

MEDICAL COLLEGE OF OHIO

**AUDITED FINANCIAL REPORT
Fiscal Year Ended June 30, 2002**

**Prepared by:
Financial Reporting**

**Diane C. Wray, CPA
Treasurer and Controller**



STATE OF OHIO
OFFICE OF THE AUDITOR

JIM PETRO, AUDITOR OF STATE

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Board of Trustees
Medical College of Ohio
Toledo, OH 43614

We have reviewed the Independent Auditor's Report of the Medical College of Ohio, Lucas County, prepared by Ernst & Young, for the audit period July 1, 2001 through June 30, 2002. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The Medical College of Ohio is responsible for compliance with these laws and regulations.

A handwritten signature in black ink, appearing to read "Jim Petro".

JIM PETRO
Auditor of State

December 16, 2002

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**REPORT OF INDEPENDENT AUDITORS
ON BASIC FINANCIAL STATEMENTS AND
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

Board of Trustees
Medical College of Ohio

We have audited the accompanying statements of net assets of the Medical College of Ohio as of June 30, 2002 and 2001, and the related statements of revenues, expenses and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial statement audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Medical College of Ohio as of June 30, 2002 and 2001, its revenues, expenses and changes in net assets and its cash flows, for the years then ended in conformity with accounting principles generally accepted in the United States.

As discussed in Note 2 to the accompanying financial statements, during 2002, the Medical College of Ohio changed its method of reporting effective July 1, 2000 in accordance with Government Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management Discussion and Analysis – for State and Local Governments*, as amended by Statement No. 35, *Basic Financial Statements – and Management’s Discussion and Analysis – for Public Colleges and Universities*.

The management’s discussion and analysis on pages 3 through 9 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries to management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with Government Auditing Standards, we have also issued reports dated September 27, 2002, on our consideration of the Medical College of Ohio’s internal control over financial reporting and our tests of its compliance with certain provisions of laws, contracts, and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Our audits were made for the purpose of forming an opinion on the basic financial statements of the Medical College of Ohio taken as a whole. The accompanying Schedule of Expenditures of Federal Awards for the year ended June 30, 2002, is presented for the purpose of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is not a required part of the basic financial statements. Such information has been subjected to the procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

Ernst + Young LLP

September 27, 2002

MEDICAL COLLEGE OF OHIO

MANAGEMENT'S DISCUSSION AND ANALYSIS

The discussion and analysis on the annual financial statements of The Medical College of Ohio ("College") provides an overview of the College's financial activity during the fiscal year ended June 30, 2002. This discussion should be read in conjunction with the accompanying financial statements and footnotes. Management has prepared the financial statements, related note disclosures, and this discussion and analysis. Responsibility for the completeness and fairness of this information rests with the College management.

Using the Annual Financial Report

This annual report consists of financial statements, prepared in accordance with Governmental Accounting Standards Board ("GASB") Statement No. 34, *Basic Financial Statements-- and Management's Discussion and Analysis--for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements--and Management's Discussion and Analysis--for Public Colleges and Universities*. These financial statements differ significantly, in both the form and the accounting principles utilized, from prior financial statements. The statements presented in prior years focused on the accountability of fund groups, while these statements focus on the financial condition of the College, the results of operations, and cash flows of the College as a whole. The college restated its financial statements for the year ended June 30, 2001 to conform to GASB Statement No. 35 format.

The financial statements prescribed by GASB Statement No. 35 (the Statement of Net Assets, Statement of Revenues, Expenses and Changes in Net Assets, and the Statement of Cash Flows) present financial information in a form similar to that used by corporations. They are prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged.

The Statement of Net Assets includes all assets and liabilities. Over time, increases or decreases in net assets (the difference between assets and liabilities) are one indicator of the improvement or erosion of the College's financial health when considered with non-financial facts such as enrollment levels and the condition of facilities.

The Statement of Revenues, Expenses and Changes in Net Assets presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. A public College's dependency on State support could result in operating deficits because State appropriations are required by GASB to be classified as nonoperating revenues. The utilization of capital assets is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life.

The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, noncapital financing, capital and related financing and investing activities, and helps measure the College's ability to meet financial obligations as they mature.

