

APPENDIX A

Information Concerning the Obligated Group

Certain statements included or incorporated by reference in this Appendix A constitute projections or estimates of future events, generally known as forward-looking statements. These statements are generally identifiable by the terminology used such as “plan,” “expect,” “estimate,” “budget” or other similar words. The achievement of certain results or other expectations contained in such forward-looking statements involves known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. The Obligated Group does not plan to issue any updates or revisions to those forward-looking statements if or when changes in its expectations, or events, conditions or circumstances on which such statements are based occur. This Appendix A should be read together with the section of the Official Statement entitled, “BONDHOLDERS’ RISKS.”

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OTSEGO MEMORIAL HOSPITAL ASSOCIATION

INTRODUCTION

Otsego Memorial Hospital Association (the “Corporation”) is a non-profit corporation incorporated under the laws of the State of Michigan. The Corporation is a tax-exempt charitable organization under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the “Code”), and exempt from federal income taxation under Section 501(a) of the Code. The Corporation owns and operates a general acute care hospital (the “Hospital”) and related health care facilities, all located in the City of Gaylord, Michigan (the “City”), together with physician practices located in the City and surrounding areas. The Corporation, together with the Otsego Memorial Hospital Foundation (the “Foundation”), are the initial Members of the Obligated Group. The Foundation is also a tax-exempt charitable organization under Section 501(c)(3) of the Code, and exempt from federal income taxation under Section 501(a) of the Code. The Foundation conducts fund-raising and other activities to support the Corporation.

The Hospital serves residents of and vacationers in Otsego County (the “County”) and parts of six adjacent counties. The Hospital is licensed for 53 acute-care beds and 34 skilled nursing beds housed in a building originally constructed in 1973 (the “Hospital Facility”). The campus on which the Hospital Facility is situated (the “Campus”) also includes McReynolds Hall, the location of the skilled nursing unit, and two other buildings, the professional medical building (the “PMB”) and the Hazel Shipp Building (the “HSB”). Together, the Hospital Facility and McReynolds Hall encompass 105,000 square feet, the PMB another 36,000 square feet, and the HSB another 8,000 square feet.

Gaylord is the largest municipality in the County, and is the seat of the County government. The City is located in the center of the County, approximately 54 miles south of the Mackinac Bridge, the connector between Michigan’s lower and upper peninsulas. The City is situated at Exit 282 of Interstate 75 (“I-75”). The Hospital is the only hospital in the County. Because of the Hospital Facility’s remote location, the Corporation is a federally-designated Sole Community Hospital (“SCH”) (see “*OTSEGO MEMORIAL HOSPITAL ASSOCIATION*” / “*Financial Information*” / “*Third-Party Reimbursement Methodologies and Sources of Revenue*” / “*Supplemental Medicare Reimbursement*” in this Appendix A).

HISTORY, FACILITIES AND SERVICES

The Corporation was formed in 1946, and commenced operations in 1952. The original hospital building was replaced by the Hospital Facility in 1973. Since then, the Hospital Facility has undergone extensive expansion and/or renovation 1979, 1981, 1987, 1990 and 1996. McReynolds Hall was constructed in 1960, and medical office buildings were added to the campus in 1972, 1978 (the HSB) and 2002 (the PMB). The building constructed in 1972 has since been demolished.

It has been necessary for the Corporation to expand its facilities and services to meet continually increasing demand, a function of the population growth of the County and the

surrounding area. At the same time, the Corporation has consistently scored highly in clinical outcome, patient satisfaction and financial performance indicators. The Corporation has been named one of The 100 Top Hospitals®: National Benchmarks for Success in 1999, 2000 and 2002 by Solucient LLC.

THE HOSPITAL FACILITY

The Hospital Facility’s current bed capacity is as follows:

<i>Bed Capacity</i>		
	<i>Licensed</i>	<i>Available</i>
Adult and Pediatric Medical/Surgical	53	28
Intensive Care Unit	0	4
Obstetrics/Gynecology	0	7
Total Acute Care	53	39
Skilled Nursing (McReynolds Hall)	34	34
TOTAL	87	73

Hospital licensure in Michigan permits the use of beds licensed as Medical/Surgical for Intensive Care and Obstetrics/Gynecology (and other) purposes. Because the Corporation continually adjusts staffing levels to correspond to inpatient volumes and acuity, the number of “available” beds varies from day to day. The Hospital does not maintain distinct-part rehabilitation or psychiatric units.

OFF-CAMPUS FACILITIES

In addition to the Hospital Facility and other on-campus facilities, the Corporation owns and operates the MedCare Walk-In Clinic (“MedCare”), located in a commercial area on the south side of the City. The Corporation also owns several small buildings surrounding the Campus, including one which houses Shared Care, LLC (“Shared Care”), an affiliated durable medical equipment (“DME”) company . The Corporation rents lower level of the Gaylord Family Practice Building, located east of downtown Gaylord. This space is used for the Otsego Diagnostic and Specialty Clinic (the “D&S Clinic”), a practice site for visiting specialists. The Hospital provides laboratory and radiology services there as well.

SERVICES

The Corporation offers most of the facilities and services typical of Sole Community Hospitals of its size. The following are certain of the more unique or specialized services provided.

ONCOLOGY CLINIC

CARDIAC AND PULMONARY SERVICES

- Cardio-Pulmonary Diagnostics
- Cardiac rehabilitation (Phases I, II and III)
- Sleep laboratory

IMAGING SERVICES

- General radiography/fluoroscopy
- Ultrasound
- Computed Tomography (CT) scans
- Mammography
- Nuclear Medicine
- Magnetic Resonance Imaging (MRI) scans (provided in a mobile unit that is on-site ten days per month)

REHABILITATION SERVICES

- Physical therapy
- Speech therapy
- Occupational therapy
- Hand therapy
- Wound and ostomy care

PHYSICIANS

To ensure an adequate supply of qualified physicians, the Corporation began to employ physicians in 1995. The Corporation now employs 24 physicians, twelve of whom are primary care physicians.

DURABLE MEDICAL EQUIPMENT AND HOME RESPIRATORY THERAPY

Shared Care is a Medicare-certified, JCAHO-accredited durable medical equipment (“DME”) company whose sole corporate member is the Corporation. Shared Care sells, rents and services various types of medical equipment for home use.

DIALYSIS

Dialysis services are provided locally by Dialysis Services of Gaylord, Inc. (“DSG”). The Corporation is one of two equal members of DSG, along with Gratiot Community Hospital, a non-profit community hospital located in Alma, Michigan.

ORGANIZATIONAL INFORMATION

The Corporation has three affiliated entities, the scopes of services delivered by two of which are outlined above:

- Shared Care, a Michigan limited liability company of which the Corporation is the sole member; and
- DSG, a Michigan non-profit corporation, of which the Corporation is one of two equal members.

The Corporation controls the Foundation through the appointment of its current directors and right to approve newly-elected directors.

The Corporation and the Foundation are the initial Members of an Obligated Group created pursuant to a Master Trust Indenture dated as of November 1, 2004 (the “Master Indenture”) among the Corporation, as Obligated Group Agent, and Wells Fargo Bank, N.A., as Master Trustee. There is no present plan or intention for any other entity to become an Obligated Group Member.

The Corporation has no governance or management affiliation, nor any formal clinical linkages, with any unrelated health care provider organizations. The Corporation has several informal clinical arrangements with other hospitals and provider organizations.

ACCOUNTING CONVENTIONS AND INFORMATION PRESENTATION

The Corporation has designated a calendar (January 1 to December 31) fiscal year (“FY”). All quantitative data are presented by FY, unless otherwise specifically indicated. For financial reporting purposes, for FY2003 and interim periods ended during FY2004, Share Care is considered to be a subsidiary (the “Subsidiary”) of the Corporation. Prior to FY2003, Shared Care was included on financial statements as an equity investment. According to the Corporation’s independent auditors, Shared Care’s financial position at the ends of FYs prior to FY2003 was not material to the overall consolidated financial statements of the Corporation plus Shared Care. In FY2003, the Corporation’s assets and revenue were 99 percent or more of the respective consolidated amounts.

For consistency with other periods, FY2003 information contained in the tables entitled “Summary of Statements of Operations” and “Balance Sheet Summary” relates to the Corporation alone.

Consolidated financial statements of the Corporation and Subsidiary, audited for FY2003, and financial statements of the Corporation, audited for the four FYs ended December 31, 2002 (the “Audited Financial Statements”), are contained in Appendix B to this Official Statement. FY2003 Audited Financial Statements include consolidating balance sheets and consolidating statements of operations in which information relating to the Corporation and the Subsidiary are presented separately. Internally-prepared consolidated financial statements of the Corporation and Subsidiary for the nine-month interim periods ended September 30, 2004 and September 30, 2003 are contained in Appendix C to this Official Statement.

Historically, the Foundation has not produced audited financial statements. Beginning with FY2004, however, the financial statements of the Foundation will be consolidated with those of the Corporation. A brief description of the Foundation’s financial position may be found in “*OTSEGO MEMORIAL HOSPITAL FOUNDATION*” / “*Financial Condition*” in this Appendix A.

Unless otherwise indicated, the sources for all information presented in this Appendix A are the records of the Corporation or the Foundation.

Gratiot Community Hospital, the other equal member of DSG, is not an Obligated Group Member and is, therefore, not liable for any amounts due under Note No. 1 or any Notes issued under the Master Indenture. The Corporation’s shares of profits and losses arising from DSG corresponds to its ownership interest, and are recorded as non-operating revenue on the Corporation’s statements of operations.

GOVERNANCE

The Corporation is organized as a membership corporation. Any individual can become a member of the Corporation by paying a nominal fee.

The Corporation is governed by a ten-member Board of Directors (the “Corporation Board”). Except for the Chief of the Medical Staff, these Directors are elected at annual meetings of Corporation members each September. Directors serve for staggered terms of three years, and may serve a maximum of three consecutive terms. The Chief of the Medical Staff, as designated by the medical staff is a voting *ex officio* member who serves two-year terms. The Corporation Board holds an annual meeting in September plus eleven other meetings each year.

COMMITTEES

The Corporation Board is responsible for setting policy for the Corporation. The Corporation Board has five standing committees: the Executive Committee, the Finance Committee, the Medical Staff Credentials Committee, the Medical Provider Recruitment Committee and the Performance Improvement Council.

DIRECTORS

The following ten individuals currently serve as Directors.

<i>Corporation Board of Directors</i>			
<i>Name</i>	<i>Year First Elected</i>	<i>Year Term Expires</i>	<i>Occupation / Affiliation</i>
Joseph A. Anders, D.O.	<i>Ex-Officio</i>		<i>Chief of the Medical Staff</i> , internist employed by the Corporation
William Boyce	2002	2005	<i>Sales Representative</i> , Pfizer, Inc. (pharmaceuticals)
R. David Briney, <i>Secretary</i>	1999	2005	Private investor
Patricia A. Duley, M.D.	2004	2007	<i>Internist (retired)</i>
Paul Hartmann	2003	2006	<i>Customer Service Manager</i> , CPI Products, Inc. (manufacturers of machine tools)
Chester G. Janssens	2004	2007	<i>President (retired)</i> , Crusader Engine Division of Thermo Electron Corporation
Lori Reichard	2000	2006	<i>Vice President</i> , Fifth Third Bank
Mary Sanders	2003	2006	<i>Township Supervisor</i> , Hayes Township
Dave Shuster, <i>Vice President</i>	1999	2005	<i>Airport Manager</i> , Otsego County Airport
Robert T. Westerman, II, Esq.	2001	2007	<i>Member</i> , Plunkett & Cooney, P.C. (Attorneys)

The two most recently elected Directors, Dr. Duley and Mr. Janssens, will begin their terms with the October 2004 Corporation Board meeting. The four Corporation Board officers, President, Vice President, Secretary and Treasurer, are scheduled to be elected by the Directors at the October 2004 Corporation Board meeting. Mr. Shuster is completing a term as Vice President, and Mr. Briney as Secretary. The Directors completing their terms as President and Treasurer could not be re-elected because of term limits.

The newly-elected Treasurer will become the Chairman of the Finance Committee. Other members of the Finance Committee, as well as those of other committees, will be designated at the October 2004 Corporation Board meeting. The Executive Committee is comprised of the four Corporation Board officers.

CERTAIN RELATIONSHIPS

The Corporation's by-laws contain a provision which requires Directors to disclose their conflicts and dualities of interest, and to refrain from voting on such matters in which they (or their

families) have pecuniary interests. The Corporation purchases certain goods and services from firms with which Directors are affiliated. The Corporation believes that such business arrangements are comparable to those available from firms that have no affiliation with Directors. The Corporation advises that Lori Reichard is an officer of Fifth Third Bank (“Fifth Third”) which has delivered a commitment to purchase the Series 2005 Bonds.

The Corporation maintains certain business relationships with physicians which are believed to be in compliance with all applicable statutes and regulations. As a condition of its commitment to purchase the Series 2005 Bonds, Fifth Third will require that it serve as the Corporation’s principal depository institution. As described elsewhere herein, Gross Revenue of the Obligated Group, including money held in the Corporation’s accounts at Fifth Third, are pledged as Collateral to secure all Obligations Outstanding under the Master Indenture. In connection with the issuance and purchase of the Series 2005 Bonds, Fifth Third will agree to waive any right of set-off it may have against the deposit accounts of the Corporation held at Fifth Third relating to amounts due on or under the Series 2005 Bonds.

MANAGEMENT

Administrative direction and oversight of the Corporation has been delegated to a management team consisting of a Chief Executive Office and four Vice Presidents. Biographical summaries of the Corporation’s administrative team follow.

THOMAS R. LEMON, CHIEF EXECUTIVE OFFICER, AGE 43. Mr. Lemon joined the Corporation in 1999 as its Chief Executive Officer. During his tenure, Mr. Lemon has managed the development of the PMB and the MedCare building, the recruitment of 22 physicians, and the significant growth of the Corporation’s revenue and market shares. The Corporation has been named one of The 100 Top Hospitals®: National Benchmarks for Success in 1999, 2000 and 2002 by Solucient LLC.

Prior to joining the Corporation, Mr. Lemon held chief executive officer positions at three other rural hospitals:

- Rochelle Community Hospital, Rochelle, Illinois;
- Burnett Medical Center, Grantsburg, Wisconsin (while employed by Brim Healthcare, Inc., a hospital management company); and
- Visitors Hospital (Buchanan, Michigan (while employed by New Medico Associates, Inc., an investor-owned hospital system).

Under Mr. Lemon’s leadership, these organizations experienced improved productivity, increased operating margins and enhanced physician complements. In addition, Mr. Lemon led the development of a facility master plan and a major construction and renovation project at Burnett Medical Center. Mr. Lemon began his hospital management career at Vice President, Business Development, at LaPorte Hospital, LaPorte, Indiana.

Mr. Lemon earned his masters degree in healthcare administration at DePaul University, Chicago, Illinois, and his bachelors degree at the University of North Dakota, Grand Forks. He

holds *Diplomate* status in the American College of Healthcare Executives (“ACHE”), and is a member of ACHE’s Regents Advisory Council. Mr. Lemon has been active in small and rural hospital councils of state hospital associations in Michigan, Illinois and Wisconsin. He is active in several civic organizations.

RICHARD L. THOMAS, VICE PRESIDENT, FINANCE, AGE 59. Mr. Thomas has served as the Corporation’s Chief Financial Officer since 1975, except for a three-year period between 1989 and 1992 during which he served as Chief Financial Officer of War Memorial Hospital, Sault Ste. Marie, Michigan. During his combined tenure with the Corporation, Mr. Thomas has been integrally involved in the planning and financing of several facilities improvement projects, the implementation of new programs, the conversion to new information systems, and the introduction of new payment systems, including the Medicare Prospective Payment System. Prior to joining the Corporation, Mr. Thomas served as Assistant Controller at West Branch (Michigan) Regional Medical Center.

Mr. Thomas holds a bachelor’s degree in accounting from Central Michigan University, Mount Pleasant. Long active in the Healthcare Financial Management Association (“HFMA”), Mr. Thomas has served terms as Chapter President and in other leadership positions. He is a recipient of the Muncie Gold Award, granted by national HFMA, and the Ernest L. Laetz Award, conferred by the Michigan chapters.

SUZANNE CLEERE, VICE PRESIDENT, PATIENT CARE SERVICES, AGE 52. Ms. Cleere joined the Corporation in her present capacity in 2001. She is responsible for all clinical services delivered by the Hospital.

Prior to joining the Corporation, Ms. Cleere held the position of Director, Birthing Services and Surgical Services at Lapeer (Michigan) Regional Hospital. Her responsibilities in this capacity encompassed the management of nine cost centers and 110 full-time equivalent (“FTE”) staff at a 222-bed community hospital. Her accomplishments included the implementation of new staffing models and the coordination of facility renovations. Earlier in her career, Ms. Cleere served as Vice President for Women and Children Services at Garden City (Michigan) Hospital. In addition to overall responsibility for obstetrics, pediatrics and related services, Ms. Cleere directed the case management, utilization review, quality assurance, social work, education and research functions. Prior to joining the Garden City Hospital, Ms. Cleere held obstetrical nurse management positions at Grace Hospital and Sinai Hospital, both located in Detroit.

Ms. Cleere is a member of several professional organizations, including the ACHE and the Michigan Organization of Nurse Executives. Ms. Cleere was conferred dual Masters Degrees in Nursing and Business at Madonna University, Livonia, Michigan. She holds a Bachelors Degree in Nursing from University of Detroit Mercy. Ms. Cleere serves as an adjunct faculty member at Davenport University in the area of health services management, and was previously a member of the clinical faculty at the Michigan State University, School of Nursing.

