

Audited Financial Statements

CMU Medical Education Partners

*Years Ended June 30, 2014 and 2013
with Report of Independent Auditors*

Audited Financial Statements
CMU Medical Education Partners
Years Ended June 30, 2014 and 2013

Table of Contents

Report of Independent Auditors	1
Balance Sheets	3
Statements of Operations	4
Statements of Changes in Net Assets	5
Statements of Cash Flows	6
Notes to Financial Statements.....	7

Report of Independent Auditors

To the Board of Trustees of
CMU Medical Education Partners

Report on the Financial Statements

We have audited the accompanying financial statements of Saginaw Cooperative Hospitals Inc. d/b/a CMU Medical Education Partners, which comprise the balance sheets as of June 30, 2014 and 2013, and the related statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of CMU Medical Education Partners as of June 30, 2014 and 2013, and the results of its operations, changes in its net assets, and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated August 19, 2014 on our consideration of CMU Medical Education Partners' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering CMU Medical Education Partners' internal control over financial reporting and compliance.

Andrews Hooper Paulik PLC

Saginaw, Michigan
August 19, 2014

CMU Medical Education Partners

Balance Sheets

	June 30	
	2014	2013
Assets		
Current assets:		
Cash	\$ 3,120,798	\$ 2,970,511
Patient accounts receivable, less allowance for doubtful accounts of \$409,157 in 2014 and \$157,825 in 2013	962,718	407,322
Other receivables	1,578,855	1,579,576
Prepaid expenses and other assets	513,862	447,821
Total current assets	<u>6,176,233</u>	5,405,230
Assets whose use is limited:		
By the Board of Trustees	169,758	115,923
Under professional liability funding arrangement – held by the trustee	614,345	1,611,054
Total assets whose use is limited	<u>784,103</u>	1,726,977
Medical education funding receivable, less allowance of \$1,476,088 in 2014 and \$1,600,093 in 2013	435,680	435,680
Leasehold improvements, furniture, and equipment, net	556,313	606,366
Total assets	<u>\$ 7,952,329</u>	<u>\$ 8,174,253</u>
Liabilities and net assets		
Current liabilities:		
Accounts payable	\$ 964,591	\$ 486,937
Other liabilities	1,041	8,761
Other accrued liabilities	34,783	34,783
Payroll and related liabilities	1,384,554	1,110,824
Total current liabilities	<u>2,384,969</u>	1,641,305
Estimated professional liability under self-insurance	393,596	557,346
Deferred revenue	49,930	2,437
Payable to CMU	242,872	310,862
Total liabilities	<u>3,071,367</u>	2,511,950
Net assets:		
Unrestricted:		
Designated for professional liability	(3,487,583)	(3,581,793)
Undesignated	8,349,260	9,224,811
Temporarily restricted	19,285	19,285
Total net assets	<u>4,880,962</u>	5,662,303
Total liabilities and net assets	<u>\$ 7,952,329</u>	<u>\$ 8,174,253</u>

See accompanying notes.

CMU Medical Education Partners

Statements of Operations

	Year Ended June 30	
	2014	2013
Unrestricted revenues and other support:		
Member hospitals	\$ 16,160,145	\$ 15,473,183
Net patient service revenue	9,336,588	4,451,105
Interest income	529	3,197
Professional liability fund	25,936	57,377
Contracts and other revenue	7,189,873	6,797,259
Total unrestricted revenues and other support	<u>32,713,071</u>	<u>26,782,121</u>
Operating expenses:		
Salaries, wages, and payroll taxes	21,514,200	17,112,208
Employee benefits	3,733,171	3,151,102
Recruiting	221,093	636,321
Facility and equipment	1,299,112	1,111,414
Consumable supplies	476,592	393,094
Educational supplies and services	424,159	385,509
Consulting and contractual services	1,022,941	1,379,035
Communications	207,342	170,045
Educational conferences and travel	698,657	632,154
Grant expenses	573,036	45,324
Other expenses	139,863	169,514
Professional liability insurance expense	1,164,294	715,655
Depreciation	347,101	349,389
Provision for bad debts	601,793	355,839
Professional liability expense	51,643	-
Total operating expenses	<u>32,474,997</u>	<u>26,606,603</u>
Unrestricted revenues and other support over operating expenses	238,074	175,518
Net unrealized gain on investments whose use is limited	119,917	141,576
Increase in unrestricted net assets	<u>\$ 357,991</u>	<u>\$ 317,094</u>

See accompanying notes.