Noteworthy Financial Activity

GASB Statements No. 34 and 35 require reporting revenues net of discounts and allowances, deferral of summer tuition and depreciation of capital assets. As a result, certain amounts previously reported as scholarship expenses are reported as an allowance against tuition and related revenues, and, the prior year fund balances (in thousands) were restated to reflect the net assets as follows:

Total of Fund Balances at July 1, 2000 as previously reported	\$363,327
Accumulated depreciation of capital assets	(159,881)
Deferred revenue for summer tuition	(1,216)
Allocation of State Unfunded Workers' Compensation	<u>(5,288)</u>
Net assets as July 1, 2000 as restated	<u>\$196,942</u>

For fiscal 2001, tuition revenue was restated from \$11.6 million to \$14.9 million, and depreciation expense of \$17.3 million was recorded for the first time in 2001.

The College's financial position, as a whole, changed during the fiscal year ended June 30, 2002 as compared to the previous year as restated as evidenced by the following:

- The College's total assets increased over the prior year by \$8.1 million. Current assets increased by \$9.7 million, of which \$3.1 million is gains from College investments and \$6.6 million in cash & cash equivalents.
- Total liabilities increased by \$8.6 million. Current liabilities increased by \$2.0 million, which is primarily due to an increase in accounts payable of \$3.8 million. Noncurrent liabilities increased by \$6.4 million primarily due to an increase in long-term debt of \$4.3 million to finance capital projects and equipment.
- The College's net assets are \$201.1 million, of which \$160.9 is either invested in capital assets or restricted. Of the remaining \$40.2 million in unrestricted assets, all but \$7.4 million is designated for specific purposes.
- Operating revenues increased by \$5.1 million compared to the prior year, primarily due to an increase in patient services.
- The College's operating expenses increased by \$8.7 million, with expected increases in all functional and natural expense categories.
- Nonoperating revenue decreased by \$2.0 million, the majority of which is related to \$2.3 million decrease in State share of instructional support.

NET ASSETS

Invested in capital assets, net of related debt	147,178	152,212
Restricted, expendable	10,312	9,136
Restricted, nonexpendable	3,392	2,555
Unrestricted	<u>40,262</u>	<u>37,707</u>
Total net assets	<u>\$201,144</u>	<u>\$201,610</u>

At June 30, 2002, total College assets were \$249.6 million, compared to \$241.5million in fiscal 2001. The College's largest asset is its investments in physical plant of \$153.6 million at June 30, 2002. This investment in physical plant decreased from prior year as previously reported as a result of recording depreciation as required by GASB Statement No. 35.

In fiscal year 2002, the College's current assets of \$67.4 million were sufficient to cover current liabilities of \$34.6 million (current ratio of 1.95:1). In fiscal 2001, current assets of \$57.7 million were sufficient to cover current liabilities of \$32.6 million (current ratio of 1.77:1). Cash and cash equivalents increased by \$6.7 million or 160%, primarily due to reimbursement of insurance receivables, gains on investments and increases in accounts payable.

College liabilities total \$48.4 million at June 30, 2002 compared to \$39.8 million in fiscal 2001. Long-term debt of \$4.9 million consists of master lease and capital leases payable.

Total net assets are \$201.1 million. Unrestricted net assets total \$40.2 million, 18% of which (\$7.4 million) is designated for ongoing academic and research programs, capital projects and other initiatives.

Statement of Revenue, Expenses and Changes in Net Assets

Changes in total net assets as presented on the Statement of Net Assets are based on the activity presented in the Statement of Revenues, Expenses and Changes in Net Assets. The purpose of this statement is to present operating and nonoperating revenues and expenses recognized or incurred by the College.

In general, operating revenues and expenses result from provided goods and services to the various customers of the College in order to carry out the College's mission. Nonoperating revenues are revenues received for which goods and services are not provided. For example, state appropriations or subsidy is considered nonoperating because these dollars are provided by the Legislature to the College without the Legislature directly receiving commensurate goods and services for those revenues. In Ohio, the state appropriations, know as the state share of instruction subsidy, is predicated upon a formula of moving average enrollments in various levels of courses. College management believes that it earns these revenues, and in fact, the estimated share of instruction is considered when budgeting for revenues to cover operating expenses. For financial reporting purposes, classification of state appropriations as nonoperating revenues is done to comply with the requirements of GASB Statement No. 35, which does not consider Ohio's system of earned appropriations.