RALPH PARDO, VICE PRESIDENT, SUPPORT SERVICES, AGE 55. Associated with the Corporation since 1991, Mr. Pardo’s role involves the management of all support services at the Hospital. He also facilitated the construction of all renovation projects at the Hospital Facility, and the

construction of the PMB. Mr. Pardo will also serve as the “Owner’s Representative” in connection with the Improvement Project.

Prior to joining the Corporation, Mr. Pardo served in several capacities at North Oakland Medical Center, Pontiac, Michigan, since his military discharge in 1971. He directed the construction of a \$38 million replacement hospital in the mid-1970s. Mr. Pardo is a former Chairman of the HSS / Amerinet Group Purchasing Organization.

VIVIAN M. KASPRZAK, FACMPE, VICE PRESIDENT OF PHYSICIAN SERVICES, AGE 57. In this capacity, Ms. Kasprzak is responsible for the management of the Corporation’s physician practices, MedCare and certain other outpatient services. She joined the Corporation in 2002.

Ms. Kasprzak has held medical group management positions since 1971. Most recently, she was the Director of the Memorial Medical Group, a network of multiple physician practices owned by Memorial Health System, South Bend, Indiana. Her role included recruitment of physicians, integration of physician practices into the system network, and the development of new facilities. Earlier positions included that of Assistant Administrator for a 35-physician, \$35 million, multi-specialty group practice located in Michigan City, Indiana, and Director of an 11-site, 45-physician network affiliated with Lakeland Regional Health System, Niles, Michigan.

Ms. Kasprzak was conferred her bachelors degree by Indiana University at South Bend. She also graduated from the Southwestern Michigan College School of Nursing, and is licensed as a registered nurse. Ms. Kasprzak is a Fellow of the American College of Medical Practice Executives. She is also active in the Medical Group Management Association, (“MGMA”), having held leadership positions at the state, regional and national level. Ms. Kasprzak is currently a member of MGMA’s National Executive Board of Directors, and is scheduled to commence a three-year term as Chairperson of MGMA’s Finance and Audit Committee in 2005.

EMPLOYEES AND LABOR RELATIONS

For the nine-month period ended September 30, 2004, the Corporation averaged 543 employees, equating to 424.3 paid FTEs. Management considers its relationship with employees to be satisfactory.

LABOR ORGANIZATION

None of the Corporation’s employees have elected to be represented by a labor union. There have been no recent attempts by any union to organize any of the Corporation’s employees. The Corporation is unaware of any other formal efforts by unions to hold a certification election.

LABOR SUPPLY

The Corporation has not experienced any material difficulty in recent years recruiting and retaining nurses, therapists and technicians. Occasionally, the Corporation has encountered difficulty recruiting operating room technicians and respiratory therapists. The ability of the Hospital to diagnose and treat patients has not been materially disrupted due to these vacant positions.

The Corporation has taken certain measures to alleviate present and possible labor shortages in the future. During FY2003, the Corporation completed a comprehensive review of its job classification system to ensure consistency of job descriptions, wage grades and wage scales. This process was extended to ensure that the Corporation's wage scales continue meet or exceed statewide medians. A consultant has been engaged to develop a multi-media recruiting tool that will be designed to highlight the Corporation's culture and advantages as an employer.

TEMPORARY STAFFING

The Corporation's expenses relating to temporary staffing were less than \$200,000 in FY2003. Corporation management expects that this issue will continue to affect the Corporation's financial performance in only an immaterial manner.

MILITARY OBLIGATIONS

None of the Corporation's employees as of September 30, 2004 are members of the military reserves. Management is not aware of any employee who could otherwise be called for active military service.

EMPLOYED PHYSICIANS

As of September 30, 2004, the Corporation employed 24 physicians (see "*OTSEGO MEMORIAL HOSPITAL ASSOCIATION*" / "*Medical Staff*" / "*The Active Staff*" / "*Employed Physicians*" in this Appendix A).

CONTRACTED SERVICES

The Corporation does not contract with any unrelated parties for the management of any clinical or support services.

ORGANIZATIONAL DEVELOPMENT

Earlier in FY2004, the Corporation completed the "Leadership IQ" program to improve the management skills of its department managers. This program commenced with a multidimensional assessment of managers' current skills and mindset. Using the assessment results to determine managers' most significant challenges, the training phase of this program focused on the following skills, individualized according to the manager's needs:

- consensus-building;
- negotiation;
- strategic positioning;
- partnering with customers;
- expense control;

- personnel development; and
- management of change.

The Leadership IQ program concluded with the implementation of a training program for new managers.

LICENSES, ACCREDITATIONS, APPROVALS AND MEMBERSHIPS

The Michigan Department of Consumer & Industry Services (“MDCIS”), as successor to the Michigan Department of Community Health (“MDCH”) no longer conducts a separate licensure survey, relying instead on the survey conducted by the Joint Commission on the Accreditation of Healthcare Organizations (“JCAHO”). The United States Center for Medicare and Medicaid Services (“CMS”), formerly the Health Care Financing Administration, recognizes JCAHO accreditation for participation in the Medicare program. In August 2003, the Hospital’s accreditation was renewed for another three-year period, the maximum awarded.

The Corporation holds separate licenses for the Hospital and for McReynolds Hall. In August 1997, MDCIS issued non-expiring licenses which need not be renewed. Certain other facilities and services are licensed by various federal and state authorities.

<i>Licensure of Clinical and Support Functions</i>			
<i>Hospital Department</i>	<i>Licensing Agency</i>	<i>Function</i>	<i>License Expiration</i>
Laboratory	CMS	Clinical Laboratory	January 2005
Radiology	U.S. Nuclear Regulatory Commission	Radioisotopes	March 2005
Radiology	MDCH Radiation Safety Section	X-ray Unit	September 2005
Radiology	MDCH Radiation Safety Section	X-ray Unit ¹	May 2005
Radiology	MDCH Radiation Safety Section	Mammography Unit	August 2005
Emergency	Federal Communications Commission	Radio Station	May 2014
Pharmacy	Michigan Board of Pharmacy	Pharmacy	June 2006
Dietary	Michigan Department of Agriculture	Food Service	April 2005

¹ Located at the D&S Clinic

Certain clinical functions maintain separate accreditations:

- American College of Radiology – Ultrasound, Mammography
- American College of Pathology – Clinical Laboratory

The Corporation maintains the following memberships:

- American Hospital Association
- Michigan Health and Hospital Association
- Voluntary Hospitals of America (“VHA”)
- Michigan Peer Review Organization

QUALITY MEASURES

The Corporation has engaged Professional Research Consultants (“PRC”) to conduct satisfaction surveys of patients treated at the Hospital or by the Corporation’s employed physicians, and of residents of McReynolds Hall. In 2002, the most recent year for which PRC survey results are available, the Hospital earned the following five awards:

- Doctors’ Explanation of Treatment and Tests - Inpatient Top Performer
- Inpatient Services - 5 Star Award
- Outpatient Surgery - 5 Star Award
- Emergency Department - 4 Star Award
- Outpatient Services - 4 Star Award

According to PRC, the “Inpatient Top Performer” means that the Hospital achieved the best patient satisfaction score in this category among all inpatient facilities surveyed by PRC. PRC’s “5 Star Awards” and “4 Star Awards” recognize organizations which achieve scores in the top ten percentile of those surveyed, and in the 75th through 89th percentile, respectively.

COMPLIANCE

The Corporation established a Corporate Compliance Program (the “Compliance Program”) in 1995. The Compliance Program is designed to ensure that the Corporation’s billing practices and procedures comply with all relevant laws, rules and regulations applicable to Medicare and Medicaid beneficiaries. Corporation personnel perform quarterly audits of coding and billing, supplemented by periodic reviews by consultants. Corporation management has no reason to believe that the Corporation is out of compliance in any material respect in a manner that would have a material adverse impact on its financial condition.

EDUCATIONAL AFFILIATIONS

The Corporation maintains affiliations with the following educational institutions, all of which are located in Michigan:

Ferris State University (Big Rapids)	Radiology technicians
North Central Michigan College (Petoskey)	Nursing
Kirtland Community College (Roscommon)	Nursing

All of these colleges participate in The University Center at Gaylord (see “*OTSEGO MEMORIAL HOSPITAL ASSOCIATION*” / “*Market Area, Competition and Market Share*” / *Market Area*” in this Appendix A).

MEDICAL STAFF

As of September 30, 2004, the Hospital’s active medical staff numbered 48 physicians, podiatrists and dentists (the “Active Staff”). Referrals attributable to the Active Staff generated substantially all of the Corporation’s net patient service revenue in FY2003.

CHARACTERISTICS OF THE ACTIVE STAFF

Certain characteristics of the Active Staff as of that date are tabulated below.

<i>Active Staff Physicians</i>					
		<i>Number</i>	<i>OMH Employees</i>	<i>Median Age</i>	<i>Number Board-Certified</i>
Family Practice		6	4	45	5
<i>Medicine</i>	Internal Medicine	5	4		
	Geriatrics	1	1		
	Oncology	1	0		
Subtotal, Medicine		7	5	52	6
<i>Surgery</i>	General	1	0		
	Ophthalmology	1	0		
	Oral Surgery	2	0		
	Orthopedics	4	0		
	Otolaryngology	1	1		
	Podiatry	1	0		
	Urology	1	0		
Subtotal, Surgery		11	1	54	9
Obstetrics/Gynecology		2	0	41	1
Pediatrics		3	3	45	3
Dentistry		3	0		1
Emergency Medicine		9	9		7
Anesthesiology		2	2		1
Pathology		3	0		3
Radiology		2	0		2
TOTAL / COMPOSITE		48	24	48	38

Another 33 physicians, most of whom are specialists, hold courtesy privileges. Among the physicians holding courtesy privileges are eight family practitioners and one pediatrician who maintain office practices in the Market Area (as hereinafter defined), and who routinely refer patients to the Hospital for diagnostic and treatment services. Their patients who are admitted as Hospital inpatients are managed by one of the Corporation's employed internists in their role as

hospitalists. The 38 members of the Active Staff who are Board-Certified represent 79 percent of the Active Staff.

AGE DISTRIBUTION

The median age of the Active Staff is 48. The distribution of the Active Staff physicians’ ages is set forth in the following table.

<i>Age Distribution of the Active Staff</i>		
<i>Age Range</i>	<i>Number of Physicians</i>	<i>Percent of Active Staff</i>
34 and under	3	6.3%
35 - 44	11	22.9%
45 - 54	20	41.7%
55 - 64	13	27.1%
65 and over	1	2.1%
TOTAL	48	
Note: Column may not add to 100.0 due to rounding		

The one member of the Active Staff over age 65 is a dentist. An internist who is currently age 63 has indicated that he plans to retire in three to four years.

EMPLOYED PHYSICIANS

Thirteen of the Corporation’s 24 employed physicians are organized as the OMH Medical Group. Offices of the following groups are situated in the PMB:

- Family Practice group 4 physicians
- Internal Medicine group 5 physicians
- Pediatrics group 3 physicians

The office of an employed otolaryngologist (ear, nose and throat surgeon) is also located in the PMB. The other 11 employed physicians are the two anesthesiologists and the nine emergency medicine physicians, two of whom staff MedCare. One of the two physicians who staffs MedCare also serves as the Director of Occupational Medicine. The Corporation also employs several mid-level practitioners to supplement the staffs of the Emergency Department (the “ED”), MedCare and the Family Practice group. An additional family practitioner is scheduled to commence employment in February 2005.

MULTIPLE AFFILIATIONS

Except for the pathologists and, after December 1, 2004, the radiologists (see “*OTSEGO MEMORIAL HOSPITAL ASSOCIATION*” / “*Medical Staff*” / “*The Active Staff*” / “*Certain Specialties*”), only two of the Active Staff members hold admitting privileges at any other hospital. The urologist holds admitting privileges at Community Memorial Hospital in Cheboygan, and the ophthalmologist performs procedures at several smaller hospitals in northern Michigan.

CERTAIN SPECIALTIES

The Active Staff includes a full complement of hospital-based specialists such as emergency medicine physicians, anesthesiologists, radiologists and pathologists. The emergency medicine physicians and anesthesiologists are Corporation employees. Anesthesiology coverage by employed physicians is supplemented by two certified registered nurse anesthetists. The Corporation contracts with Northern Pathology Associates, P.C. for pathology coverage. This group of three pathologists also serves Northern Michigan Hospital (“NMH”), located in Petoskey. Corporation management is satisfied with this arrangement. The Corporation has notified its present group of radiologists that its current contract will terminate on December 1, 2004. The Corporation has reached an agreement with Northern Imaging Associates, the radiology group that serves NMH, to commence providing radiology services at the Hospital on December 1, 2004.

The Hospital’s Active Staff is supplemented by visiting specialists, who are not counted among the 48 members of the Active Staff. Two groups of cardiologists, a group of gastroenterologists, a group of sleep medicine specialists and other visiting specialists hold office hours in the City regularly. These visiting specialists do not typically admit inpatients to the Hospital, but refer their patients to the Hospital for ancillary services such as laboratory and radiology.

Prior to FY2003, the four-physician Orthopedic Surgery group had maintained an office in Grayling, Michigan, in addition to its office adjacent to the Campus. Patients seen at the Grayling office were routinely referred to Mercy Hospital Grayling for surgery. During FY2002, the group discontinued its Grayling office, and consolidated its practice at the Gaylord office. Since then, referrals for surgery were directed predominantly to the Hospital. This change was a major factor in the service volume increases experienced by the Corporation between FY2002 and FY2003, and in market share increases (see “*OTSEGO MEMORIAL HOSPITAL ASSOCIATION*” / “*Market Area, Competition and Market Share*” / “*Market Shares*” in this Appendix A).

The internist who subspecializes in geriatrics, a Corporation employee, is scheduled to become medical director of McReynolds Hall in November 2004. He will succeed a physician who is not a member of the Active Staff.

REFERRAL PATTERNS

The following table details the top ten referring physicians, measured by gross patient service revenue, during FY2003.

<i>Leading Referring Physicians, FY2003</i>						
<i>Rank</i>	<i>Specialty or Subspecialty</i>	<i>Age</i>	<i>OMH Employee</i>	<i>Gross Patient Service Revenue</i>	<i>Percent of Gross Patient Service Revenue</i>	<i>Cumulative Percent</i>
1	Orthopedic Surgery	43		4,863,530	8.7%	8.7%
2	Orthopedic Surgery	54		4,163,004	7.5%	16.2%
3	Orthopedic Surgery	57		2,826,063	5.1%	21.3%
4	Internal Medicine	44	✓	2,704,895	4.9%	26.1%
5	Orthopedic Surgery	46		2,440,519	4.4%	30.5%
6	General Surgery	51		2,351,046	4.2%	34.7%
7	Internal Medicine	49	✓	2,006,012	3.6%	38.3%
8	Family Practice	56		1,673,075	3.0%	41.3%
9	Emergency Medicine	40	✓	1,528,432	2.7%	44.1%
10	Internal Medicine	55	✓	1,457,173	2.6%	46.7%

The median age of these physicians is 50. All but one are Board-Certified. The four orthopedic surgeons comprise a single group practice. Since the end of FY2003, the family practitioner ranked eighth has largely discontinued his office practice, and now concentrates on administering to residents of area nursing homes, for some of which he serves as medical director.

The three internists serve as hospitalists in addition to their office practices. A certain amount of the revenue assigned to these physicians is attributable to referrals for inpatient admissions from family practitioners who are not members of the Active Staff. These family practitioners maintain active office practices, but request that hospitalists treat their hospitalized patients. As a result of these arrangements, the concentration of gross revenue among the leading referring physicians is greater than would have been the case had the revenue attributed to these inpatient admissions been credited to the family practitioners.

RECENT DEVELOPMENTS AND PHYSICIAN RECRUITING

Recent changes in Active Staff membership is tabulated below.

<i>Changes in Active Staff Membership</i>			
	<i>Additions</i>	<i>Deletions</i>	<i>Count</i>
At December 31, 1998			29
During FY1999	9	3	35
During FY2000	8	4	39
During FY2001	9	8	40
During FY2002	12	12	40
During FY2003	13	1	52
Through August 2004	8	12	48
Total additions / deletions	59	40	

Certain of the additions to the Active Staff were direct replacements for physicians who had recently departed. There has been little or no gap in coverage in connection with most of these replacements.

So far in FY2004, the following physicians have become members of the Active Staff:

- one family practitioner;
- the internist who subspecializes in geriatrics;
- the otolaryngologist; and
- two emergency medicine physicians, one of whom staffs MedCare.

All of these physicians are employed by the Corporation.

During FY2002, several family practitioners relinquished their Active Staff privileges in order to focus on their office practices. These are the family practitioners referred to above, under the caption "Referral Patterns." These family practitioners still maintain active practices in the Market Area, and refer patients to the Hospital for diagnostic and treatment services. Also during FY2002, a group of radiologists were added to the Active Staff, but left within that FY. Similarly, in FY2004, three physicians joined the Active Staff to cover the ED, but departed later in that FY.

Among the physicians who joined the Active Staff in 2003 is a family practitioner who joined an existing private practice in Lewiston, a town located southeast of Gaylord. This physician is not employed by the Corporation.

