue Shield of Michigan programs. The Hospital has agreements with third-party payors that provide for reimbursement at amounts different from established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Hospital's established rates for services and amounts reimbursed by third-party payors. A summary of the basis of reimbursement with these third-party payors is as follows:

- **Medicare** - Inpatient and 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 based on clinical, diagnostic, and other factors. Inpatient psychiatric and substance abuse services are reimbursed at cost subject to a per-case limit. Outpatient and home care services related to Medicare beneficiaries are reimbursed based on a prospectively determined amount per episode of care.
- **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. Outpatient and physician services are reimbursed 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. Outpatient services are reimbursed on a fee-for-service and percentage-of-charge basis.

# Hillsdale Community Health Center

## Notes to Financial Statements June 30, 2006 and 2005

### Note 7 - Long-term Debt

A summary of long-term debt and capital lease obligations at June 30, 2006 and 2005 is as follows:

	<u>2006</u>	<u>2005</u>
Series 1998 Bonds payable to the City of Hillsdale Hospital Finance Authority, interest at 4.90% to 5.75%, annual principal payments ranging from \$300,000 in 2007 to \$795,000 in 2026	\$ 10,156,667	\$ 10,445,000
Michigan State Hospital Finance Authority, Healthcare Equipment and Loan Program (HELP), Series C, payable in monthly payments of \$32,285, plus interest at 3.85%, balance due in November 2008	4,218,318	3,942,510
Note payable, interest at 8.75%, payable in monthly installments of \$607, collateralized by vehicle purchase	-	5,300
Note payable, no interest due, payable in monthly installments of \$371, collateralized by vehicle purchase	2,968	7,790
Note payable, interest at 7.00% adjusting every five years to 1% over prime, payable in monthly installments of \$1,011, collateralized by property purchased	108,101	112,500
Capital lease obligation, interest at 8.92%, payable in monthly installments totaling \$4,222, collateralized by leased equipment	<u>47,967</u>	<u>94,462</u>
Total	14,534,021	14,607,562
Less current portion	<u>742,687</u>	<u>698,530</u>
Long-term portion	<u>\$ 13,791,334</u>	<u>\$ 13,909,032</u>

Currently, the HELP loan is secured with a letter of credit up to \$5,000,000, expiring in November 2008, and the Hospital pays 1.4 percent on the outstanding principal balance of the loan. The additional percentage is included in interest expense during the year.

# Hillsdale Community Health Center

## Notes to Financial Statements June 30, 2006 and 2005

### Note 7 - Long-term Debt (Continued)

Principal payments on notes payable and lease payments on capital leases over the next five years and in aggregate as of June 30, 2006 are as follows:

<u>Years Ending June 30</u>	<u>Long-term Debt</u>	<u>Capital Lease Obligations</u>
2007	\$ 695,105	\$ 50,652
2008	707,478	8,442
2009	3,778,899	-
2010	350,815	-
2011	371,235	-
Thereafter	<u>8,582,522</u>	<u>-</u>
Subtotal	14,486,054	59,094
Less amount representing interest under capital lease obligations	<u>-</u>	<u>(11,127)</u>
Total	<u>\$ 14,486,054</u>	<u>\$ 47,967</u>

### Note 8 - Operating Leases

The Hospital is obligated under certain operating leases, primarily for facilities, office equipment, and automobiles. Total rent expense under these leases was \$462,720 and \$154,240 for the years ended June 30, 2006 and 2005, respectively.

Future minimum rental commitments are as follows:

<u>Years Ending June 30</u>	<u>Amount</u>
2007	\$ 462,720
2008	462,720
2009	462,720
2010	<u>308,480</u>
Total	<u>\$ 1,696,640</u>

# Hillsdale Community Health Center

## Notes to Financial Statements June 30, 2006 and 2005

### Note 9 - Temporarily Restricted Net Assets

Temporarily restricted net assets are available for the following purposes at June 30, 2006 and 2005:

	2006	2005
Health care programs	\$ 32,450	\$ 28,990
Purchase of equipment and expansion	79,068	53,012
Total temporarily restricted	<u>\$ 111,518</u>	<u>\$ 82,002</u>

### Note 10 - Defined Contribution Pension Plan

The Hospital has established a defined contribution retirement plan covering substantially all employees. The Hospital contributed 3 percent of eligible wages, resulting in pension expense of approximately \$398,000 and \$310,000 for the years ended June 30, 2006 and 2005, respectively.