Both the Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets report information on the College as a whole. Over time, increases or decreases in the College's net assets are one indicator of whether its financial health is improving or deteriorating. Many other nonfinancial factors must also be considered in assessing the overall health of the College, such as quality of student applicants, student retention, strength of faculty, condition of buildings and regulatory changes in healthcare.

Statement of Net Assets

The Statement of Net Assets presents the assets, liabilities, and net assets of the College as of the end of the fiscal year. The purpose of the Statement of Net Assets is to present the readers of the financial statements with a financial picture of the College as a whole.

Net assets are divided into three major categories. The first category, investment in capital assets, net of debt, provides the College's equity in property, plant and equipment. The next category is restricted assets, which is divided into nonexpendable and expendable. The corpus of the nonexpendable restricted assets is only available for investment purposes. Expendable restricted net assets are available for expenditure by the College but must be spent for purposes as determined by donors or external entities that have placed time or purpose restrictions on the use of the assets. The last category is unrestricted assets, which are available to the College for any lawful purpose of the institution.

From the data presented in the Statement of Net Assets, the readers are able to determine the assets available for continued operations. They are also able to determine how much the institution owes vendors and lending institutions. Finally, the Statement of Net Assets provides a picture of the net assets (assets minus liabilities) and their availability for expenditure by the College.

Medical College of Ohio
Condensed Statements of Net Assets
As of June 30, 2002 and 2001 (in thousands)

	<u>2002</u>	<u>2001</u>
ASSETS		
Current assets	\$ 67,436	\$ 57,672
Capital assets	153,569	153,441
Other noncurrent assets	<u>28,543</u>	<u>30,341</u>
Total assets	249,548	241,454
LIABILITIES		
Current liabilities	35,661	33,474
Noncurrent liabilities	<u>12,743</u>	<u>6,372</u>
Total liabilities	<u>48,404</u>	<u>39,846</u>

Medical College of Ohio
Condensed Statement of Revenues, Expenses and Changes in Net Assets
For the years ended June 30, 2002 and 2001 (in thousands)

	<u>2002</u>	<u>2001</u>
Operating revenues	\$214,548	\$209,518
Operating expenses	<u>264,175</u>	<u>255,495</u>
Operating loss	(49,627)	(45,977)
Nonoperating revenues, net	<u>42,031</u>	<u>43,932</u>
Loss before other changes	(7,596)	(2,045)
Other changes	<u>7,130</u>	<u>6,713</u>
Increase/(Decrease) in net assets	(466)	4,668
Net assets, beginning of year	<u>201,610</u>	<u>196,942</u>
Net assets, end of the year	<u>\$201,144</u>	<u>\$201,610</u>

The most significant sources of operating revenues for the College is patient care services, tuition and fees, and grants and contracts.

At June 30, 2002, operating expenditures, including depreciation of \$17.3 million, totaled \$264.2 million. Research and instruction functional categories have increased proportionally to the additional revenue from grants and contracts. Expenses for patient services grew proportionally with increases in patient service revenue.

State appropriations were the most significant nonoperating revenue, totaling, 35.6 million.

Statement of Cash Flows

The primary purpose of the Statement of Cash Flows is to provide relevant information about the cash receipts and cash payments during this period of time. The Statement of Cash Flows also helps users assess the College's ability to generate future net cash flows, meet its obligations as they come due, and needs for external financing.

The Statement of Cash Flows has five parts. The first part is operating cash flows, which presents the net cash used in operating activities. The second section reflects cash flows from noncapital financing activities. This section reflects cash received and spent for nonoperating, noninvesting, and noncapital financing purposes. The third section deals with cash flows from

capital and related financing activities including cash used for capital acquisition and construction. The fourth section reflects the cash flows from investing and shows the purchases, proceeds, and interest received from investing activities. The last section reconciles the net cash to operating income or loss reflected in the Statement of Revenues, Expenses, and Changes in Net Assets.