RECRUITING PRIORITIES

The Medical Provider Recruitment Committee of the Corporation Board establishes physician recruiting priorities. It conducts a needs assessment approximately every 18 months, the most recent being in the summer of 2003. The top priority identified at this time was the addition of a second general surgeon who would replace a general surgeon who departed in April 2004. Other recruiting priorities include an internist, a neurologist and a psychiatrist. The Corporation plans to partner with Alpena General Hospital, which maintains an inpatient psychiatric unit, to recruit the psychiatrist.

The Corporation has been successful in recruiting a family practitioner, an internist and an otolaryngologist, all of whom commenced employment since July 2004. Another family practitioner is scheduled to commence practice in February 2005. The Corporation employs all of these physicians, a strategy that is expected to continue.

The County is designated as a “Health Professional Shortage Area” and a “Medically Underserved Population” by the U.S. Department of Health and Human Services. This designation enables the Corporation to recruit foreign physicians who qualify for “J-1” visas. However, this program has been used only once in recent years, and is expected to have only limited utility in the future.

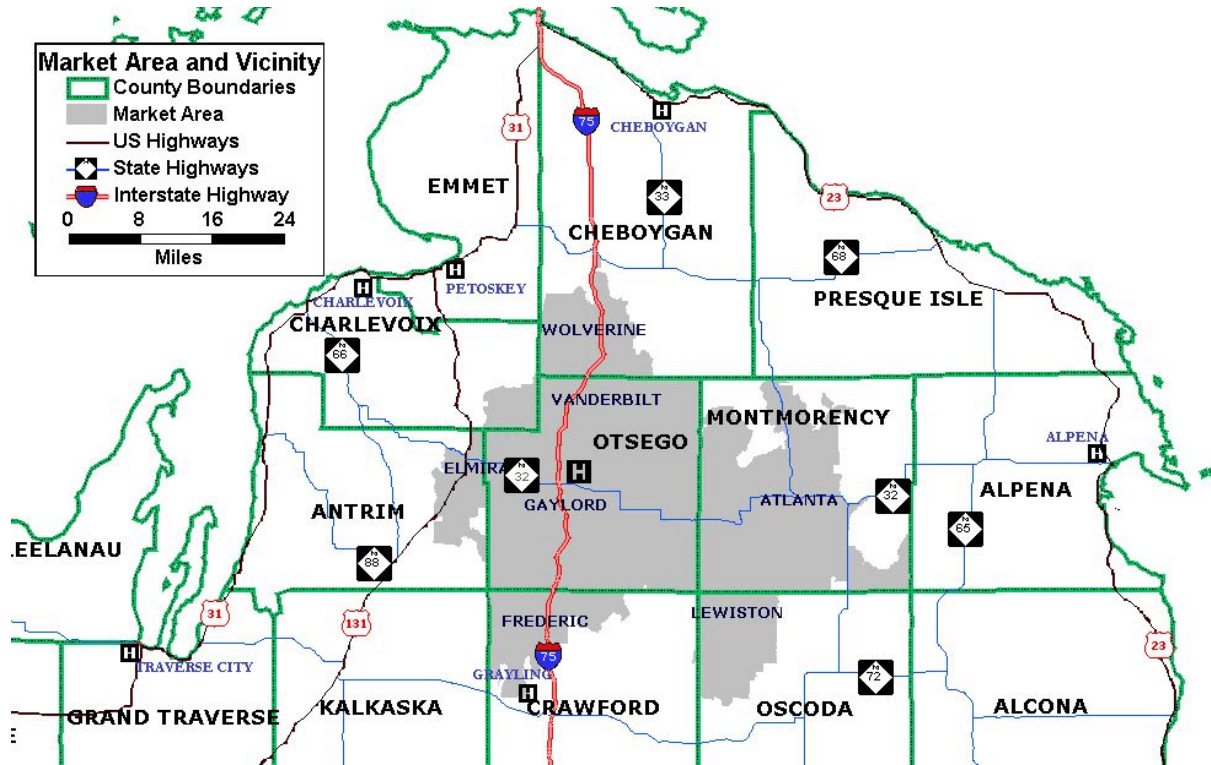
MARKET AREA, COMPETITION AND MARKET SHARE

MARKET AREA

The Hospital’s market area (the “Market Area”) is defined as eight ZIP codes which encompass the County and parts of six neighboring counties. The Market Area is rural in nature, with most economic activity occurring in Gaylord and vicinity. The Market Area is a major four-season tourist destination in Michigan, featuring golf, skiing, snowmobiling, hunting, fishing and canoeing. Approximately 180,000 acres of public-access land is available for hunting and other outdoor activities. In the 1960s, Gaylord adopted an “Alpine Village” theme as an additional attraction for tourists. According to the local chamber of commerce, the County attracts over 400,000 visitors annually.

Golf is a major industry in the Market Area, and is promoted by the local tourism bureau as the “Gaylord Golf Mecca.” There are numerous golf resorts and golf courses located in the Market Area, some of which are cited among the “best-in-class” by leading golf magazines. In 2003, spending by golfers on greens fees, cart rentals, driving range fees, and food and beverages, and at pro shops totaled over \$18 million. Close to 3,000 area residents are employed at golf complexes or in the related hospitality trade.

A map of the Market Area and vicinity appears below.



The table below sets forth certain population figures for the County, for the Market Area as a whole, and statewide.

<i>Population Data</i>				
	<i>Census</i>		<i>Estimated</i>	<i>Projected</i>
	<i>1990</i>	<i>2000</i>	<i>2004</i>	<i>2009</i>
Population Count				
County	17,957	23,301	26,481	28,468
Market Area		36,666	38,713	41,383
State of Michigan	9,295,287	9,938,444	10,109,429	10,305,664
Change over Prior Period				
County		29.8%	13.6%	7.5%
Market Area			5.6%	6.9%
State of Michigan		6.9%	1.7%	1.9%
Source: U.S. Census Bureau, Claritas Inc.				

Population of both the County and the Market Area has increased, and is projected to increase, at rates significantly in excess of statewide growth rates. The County’s growth rate between 2000 and 2003 was the 11th greatest among Michigan’s 83 counties.

A list of the ten leading non-governmental employers follows.

<i>Leading Non-Governmental Employers in Otsego County</i>				
<i>Rank</i>	<i>Organization</i>	<i>Sector¹</i>	<i>Product(s) / Service(s)</i>	<i>Local Employment</i>
1	Otsego Memorial Hospital	S	Hospital	500
2	Treetop Resort	S	Golf and ski resort	400
3	Reptron Electronics	M	Printed circuit boards	300
4	Georgia-Pacific	M	Particleboard and wood flooring	252
5	Cooper-Standard Automotive	M	Adhesives and sealants	250
5	Tandem Transport	S	Long-distance trucking	250
7	Wal-Mart	S	Discount department store	220
8	Home Depot	S	Home center store	200
8	Otsego Club & Resort	S	Golf resort	200
10	H & H Tube & Manufacturing	M	Steel pipe and tubing	150
10	Unipro Unlimited	M	Tubing	150

¹ M = Manufacturing Sector; S = Service Sector
Sources: Harris InfoSource database, accessed via the Internet on September 28, 2004

Employees of the largest non-governmental employers in the County are all covered by health insurance, principally Blue Cross and PPOM, a preferred provider organization (“PPO”).

Because of its central location in northern Michigan and growing population, the City has become a retail hub. Wal-Mart, Home Depot, Lowe’s and other national retailers have opened stores in the City within the past several years.

Historical unemployment rates for the City, the County and the Market Area, together with comparable State and national rates, are presented in the table below.

<i>Unemployment Rates, Annual or Year-to-Date Averages (not seasonally adjusted)</i>				
<i>Year</i>	<i>City</i>	<i>County</i>	<i>State</i>	<i>U.S.</i>
August 2004	4.1%	6.9%	6.9%	5.7%
2003	4.9%	8.2%	7.3%	6.0%
2002	4.2%	7.1%	6.2%	5.8%
2001	3.7%	5.9%	5.3%	4.7%
2000	2.6%	4.4%	3.5%	4.0%
1999	2.8%	4.7%	3.8%	4.2%
Sources: Michigan Department of Labor and Economic Growth / Employment Security Agency / Office of Labor Market Information, as posted on the Internet				

Economic activity in the Market Area is supported by The University Center at Gaylord (the “University Center”) a consortium of eight colleges and universities, including the three with which the Corporation maintains educational affiliations, plus Michigan State University, Central Michigan University and three others. The mission of the University Center is to facilitate the delivery of quality, state-of-the-art education and training that is responsive to personal growth and business needs throughout the County and the surrounding area. These educational institutions offer associate, undergraduate and advanced degrees, career enrichment and skill certification programs at a site in the City. The City was selected as the site for the University Center because of its central location in northern Michigan and accessibility to I-75.

COMPETING HOSPITALS

The Corporation operates the only hospital located in the County and in the Market Area. Certain information regarding the Hospital's competitors ("Competing Hospitals") is tabulated below.

<i>Competing Hospitals</i>							
<i>Formal Name</i>	<i>Short Name</i>	<i>City</i>	<i>Miles from the Hospital</i>	<i>Direction</i>	<i>Staffed Beds¹</i>	<i>Annual Admissions¹</i>	<i>Annual Expenses¹</i>
Otsego Memorial Hospital	Hospital	Gaylord			53	1,916	33,999
Mercy Hospital Grayling	Mercy	Grayling	28	South	36	Not reported	Not reported
Northern Michigan Hospital	NMH	Petoskey	37	NW	219	Not reported	Not reported
Charlevoix Hospital	Charlevoix	Charlevoix	43	NW	33	1,514	20,006
Community Memorial Hosp.	CMH	Cheboygan	53	North	42	2,281	29,692
Alpena General Hospital	Alpena	Alpena	62	East	124	5,891	75,281
Munson Medical Center	Munson	Traverse City	69	SW	368	18,610	239,677

¹ Source: *The AHA Guide to the Health Care Field, 2004 edition*. Data relate to a recent 12-month period. Annual expenses data omit \$000s.

None of the Competing Hospitals are designated as Critical Access Hospitals by CMS. Most Market Area residents in need of specialized tertiary care are admitted to NMH, followed by Munson.

The Corporation has experienced little competition from physicians establishing outpatient hospital service ventures. The one exception is a clinic established by a physician who is not a member of the Medical Staff with the backing of real estate investors. This clinic competes with MedCare, and has been a principal factor in curtailing MedCare's service volume growth recently.

MARKET SHARES

Historically, substantially all of the Hospital's inpatients have been residents of the Market Area. The Michigan Health and Hospital Association ("MHA") compiles patient origin data on all inpatient admissions and certain outpatient invasive procedures. In the case of inpatient market shares, the Corporation limits admissions to those requiring a secondary, but not a tertiary level of care. Historical market share data for the Hospital is tabulated below.

<i>Hospital Market Shares among Market Area Residents for Secondary Inpatient Admissions, Outpatient Invasive Procedures and Selected Specialties</i>					
	Calendar Years				
	2003	2002	2001	2000	1999
Cardiology	55.9%	51.7%	52.4%	54.8%	52.3%
Gastroenterology	39.0%	46.8%	46.9%		
General Surgery	49.6%	47.3%	48.2%	46.9%	50.0%
Pulmonology	61.7%	53.4%	54.2%		
Obstetrics	57.8%	60.1%	59.3%	55.9%	56.5%
Orthopedics	70.5%	65.6%	66.0%	60.2%	59.1%
All Secondary Inpatient Admissions	52.7%	50.7%	51.7%	50.8%	50.5%
Gastroenterology	54.0%	52.4%	44.9%		
General Medicine	77.3%	69.7%	58.4%		
General Surgery	69.8%	70.3%	69.6%		
Neurosurgery	61.6%	40.2%	57.7%		
Obstetrics	93.1%	95.4%	87.0%		
Ophthalmology	57.1%	56.4%	56.5%		
Orthopedics	77.7%	73.1%	73.4%		
All Outpatient Invasive Procedures	62.5%	58.8%	57.0%		
Source: MHA					
Shaded cells indicate information not available; data on invasive outpatient procedures were not compiled prior to 2001					

Because of small sample sizes, year-to-year variation among specialties may not be statistically significant. Management believes that the volatility of neurosurgery invasive procedures is attributable to small sample sizes.

Except for a decrease in inpatient market share between 2001 and 2002, all other year-to-year trends for all secondary inpatient admissions and all outpatient invasive procedures are positive.

The most significant market share increases are in orthopedics, largely attributable to the consolidation of the orthopedic physicians group's practice at its Gaylord office During FY2002.

Comparative market shares are set forth in the table below.

<i>Comparative Market Shares among Market Area Residents, 2003</i>		
	Secondary Inpatient Admissions	Outpatient Invasive Procedures
Otsego Memorial Hospital	52.7%	62.4%
Mercy Hospital Grayling	7.0%	3.6%
Northern Michigan Hospital	19.3%	21.9%
Charlevoix Hospital	N/A	0.5%
Community Memorial Hospital	0.7%	1.3%
Alpena General Hospital	7.0%	3.2%
Munson Medical Center	3.8%	N/A
Other	9.5%	7.1%
<i>Total</i>	100.0%	100.0%
Source: MHA		

These comparative market shares validate management's belief that Mercy, the competitor located closest to the Hospital, is not a significant competitive threat.

The union representing nurses at NMH commenced a strike in November 2002. Corporation management does not believe that any service disruption or other effect of this strike has caused the Hospital's market share to increase versus that of NMH. Thus, management does not believe that the Hospital's market share will materially decrease when this strike is settled.

SERVICE VOLUMES AND UTILIZATION

INPATIENT CARE

The prevalent inpatient reimbursement systems to which the Corporation is subject feature per-case, rather than per diem rates. Consequently, trends in the number of cases (as measured by admissions or discharges) per period are more meaningful than are trends measured in patient-days. Moreover, declines in patient-days given a certain number of cases, as well as average length of stay ("LOS"), are favorable. The Corporation does not report occupancy rates, preferring to adjust its staffing and other resource utilization to the daily census.

Management believes that the supply of skilled nursing beds in the Market Area, including those in McReynolds Hall, is adequate to enable the Hospital to avoid unnecessarily excessive LOS. Several home health agencies operating in the market area represent another resource for the continued care of discharged inpatients.

The Hospital's inpatient acute care volume and utilization data are presented in the table below. Occupancy rates are calculated on the basis of staffed beds rather than licensed beds.

<i>Historical Acute Care Utilization (excludes newborns)</i>							
	<i>Nine Months Ended Sept. 30</i>		<i>Fiscal Years Ended December 31</i>				
	<i>2004</i>	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Days in Period	274	273	365	365	365	366	365
Licensed Beds	53	53	53	53	53	53	53
Staffed Beds	39	39	39	39	39	39	39
Admissions	1,615	1,546	2,146	1,807	1,709	1,648	1,691
Change over Previous Period	4.5%		18.8%	5.7%	3.7%	(2.5)%	(7.0)%
Patient Days	4,463	4,489	6,100	5,282	4,925	4,723	5,138
Births	228	217	296	285	278	257	250
Average Daily Census	16.3	16.4	16.7	14.5	13.5	12.9	14.1
Average Length of Stay	2.8	2.9	2.8	2.9	2.9	2.9	3.0
Occupancy Rate ¹ (%)	41.8	42.2	42.9	37.1	34.6	33.1	36.1
¹ Based on Staffed Beds							

Inpatient admissions have increased by nearly 27 percent between FY1999 and FY2003. This increase is principally due to population growth in the Market Area and expanded capabilities among the Hospital and its affiliated physicians.

SKILLED NURSING CARE

Volume and utilization data for McReynolds Hall are presented in the table below.

<i>McReynolds Hall (Skilled Nursing) Utilization</i>							
	<i>Nine Months Ended Sept. 30</i>		<i>Fiscal Years Ended December 31</i>				
	<i>2004</i>	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Days in Period	274	273	365	365	365	366	365
Licensed and Staffed Beds	34	34	34	34	34	34	34
Patient Days	8,107	7,779	10,514	10,969	11,144	11,250	11,553
Average Daily Census	29.6	28.5	28.8	30.1	30.5	30.7	31.7
Occupancy Rate	87.0	83.8	84.7	88.4	89.8	90.4	93.1

OUTPATIENT AND ANCILLARY SERVICES

The following tables portray volume and utilization data for the Hospital's outpatient and ancillary services.

<i>Emergency Department and MedCare Volumes</i>							
	<i>Nine Months Ended Sept. 30</i>		<i>Fiscal Years Ended December 31</i>				
	<i>2004</i>	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
ED Visits	9,313	9,443	12,635	12,869	12,221	11,661	11,513
Change over Previous Period	(1.4)%		(1.8)%	5.3%	4.8%	1.3%	4.4%
MedCare Visits	9,864	11,055	15,204	15,589	15,320	13,630	12,465
Change over Previous Period	(10.8)%		(2.5)%	1.8%	12.4%	9.3%	34.4%

MedCare visits have declined recently due to the presence of a competing facility.

SURGICAL AND OTHER PROCEDURES

Volumes and utilization of the Hospital's operating and procedures rooms are detailed below.

<i>Surgical and Other Procedures</i>								
		<i>Nine Months Ended Sept. 30</i>		<i>Fiscal Years Ended December 31</i>				
		<i>2004</i>	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Inpatient Surgeries		770	391	527	667	738	911	872
Outpatient	Surgeries	2,782	3,109	4,210	3,240	2,671	2,225	2,393
	Other Procedures	3,233	3,242	170	534	632	860	825
	Total Outpatient	6,015	6,351	4,380	3,774	3,303	3,085	3,218
Grand Total		6,785	6,742	4,907	4,441	4,041	3,996	4,090
Change over Previous Period		0.6%		10.5%	9.9%	1.1%	(2.3)%	13.9%
Percent Outpatient		88.7%	94.2%	89.3%	85.0%	81.7%	77.2%	78.7%

Total surgical and other procedures increased by nearly 20 percent between FY1999 and FY2003.