CMU Medical Education Partners

Statements of Changes in Net Assets

	Unrestricted Net Assets				
	Designated for Professional Liability	Undesignated	Total Unrestricted Net Assets	Temporarily Restricted	Total
Net assets (deficit) at June 30, 2012	\$ (3,780,746)	\$ 9,106,670	\$ 5,325,924	\$ 19,285	\$ 5,345,209
Revenues over expenses	57,377	118,141	175,518	-	175,518
Net unrealized gain	141,576	-	141,576	-	141,576
Net assets (deficit) at June 30, 2013	(3,581,793)	9,224,811	5,643,018	19,285	5,662,303
Revenues over expenses	(25,707)	263,781	238,074	-	238,074
Net unrealized gain	119,917	-	119,917	-	119,917
Equity transfer of net assets	-	(1,139,332)	(1,139,332)	-	(1,139,332)
Net assets (deficit) at June 30, 2014	\$ (3,487,583)	\$ 8,349,260	\$ 4,861,677	\$ 19,285	\$ 4,880,962

CMU Medical Education Partners

Statements of Cash Flows

	Year Ended June 30	
	2014	2013
Operating activities		
Increase in unrestricted net assets	\$ 357,991	\$ 317,094
Adjustments to reconcile increase in unrestricted net assets to net cash provided by (used in) operating activities:		
Depreciation	347,101	349,389
Net unrealized gain on investments	(119,917)	(141,576)
Change in assets and liabilities:		
Patient accounts receivable	(555,396)	18,714
Other receivables	721	(602,974)
Prepaid expenses and other assets	(66,041)	(195,768)
Accounts payable	477,654	199,695
Other accrued liabilities and payroll and related liabilities	266,010	273,802
Estimated professional liability under self-insurance	(163,750)	(166,016)
Deferred revenue	47,493	(1,005,370)
Net cash provided by (used in) operating activities	<u>591,866</u>	<u>(953,010)</u>
Investing activities		
Purchases of leasehold improvements, furniture, and equipment	(297,048)	(146,748)
Increase in Board restricted funds	(53,835)	(442)
Decrease (increase) in funds held by the trustee	1,116,626	(4,869)
Net cash provided by (used in) investing activities	<u>765,743</u>	<u>(152,059)</u>
Financing activities		
Equity distribution to member hospitals	(1,139,332)	-
Decrease in payable to CMU	(67,990)	(120,693)
Net cash used in financing activities	<u>(1,207,322)</u>	<u>(120,693)</u>
Increase (decrease) in cash	150,287	(1,225,762)
Cash at beginning of period	2,970,511	4,196,273
Cash at end of period	<u>\$ 3,120,798</u>	<u>\$ 2,970,511</u>

CMU Medical Education Partners

Notes to Financial Statements

June 30, 2014

1. Summary of Accounting Policies

Organization and Nature of Operations

Saginaw Cooperative Hospitals, Inc. (Corporation), d/b/a CMU Medical Education Partners is a Michigan nonprofit corporation located in Saginaw, Michigan. The Corporation was incorporated in Michigan in 1968 and is a tax-exempt organization pursuant to §501(c)(3) of the Internal Revenue Code. The Corporation is organized on a non-stock membership basis. Effective January 1, 2011 the Corporation is subject to a Members' Agreement that provides Central Health Advancement Solutions (CHAS) with a 90% membership interest in CMU Medical Education Partners (CMU Partners); St. Mary's of Michigan (St. Mary's) with a 5% membership interest; and Covenant Medical Center, Inc. (Covenant) with a 5% membership interest. All members are entitled to vote on any matter reserved to them in accordance with their membership interests. CHAS is a Michigan nonprofit corporation organized on a non-stock membership basis. The sole member of CHAS is the Board of Trustees of Central Michigan University.

The purpose of the Corporation is to integrate medical education, research, and service primarily for the training of medical residents and other medical related personnel. The two member hospitals, Covenant and St. Mary's, both of Saginaw, have provided greater than 50 percent of the total support of the Corporation. The Corporation operates under a Master Affiliation Agreement (Agreement) between the Corporation, St. Mary's, and Covenant. The Agreement was effective July 1, 2010 and expired June 30, 2013 and has continued on a month-to-month basis until a new agreement can be reached and covers the operation and funding of the Corporation's medical residency program as it relates to training the hospitals' medical residents.