### Note 11 - Professional Liability

Effective June 1, 2004, the Hospital is self-insured with respect to medical malpractice risk. The Hospital has purchased self-insurance retention insurance for claims greater than \$1 million per occurrence. Losses from asserted claims and from unasserted claims identified under the Hospital's incident reporting system are accrued based on estimates that incorporate the Hospital's past experience, as well as other considerations, including the nature of each claim or incident and relevant trend factors.

The Hospital has established a trust fund for the payment of medical malpractice claim settlements. An actuary has been retained to assist the Hospital with determining amounts to be deposited in the trust fund. Professional liability investments will be established in an amount equal to the provision for medical malpractice.

The Hospital has been named in several malpractice lawsuits. At this time, it is premature to evaluate the likely outcome and amount of settlement, if any. Management intends to vigorously defend these suits and does not expect an unfavorable impact.

# Hillsdale Community Health Center

## Notes to Financial Statements June 30, 2006 and 2005

### Note 12 - Commitments and Contingencies

The Hospital has entered into agreements with newly recruited physicians that include provisions for income guarantees ranging from one to three years. The maximum amounts of such guarantees entered into during the years ended June 30, 2006 and 2005 total approximately \$150,000 and \$500,000, respectively. The Hospital has recorded a liability for future payments totaling approximately \$241,000 and \$845,000 for the years ended June 30, 2006 and 2005, respectively. The amounts advanced to the physicians depend on income levels earned in their practices. Per contractual agreements, these advances are amortized over two to six years if the physician remains practicing in the area; otherwise, the unamortized balance can be collected by the Hospital. Amortization of these advances, which is included in physician recruitment expenses, has approximated \$1,289,000 and \$1,445,000 for 2006 and 2005, respectively.

The Hospital has entered into guarantee agreements with two financial institutions. The Hospital has guaranteed the obligations of an unrelated party to construct a medical office building up to \$4.8 million. In the event that the Hospital is required to make payments under this guarantee, the Hospital could seek to recover those amounts; however, the Hospital does not have specific recourse or collateral rights in connection with the guarantee. The Hospital is unaware of any default or potential default resulting in any Hospital liability. The balance of the mortgage outstanding at June 30, 2006 was approximately \$5.1 million.

### Note 13 - Functional Expenses

The Hospital provides general health care services to residents within its geographic area, including residential care, assisted living, and independent living. Expenses related to providing these services for the years ended June 30, 2006 and 2005 are as follows.

	<u>2006</u>	<u>2005</u>
Health care services	\$ 39,285,570	\$ 35,898,636
General and administrative	<u>5,348,455</u>	<u>5,645,274</u>
Total	<u>\$ 44,634,025</u>	<u>\$ 41,543,910</u>

# Hillsdale Community Health Center

## Notes to Financial Statements June 30, 2006 and 2005

### Note 14 - Cash Flows

A reconciliation of increase in net assets to net cash from operating activities is as follows:

	<u>2006</u>	<u>2005</u>
Increase in net assets	\$ 1,364,036	\$ 1,099,276
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation	2,210,938	1,799,329
Realized and unrealized net gains and losses on investments	(301,460)	(190,894)
Gain on the sale of fixed assets	(38,100)	-
Bad debt expense	2,545,282	2,208,718
Temporarily restricted donations	(150,060)	(144,200)
Amortization of bond costs	15,269	15,269
Amortization of physician advances	1,288,756	1,444,986
(Increase) decrease in assets:		
Accounts receivable	(4,191,879)	(1,990,339)
Other current assets	285,168	(372,689)
Increase (decrease) in liabilities:		
Accounts payable	(1,005,735)	455,006
Accrued liabilities	829,301	324,346
Cost report settlements payable	860,000	(60,000)
Net cash provided by operating activities	<u>\$ 3,711,516</u>	<u>\$ 4,588,808</u>

Significant noncash financing and investing activities for the years ended June 30, 2006 and 2005 are as follows:

During the years ended June 30, 2006 and 2005, the Hospital sold assets on land contracts. The total land contract receivables were \$494,596 and \$256,961 at June 30, 2006 and 2005, respectively. During the year ended June 30, 2005, the Hospital purchased property, issuing a note payable for \$112,500.