ANCILLARY SERVICES

Due to the prevalence of "per-case" reimbursement, stable or even decreasing volumes of ancillary services rendered to acute care inpatients is beneficial to the Corporation, all other factors being equal.

<i>Ancillary Services Provided to Inpatients</i>								
		<i>Nine Months Ended Sept. 30</i>		<i>Fiscal Years Ended December 31</i>				
		<i>2004</i>	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Laboratory		91,953	79,627	108,585	90,629	85,048	89,335	87,088
Electrocardiology		1,544	1,586	2,132	1,686	1,527	1,677	1,709
Radiology		3,363	3,033	4,087	3,654	3,195	2,909	3,171
Cardio-Pulmonary		9,887	7,859	11,253	8,421	7,688	8,047	8,698
Physical Therapy		4,393	3,642	5,153	3,724	3,168	2,336	2,226
Occupational Therapy		1,788	889	N/A	N/A	N/A	N/A	N/A

The Radiology category includes CT, MRI, nuclear medicine and ultrasound, together with routine radiographic / fluoroscopic examinations.

The Hospital provides ancillary services to ER patients and outpatients who are referred by physicians. Due to the prevalence of fee-for-service reimbursement, increasing volumes are financially beneficial to the Corporation.

<i>Ancillary Services Provided to Outpatients</i>							
	<i>Nine Months Ended Sept. 30</i>		<i>Fiscal Years Ended December 31</i>				
	<i>2004</i>	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Laboratory	688,679	625,672	849,157	786,482	648,182	569,262	465,131
Electrocardiology	1,544	1,586	6,187	5,610	4,766	4,374	4,357
Electroencephalography	131	136	188	173	147	123	120
Radiology	28,561	26,898	36,322	33,592	32,135	27,696	23,811
Cardio-Pulmonary	4,993	4,415	6,041	5,828	6,025	6,218	5,715
Physical Therapy	9,669	8,904	10,779	10,470	9,965	7,468	7,419
Occupational Therapy	3,538	3,310	6,214	3,855	3,643	1,197	N/A
Cardiac Rehabilitation	3,239	4,231	5,358	3,853	N/A	N/A	N/A

FINANCIAL INFORMATION

THIRD-PARTY REIMBURSEMENT METHODOLOGIES AND SOURCES OF REVENUE

The following information relating to third-party reimbursement methodologies is limited to those characteristics that are particular to the Corporation. See “*BONDHOLDERS’ RISKS – Federal and State Policies Affecting Health Care Providers*” in this Official Statement.

MEDICARE

The federal Social Security Act, as amended, provides the legal basis for the Medicare program (Title XVIII). The Medicare program is administered by CMS through its fiscal intermediary (the “FI”).

Medicare consists of two distinct parts: Part A describes coverage of and conditions for payment for inpatient hospital services and services provided by other institutional health care providers, such as skilled nursing facilities (“SNFs”) like McReynolds Hall, home care agencies and hospices. Part B relates to a voluntary supplementary medical insurance benefit for the aged and disabled that covers, among other services, certain physician care, diagnostic testing, durable medical equipment and medical supplies.

INPATIENT CARE

The Corporation is reimbursed for providing inpatient acute care according to the patient's diagnosis-related group ("DRG") under the Prospective Payment System ("PPS"). The Corporation maintains no "distinct-part" units which are reimbursed in a different manner.

OUTPATIENT AND PHYSICIAN CARE

As of August 2000, outpatient services such as radiology and ambulatory surgery procedures have been reimbursed according to their prospectively-determined Ambulatory Payment Classifications ("APCs"). APCs are the outpatient equivalent of inpatient DRGs. Laboratory tests were never included among the APCs, and continue to be reimbursed according to a system of fee screens.

Pursuant to a "hold-harmless" provision of the 1997 Balanced Budget Act ("BBA"), the Corporation is reimbursed for certain capital expenses relating to outpatient services delivered to Medicare enrollees. This provision, which expires in 2006, supplemented Medicare reimbursement by approximately \$583,000 and \$770,000 in FY2002 and FY2003, respectively.

Certain physician services are reimbursed on the basis of a national fee schedule called the "resource based-relative value scale" ("RB-RVS"). The RB-RVS fee schedule establishes payment amounts for all physician services, including services of provider-based physicians, and is subject to annual updates. The Corporation bills for the professional services of its employed physicians according to fee schedules based on RB-RVS. The family practice and internal medicine practices staffed by Corporation-employed physicians do not qualify as rural health clinics under Medicare regulations.

SKILLED NURSING CARE

Under BBA, a prospective payment system for SNFs became effective on January 1, 1999. CMS, through the FI, reimburses the Corporation at a prospectively-determined national per diem rate, adjusted for the Michigan rural wage index and for patient acuity, the latter measured by resource utilization groups ("RUGs"). Residents must pay to the Corporation a deductible for each SNF stay and a coinsurance amount applicable to the 21st through the 100th days of each Medicare-covered SNF stay.

Medicare provides coverage for SNF care under Part A for a limited number of days. Medicare coverage of SNF services is available only if:

- the required skilled nursing or rehabilitative services can only be provided in a SNF;
- the SNF resident had been hospitalized for at least three consecutive days (not including the day of discharge) prior to the SNF admission;
- the need for the SNF services is directly related to the reason for the hospitalization;

- the resident was admitted to the SNF within 30 days of discharge from the hospital; and
- a medical professional certifies that daily skilled nursing or rehabilitative care is necessary.

There is no annual limitation on the number of covered benefit periods that a SNF resident might ever encounter, but Medicare limits coverage of SNF services to 100 days per benefit period.

SUPPLEMENTAL MEDICARE REIMBURSEMENT

The Corporation is designated as a sole community hospital (“SCH”) by Medicare reimbursement purposes by CMS. This designation is permanent, provided that the SCH program’s enabling legislation is not repealed by Congress, so the Corporation does not need to requalify periodically. Management estimates this benefit to add approximately \$100,000 annually to aggregate Medicare inpatient reimbursement. The value of the SCH designation has diminished in recent years due to other changes in the Medicare PPS, most notably the reduced disparity between urban and rural wage indices. The Corporation’s SCH designation disqualifies it from receiving supplemental disproportionate share (“DSH”) reimbursement reimbursement.

MEDICAID

The federal Social Security Act, as amended, also provides the legal basis for the Medicaid program under Title XIX. The Medicaid program is a joint federal/state health insurance program for the categorically needy, aged or disabled. It is administered by CMS and MDCH. CMS funds approximately half of the aggregate payments to institutional health care providers in Michigan, with the State funding the other half through MDCH.

MDCH requires that non-elderly Medicaid recipients residing in the Market Area join qualified managed care plans (“QHPs”). Since this requirement was implemented, a substantial number of non-elderly Medicaid recipients have joined one of the three QHPs which operate in the Market Area: Molina Healthcare of Michigan, Community Choice Michigan, and Priority Health Government Programs. The Corporation contracts with all three of these QHPs, under the terms of which the Corporation is reimbursed according to percentages of their charges.

The Michigan Medicaid program’s Quality Assurance Assessment Program (“QAAP”) for hospitals is intended to increase Medicaid reimbursements to the maximum allowed by CMS. It is comprised of three elements:

- a uniform assessment on all hospitals;
- Federal matching funds; and
- a Medicaid payment increase.

In State fiscal years 2003 and 2004, hospitals contributed an amount equivalent to 1.2 percent and 1.0 percent, respectively, of their total patient care revenue attributable to payors other than Medicare. These contributions will allow the State to earn additional federal funding for the Medicaid program. The funds were distributed in the form of increased Medicaid payments to hospitals. The Corporation's share of such increased payments was approximately \$8,000 over the two State fiscal years. The State has applied to CMS to extend QAAP, with certain modifications, through State fiscal year 2005.

INPATIENT, OUTPATIENT AND PHYSICIAN CARE

Michigan Medicaid reimbursement payments to the Corporation for inpatient care are based on a DRG methodology similar to that used by Medicare with respect to all routine and ancillary services. MDCH plans to rebase DRG payments effective April 1, 2005. Though management cannot estimate the financial impact of such rebasing, management believes that the Corporation will be largely insulated from material adverse impact because much of the inpatient utilization among Medicaid beneficiaries treated at the Hospital is related to obstetrical and pediatric care. Medicaid reimburses the Corporation for ancillary services provided to outpatients on the basis of fee screens.

SNF CARE

Medicaid coverage of SNF services is conditional on financial eligibility rather than prior hospitalization. While Medicare Part A coverage is virtually universal among persons age 65 and over, eligibility for Medicaid coverage involves a "means-testing" procedure. The Medicaid program reimburses the Corporation a per-diem rate with respect to each Medicaid-eligible SNF resident, without any limit on the number of days of care. Typical of Medicaid programs nationwide, residents are required to assign their social security and similar benefits to the Corporation, except for a nominal spending allowance. The Medicaid reimbursement formula recognizes these resident payments, and funds a net amount so that the Corporation realizes no more than the allowable Medicaid per diem rate.

The Medicaid per-diem rate formula includes the recognition of certain variable operating and capital costs, supplemented by an amount that recognizes the extra costs of operating a hospital-based SNF. For FY2004, the Medicaid per-diem rate is approximately \$185. This rate represents an approximately 7½ percent discount from than the Corporation's per diem charge of \$200.

BLUE CROSS

The Corporation has a contractual relationship with Blue Cross/Blue Shield of Michigan ("Blue Cross"), which dominates the non-governmental health insurance market. Employees of many major employers in the Market Area are covered by Blue Cross.

Blue Cross reimburses the Corporation under a prospective payment system. Under this system, Blue Cross payments for inpatient services are based on DRGs using a rate higher than that applied by Medicare. Blue Cross reimburses the Corporation for most outpatient services according to a fee schedule. Blue Cross reimburses the Corporation for services provided by employed physicians on the basis of a fee schedule.

Because the number of the Hospital's annual inpatient cases has grown to exceed 2000, the Corporation will no longer qualify for favorable Blue Cross reimbursement as a Peer Group 5 hospital after FY2004. Blue Cross has agreed to a modification of its standard Participating Hospital Agreement ("PHA") entailing a seven-year transitional reimbursement arrangement beginning in FY2005 that is more favorable to the Corporation than reimbursement as a Peer Group 4 hospital, which would have been the alternative. Management's financial projections (*See "MANAGEMENT'S FINANCIAL PROJECTIONS" in this Appendix A*) reflect this arrangement.

Blue Cross remits interim payments biweekly, which are reconciled after the completion of the annual cost report. The magnitude of the interim payments is set according to service volumes recorded on the prior year's cost reports.

MANAGED CARE PLANS AND COMMERCIAL INSURERS

Other than Blue Cross MCPs (which are categorized with traditional Blue Cross indemnity plans because of the similarity in reimbursement to the Corporation) and the QHPs, there are a limited number of managed care plans ("MCPs") operating in the Market Area. The Corporation and its employed physicians maintain contracts with the two most significant MCPs, both of which are PPOs:

- Preferred Choices PPO, an affiliate of Trinity Health, which also owns and operates Mercy Hospital Grayling, the Competing Hospital located most proximal to the Hospital; and
- PPOM (formerly known as PPO of Michigan), which was acquired from Blue Cross by private investors in August 2004.

Contracts between the Corporation and these PPOs and various commercial insurers feature neither:

- capitated payment arrangements, whereby the Corporation assumes insurance-type risk; nor
- exclusionary clauses, whereby the Corporation would experience a decrease in service volumes if it failed to renew a contract (or, conversely, the Corporation would increase service volumes by having entered into an exclusive contract).

The PPOs and commercial insurers typically reimburse the Corporation according to percentages of charges, most of which exceed ninety percent. Several of the major private-sector employers in the Market Area offer health insurance coverage for their employees through PPOM.

There are no managed care plans that offer the "Medicare Advantage" (formerly "Medicare + Choice") option to Medicare enrollees residing in the Market Area.

REIMBURSEMENT AUDITS

Medicare and Medicaid reimbursement is subject to audit. These third-party payors have completed final audits of the Corporation’s cost reports and other records through the following Federal fiscal years:

	<u>Federal fiscal year</u>
Medicare	2001
Medicaid	2000

Corporation management believes that adequate levels of reserves are maintained so that any liabilities arising from FYs for which cost reports have not been settled and from other factors will not have a material adverse effect on the Corporation.

PAYOR MIX

The Hospital’s payor mix is typical of small hospitals in Michigan.

<i>Payor Mix by Gross Revenue (excludes physician revenue)</i>					
	<i>Fiscal Years Ended December 31</i>				
	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Medicare	41.1%	39.4%	37.0%	37.9%	39.1%
Medicaid	11.3%	11.5%	10.6%	9.4%	9.9%
Blue Cross	31.2%	30.3%	32.0%	32.5%	29.5%
Self-Pay	4.4%	5.6%	5.2%	5.0%	5.5%
Other	12.0%	13.2%	15.2%	15.2%	16.0%
Total	100.0%	100.0%	100.0%	100.0%	100.0%

The “Other” category includes the PPOs, commercial insurers and worker’s compensation insurers. Most contracts with these insurers provide for reimbursement on the basis of percentages of charges, and such percentages are mostly in excess of ninety percent.

Bills for physician services are generated by a different information system than that which generates bills for other hospital services. Corporation management does not believe that there would be a material change in these percentages if physician revenue had been included.

The split between inpatient, outpatient and skilled nursing gross patient service revenue is set forth below.

<i>Percentage of Gross Patient Service Revenue</i>					
	<i>Fiscal Years Ended December 31</i>				
	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Inpatient	30.4%	25.7%	24.3%	26.7%	28.0%
Outpatient	65.2%	69.4%	70.6%	68.5%	66.4%
Skilled Nursing	4.4%	4.9%	5.1%	4.8%	5.6%

Revenue from the physician practices is included in outpatient revenue.

FINANCIAL PERFORMANCE

Management prepares the Corporation's annual budget in the months preceding the commencement of each FY, and presents it to the Corporation Board for adoption at its November meeting. The Corporation Board establishes a set of global budget assumptions which include a target operating margin.

The Corporation's recent financial performance is summarized in the following table for the FYs ended December 31, 1999 through 2003, and for the nine-month interim periods ended September 30, 2004 and September 30, 2003.

<i>Summary of the Corporation's Statements of Operations</i> (<i>\$000s omitted</i>)							
	<i>Nine Months Ended Sept. 30</i>		<i>Fiscal Years Ended December 31</i>				
	<i>2004</i>	<i>2003</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Net Patient Service Revenue	34,661	31,084	42,225	35,433	31,572	27,873	23,884
Other Operating Revenue	<u>463</u>	<u>383</u>	<u>541</u>	<u>887</u>	<u>250</u>	<u>233</u>	<u>177</u>
Total Operating Revenue	35,124	31,467	42,766	36,320	31,822	28,106	24,061
Depreciation Expense	1,444	1,449	1,926	1,925	1,697	1,579	1,734
Interest Expense	537	515	702	653	572	498	547
Provision for Bad Debts	985	1,083	1,601	1,186	682	861	704
Other Operating Expenses	<u>31,529</u>	<u>27,618</u>	<u>37,437</u>	<u>31,421</u>	<u>27,849</u>	<u>24,754</u>	<u>20,821</u>
Total Operating Expenses	34,495	30,665	41,666	35,185	30,800	27,692	23,806
Income from Operations	629	802	1,100	1,135	1,022	414	255
Net Nonoperating Revenue	<u>231</u>	<u>67</u>	<u>219</u>	<u>8</u>	<u>475</u>	<u>461</u>	<u>376</u>
Revenue over Expenses	860	869	1,319	1,143	1,497	875	631
EBIDA	2,841	2,833	3,947	3,721	3,766	2,952	2,912
Note: some figures might not add precisely due to rounding							

The Corporation has posted operating surpluses consistently. As additional evidence of the Corporation's growth, total operating revenue increased by nearly 78 percent between FY1999 and FY2003, and has increased by another 11.6 percent between the first nine months of FY2003 and the first nine months of FY2004.

The following ratios are calculated from the data in the preceding table.

<i>Statement of Operations Ratios¹</i>					
	<i>Fiscal Years Ended December 31</i>				
	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
<i>Pro Forma MADS² Coverage Ratio</i>	1.74	1.64	1.66	1.30	1.29
<i>Pro Forma MADS² / Total Operating Revenue</i>	5.3%	6.2%	7.1%	8.1%	9.4%
<i>Non-Operating Revenue / Total Revenue</i>	0.5%	0.0%	1.5%	1.6%	1.5%
<i>EBIDA Margin</i>	9.2%	10.2%	11.7%	10.3%	11.9%
<i>Operating Cash Flow Margin</i>	8.7%	10.2%	10.3%	8.9%	10.5%
<i>Operating Margin</i>	2.6%	3.1%	3.2%	1.5%	1.1%
<i>Excess Margin</i>	3.1%	3.1%	4.6%	3.1%	2.6%
<i>Bad Debt Expense / Total Operating Revenue</i>	3.8%	3.4%	2.2%	3.1%	3.0%
¹ Calculated from the Corporation's audited financial statements, using definitions defined in 2003 <i>U.S. Not-For-Profit Median Health Care Ratios</i> published by Standard & Poor's on September 22, 2003 ² Based on estimated Maximum Annual Debt Service ("MADS") of \$2,263,000 on the Series 2004 Bonds and the Series 2005 Bonds					

FINANCIAL POSITION, CAPITALIZATION AND LIQUIDITY

Presented below is a summary of the Corporation's balance sheets at FYs ended December 31, 1999 through 2003, plus the interim period ended September 30, 2004.