Effective August 26, 2013, the corporation acquired the assets of a medical practice group in Saginaw. The cost of the assets was not considered significant to the overall assets of the Corporation. Most of the employees of the acquired practice group became employees of the Corporation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Basis of Accounting and Presentation

The financial statements of the Corporation have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

1. Summary of Accounting Policies (continued)

Designated Net Assets

Designated net assets represent amounts that have been contributed by the member hospitals and the accumulated earnings from investment of those amounts for the purpose of self-funding medical malpractice insurance at the Corporation.

Temporarily Restricted Net Assets

Temporarily restricted net assets consist of grant funds received from outside sources that carry restrictions as to how they are to be spent.

Donor-Restricted Gifts

Unconditional promises to give cash and other assets to the Corporation are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. Gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the contributions. When a donor restriction expires, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statement of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying financial statements. There were no permanently restricted net assets at June 30, 2014 or 2013.

Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Corporation uses various methods including market, income, and cost approaches. Based on these approaches, the Corporation often utilizes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and/or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable inputs. The Corporation utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based on the observability of the inputs used in the valuation techniques the Corporation is required to provide the following information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Financial assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

1. Summary of Accounting Policies (continued)

Fair Value Measurements (continued)

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities that the Foundation has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets, and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset.

In determining the appropriate levels, the Corporation performs a detailed analysis of the assets and liabilities. At each reporting period, all assets and liabilities for which the fair value measurement is based on significant unobservable inputs are classified as Level 3.

For the fiscal year ended June 30, 2014, the application of valuation techniques applied to similar assets and liabilities has been consistent.

Investments

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value based on quoted market prices as of the balance sheet date. Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in revenue over operating expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from revenue over operating expenses unless the investments are trading securities.

Assets Whose Use is Limited

Assets whose use is limited primarily include investments held by trustees under indenture agreements and designated assets set aside by the Board of Trustees for specific purposes, over which the Board retains control and may at its discretion subsequently use for other purposes.

Revenues Over Operating Expenses

The statements of operations include revenues over operating expenses. Changes in unrestricted net assets, which are excluded from revenues over operating expenses, include unrealized gains and losses.

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

1. Summary of Accounting Policies (continued)

Deposits with Financial Institutions

The Corporation maintains interest-bearing deposits, with a bank located in Saginaw, Michigan, which are recorded in the financial statements as cash, funds held by trustee, and donor restricted funds. At year end and at times during the year, the Corporation had balances in these accounts that exceeded federal deposit insurance limits.

Significant Concentrations of Credit Risk

Financial instruments which potentially subject the Corporation to concentrations of credit risk consist principally of cash and investments included in assets whose use is limited. The Corporation invests temporary cash in money market securities in various banks, commercial paper of industrial and other companies with high credit ratings, and securities backed by the United States Government. The Corporation holds the majority of its investments in equity and fixed income mutual funds. Included in investments are nine equity mutual funds and eight fixed income mutual funds that represent 83% of total investments at June 30, 2014 and nine equity mutual funds and eight fixed income mutual funds that represent 91% of total investments at June 30, 2013.

Leasehold Improvements, Furniture, and Equipment

Leasehold improvements, furniture, and equipment are stated at cost. Leasehold improvements, furniture, and equipment purchases in excess of \$500 are depreciated over their estimated useful lives using the straight-line method. Assets under capital lease obligations are amortized on the straight-line method over the estimated useful lives of the related assets. Such amortization is included in depreciation in the financial statements.

Net Patient Service Revenue

The Corporation has agreements with third-party payors that provide for reimbursements to the Corporation at amounts different from its established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Corporation's established rates for services and amounts reimbursed by third-party payors.

The Corporation grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. Significant concentrations of accounts receivable at June 30, 2014 and June 30, 2013 include Medicare (25.7% and 7.9%), Blue Cross (8.9% and 7.6%), Medicaid (20.5% and 37.9%), and other commercial insurers and self-pay (44.9% and 46.6%), respectively.

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

1. Summary of Accounting Policies (continued)

Patient Accounts Receivable

Patient accounts receivable and revenue are recorded when patient services are performed. Patient accounts receivable are recorded at the Corporation's established rates with contractual adjustments, charity allowances, policy discounts, and the provision for uncollectible accounts deducted to arrive at net patient accounts receivable. The Corporation pursues collection of all past due accounts. Accounts are written off when they are deemed uncollectible.