Medical College of Ohio
Condensed Statements of Cash Flows
For the years ended June 30, 2002 and 2001 (in thousands)

	<u>2002</u>	<u>2001</u>
Cash provided by (used in):		
Operating activities	\$ (28,950)	\$ (38,788)
Noncapital financing activities	39,529	40,444
Capital and related financing activities	(5,178)	(5,779)
Investing activities	<u>3,121</u>	<u>4,353</u>
Net increase in cash	8,522	230
Cash and cash equivalents, beginning of year	<u>4,167</u>	<u>3,937</u>
Cash and cash equivalents, end of year	<u>\$ 12,689</u>	<u>\$ 4,167</u>

Major sources of cash included student tuition and fee (\$15.2 million), state appropriations (\$35.6 million), patient care services (\$156.4 million), and grants and contracts (\$23.3 million). The largest payments were for suppliers (\$38.9 million) and employees (\$162.5 million).

Capital Assets

The College has \$153.6 million invested in capital assets, net of accumulated depreciation of \$188.3 million. Depreciation charges for the current year are \$17.3 million. Detailed information about the College's capital assets is presented in the notes to the financial statements.

Economic Factors That Will Affect the Future

The ability of the College to fulfill its mission and execute its strategic plan is directly influenced by enrollment, State support, and the cost of health care, utilities, employee compensation and unfunded State and Federal mandates.

Additional challenges include major capital needs, with the highest priorities being a new Center for Creative Instruction, development of the Northwest Ohio Technology Park, and the continued investment in facility renewal and information system technology. An additional \$9.8 million has been allocated to capital budget for fiscal 2003.

Paramount to the College's continuing success is the recent accreditation by the Liaison Committee on Medical Education, which awarded the Medical College of Ohio a seven-year renewal with enthusiasm and without condition.

The economic position of the College is closely tied to the economic condition of the State, as all state universities in Ohio receive State financial assistance for both operations and designated capital improvements through appropriations by the Legislature. These appropriations contribute substantially to the successful maintenance and operation of the College.

Requests for Information

This financial report is designed to provide a general overview of the Medical College of Ohio finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Diane C. Wray, Treasurer and Controller, Medical College of Ohio, 3065 Arlington Avenue, Office 10B Dowling Hall, Toledo, Ohio 43614.

MEDICAL COLLEGE OF OHIO
Statements of Net Assets
(Dollars in Thousands)

	June 30	
	2002	2001
Assets		
Current Assets		
Cash and Cash Equivalents	\$ 10,850	\$ 4,167
Investments	4,123	1,018
Accounts Receivable, Net	42,635	43,209
Loans Receivable, Net	5,595	5,377
Inventories	3,671	3,441
Other Assets	562	612
Total Current Assets	67,436	57,824
Noncurrent Assets		
Restricted Cash and Cash Equivalents	1,839	-
Other Long-Term Investments	24,652	28,276
Restricted Investments	2,052	1,915
Capital Assets, Net	153,569	153,441
Total Noncurrent Assets	182,112	183,632
Total Assets	249,548	241,456
Liabilities		
Current Liabilities		
Accounts Payable	13,763	9,935
Accrued Liabilities	18,784	20,862
Deferred Revenue	1,485	1,247
Long-Term Debt - Current Portion	1,529	630
Malpractice - Current Portion	100	800
Total Current Liabilities	35,661	33,474
Noncurrent Liabilities		
Long-Term Debt	4,863	600
Allocation of State Unfunded Workers'		
Compensation	4,880	3,572
Malpractice	3,000	2,200
Total Noncurrent Liabilities	12,743	6,372
Total Liabilities	48,404	39,846
Net Assets		
Invested in Capital Assets, Net of Related Debt	147,178	152,212
Restricted		
Expendable	10,312	9,136
Nonexpendable	3,392	2,555
Unrestricted	40,262	37,707
Total Net Assets	\$ 201,144	\$ 201,610

See accompanying notes to financial statements

MEDICAL COLLEGE OF OHIO
Statements of Revenues, Expenses, and Changes in Net Assets
(Dollars in Thousands)