<i>Balance Sheet Summary (Corporation only)</i>						
<i>(\$000s omitted)</i>						
	<i>Sept. 30</i>	<i>Fiscal Years Ended December 31</i>				
	<i>2004</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Cash and Cash Equivalents ¹	1,127	1,684	1,206	2,618	1,968	2,034
Net Patient Accounts Receivable	6,212	4,993	3,012	2,092	2,460	2,472
Other Current Assets	<u>1,508</u>	<u>1,655</u>	<u>2,609</u>	<u>1,585</u>	<u>1,116</u>	<u>651</u>
Total Current Assets	8,847	8,332	6,827	6,295	5,544	5,157
Investments ¹	2,220	2,134	1,802	1,646	1,441	1,330
Net Property and Equipment	16,824	16,446	16,760	15,587	11,318	10,829
Other Non-Current Assets	<u>1,459</u>	<u>1,577</u>	<u>1,849</u>	<u>2,516</u>	<u>1,365</u>	<u>1,266</u>
Total	29,350	28,489	27,238	26,044	19,668	18,582
Current Liabilities	4,731	4,367	4,387	3,642	2,734	2,734
Long-Term Debt	9,094	9,434	9,831	10,325	6,077	5,875
Other Non-Current Liabilities	168	186	208	228	247	264
Unrestricted Net Assets	<u>15,357</u>	<u>14,502</u>	<u>12,812</u>	<u>11,849</u>	<u>10,610</u>	<u>9,709</u>
Total	29,350	28,489	27,239	26,044	19,667	18,581

¹ Used in "Days' Cash on Hand" and "Cushion Ratio" calculations
 Note: some figures might not add precisely due to rounding

The Corporation owns a parcel of undeveloped land adjacent to the MedCare facility, which has been recently appraised at \$1.9 million. This value of this asset is recorded on Corporation's balance sheet at its cost, \$160,000.

Heretofore, the Foundation has been an unrelated organization. The Foundation has since amended its by-laws so that the Corporation controls the appointment of its governing board members. Beginning with FY2004, the Foundation will become a consolidated entity on the Corporation's financial statements. As of December 31, 2003, the Foundation's assets were approximately \$800,000, most of which is unrestricted. (See "OTSEGO MEMORIAL HOSPITAL FOUNDATION" / "Financial Condition" in this Appendix A.)

Liquidity has been a long-standing issue for the Corporation. Yet, the Corporation has not had to borrow to pay any operating expenses in nearly 30 years. Moreover, the Corporation has not

extended payables, as evidenced by a relatively low average payment period. The Corporation has been consistently profitable – its most recent operating loss was recorded in FY1990. Excess cash flow has been applied toward facilities improvements and equipment acquisition, which accounts for the Corporation’s relatively low average age of plant, and, to a lesser extent, to debt repayment. As indicated by low numbers of days’ in accounts receivable, cash is not tied up in accounts receivable. Upon the conclusion of the Series 2004 Improvement Project, the Corporation will have substantially replaced the Hospital Facility that was originally constructed in 1973. The following summary of the Corporation’s statements of cash flows illustrates further how the magnitude of capital expenditures and other factors have inhibited the Corporation’s ability to increase its financial reserves.

Cash Flow Statement Summary						
(Corporation only except FY2003, which are Consolidated Data)						
(\$000s omitted)						
	Fiscal Years Ended December 31					Five-FY Totals
	2003	2002	2001	2000	1999	
Cash and Cash Equivalents, Beginning of FY	1,206	2,618	1,968	2,034	1,938	
Net Cash Provided by Operating Activities	2,442	2,213	3,274	1,942	1,768	11,639
Acquisition of Property and Equipment	(1,611)	(3,497)	(5,566)	(2,067)	(1,180)	(13,922)
Net Cash Provided by (Used in) Other Investing Activities	202	434	(1,379)	(211)	279	
Proceeds from Issuance of Long-Term Debt	0	0	4,809	516	0	5,325
Principal Repayments of Long- Term Debt	(455)	(563)	(353)	(247)	(771)	(2,389)
Net Cash Provided by (Used in) Other Financing Activities	0	0	(134)	0	0	
Net Increase (Decrease) in Cash and Cash Equivalents	577	(1,412)	650	(66)	96	
Cash and Cash Equivalents, End of FY	1,783	1,206	2,618	1,968	2,034	

Over the past five FYs, the Corporation has acquired nearly \$14 million of property and equipment (“Capital Assets”), almost \$2.3 million more than cash flow generated by operations. Management believes that these expenditures were essential to meet the growth in service volumes, especially among outpatient and physician services. Such expenditures on Capital Assets exceeded aggregate depreciation expense by over \$5 million, or 57 percent. Because proceeds of the Corporation’s debt issuance over this five FY period of \$5.3 million were offset by debt repayments of \$2.4 million,

the Corporation increased its net outstanding debt by only \$2.9 million. Thus, the sum of cash flow generated by operations plus net borrowing exceeded expenditures on Capital Assets by only \$653,000.

Indicators of the Corporation's liquidity and other balance sheet ratios are set forth below.

<i>Balance Sheet Ratios¹</i>					
	<i>Fiscal Years Ended December 31</i>				
	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
<i>Pro Forma</i> Cushion Ratio ²	1.7	1.3	1.9	1.5	1.5
Days' Cash on Hand	35.1	33.0	53.5	47.8	55.6
Days in Patient Accounts Receivable	43.2	31.0	24.2	32.3	37.8
Cash Flow / Total Liabilities	23.2%	21.3%	22.5%	27.1%	26.7%
Unrestricted Cash / <i>Pro Forma</i> Long-Term Debt ³	14.2%	11.2%	15.9%	12.7%	12.5%
<i>Pro Forma</i> Long-Term Debt / Capitalization ³	64.9%	67.7%	69.4%	71.7%	73.5%
Payment Period (days)	40.1	48.1	45.7	38.2	45.2
¹ Calculated from the Corporation's audited financial statements, using definitions defined in <i>2003 U.S. Not-For-Profit Median Health Care Ratios</i> published by Standard & Poor's on September 22, 2003 ² Based on estimated Maximum Annual Debt Service ("MADS") of \$2,263,000 on the Series 2004 Bonds and the Series 2005 Bonds ³ Based on \$26,860,000 aggregate principal amount of Series 2004 Bonds and Series 2005 Bonds					

The increase in Days' in Patient Accounts Receivable between FY2002 and FY2003 is largely attributable to billing and payment issues with respect to physician services.

OUTSTANDING INDEBTEDNESS

Below is a summary of the Obligated Group Members' debt instruments that will be outstanding upon issuance of the Series 2004 Bonds.

<i>Pro Forma Schedule of Indebtedness and Debt-to-Capitalization</i> <i>(\$000s omitted)</i>			
		<i>Outstanding Balance</i>	
<i>Indebtedness</i>	<i>FY of Final Maturity</i>	<i>Prior to Issuance of Series 2004 Bonds</i>	<i>After Issuance of Series 2004 Bonds & Series 2005 Bonds</i>
Series 1995 Bonds	2019	\$5,315	\$0
Series 2001 Bonds	2026	4,150	0
Series 2004 Bonds	2036	0	17,860
Series 2005 Bonds	2014	0	9,000
Bank note payable	2010	330	0
Total Outstanding Balance		\$9,795	\$26,860
Unrestricted Net Assets, at September 30, 2004 ¹		\$15,357	\$15,357
<i>Pro Forma</i> Long-Term Debt-to-Capitalization ²		38.9%	63.6%

¹ Figures do not reflect any loss incurred as a result of refunding the Corporation's Series 1995 and Series 2001 Bonds
² As defined in 2003 U.S. Not-For-Profit Median Health Care Ratios published by Standard & Poor's on September 22, 2003

The outstanding balance of Indebtedness after the issuance of the Series 2004 Bonds does not take into account any Indebtedness associated with the 2001 Swap or the Line of Credit (both as hereinafter defined), as measured in accordance with the Master Indenture.

<i>Pro Forma Debt Service Coverage Ratio Calculations</i> <i>(\$000s omitted, except for Debt Service Coverage Ratios)</i>					
	<i>Fiscal Years Ended December 31</i>				
	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Net Income Available for Debt Service	3,947	3,721	3,766	2,952	2,912
<i>Pro Forma</i> Maximum Annual Debt Service ¹	2,263	2,263	2,263	2,263	2,263
<i>Pro Forma</i> Debt Service Coverage Ratio (x) ²	1.74	1.64	1.66	1.30	1.29

¹ Calculated in accordance with the Master Indenture
² As defined in 2003 U.S. Not-For-Profit Median Health Care Ratios published by Standard & Poor's on September 22, 2003

INTEREST RATE MANAGEMENT

The Corporation is the fixed-rate payer in an interest rate swap that was executed in connection with the issuance of the Series 2001 Bonds (the “2001 Swap”). Under its terms, the Corporation has contracted to pay a fixed interest rate of 4.10 percent per annum and receive periodic payments at the *Bond Market Association* Municipal Swap Index (the “BMA Index”). The 2001 Swap had an outstanding balance at September 30, 2004 of \$4,130,000, and terminates in December 2006. In connection with the issuance of the Series 2004 Bonds, the Corporation’s payment obligations under the 2001 Swap will become secured by an Obligation issued under the Master Indenture. The assumption regarding Debt Service Requirements on the Series 2005 Bonds used in this Official Statement takes into account the Corporation’s payment obligations with respect to the 2001 Swap.

Fifth Third’s commitment to purchase the Series 2005 Bonds specifies that their interest rate will float at a rate based on either the one-month, two-month, three-month or four-month London Interbank Offering Rate (“LIBOR”), as selected by the Corporation. In order to hedge a portion of the interest rate risk associated with changes in LIBOR, the Corporation has determined to maintain the 2001 Swap, even though the Series 2001 Bonds will be refunded by the Series 2004 Bonds. Corporation management recognizes that using the 2001 Swap for this purpose, assuming no further hedging will have occurred, will leave the Corporation exposed to certain risks:

- the basis risk associated with the BMA Index-based 2001 Swap hedging the LIBOR-based interest rate on the Series 2005 Bonds;
- the maturity of the 2001 Swap is significantly sooner than the January 1, 2015 final maturity of the Series 2005 Bonds; and
- the greater principal amount of the Series 2005 Bonds (\$9 million), together with significant differences in the schedules over which the 2001 Swap and the Series 2005 Bonds, respectively, will amortize.

The Corporation may, but is not obligated to address the latter two risks by entering into some form of Financial Products Agreement that would be designed to “complement” the 2001 Swap in terms of principal amount, amortization schedule and final maturity. The Corporation advises that no assurance can be given that such a Financial Products Agreement can or will be executed, especially if there is a material adverse change in market conditions. The Corporation’s payment obligations under a Financial Products Agreement, if consummated, may be secured by an Obligation issued under the Master Indenture.

LINE OF CREDIT

In connection with its commitment to purchase the Series 2005 Bonds, Fifth Third has committed to extend to the Corporation a \$1,000,000 line of credit (the “Line of Credit”) for working capital purposes. The Corporation will have executed the documents necessary to implement the Line of Credit at or prior to delivery of the Series 2005 Bonds, but management does not expect to draw on it. The Corporation’s payment obligations under the Line of Credit will become secured by an Obligation issued under the Master Indenture.

INVESTMENT POLICY

The Corporation maintains an investment policy which addresses the investment of financial reserves. It was most recently revised in January 2002. The Corporation strives to achieve a rate of return of three to five percentage points above the rate of inflation. The Corporation has determined that it willing to tolerate a prudent degree of risk in order to achieve this goal, but also desires to limit any decrease in market value of its investment portfolio to less than ten percent in any given year.

Portfolio diversification is a cornerstone of the investment policy. The investment policy targets a mix of 50 percent common stocks (in the form of individual companies or mutual funds) and 50 percent fixed-income securities, subject to a “collar” of \pm five percent. No more that five percent of the Corporation’s financial assets can be invested in the equity securities of a single company, nor more than 15 percent in a single mutual fund. The investment policy requires that financially complex and illiquid securities be avoided, and that fixed-income securities be rated “A” or better.

The investment policy requires that the Corporation’s financial reserves be professionally-managed by an “fee-only” investment advisor who is compensated on a non-commissioned basis. The investment advisor reports to the Corporation Board quarterly, and the investment advisor’s performance is evaluated annually.

The Corporation utilizes the Bank’s comprehensive cash management system for its working capital cash and cash equivalents.

OTHER FINANCIAL INFORMATION

Certain other financial and related information appears below.

INFORMATION SYSTEMS

Except for its physician practice management system, the Keane InSight Healthcare Information System (“InSight”) performs substantially all of the Corporation’s financial and clinical information processing. InSight integrates patient management, health information management, enterprise information, financial management, clinical, and patient care systems into a common database accessed through a single point of entry. InSight operates on the Corporation’s IBM AS/400 mainframe computer. InSight enables the Corporation to comply fully with certain relevant provisions of the Health Insurance Portability and Accountability Act of 1996. Corporation management takes prudent measures relating to the security and integrity of its data.

Corporation personnel are in the process of integrating the physician practice management information system with InSight. Other minor systems have already been interfaced.

RETIREMENT PLANS

The Corporation maintains a defined contribution “403(b)” pension plan which covers substantially all employees at the time of employment. The Corporation matches certain employee contributions. Participants become fully vested after five years. This pension plan is considered to be fully funded.

The Corporation is also the beneficiary of three life insurance policies covering retired executives. During their lifetimes, these retirees have use of the dividends on these policies.

INSURANCE

The Corporation maintains healthcare professional, commercial general and umbrella liability insurance coverage through the Michigan Hospital Association Insurance Company. The Corporation also maintains an “all-risk” property and automobile insurance policy, including boiler and machinery and business interruption coverage, in an amount deemed sufficient by the Corporation’s management. The Corporation maintains fidelity bonds, directors and officers coverage, automobile insurance and other coverages typical of similar hospitals.

The Corporation carries a workers’ compensation insurance policy, as required by Michigan law. The Corporation offers health insurance coverage for its employees through Blue Cross.

PROFESSIONAL LIABILITY LITIGATION

There is currently asserted one medical malpractice claims pending against the Corporation. This claim is in its early stages of litigation, and neither Corporation management nor its litigation counsel can evaluate the likely outcome or the financial impact of this claim.

OTHER PENDING LITIGATION

There is currently one other lawsuit pending against the Corporation involving other than the medical malpractice claim. Corporation management is of the opinion, based upon the advice of counsel, that the final disposition of this matter will not have a material adverse effect on the financial condition of the Corporation.

PPS AND RELATED INFORMATION

The Corporation tracks its case-mix indices monthly with respect to Medicare patients. Such case-mix indices are tabulated below.

<i>Case-Mix Indices (Acute Care Only)</i>					
	<i>Fiscal Years Ended December 31</i>				
	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1999</i>
Medicare	1.4317	1.2781	1.2745	1.2728	1.2316
Medicaid	0.8372	0.7648	0.7721	0.7419	0.7866

The increase in the Medicare case-mix index between FY2002 and FY2003 is largely attributable to the greater volume of orthopedic surgery, especially total hip and knee replacements.

The Corporation verifies the accuracy of its DRG assignments through audits conducted by internal personnel and by external consultants.

The most prevalent DRGs encountered during FY2003 are enumerated in the table below.

<i>Most Prevalent DRGs, FY2003 (includes newborns)</i>				
<i>DRG</i>	<i>Description</i>	<i>Discharges</i>	<i>Percent</i>	<i>Cumulative Percent</i>
209	Major joint and limb reattachment procedures of lower extremity	276	11.5%	11.5%
391	Normal newborn	202	8.4%	19.9%
373	Vaginal delivery without comorbidities and/or complications	140	5.8%	25.7%
89	Simple pneumonia and pleurisy, age > 17, with comorbidities and/or complications	90	3.7%	29.4%
127	Heart failure and shock	73	3.0%	32.5%
359	Uterine and adnexa procedures for non-malignancy, with comorbidities and/or complications	73	3.0%	35.5%
371	Cesarean section without comorbidities and/or complications	57	2.4%	37.9%
390	Neonate with other significant problems	50	2.1%	40.0%
224	Shoulder, elbow or forearm procedures, except major joint procedures	45	1.9%	41.8%
143	Chest pain	44	1.8%	43.7%

OTSEGO MEMORIAL HOSPITAL FOUNDATION

The Otsego Memorial Hospital Foundation (the “Foundation”) was established in 1977. The Foundation is exclusively organized to support and benefit the Corporation.

GOVERNANCE AND MANAGEMENT

The Foundation is governed by a Board of Directors (the “Foundation Board”) consisting initially of 26 directors (“Directors”) selected by the Corporation Board. Vacancies on the Foundation Board are filled by election of the Directors, but must be approved by the Corporation. Six serve in *ex-officio* capacities: the Corporation’s chief executive and chief financial officers and director of human resources, and liaisons designated by the Corporation Board, the Medical Staff and the Auxiliary. All other Directors are elected at-large.

The following 26 individuals current serve on the Foundation Board.