The allowance is calculated as a percentage of outstanding receivable balances for patient pay receivables and commercial insurance receivables. Percentages have been developed based on historical collection information. The allowance is increased by the provision charged to operations and reduced by charge-offs.

Estimated Professional Liability

The provision for estimated self-insured medical malpractice claims is actuarially determined and includes estimates of the costs for both reported claims and claims incurred but not reported.

Advertising

The Corporation expenses advertising costs as incurred. Advertising costs were approximately \$29,000 for the year ended June 30, 2014 and \$43,000 for the year ended June 30, 2013.

Reclassification

Certain prior year amounts were reclassified to conform to the current year presentation.

Subsequent Events

Subsequent events have been evaluated through August 19, 2014 as part of the annual audit of the Corporation's financial statements. This is also the date the financial statements were available to be issued.

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

2. Patient Accounts Receivable

The detail of patient accounts receivable is as follows:

	June 30, 2014			June 30, 2013
	Patient	Insurance	Total	Total
Family Practice Department	\$ 37,117	\$ 162,927	\$ 200,044	\$ 231,359
OB/GYN Department	73,695	162,955	236,650	333,506
Internal Medicine Department	80,832	142,467	223,299	207,856
Pediatrics Department	35,291	77,705	112,996	81,539
Surgery Department	24,875	41,153	66,028	92,328
Surgery – Tawas	7,471	190,067	197,538	-
Surgery – MSA	413,990	899,639	1,313,629	-
Psychiatry Department	8,013	32,101	40,114	46,036
Geriatrics Home Care	2,277	56,195	58,472	17,946
	683,561	1,765,209	2,448,770	1,010,570
Less:				
Contractual allowances	-	1,076,895	1,076,895	445,423
Allowance for doubtful accounts	409,157	-	409,157	157,825
Net patient accounts receivable	\$ 274,404	\$ 688,314	\$ 962,718	\$ 407,322

The receivable for “Surgery – Tawas” represents amounts billed by CMEP on behalf of St. Joseph Health System in accordance with its agreement dated March 1, 2014. Under this agreement, CMEP has agreed to provide general surgical services and medical director services to St. Joseph Health System located in Tawas, Michigan. In addition, CMEP has agreed to bill and collect for these surgical services on behalf of St. Joseph Health System in exchange for a fee representing 5% of the surgical services collected. The outstanding fees receivable (net of contractual adjustments and allowance for doubtful accounts) billed on behalf of St. Joseph Health System at June 30, 2014 were approximately \$120,000.

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

3. Leasehold Improvements, Furniture, and Equipment

The detail of leasehold improvements, furniture, and equipment by department is as follows:

	June 30	
	2014	2013
Leasehold improvements, furniture, and equipment:		
Clinical Trials	\$ 2,482	\$ 2,482
North Building	259,770	259,770
Student Programs	12,162	12,162
Administration	421,216	399,338
Family Practice Department	354,200	348,451
OB/GYN Department	198,542	168,135
Internal Medicine Department	158,084	162,195
Pediatrics Department	27,043	28,937
Surgery Department	125,913	36,182
Library Department	181,647	182,620
Graduate Medical Education	29,639	29,514
Emergency Medicine	38,836	40,782
Information Systems	447,092	382,138
Leasehold Improvements	1,093,725	1,063,725
Business Office	463,837	489,869
Geriatrics Home Care	16,671	17,617
Research Department	33,789	38,759
Psychiatry Department	29,960	24,418
Saginaw Medical Control	167,560	173,290
Sexual Assault Response Team	28,261	28,261
Human Resources	25,938	22,287
Stimulation Lab	450,993	412,853
Continuing Medical Education	15,621	13,944
	4,582,981	4,337,729
Less: accumulated depreciation	4,026,668	3,731,363
	\$ 556,313	\$ 606,366

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

4. Assets Whose Use is Limited

The composition of assets whose use is limited at June 30 is as follows:

	2014		2013	
	Cost	Fair Value	Cost	Fair Value
Board designated:				
Cash	\$106,918	\$160,495	\$ 106,755	\$ 106,755
Mutual funds: fixed income	9,152	9,263	9,057	9,168
	116,070	169,758	115,812	115,923
Malpractice funding – held by trustee:				
Cash and short-term investments	15,900	15,900	41,124	41,124
Mutual funds:				
Equities	215,425	374,240	699,700	1,019,975
Fixed income	211,843	224,205	539,015	549,955
	443,168	614,345	1,279,839	1,611,054
	\$559,238	\$784,103	\$1,395,651	\$1,726,977