	Year Ended June 30	
	2002	2001
Revenues		
Operating Revenues		
Student Tuition and Fees, net of student aid of \$1,550 and \$1,457, respectively	\$ 13,690	\$ 13,401
Federal Grants and Contracts	14,385	13,635
State Grants and Contracts	1,199	3,564
Private Grants and Contracts	7,748	7,680
Net Patient Services	155,870	147,723
Sales and Services	4,991	6,730
Auxillary Enterprises	3,324	4,247
Residency Reimbursement	3,448	3,223
Interest on Student Loans	135	119
Other Sources	9,758	9,196
Total Operating Revenues	214,548	209,518
Expenses		
Operating Expenses		
Salaries	130,972	125,728
Benefits	29,514	25,412
Supplies	42,764	41,773
Travel	1,568	2,121
Information and Communication	3,288	3,499
Outside Purchased Services	27,598	29,126
Provision for Doubtful Accounts	3,250	6,668
Miscellaneous	6,572	5,553
State Unfunded Workers' Compensation	1,308	(1,716)
Depreciation	17,341	17,331
Total Operating Expenses	264,175	255,495
Operating Loss	(49,627)	(45,977)
Nonoperating Revenues (Expenses)		
State Appropriations	35,581	37,833
Federal Grants and Contracts	3,452	3,330
Excess of Restricted Receipts	1,032	88
Early Retirement	(536)	(807)
Investment Income	2,738	3,722
Interest on Debt	(236)	(234)
Total Nonoperating Revenues	42,031	43,932
Net Loss Before Other Changes	(7,596)	(2,045)
Other Changes		
Capital Appropriations	6,043	3,775
Capital Grants and Gifts	1,817	2,724
Net Disposal and Write off of Plant Facilities	(730)	214
Total Other Changes	7,130	6,713
Increase in Net Assets	(466)	4,668
Net Assets		
Net Assets at Beginning of Year (Note 2)	201,610	196,942
Net Assets at End of Year	\$ 201,144	\$ 201,610

See accompanying notes to financial statements

MEDICAL COLLEGE OF OHIO
Statement of Cash Flows
(Dollars in Thousands)

	Year ended June 30	
	2002	2001
Cash flows from Operating Activities		
Tuition and fees	\$ 15,259	\$ 14,767
Grants and contracts	23,332	24,878
Hospital Revenues	156,479	139,029
Miscellaneous income	4,911	6,772
Auxiliary Enterprises	6,771	7,470
Payments to employees	(162,563)	(150,834)
Payments for supplies	(38,935)	(29,126)
Payments for outside purchased services	(27,597)	(41,431)
Other receipts (payments)	(6,607)	(10,313)
Net cash used in operating activities	<u>(28,950)</u>	<u>(38,788)</u>
Cash Flows from Noncapital Financing Activities		
State appropriations	35,581	37,833
Grants and contracts for other than capital purposes	3,452	3,330
Excess of restricted receipts	1,032	88
Early Retirement	(536)	(807)
Financial aid loan receipts	18,166	14,181
Financial aid loan disbursements	(18,166)	(14,181)
Net cash provided by noncapital financing activities	<u>39,529</u>	<u>40,444</u>
Cash flows from Capital Financing Activities		
Proceeds from Capital Debt	4,977	-
Capital appropriations	6,043	3,775
Capital grants and gifts received	1,817	2,724
Net disposal and write off of plant facilities	1,008	2,127
Purchases of capital assets	(18,056)	(13,436)
Principal paid on capital debt and leases	(954)	(956)
Interest paid on capital debt and leases	(13)	(13)
Net cash used in capital financing activities	<u>(5,178)</u>	<u>(5,779)</u>
Cash Flows from Investing Activities		
Net change in investments	383	631
Interest on investments	2,738	3,722
Net cash provided by investing activities	<u>3,121</u>	<u>4,353</u>
Net Increase (Decrease) in Cash	8,522	230
Cash-beginning of the year	4,167	3,937
Cash-end of year	<u>\$ 12,689</u>	<u>\$ 4,167</u>
Reconciliation of Net Operating Revenues (Expenses) To Net Cash Provided (Used) by Operating Activities:		
Operating loss	\$ (49,627)	\$ (45,977)
Adjustments to reconcile operating loss to net cash by operating activities:		
Depreciation expense	17,341	17,331
Provision for bad debts	3,250	6,668
Changes in assets and liabilities:		
Receivables, net	(2,985)	(15,484)
Inventories	(230)	192
Other assets	(95)	(480)
Malpractice accrual	100	-
Accounts payable	3,828	341
Accrued liabilities	(770)	(1,410)
Deferred revenue	238	31
Net cash used in operating activities	<u>\$ (28,950)</u>	<u>\$ (38,788)</u>

Supplemental disclosure of cash flow information:

This amount represents a noncash capital and related financing activity and are not included in the Acquisition of Property, Plant and Equipment above. During fiscal 2002 and 2001, MCO entered into capital lease obligations of \$1,139 and \$427, respectively, for certain hospital equipment, which is also excluded from the statement of cash flows.