<i>Foundation Board</i>			
<i>Name</i>	<i>Year Term Expires</i>	<i>Basis for Membership</i>	<i>Occupation / Affiliation</i>
David Becker	2006	At-Large	Business Executive, Ward Lake Energy
William Boyce	2005	At-Large	Sales Representative, Pfizer, Inc. (pharmaceuticals)
R. David Briney	<i>Ex-officio</i>	Corporation Board Liaison	Private investor
Claudia Bryant	2006	At-Large	Community Leader
Scott Chesley, President-Elect	2007	At-Large	Real Estate Broker, Otsego Properties
William Cleaver	2007	At-Large	Investment Broker, Robert W. Baird & Co., Inc.
Jeffrey Cook, CPA, Treasurer	2005	At-Large	Certified Public Accountant, Keskin, Cook, Miller
Jack Deming	2005	At-Large	Business Owner (retired)
Terra Deming	<i>Ex-officio</i>	By position	<i>Director of Human Resources</i> , Otsego Memorial Hospital
David Engel	2007	At-Large	Insurance Agent, Northwestern Mutual Financial Network
Nick Florian	2007	At-Large	<i>Vice President</i> , Citizens Bank
Al Glasby	2007	At-Large	Pharmacist (retired)
Mark Huston	2005	At-Large	<i>Real Estate Broker (retired)</i> , Huston Real Estate, Inc.
Scott Lampert	2006	At-Large	Business Owner, Paxton Energy
Barbara Lawnichak, Secretary	2005	At-Large	<i>Business Manager</i> , Ward Lake Energy
Thomas Lemon	<i>Ex-officio</i>	By position	<i>Chief Executive Officer</i> , Otsego Memorial Hospital

<i>Foundation Board</i>			
<i>Name</i>	<i>Year Term Expires</i>	<i>Basis for Membership</i>	<i>Occupation / Affiliation</i>
John Makranyi	2007	At-Large	Investment Broker, Raymond James & Associates
Reverend Jim Mathis	2007	At-Large	Pastor, Gaylord Evangelical Free Church
Robert Mee, M.D.	<i>Ex-officio</i>	Physician liaison	<i>Internist</i> , Otsego Memorial Hospital
Sandra Nemecek, R.N.	2007	At-Large	<i>Manager, Cardiac Rehabilitation</i> , Otsego Memorial Hospital
Kevin Reynolds, C.P.A.	2007	At-Large	Certified Public Accountant, Plante & Moran
Mary Sanders, President	2005	At-Large	Educator (retired), Garlord Community Schools
Carolyn Study	<i>Ex-officio</i>	Auxiliary liaison	Community Leader
David Taylor	2006	At-Large	<i>President</i> , Fifth Third Bank, Gaylord
Richard Thomas	<i>Ex-officio</i>	By position	<i>Vice President, Finance</i> , Otsego Memorial Hospital
Marcus Wegmeyer	2007	At-Large	Insurance Agent, Michigan Insurance Services Agency

Deborah B. Allen has served as the Executive Director of the Foundation since 1999. In this capacity, Ms. Allen directs the *Growing with the Community* capital campaign in connection with the development of the Improvement Project. She is also responsible for annual, planned and major gift solicitation, as well as grant writing. Prior to joining the Foundation, Ms. Allen operated her own consulting business oriented toward local chambers of commerce, building on her experience as the Executive Director of Chambers of Commerce in Gaylord / Otsego County, in Grayling, Michigan, and in Clinton County (Lock Haven), Pennsylvania. Ms. Allen was honorably discharged from the U.S. Naval Reserves as a lieutenant.

Ms. Allen holds a bachelors degree from Millersville University of Pennsylvania, Millersville, where she also earned credits toward a masters degree. She has been active in the Michigan and U.S. Chambers of Commerce, and served on the Governor's Rural Development Council of Michigan. Ms. Allen was the 2002 recipient of a scholarship from the Association for Healthcare Philanthropy.

FUNDRAISING ACTIVITIES

The Foundation conducts several annual fundraising events and has periodically undertaken special capital development campaigns.

CAPITAL CAMPAIGN FOR THE IMPROVEMENT PROJECT

During FY2004, the Foundation commenced the *Growing with the Community* capital campaign in support of the Improvement Project. The theme for this campaign is the need for improved facilities necessitated by population growth in the Market Area and the Hospital's expanded clinical capabilities. As of October 15, 2004, the Foundation had recorded pledges of over \$1.3 million toward a goal of \$1.5 million, largely through the solicitation of the "hospital family" –

members of the Corporation and Foundation Boards, the Auxiliary and the Medical Staff together with Corporation employees, and local businesses. The pledges are payable through FY2009, but over 80 percent of the amount pledged is scheduled to be paid by the end of FY2006. Corporation management, Foundation management and the Foundation's fundraising consultant believe that the \$1.5 million goal is achievable.

The Corporation and/or the Foundation have completed two successful capital campaigns in the past. A capital campaign in 1971 raised \$1.25 million to support the construction of an addition to the Hospital Facility. A 1994 effort garnered \$1.5 million to defray the cost of a new emergency room and additional surgical suites.

ANNUAL FUNDRAISING

The Foundation's goal is to contribute \$50,000 of support to the Corporation annually. The Foundation conducts a number of annual fundraising events, the most significant of which is a golf outing that raises approximately half of the annual goal. The *Circle of Friends* annual campaign recognizes those who contribute self-designated amounts annually.

FINANCIAL CONDITION

At the end of FY2003, the Foundation held approximately \$800,000 in cash and investments. The Foundation has no material liabilities.

The Foundation's expenses for FY2004, other than the fees of its fundraising consultant who assisted with the *Growing with the Community* campaign, are expected to be less than \$75,000. The Foundation's expenses have been funded by the application of certain donations. Corporation management believes that including the Foundation as a Member of the Obligated Group would not have changed the Corporation's historical statements of operations in a material way.

The Foundation's investment policy is identical to that of the Corporation.

MANAGEMENT'S FINANCIAL PROJECTIONS

The remainder of this Appendix A entitled “Management’s Financial Projections” is comprised entirely of Management’s forward-looking statements. These Management’s Financial Projections are the sole responsibility of Corporation management. These forward-looking statements are not historical facts, and are subject to risks and uncertainties that could cause actual results to differ materially from those projected. Such risks and uncertainties include, but are not limited to, those enumerated in the disclaimer notice posted at the beginning of this Appendix A.

Corporation management has prepared the Management’s Financial Projections that are presented on the following pages for the six FYs ending December 31, 2009. The assumptions and parameters used in Management’s Financial Projections are believed by management to be reasonable, and reflect all information known as of October 20, 2004, the date of the Preliminary Official Statement relating to the Series 2004 Bonds. Management does not intend to update these Management’s Financial Projections to reflect information that becomes known after October 20, 2004 such as the final pricing and other data relating to the Series 2004 Bonds. If the actual interest rates, yields and / or structure of the Series 2004 Bonds vary from those assumed herein, the Corporation’s actual financial statements could vary materially and adversely from these projected financial statements.

The capital financing assumptions used in Management’s Financial Projections are consistent with those used to compute figures relating to the Series 2004 Bonds and Series 2005 Bonds that were contained in the Preliminary Official Statement relating to the Series 2004 Bonds dated October 20, 2004. Such figures have not been updated to reflect the actual terms of the Series 2004 Bonds, as set forth in the Official Statement relating to the Series 2004 Bonds dated November 11, 2004. In addition to the capital assets to be added through the Improvement Project, the Corporation plans to expend \$1 million on routine capital assets in FY2005, and \$1.25 million per FY through FY2009.

Despite the significant growth of many of the Hospital’s patient care service volumes in recent FYs, management has not assumed that such increases will continue at the same rate. The service volume and utilization assumptions reflect a more moderate growth pattern.

Assumptions regarding reimbursement rates and related parameters take into account update factors and other information known as of the date of the Preliminary Official Statement. A key assumption relates to parameters associated with the modifications to the Blue Cross PHA which will become effective in FY2005.

The following projected key financial ratios are derived from the projected financial statements.

<i>Projected Key Financial Ratios</i>					
	<i>Fiscal Years Ending December 31</i>				
	<i>2005</i>	<i>2006</i>	<i>2007</i>	<i>2008</i>	<i>2009</i>
Debt Service Coverage Ratio ¹	2.39	2.09	1.80	2.02	2.26
Days' Cash on Hand	59.5	61.4	62.2	63.8	68.3
Unrestricted Cash / Long-Term Debt ²	27.7%	30.6%	33.2%	35.9%	40.4%
Long-Term Debt / Capitalization ²	59.6%	58.0%	56.9%	55.9%	54.1%
¹ Based on Maximum Annual Debt Service (MADS) of \$2,357,000 on the Series 2004 Bonds and Series 2005 Bonds, as set forth in the Preliminary Official Statement relating to the Series 2004 Bonds dated October 20, 2004; calculations for FY2005 and FY2006 take into account capitalized interest on the Series 2004 Bonds ² Based on \$27,120,000 estimated aggregate principal amount of Series 2004 Bonds and Series 2005 Bonds, as set forth in the Preliminary Official Statement relating to the Series 2004 Bonds dated October 20, 2004 Note: Calculated from Management's Financial Projections, using definitions published by Standard & Poor's Ratings Services					

FY2007 will be the first full FY after completion of the Improvement Project.

Projected financial statements and statements of assumptions are contained on the following pages.

OTSEGO MEMORIAL HOSPITAL PROJECTED BALANCE SHEET

ASSETS	Fiscal Years Ending December 31					
	2004	2005	2006	2007	2008	2009
CURRENT ASSETS						
Cash and cash equivalents	\$2,157,625	\$2,379,541	\$2,374,388	\$2,573,127	\$2,740,838	\$3,031,063
Accounts receivable	5,418,305	5,894,727	6,352,869	6,900,096	7,426,831	8,003,874
Cost report settlements receivable	250,000	250,000	250,000	250,000	250,000	250,000
Inventories	944,097	991,302	1,040,867	1,092,910	1,147,556	1,204,934
Prepaid expenses	630,375	661,894	694,989	729,738	766,225	804,536
Total current assets	9,400,402	10,177,464	10,713,113	11,545,871	12,331,450	13,294,407
INVESTMENTS	18,053,800	10,417,653	8,805,306	9,344,722	9,938,879	10,938,252
PROPERTY AND EQUIPMENT	18,819,722	26,545,273	27,772,724	26,106,649	24,312,003	22,388,786
DEFERRED CHARGES	352,123	430,386	408,649	386,912	365,175	343,438
Total assets	\$46,626,047	\$47,570,776	\$47,699,792	\$47,384,154	\$46,947,507	\$46,964,883
LIABILITIES AND NET ASSETS						
CURRENT LIABILITIES						
Current portion of long term debt	\$375,000	\$767,470	\$802,015	\$837,293	\$875,803	\$914,313
Accounts payable	1,457,140	1,566,540	1,686,388	1,832,746	1,976,498	2,133,180
Cost report settlements payable	275,000	275,000	275,000	275,000	275,000	275,000
Accrued expenses	2,020,731	2,121,768	2,227,856	2,339,249	2,456,211	2,579,022
Total current liabilities	4,127,871	4,730,778	4,991,259	5,284,288	5,583,512	5,901,515
OTHER LIABILITIES	163,622	140,399	116,479	91,842	66,466	40,328
LONG TERM DEBT	26,341,174	25,145,034	24,360,146	23,539,980	22,681,304	21,784,118
Total liabilities	30,632,667	30,016,211	29,467,884	28,916,110	28,331,282	27,725,961
NET ASSETS	15,993,380	17,554,565	18,231,908	18,468,044	18,616,225	19,238,922
Total liabilities and fund balance	\$46,626,047	\$47,570,776	\$47,699,792	\$47,384,154	\$46,947,507	\$46,964,883

OTSEGO MEMORIAL HOSPITAL
PROJECTED STATEMENT OF REVENUE AND EXPENSES

	Fiscal Years Ending December 31					
	2004	2005	2006	2007	2008	2009
OPERATING REVENUE						
Net patient service revenue	\$45,883,002	\$48,139,293	\$50,849,481	\$54,283,125	\$57,572,803	\$61,116,146
Other operating revenue	607,083	676,146	701,324	727,575	754,948	783,493
Total operating revenue	46,490,085	48,815,439	51,550,805	55,010,700	58,327,751	61,899,639
OPERATING EXPENSES						
Salaries and wages	19,378,354	20,806,362	21,733,402	22,547,330	23,342,144	24,162,607
Benefits	5,135,264	5,565,702	5,868,019	6,144,147	6,419,090	6,705,123
Insurance	931,868	987,780	1,047,047	1,109,870	1,176,462	1,247,050
Supplies	7,013,820	7,651,979	8,348,230	9,197,156	10,034,069	10,947,175
Drugs	1,882,934	2,112,652	2,370,396	2,734,489	3,068,097	3,442,405
Depreciation	1,997,563	2,090,420	2,494,319	2,916,075	3,044,646	3,173,218
Interest	627,411	501,352	1,055,097	1,593,717	1,558,439	1,519,930
Provision for bad debts	1,272,341	1,386,462	1,496,029	1,626,995	1,753,180	1,891,427
Professional Fees	2,340,000	2,433,600	2,530,944	2,632,183	2,737,470	2,846,969
Purchased Services	1,298,052	1,349,974	1,403,973	1,460,132	1,518,537	1,579,278
Other	3,153,840	3,332,346	3,534,759	3,770,923	4,009,794	4,268,701
Total operating expenses	45,031,447	48,218,629	51,882,215	55,733,017	58,661,928	61,783,883
INCOME (LOSS) FROM OPERATIONS	1,458,638	596,810	(331,410)	(722,317)	(334,177)	115,756
OTHER INCOME	447,987	464,375	508,753	458,453	482,358	506,941
REVENUE AND GAINS IN EXCESS OF EXPENSES	1,906,625	1,061,185	177,343	(263,864)	148,181	622,697
LOSS ON DEFEASANCE	(415,470)	0	0	0	0	0
TRANSFER FROM FOUNDATION	0	500,000	500,000	500,000	0	0
INCREASE IN NET ASSETS	1,491,155	1,561,185	677,343	236,136	148,181	622,697
Net Assets - Beginning of Year	14,502,225	15,993,380	17,554,565	18,231,908	18,468,044	18,616,225
Net Assets - End of Year	\$15,993,380	\$17,554,565	\$18,231,908	\$18,468,044	\$18,616,225	\$19,238,922

OTSEGO MEMORIAL HOSPITAL
PROJECTED STATEMENT OF CASH FLOWS

	Fiscal Years Ending December 31					
	2004	2005	2006	2007	2008	2009
CASH FLOWS FROM OPERATING ACTIVITIES AND NONOPERATING GAINS, NET						
Increase in net assets	\$1,491,155	\$1,561,185	\$677,343	\$236,136	\$148,181	\$622,697
Adjustments to reconcile increase in net assets to net cash from operating activities:						
Depreciation and amortization	2,019,483	2,129,284	2,533,183	2,954,939	3,083,510	3,212,082
Provision for bad debts	1,272,341	1,386,462	1,496,029	1,626,995	1,753,180	1,891,427
Loss on defeasance	415,470	0	0	0	0	0
Transfer from foundation	0	(500,000)	(500,000)	(500,000)	0	0
Changes in assets and liabilities:						
(Increase) decrease in assets:						
Accounts receivable	(1,696,943)	(1,862,884)	(1,954,171)	(2,174,222)	(2,279,915)	(2,468,470)
Other current assets	(169,957)	(78,724)	(82,660)	(86,792)	(91,133)	(95,689)
Increase (decrease) in liabilities:						
Accounts payable	146,888	109,399	119,848	146,358	143,753	156,681
Accrued expenses	96,225	101,037	106,088	111,393	116,962	122,811
Cost report settlements payable	(463,200)	0	0	0	0	0
Other long-term liabilities	(22,547)	(23,223)	(23,920)	(24,637)	(25,377)	(26,138)
Net cash provided by operating activities	3,088,915	2,822,536	2,371,740	2,290,170	2,849,161	3,415,401
CASH FLOWS FROM INVESTING ACTIVITIES						
Increase (decrease) in assets whose use is limited	(14,673,623)	7,636,147	1,612,347	(539,416)	(594,157)	(999,373)
Transfer from foundation	0	500,000	500,000	500,000	0	0
Purchase of property, plant, and equipment	(4,371,492)	(9,815,970)	(3,721,770)	(1,250,000)	(1,250,000)	(1,250,000)
Decrease in amounts due from affiliate	(19,045,115)	(1,679,823)	(1,609,423)	(1,289,416)	(1,844,157)	(2,249,373)
CASH FLOWS FROM FINANCING ACTIVITIES						
Proceeds from issuance of long-term debt	17,606,174	9,000,000	0	0	0	0
Cash loss on defeasance	(106,300)	0	0	0	0	0
Increase in deferred charges	(718,056)	(9,820,797)	(767,470)	(802,015)	(837,293)	(875,803)
Principal payments on long-term debt	(352,123)	(100,000)	0	0	0	0
Net cash provided by (used in) capital and related financing activities	16,429,695	(920,797)	(767,470)	(802,015)	(837,293)	(875,803)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	473,495	221,916	(5,153)	198,739	167,711	290,225
CASH AND EQUIVALENTS - Beginning of year	1,684,130	2,157,625	2,379,541	2,374,388	2,573,127	2,740,838
CASH AND EQUIVALENTS - End of year	\$2,157,625	\$2,379,541	\$2,374,388	\$2,573,127	\$2,740,838	\$3,031,063