Fair values of assets and liabilities measured on a recurring basis at June 30, 2014 and 2013 are as follows:

	Fair Value Measurements at Reporting Date Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets/Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
June 30, 2014				
Assets whose use is limited	\$ 784,103	\$ 784,103	\$ –	\$ –
June 30, 2013				
Assets whose use is limited	\$1,726,977	\$1,726,977	\$ –	\$ –

On October 31, 2013, the Corporation made an equity distribution of \$1,139,332 to the Hospitals which represents the amount by which “assets whose use is limited under professional liability funding arrangement” exceeded the “estimated professional liability under self-insurance” at the time of the distribution.

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

5. Medical Educational Funding Receivable

A master affiliation agreement between St. Mary's and Covenant (the Hospitals) provides for 100% of the direct graduate medical education (DGME), indirect medical education (IME), and other graduate medical education (GME) funding received by the Hospitals to pass through to the Corporation. An independent firm (The Rybar Group) was hired to review hospital cost report information and provide a report on filed cost report amounts. The initial affiliation agreement covered the 3 years ending June 30, 2009 and, through an amendment, was extended one year through June 30, 2010. The Hospitals are operating under a master affiliation agreement that was effective July 1, 2010 through June 30, 2013 and that is continuing on a month-to-month basis until a new agreement is reached. Under the agreement, the Hospitals agreed to pay CMEP for amounts not previously paid under the 2006 agreement subject to adjustment based on the Hospitals' receipt of their final cost reports.

As of June 30, 2014, the Rybar Group has updated its report with the allocation of the receivable as follows:

	<u>St. Mary's</u>	<u>Covenant</u>
Fiscal year 2011	\$ 642,515	\$ 837,208
Fiscal year 2012	(143,332)	648,600
Fiscal year 2013	(396,788)	130,978
Fiscal year 2014	30,742	161,845
Total receivable	<u>133,137</u>	<u>1,778,631</u>
Allowance	<u>(133,137)</u>	<u>(1,342,951)</u>
Net receivable	<u>\$ -</u>	<u>\$ 435,680</u>

The Corporation recognized an allowance of approximately \$1,500,000 in 2014 and \$1,600,000 in 2013, in anticipation of a variance between filed and final audited cost reports.

As of June 30, 2014, the cost reports for St. Mary's and Covenant have been finalized through the fiscal years shown below.

	<u>St. Mary's</u>	<u>Covenant</u>
Medicare	2010	2010
Blue Cross Traditional, Blue Cross Trust, and Blue Care Network	2013	2012
Medicaid	2011	2010

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

6. Payable to Hospitals

The Corporation has recorded a payable of \$-0- for both the years ended June 30, 2014 and 2013.

Under the Master Affiliation Agreement, as of the end of each fiscal year, the Corporation should have a cash balance equal to 1) the sum of 45 days cash on hand plus 2) an amount equal to the budgeted capital expenditures, less budgeted depreciation (Annual Funding Reserve), for the following fiscal year. Under the agreement, two-thirds of the excess funding is payable to Covenant and one-third of the excess funding is payable to St. Mary's within 30 days of the calculation of the Annual Funding Reserve.

7. Notes Payable to Hospitals

Under the Members' Agreement described in Note 1, the Hospitals were to receive their allocable share of net assets as of December 31, 2010. On February 7, 2012 an amendment to the Members' Agreement was made to maintain the Hospitals' allocable shares of net assets in the possession of the Corporation and the notes payable to hospitals were reclassified as additional members' equity. There were no notes payable to St. Mary's and Covenant at June 30, 2014 or 2013.

8. Money Accumulation Pension Plan

In 1974, the Corporation established a money accumulation pension plan for all eligible employees. Any employee who has completed more than 1,000 hours of service is eligible to participate.

The Corporation contributed 4 percent of the participants' pay into the program for both the years ended June 30, 2014 and 2013. The cost to the Corporation was approximately \$537,000 for the year ended June 30, 2014 and \$405,000 for the year ended June 30, 2013.