**OTSEGO MEMORIAL HOSPITAL
KEY ASSUMPTIONS**

	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009
INPATIENT ASSUMPTIONS						
Admissions						
Acute	2,146	2,196	2,246	2,271	2,296	2,321
Nursery	300	300	300	300	300	300
Increase		50	50	25	25	25
Acute	2.90	2.90	2.90	2.90	2.90	2.90
Nursery	1.80	1.80	1.80	1.80	1.80	1.80
Inpatient Annual Charge Increase	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
LONG-TERM CARE ASSUMPTIONS						
Patient Days	11,150	11,150	11,150	11,150	11,150	11,150
Patient Days Available	12,444	12,410	12,410	12,410	12,410	12,410
Occupancy Percentage	89.60%	89.85%	89.85%	89.85%	89.85%	89.85%
Daily Room Rate	206	212	219	225	232	239
Admissions	100	100	100	100	100	100
OUTPATIENT ASSUMPTIONS						
Annual Charge Increase	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
VOLUME INCREASES						
Operating and Recovery Room	1.00%	3.00%	3.00%	5.00%	3.00%	3.00%
Anesthesiology	-1.00%	2.00%	2.00%	4.00%	2.00%	2.00%
Radiology	0.00%	3.00%	3.00%	5.00%	3.00%	3.00%
Laboratory	8.00%	8.00%	8.00%	10.00%	8.00%	8.00%
Emergency Room	2.00%	2.00%	2.00%	4.00%	2.00%	2.00%
MRI	6.00%	6.00%	6.00%	8.00%	6.00%	6.00%
CT Scan	12.00%	8.00%	8.00%	10.00%	8.00%	8.00%
Nuclear Medicine	10.00%	8.00%	12.00%	14.00%	12.00%	12.00%
Medical Supplies	10.00%	10.00%	6.00%	8.00%	6.00%	6.00%
Physical Therapy	16.00%	12.00%	12.00%	14.00%	12.00%	12.00%
EKG	7.00%	7.00%	7.00%	9.00%	7.00%	7.00%
Drugs	30.00%	10.00%	10.00%	12.00%	10.00%	10.00%
All Other	-20.00%	2.00%	2.00%	4.00%	2.00%	2.00%
Overall outpatient increase	9.61%	10.13%	10.03%	12.20%	10.22%	10.31%

**OTSEGO MEMORIAL HOSPITAL
KEY ASSUMPTIONS**

MEDICARE ASSUMPTIONS

Inpatient

DRG Increase	4.64%	3.00%	3.00%	3.00%	3.00%	3.00%
Federal Capital Rate Increase	0.42%	1.00%	1.00%	1.00%	1.00%	1.00%
Case Mix Index	1.42000	1.42000	1.42000	1.42000	1.42000	1.42000

Skilled Nursing

Reimbursement per day	280.00	282.80	285.63	288.48	291.37	294.28
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Outpatient

Laboratory	28.29%	27.64%	26.99%	26.34%	25.69%	25.04%
Rehabilitative Therapy						
APC (after 08-01-00)	35.51%	34.86%	34.21%	33.56%	32.91%	32.26%

Hold Harmless Reimbursement	500,000	500,000	0	0	0	0
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Decrease in Expected Outpatient Reimbursement	0.65%	0.65%	0.65%	0.65%	0.65%	0.65%
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BLUE CROSS

Annual Allowable Increase	3.30%	3.30%	3.30%	3.30%	3.30%	3.30%
Reimbursement Percentage, per PHA modification		90.00%	88.50%	87.00%	85.50%	84.00%
			99.33%	98.66%	97.99%	97.33%
Reimbursement Percentage	97.609%	90.000%	87.904%	85.833%	83.785%	81.761%
		90.000%	87.938%	85.888%	83.851%	81.827%

MEDICAID

Inpatient Reimbursement %	54.00%	54.00%	54.00%	54.00%	54.00%	54.00%
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Outpatient Reimbursement %	29.31%	28.66%	28.01%	27.36%	26.71%	26.06%
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LTC RATE

Variable Costs	181.60	183.42	185.25	187.10	188.97	190.86
Capital Costs	5.41	5.41	5.41	5.41	5.41	5.41
Executive Order Reduction	(3.33)					
	<u>183.68</u>	<u>188.83</u>	<u>190.66</u>	<u>192.51</u>	<u>194.38</u>	<u>196.27</u>

LTC Rate Increase	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%
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**OTSEGO MEMORIAL HOSPITAL
KEY ASSUMPTIONS**

EXPENSES

FTEs	419.00	425.00	431.00	437.00	442.00	447.00
Physician FTEs	63.70	63.70	63.70	63.70	63.70	63.70
Net Hospital FTE's	355.30	361.30	367.30	373.30	378.30	383.30
FTE Increase	10	6	6	6	5	5
Annual Salary Increase	4.00%	3.00%	3.00%	2.50%	2.50%	2.50%
Fringe Benefit Percentage	26.50%	26.75%	27.00%	27.25%	27.50%	27.75%
Insurance Cost	27.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Supplies	9.00%	7.00%	7.00%	7.00%	7.00%	7.00%
Drugs	8.00%	10.00%	10.00%	12.00%	10.00%	10.00%
Food	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Utilities	1.00%	3.00%	3.00%	3.00%	3.00%	3.00%
Professional Fees	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
Purchased Services	0.00%	4.00%	4.00%	4.00%	4.00%	4.00%
Other	20.00%	8.00%	8.00%	8.00%	8.00%	8.00%
Volume Adjustments	2.00%	2.00%	2.00%	3.00%	2.00%	2.00%
Bad Debt Percentage (of Gross Revenue)	1.85%	1.85%	1.85%	1.85%	1.85%	1.85%

OTHER

Charity Care Percentage (of Gross Revenue)	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%
Other Contractuals as Percentage (of Gross Revenue)	2.71%	2.81%	2.91%	3.01%	3.11%	3.21%
Interest Income Earnings Percentage	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
Fixed Asset Additions	1,000,000	1,000,000	1,250,000	1,250,000	1,250,000	1,250,000
Days in accounts receivable	60	60	60	60	60	60
Days in Accounts Payable	32	32	32	32	32	32

OTHER OPERATING REVENUE

CAFETERIA	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
OTHER	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%

OTSEGO MEMORIAL HOSPITAL
DETAILED ASSUMPTIONS - PATIENT DAYS AND DISCHARGES

	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009
PATIENT DAYS						
MEDICAL/SURGICAL	6,223	6,368	6,513	6,586	6,658	6,731
SKILLED NURSING FACILITY	11,150	11,150	11,150	11,150	11,150	11,150
NURSERY	540	540	540	540	540	540
TOTAL PATIENT DAYS	17,913	18,058	18,203	18,276	18,348	18,421
PATIENT DAYS (NET OF NURSERY AND SNF)	6,223	6,368	6,513	6,586	6,658	6,731
DISCHARGES						
MEDICAL/SURGICAL	2,146	2,196	2,246	2,271	2,296	2,321
SKILLED NURSING FACILITY	99	101	104	105	106	107
NURSERY	300	300	300	300	300	300
TOTAL DISCHARGES	2,545	2,597	2,650	2,676	2,702	2,728
DISCHARGES (NET OF NURSERY AND SNF)	2,146	2,196	2,246	2,271	2,296	2,321
LENGTH OF STAY						
MEDICAL/SURGICAL	2.90	2.90	2.90	2.90	2.90	2.90
SKILLED NURSING FACILITY	112.51	109.95	107.50	106.32	105.16	104.03
NURSERY	1.80	1.80	1.80	1.80	1.80	1.80

OTSEGO MEMORIAL HOSPITAL
DETAILED ASSUMPTIONS - INPATIENT PROGRAM REVENUE, DAYS & DISCHARGES

	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009
INPATIENT DAYS (NET OF NURSERY)						
MEDICARE	3,359	3,437	3,515	3,554	3,593	3,632
MEDICAID	629	644	659	666	673	681
BLUE CROSS	529	542	554	560	567	573
BLUE CROSS TRUST	860	880	900	910	920	930
ALL OTHER	846	865	885	895	905	915
TOTAL INPATIENT DAYS	6,223	6,368	6,513	6,586	6,658	6,731
DISCHARGES (NET OF NURSERY)						
MEDICARE	982	1,006	1,029	1,041	1,052	1,064
MEDICAID	271	259	265	268	271	274
BLUE CROSS	202	159	163	165	166	168
BLUE CROSS TRUST	340	407	416	421	426	430
ALL OTHER	351	365	373	377	381	385
TOTAL DISCHARGES	2,146	2,196	2,246	2,271	2,296	2,321
LENGTH OF STAY (BY PROGRAM)						
MEDICARE	3.42	3.42	3.42	3.42	3.42	3.42
MEDICAID	2.32	2.49	2.49	2.49	2.49	2.49
BLUE CROSS	2.62	3.40	3.40	3.40	3.40	3.40
BLUE CROSS TRUST	2.53	2.16	2.16	2.16	2.16	2.16
ALL OTHER	2.41	2.37	2.37	2.37	2.37	2.37
TOTAL DISCHARGES	2.90	2.90	2.90	2.90	2.90	2.90
IP REVENUE						
MEDICARE	11,593,492	12,354,698	13,141,315	13,819,343	14,530,120	15,275,396
MEDICAID	1,913,260	1,900,501	2,021,609	2,125,758	2,235,223	2,349,845
BLUE CROSS	1,739,826	1,426,122	1,516,884	1,595,178	1,677,321	1,763,395
BLUE CROSS TRUST	3,096,040	3,855,396	4,100,988	4,312,518	4,534,511	4,767,189
ALL OTHER	3,093,363	3,341,760	3,554,696	3,737,913	3,930,391	4,131,945
TOTAL	21,435,981	22,878,477	24,335,492	25,590,710	26,907,566	28,287,770
AVERAGE REVENUE PER DISCHARGE						
MEDICARE	11,806	12,278	12,769	13,280	13,811	14,363
MEDICAID	7,060	7,342	7,636	7,941	8,259	8,589
BLUE CROSS	8,613	8,958	9,316	9,689	10,077	10,480
BLUE CROSS TRUST	9,106	9,470	9,849	10,243	10,653	11,079
ALL OTHER	8,813	9,166	9,533	9,914	10,311	10,723
TOTAL	9,989	10,388	10,804	11,236	11,685	12,152

OTSEGO MEMORIAL HOSPITAL
DETAILED ASSUMPTIONS - SNF PROGRAM REVENUE, DAYS & DISCHARGES

SNF DAYS	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009
MEDICARE	2,148	2,093	2,093	2,093	2,093	2,093
MEDICAID	6,333	6,450	6,450	6,450	6,450	6,450
BLUE CROSS	0	0	0	0	0	0
ALL OTHER	2,669	2,607	2,607	2,607	2,607	2,607
TOTAL INPATIENT DAYS	11,150	11,150	11,150	11,150	11,150	11,150
BED DAYS AVAILABLE	12,444	12,410	12,410	12,410	12,410	12,410
PERCENT OCCUPANCY	89.60%	89.85%	89.85%	89.85%	89.85%	89.85%
SNF DAILY ROUTINE RATE	206	212	219	225	232	239
SNF ROUTINE REVENUE						
MEDICARE	442,488	444,093	457,416	471,138	485,272	499,830
MEDICAID	1,304,598	1,368,561	1,409,618	1,451,906	1,495,464	1,540,327
BLUE CROSS	0	0	0	0	0	0
ALL OTHER	549,814	553,153	569,748	586,840	604,446	622,579
	2,296,900	2,365,807	2,436,781	2,509,885	2,585,181	2,662,737
SNF ANCILLARY REVENUE						
MEDICARE	403,413	419,549	436,331	453,785	471,936	490,813
MEDICAID BILLABLE	189,495	197,075	204,958	213,156	221,683	230,550
MEDICAID NON BILLABLE	0	0	0	0	0	0
BLUE CROSS	0	0	0	0	0	0
ALL OTHER	105,779	110,011	114,411	118,987	123,747	128,697
	698,688	726,635	755,701	785,929	817,366	850,060

OTSEGO MEMORIAL HOSPITAL
GROSS REVENUE AND PAYOR MIX ASSUMPTIONS

TOTAL CHARGES BY PROGRAM						
MEDICARE	24,990,629	27,041,527	29,244,726	31,810,186	34,296,976	37,015,520
MEDICAID	6,853,628	7,261,659	7,812,402	8,476,722	9,117,057	9,818,042
BLUE CROSS	15,067,790	16,104,750	17,667,791	19,717,215	21,650,996	23,796,948
ALL OTHER	11,365,688	12,393,540	13,468,856	14,800,212	16,073,240	17,475,066
TOTAL	58,277,736	62,801,476	68,193,774	74,804,335	81,138,269	88,105,576
REVENUE BY PAYOR						
MEDICARE	42.88%	43.06%	42.88%	42.52%	42.27%	42.01%
MEDICAID	11.76%	11.56%	11.46%	11.33%	11.24%	11.14%
BLUE CROSS	25.86%	25.64%	25.91%	26.36%	26.68%	27.01%
ALL OTHER	19.50%	19.73%	19.75%	19.79%	19.81%	19.83%
TOTAL	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%

**OTSEGO MEMORIAL HOSPITAL
DETAILED ASSUMPTIONS - OUTPATIENT REVENUE**

OUTPATIENT REVENUE	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009
OPERATING/RECOVERY ROOM	3,646,179	3,905,787	4,183,879	4,568,796	4,894,094	5,242,554
ANESTHESIOLOGY	1,896,843	2,012,171	2,134,512	2,308,688	2,449,056	2,597,958
RADIOLOGY	4,151,515	4,447,102	4,763,736	5,202,000	5,572,382	5,969,136
LAB	6,668,482	7,490,039	8,412,812	9,624,257	10,809,965	12,141,753
EMERGENCY ROOM	4,256,465	4,515,258	4,789,786	5,180,633	5,495,615	5,829,749
CT SCAN	3,052,294	3,364,849	3,709,410	4,166,409	4,593,049	5,063,378
MRI	1,756,708	1,973,135	2,216,225	2,535,361	2,847,718	3,198,557
NUCLEAR MEDICINE	1,065,678	1,196,970	1,394,231	1,653,000	1,925,414	2,242,722
MEDICAL SUPPLIES	2,769,020	3,167,759	3,492,137	3,922,369	4,324,019	4,766,799
PHYSICAL THERAPY	1,026,715	1,195,918	1,393,005	1,651,547	1,923,722	2,240,751
EKG	1,800,899	2,004,040	2,230,096	2,528,037	2,813,199	3,130,528
PHARMACY	3,203,715	3,665,050	4,192,818	4,883,794	5,587,060	6,391,597
ALL OTHER	1,647,693	1,747,873	1,854,143	2,005,441	2,127,372	2,256,716
	<u>36,942,207</u>	<u>40,685,952</u>	<u>44,766,789</u>	<u>50,230,331</u>	<u>55,362,667</u>	<u>61,072,198</u>
VOLUME INCREASE						
Operating and Recovery Room	1.00%	3.00%	3.00%	5.00%	3.00%	3.00%
Anesthesiology	-1.00%	2.00%	2.00%	4.00%	2.00%	2.00%
Radiology	0.00%	3.00%	3.00%	5.00%	3.00%	3.00%
Laboratory	8.00%	8.00%	8.00%	10.00%	8.00%	8.00%
Emergency Room	2.00%	2.00%	2.00%	4.00%	2.00%	2.00%
MRI	6.00%	6.00%	6.00%	8.00%	6.00%	6.00%
CT Scan	12.00%	8.00%	8.00%	10.00%	8.00%	8.00%
Nuclear Medicine	10.00%	8.00%	12.00%	14.00%	12.00%	12.00%
Medical Supplies	10.00%	10.00%	6.00%	8.00%	6.00%	6.00%
Physical Therapy	16.00%	12.00%	12.00%	14.00%	12.00%	12.00%
EKG	7.00%	7.00%	7.00%	9.00%	7.00%	7.00%
Pharmacy	30.00%	10.00%	10.00%	12.00%	10.00%	10.00%
All Other	-20.00%	2.00%	2.00%	4.00%	2.00%	2.00%
Overall	9.61%	10.13%	10.03%	12.20%	10.22%	10.31%
OUTPATIENT REVENUE BY PROGRAM						
MEDICARE	12,551,236	13,823,186	15,209,664	17,065,920	18,809,648	20,749,480
MEDICAID	3,446,275	3,795,522	4,176,217	4,685,901	5,164,688	5,697,320
BLUE CROSS	13,327,964	14,678,628	16,150,907	18,122,037	19,973,675	22,033,553
ALL OTHER	7,616,732	8,388,616	9,230,001	10,356,472	11,414,656	12,591,845
	<u>36,942,207</u>	<u>40,685,952</u>	<u>44,766,789</u>	<u>50,230,330</u>	<u>55,362,667</u>	<u>61,072,198</u>
MEDICARE OP REVENUE SPLIT						
Fee Screen	2,889,501	3,182,325	3,501,515	3,928,855	4,330,290	4,776,871
APC's (after 08-01-00)	9,661,735	10,640,861	11,708,149	13,137,065	14,479,358	15,972,609
	<u>12,551,236</u>	<u>13,823,186</u>	<u>15,209,664</u>	<u>17,065,920</u>	<u>18,809,648</u>	<u>20,749,480</u>

OTSEGO MEMORIAL HOSPITAL
DETAILED ASSUMPTIONS - MEDICARE CONTRACTUAL COMPUTATION

	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009
INPATIENT						
I/P REVENUE	11,593,492	12,354,698	13,141,315	13,819,343	14,530,120	15,275,396
REIMBURSEMENT/CASE	4,103	4,226	4,353	4,484	4,619	4,758
CASE MIX	1.4200	1.4200	1.4200	1.4200	1.4200	1.4200
MEDICARE DISCHARGES	982	1,006	1,029	1,041	1,052	1,064
REIMBURSEMENT	5,721,178	6,038,407	6,361,491	6,625,875	6,900,497	7,185,552
MEDICARE BAD DEBTS	25,000	25,000	25,000	25,000	25,000	25,000
TOTAL IP REIMBURSEMENT	5,746,178	6,063,407	6,386,491	6,650,875	6,925,497	7,210,552
CONTRACTUAL ADJUSTMENT	5,847,314	6,291,292	6,754,823	7,168,467	7,604,623	8,064,845
	50.44%	50.92%	51.40%	51.87%	52.34%	52.80%
INPATIENT CAPITAL						
BLENDED RATE	381.28	385.09	388.94	392.83	396.76	400.73
MEDICARE CASES	982	1,006	1,029	1,041	1,052	1,064
CASE MIX	1.4200	1.4200	1.4200	1.4200	1.4200	1.4200
MEDICARE INPATIENT CAPITAL	531,672	550,244	568,398	580,473	592,735	605,184
SKILLED NURSING FACILITY						
SNF REVENUE	845,901	863,642	893,747	924,923	957,208	990,644
REIMBURSEMENT	601,440	591,900	597,819	603,798	609,836	615,934
REIMBURSEMENT %	71.10%	68.54%	66.89%	65.28%	63.71%	62.18%
MEDICARE DAYS	2,148	2,093	2,093	2,093	2,093	2,093
REIMBURSEMENT PER DAY	280.00	282.80	285.63	288.48	291.37	294.28
OUTPATIENT SERVICES						
<i>MEDICARE FEE SCREEN REVENUE</i>	2,889,501	3,182,325	3,501,515	3,928,855	4,330,290	4,776,871
REIMBURSEMENT	817,368	879,516	944,972	1,034,763	1,112,344	1,196,010
CONTRACTUAL	2,072,133	2,302,809	2,556,543	2,894,092	3,217,946	3,580,861
PERCENTAGE	28.29%	27.64%	26.99%	26.34%	25.69%	25.04%
<i>MEDICARE O/P APC'S</i>	9,661,735	10,640,861	11,708,149	13,137,065	14,479,358	15,972,609
REIMBURSEMENT	3,430,882	3,709,404	4,005,358	4,408,799	4,765,157	5,152,764
CONTRACTUAL	6,230,853	6,931,457	7,702,791	8,728,266	9,714,201	10,819,845
PERCENTAGE	35.51%	34.86%	34.21%	33.56%	32.91%	32.26%
BBA O/P "HOLD HARMLESS" CAPITAL REIMBURSEMENT	500,000	500,000	0	0	0	0
TOTAL MEDICARE REVENUE	24,990,629	27,041,527	29,244,726	31,810,186	34,296,976	37,015,520
TOTAL MEDICARE REIMBURSEMENT	11,627,540	12,294,471	12,503,039	13,278,708	14,005,568	14,780,443
CUSHION	100,000	100,000	100,000	100,000	100,000	100,000
O/P Bad Debts	50,000	50,000	50,000	50,000	50,000	50,000
TOTAL MEDICARE CONTRACTUALS	13,413,088	14,797,056	16,791,687	18,581,477	20,341,408	22,285,077
MEDICARE CONTRACTUAL PERCENTAGE	53.67%	54.72%	57.42%	58.41%	59.31%	60.20%

OTSEGO MEMORIAL HOSPITAL
DETAILED ASSUMPTIONS - MEDICAID CONTRACTUAL COMPUTATION

	PROJECTED	PROJECTED	PROJECTED	PROJECTED	PROJECTED	PROJECTED
	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009
INPATIENT						
TOTAL I/P MEDICAID REVENUE	1,913,260	1,900,501	2,021,609	2,125,758	2,235,223	2,349,845
REIMBURSEMENT %	54.00%	54.00%	54.00%	54.00%	54.00%	54.00%
I/P REIM	1,033,160	1,026,271	1,091,669	1,147,909	1,207,020	1,268,916
INPATIENT CAPITAL						
TOTAL ESTIMATED CAPITAL REIMBURSEMENT	75,000	85,000	85,000	85,000	85,000	85,000
SKILLED NURSING FACILITY						
SNF ROUTINE REVENUE	1,304,598	1,368,561	1,409,618	1,451,906	1,495,464	1,540,327
SNF DAILY ROUTINE DAYS	6,333	6,450	6,450	6,450	6,450	6,450
SNF DAILY REIMBURSEMENT RATE	183.68	188.83	190.66	192.51	194.38	196.27
ROUTINE REIMBURSEMENT	1,163,245	1,217,928	1,229,758	1,241,707	1,253,775	1,265,964
SNF ANCILLARY BILLABLE REVENUE	189,495	197,075	204,958	213,156	221,683	230,550
SNF ANCILLARY REIMBURSEMENT	93,801	96,567	99,405	102,316	105,300	108,359
REIMBURSEMENT %	49.50%	49.00%	48.50%	48.00%	47.50%	47.00%
	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%
OUTPATIENT						
O/P MEDICAID ANCILLARY REVENUE	3,446,275	3,795,522	4,176,217	4,685,901	5,164,688	5,697,320
REIMBURSEMENT	1,010,228	1,087,934	1,169,910	1,282,232	1,379,675	1,484,928
CONTRACTUAL	2,436,047	2,707,588	3,006,307	3,403,669	3,785,013	4,212,392
	29.31%	28.66%	28.01%	27.36%	26.71%	26.06%
TOTAL MEDICAID REVENUE	6,853,628	7,261,659	7,812,402	8,476,722	9,117,057	9,818,042
TOTAL MEDICAID REIMBURSEMENT	3,375,435	3,513,700	3,675,742	3,859,164	4,030,770	4,213,167
CUSHION	50,000	50,000	50,000	50,000	50,000	50,000
TOTAL MEDICAID CONTRACTUALS	3,528,194	3,797,960	4,186,660	4,667,558	5,136,287	5,654,875
MEDICAID CONTRACTUAL PERCENTAGE	51.48%	52.30%	53.59%	55.06%	56.34%	57.60%

**OTSEGO MEMORIAL HOSPITAL
DETAILED ASSUMPTIONS - BLUE CROSS CONTRACTUAL COMPUTATION**

ANNUAL UPDATE FACTOR	3.30%	3.30%	3.30%	3.30%	3.30%	3.30%	3.30%
	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009	PROJECTED FY2009
TOTAL BLUE CROSS REVENUE	15,067,790	16,104,750	17,667,791	19,717,215	21,650,996	23,796,948	23,796,948
BLUE CROSS TRUST INPATIENT	3,096,040	3,855,396	4,100,988	4,312,518	4,534,511	4,767,189	4,767,189
BLUE CROSS TRADITIONAL %	18,163,830	19,960,145	21,768,779	24,029,734	26,185,507	28,564,137	28,564,137
BLUE CROSS TRUST %	97.66%	90.00%	87.90%	85.83%	83.79%	81.76%	81.76%
	81.05%	74.70%	79.11%	77.25%	75.41%	73.59%	73.59%
TOTAL BLUE CROSS REIMBURSEMENT	14,714,573	14,494,275	15,530,753	16,923,836	18,140,320	19,456,668	19,456,668
BLUE CROSS TRUST REIMBURSEMENT	2,509,474	2,879,981	3,244,452	3,331,399	3,419,322	3,507,939	3,507,939
CUSHION	17,224,047	17,374,255	18,775,204	20,255,235	21,559,642	22,964,608	22,964,608
	(200,000)	(175,000)	(150,000)	0	0	0	0
BLUE CROSS CONTRACTUALS	739,783	2,410,890	2,843,575	3,774,499	4,625,865	5,599,529	5,599,529
PHYSICIAN PROVISION	2,833,299	3,132,669	3,237,464	3,334,588	3,434,626	3,537,665	3,537,665
TOTAL CONTRACTUALS	20,514,364	24,138,575	27,059,386	30,358,122	33,538,186	37,077,146	37,077,146
BLUE CROSS CONTRACTUAL PERCENTAGE	4.07%	12.08%	13.06%	15.71%	17.67%	19.60%	19.60%
TOTAL ALLOWANCE PERCENTAGE	29.83%	32.21%	33.46%	34.52%	35.39%	36.27%	36.27%

OTSEGO MEMORIAL HOSPITAL
DETAILED EXPENSE ASSUMPTIONS AND PROJECTIONS

	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009
DAYS REV IN A/R	60	60	60	60	60	60
DAYS EXP IN A/P	32	32	32	32	32	32
TOTAL SALARY EXPENSE	19,378,354	20,806,362	21,733,402	22,547,330	23,342,144	24,162,607
LESS PHYSICIAN SALARY	4,642,968	5,372,611	5,572,646	5,711,962	5,854,761	6,001,130
	14,735,386	15,433,752	16,160,757	16,835,368	17,487,384	18,161,478
TOTAL FTE'S	419.00	425.00	431.00	437.00	442.00	447.00
PHYSICIAN FTE'S	63.70	63.70	63.70	63.70	63.70	63.70
NET FTE'S	355.30	361.30	367.30	373.30	378.30	383.30
SALARY PER FTE - EXCLUDING PHYSICIAN	41,473	42,717	43,999	45,099	46,226	47,382
SALARY PER FTE - PHYSICIAN OFFICES	67,793	69,826	71,921	73,719	75,562	77,451
AVERAGE ANNUAL SALARY INCREASE	4.00%	3.00%	3.00%	2.50%	2.50%	2.50%
ESTIMATED SALARY COST - NON PHYSICIAN	14,735,386	15,433,752	16,160,757	16,835,368	17,487,384	18,161,478
FRINGE BENEFIT PERCENTAGE	26.50%	26.75%	27.00%	27.25%	27.50%	27.75%
ANNUAL INCREASE IN:						
Insurance Cost	27.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Supplies	9.00%	7.00%	7.00%	7.00%	7.00%	7.00%
Drugs	8.00%	10.00%	10.00%	12.00%	10.00%	10.00%
Food	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Utilities	1.00%	3.00%	3.00%	3.00%	3.00%	3.00%
Professional Fees	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
Purchased Services	0.00%	4.00%	4.00%	4.00%	4.00%	4.00%
Other	20.00%	8.00%	8.00%	8.00%	8.00%	8.00%
OTHER COSTS	22.40%	10.16%	10.16%	11.24%	10.16%	10.16%
HOSPITAL	1,310,527	1,443,677	1,590,354	1,769,110	1,948,851	2,146,855
MISCELLANEOUS FEES AND CHARGES	25,000	25,000	25,000	25,000	25,000	25,000
ANNUNTY FOR RETIRED EXECUTIVE	5,800	5,800	5,800	5,800	5,800	5,800
PHYSICIAN OFFICE	1,077,829	1,101,143	1,134,177	1,168,203	1,203,249	1,239,346
TOTAL	2,419,156	2,575,620	2,755,332	2,968,113	3,182,900	3,417,001
	21.177%	2.163%	3.000%	3.000%	3.000%	3.000%
PROFESSIONAL FEES	23.42%	6.47%	6.98%	7.72%	7.24%	7.35%
Laboratory	525,000	546,000	567,840	590,554	614,176	638,743
Anesthesia						
Sleep Lab	175,000	182,000	189,280	196,851	204,725	212,914
Administratiron	245,000	254,800	264,992	275,592	286,616	298,081
Marketings	125,000	130,000	135,200	140,608	146,232	152,081
ER Physicians	200,000	208,000	216,320	224,973	233,972	243,331
MRI	400,000	416,000	432,640	449,946	467,944	486,662
Blood Bank	140,000	145,600	151,424	157,481	163,780	170,331
Operating Room	5,000	5,200	5,408	5,624	5,849	6,083
Other	525,000	546,000	567,840	590,554	614,176	638,743
Total	2,340,000	2,433,600	2,530,944	2,632,183	2,737,470	2,846,969
VOLUME INCREASES	2.00%	2.00%	2.00%	3.00%	2.00%	2.00%

OTSEGO MEMORIAL HOSPITAL
DETAILED ASSUMPTIONS - IMPROVEMENT PROJECT COST AND DEPRECIATION

	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009
DEPRECIATION CALCULATION						
OLD	1,926,134	1,926,134	1,926,134	1,926,134	1,926,134	1,926,134
NEW	71,429	214,286	375,000	553,571	732,143	910,714
NEW BUILDING			293,185	586,369	586,369	586,369
ESTIMATED REDUCTION FOR FULLY DEPRECIATED EQUIPMENT		(50,000)	(100,000)	(150,000)	(200,000)	(250,000)
	<u>1,997,563</u>	<u>2,090,420</u>	<u>2,494,319</u>	<u>2,916,075</u>	<u>3,044,646</u>	<u>3,173,218</u>
ROUTINE CAPITAL ADDITIONS						
AVERAGE LIFE	7.00	7.00	7.00	7.00	7.00	7.00
DEPRECIATION	<u>142,857</u>	<u>142,857</u>	<u>178,571</u>	<u>178,571</u>	<u>178,571</u>	<u>178,571</u>
IMPROVEMENT PROJECT						
Cost			14,659,232			
Years (life)			<u>25</u>			
			<u>586,369</u>			
Fixed Asset Addition Summary						
Routine Capital Additions	1,000,000	1,000,000	1,250,000	1,250,000	1,250,000	1,250,000
Improvement Project Costs	3,269,846	7,776,177	1,908,504			
Capitalized Interest Expense	121,001	1,146,330	573,165			
Capitalized Interest Income	(19,355)	(106,537)	(9,899)			
	<u>4,371,492</u>	<u>9,815,970</u>	<u>3,721,770</u>	<u>1,250,000</u>	<u>1,250,000</u>	<u>1,250,000</u>
Improvement Project Funds Summary						
Project Fund						
Beginning Balance	12,954,527	9,684,681	1,908,504	0	0	0
Earnings	16,779	87,122	5,843			
Draws	(1,468,092)	(7,776,177)	(1,908,504)	0	0	0
Draw at Close	(1,801,754)					
Transfer to Capitalized Interest Fund	(16,779)	(87,122)	(5,843)			
Ending Balance	<u>9,684,681</u>	<u>1,908,504</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Capitalized Interest Fund						
Beginning Balance	1,626,617	1,530,105	538,948	0	0	0
Earnings	2,576	19,415	4,056			
Interest Payments	(121,001)	(1,146,330)	(573,165)	0	0	0
Transfer from Project Fund	16,779	87,122	5,843			
Transfer from Debt Service Reserve Fund	5,134	48,636	24,318			
Ending Balance	<u>1,530,105</u>	<u>538,948</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total Interest Income	19,355	106,537	9,899			

OTSEGO MEMORIAL HOSPITAL CAPITAL FINANCING ASSUMPTIONS

	PROJECTED FY2004	PROJECTED FY2005	PROJECTED FY2006	PROJECTED FY2007	PROJECTED FY2008	PROJECTED FY2009
INTEREST CALCULATION						
Series 1995 Bonds	319,182					
Letter of Credit Fees	87,000					
Series 2001 Bonds	170,150					
Mortgage Loan	19,348					
Series 2004 Bonds	130,812	1,239,275	1,239,275	1,239,275	1,239,275	1,239,275
Less Capitalized Interest	(121,001)	(1,146,330)	(573,165)			
Series 2005 Bonds		369,543	350,123	315,578	280,300	241,791
AMORTIZATION - BOND DISCOUNT	21,920	38,864	38,864	38,864	38,864	38,864
	<u>627,411</u>	<u>501,352</u>	<u>1,055,097</u>	<u>1,593,717</u>	<u>1,558,439</u>	<u>1,519,930</u>
REPAYMENT OF DEBT						
Series 1995 Bonds	170,000	5,145,000				
Series 2001 Bonds	185,000	3,965,000				
Mortgage Loan	363,056					
Series 2004 Bonds		0	0	0	0	0
Series 2005 Bonds	0	710,797	767,470	802,015	837,293	875,803
	<u>718,056</u>	<u>9,820,797</u>	<u>767,470</u>	<u>802,015</u>	<u>837,293</u>	<u>875,803</u>
ANNUAL DEBT SERVICE (Net of Amortization)	1,323,547	10,283,285	1,783,703	2,356,868	2,356,868	2,356,869
SERIES 2004 BONDS						
BEGINNING	0	352,123	340,386	328,649	316,912	305,175
ADDITIONS	352,123					
AMORTIZATION		(11,737)	(11,737)	(11,737)	(11,737)	(11,737)
ENDING	<u>352,123</u>	<u>340,386</u>	<u>328,649</u>	<u>316,912</u>	<u>305,175</u>	<u>293,438</u>
SERIES 2005 BONDS						
BEGINNING	0	0	90,000	80,000	70,000	60,000
ADDITIONS		100,000				
AMORTIZATION		(10,000)	(10,000)	(10,000)	(10,000)	(10,000)
ENDING	<u>0</u>	<u>90,000</u>	<u>80,000</u>	<u>70,000</u>	<u>60,000</u>	<u>50,000</u>
BOND DISCOUNT						
BEGINNING	0	513,826	496,699	479,572	462,445	445,318
ADDITIONS	513,826					
AMORTIZATION		(17,127)	(17,127)	(17,127)	(17,127)	(17,127)
ENDING	<u>513,826</u>	<u>496,699</u>	<u>479,572</u>	<u>462,445</u>	<u>445,318</u>	<u>428,191</u>

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