9. Lease Commitments

During 1976, the Corporation entered into a 25-year lease agreement beginning in 1978 upon completion of construction with Saginaw Medical Center for the occupancy of a portion of the Clinical Arts and Education Center. During the year ended June 30, 2002, the lease was amended and provided for a renewal option for an additional 5 years ending in August 2006. During the year ended June 30, 2007, the lease was not amended and the Corporation has continued payments on a month to month basis. Total lease expense related to this rental was \$549,868 for the year ended June 30, 2014 and \$578,974 for the year ended June 30, 2013.

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

9. Lease Commitments (continued)

In 2003, the Corporation began a 10-year lease agreement with SSP Associates upon the completion of construction for the occupancy of an office complex in Saginaw, Michigan. The Corporation exercised a renewal option for an additional 5 years and covers the period through February 2018. In 2013, the Corporation entered into a 15-year lease with MSA Ventures II LLC for commercial office space in Saginaw, Michigan. Total lease expense for multi-year non-cancelable and cancelable leases was approximately \$274,000 for the year ended June 30, 2014 and \$129,000 for the year ended June 30, 2013. The future lease commitments as of June 30, 2014 for all non-cancelable leases are as follows:

2014-15	\$ 274,249
2015-16	184,615
2016-17	184,615
2017-18	184,615
2018-19	197,047
Thereafter	1,782,748
	<u>\$2,807,889</u>

10. Professional Liability Insurance

The Corporation was self-insured for professional medical malpractice through December 31, 2010 for claims based on occurrences on or before December 31, 2010. In connection with the self-insurance program, the Corporation has:

- Determined aggregate limits of \$100,000/\$300,000 for residents and \$200,000/\$600,000 for doctors.
- Established a trust fund and placed the management of the fund in the hands of an independent fiduciary who has legal title to it and is responsible for its proper administration and control.

	June 30	
	2014	2013
Estimated professional liability under self-insurance	\$ 393,596	\$ 557,346
Total malpractice assets:		
Investments under professional liability funding arrangement – held by the trustee, at fair value	614,345	1,611,054
Over funding of liability	\$(220,749)	\$(1,053,708)

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

10. Professional Liability Insurance (continued)

Claim losses based upon occurrences prior to July 1, 1986 remain insured under prior insurance policies subject to the policy limits.

Effective January 1, 2011, the Corporation purchased commercial insurance coverage for professional medical malpractice. Coverage consists of \$1,000,000 per occurrence with annual aggregates ranging from \$3,000,000 to \$9,000,000.

Effective April 1, 2012, the Corporation purchased commercial insurance coverage for professional medical malpractice. Coverage consists of \$1,000,000 per occurrence with annual aggregates ranging from \$3,000,000 to \$8,500,000.

Malpractice and other claims have been asserted against the Corporation by various claimants. Such claims are in various stages of processing and some may be litigated. Accordingly, management and counsel cannot determine the ultimate outcome of the actions commenced. In the opinion of management, all such matters are adequately covered by prior and existing insurance policies and the Self-Insurance Trust Fund.

11. Managed Care Risk Pool Liability

The Corporation also entered into an agreement with Great Lakes Health Plan, Inc. (GLHP) for Medicaid covered services on October 1, 2000. The agreement is effective for one year and is automatically renewable for yearly terms unless terminated by the Corporation or GLHP. Under the agreement, the Corporation receives capitated and covered services compensation. Covered services are reimbursed according to GLHP's fee schedule. The Corporation agrees to bear the risk for the cost of the covered services which exceeds the covered service compensation. Since the Corporation bears the risk of loss, there is no risk pool liability associated with their plan.

12. Claims and Contingencies

The Corporation periodically is subject to claims and lawsuits that arise in the ordinary course of business. It is the opinion of management that, as of June 30, 2014, the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the financial position of the Corporation.

CMU Medical Education Partners

Notes to Financial Statements (continued)

June 30, 2014

13. Net Assets

Temporarily restricted net assets were available for health care services and education in the amount of \$19,285 at June 30, 2014 and at June 30, 2013.

14. Functional Expenses

The Corporation provides general health care services to residents within its geographic location. Expenses related to providing these services for the year ended June 30 are as follows:

	<u>2014</u>	<u>2013</u>
Health care services	\$29,075,171	\$22,461,221
General and administrative	3,399,826	4,145,382
Total operating expenses	<u>\$32,474,997</u>	<u>\$26,606,603</u>