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Accounting and Reporting Principles

The Medical College of Ohio (MCO), a component unit of the State of Ohio, is a nonprofit, state-supported medical school operating in Toledo, Ohio. Its financial statements have been prepared on an accrual basis in accordance with accounting principles generally accepted in the United States as presented by the Governmental Accounting Standards Board (GASB). The financial statements have been prepared to incorporate all fund groups internally utilized by MCO.

Pursuant to GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, MCO has elected not to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, for its proprietary funds. The restricted funds are available for current operating purposes in compliance with donor and grantor restrictions. Revenues relating to restricted funds are recognized to the extent expended for the specified purpose. When both restricted and unrestricted resources are available for use, it is MCO's policy to use restricted resources first, then unrestricted resources as needed.

The Medical College Hospitals (the hospital) is operated as part of MCO as a nonprofit teaching hospital.

Patient accounts receivable and revenue

Patient accounts receivable and revenue are recorded at net realizable value when patient services are performed. MCO has agreements with third-party payors that provide for payments to MCO at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows.

- **Medicare and Medicaid**

MCO is a provider of services under the Medicare and Medicaid programs. MCO is paid a prospectively determined fixed price for each Medicare and Medicaid inpatient. The price varies depending on the type of illness or the patient's diagnostic related group classification. Capital costs, certain Medicare outpatient services, and Medicaid outpatient services are also reimbursed on a prospectively determined fixed price. Graduate medical education is reimbursed on a per resident basis under the Medicare program. MCO receives payment for other Medicare outpatient services and certain inpatient costs on a reasonable cost basis.

- **Other Payors**

MCO has also entered into payment agreements with certain commercial carriers to provide health care services. The basis for payment to MCO under these agreements is based on prospectively determined fixed prices, fee screens, or on a percentage of billed charges.

Provision is made in the financial statements for the differences between MCO's standard rates charged for services rendered and third-party reimbursements and for estimated settlements based on third-party reimbursement contracts. Retroactive settlements resulting from third-party audits of filed cost reports are reflected in the financial statements in the year of settlement. These provisions and settlements are included in deductions from patient service revenue. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. These amounts qualify as charity care and are not reported as revenue.

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

Measurement Focus

Operating revenues and expenses generally result from providing service and producing and delivering goods in connection with MCO's principal ongoing operations. The principal operating revenues include hospital services and student tuition. MCO also recognizes as operating revenue grants classified as exchange transactions and auxiliary activities. Operating expenses include the hospital costs, educational costs, administrative expense and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Inventories

Inventories are stated at the lower of cost or market. Cost is determined on an average cost basis.

Investments

Investments are made in accordance with policies of the Board of Trustees of MCO. The types of investments that may be purchased by the institution include United States treasury obligations, certificates of deposit, bankers' acceptances, corporate notes and bonds, money market funds, government agency securities and commercial paper. Investments qualifying as "derivatives" may not be purchased. Investments are carried at market value. Investment income includes realized and unrealized gains and losses on investments, interest income, and dividends.

Capital Assets

Capital assets are recorded at historical cost or, if acquired by donation, at appraised values. When capital assets are sold or otherwise disposed of the carrying value of such assets are removed from asset accounts, the investment in capital assets along with the necessary adjustments to accumulated depreciation. MCO capitalizes assets greater than \$1,000.

Deferred Revenue

Summer tuition and fees, and corresponding expenses relating to various sessions offered during this term are recorded in the Statement of Net Assets as deferred revenue and prepaid expenses, respectively. Revenue and expenses are recorded in the fiscal year when the classes take place.

Grants and Contracts

MCO receives grants and contracts from federal, state and private agencies to fund research and other activities. Grants and contracts generally provide for the recovery of direct and indirect costs. MCO recognizes revenues associated with grants and contracts as the related costs are incurred. Indirect cost recovery is recorded as a percentage of direct costs at negotiated fixed rates. Revenues received under grants and contracts are subject to the examination and retroactive adjustments by the awarding agency.

Cash Equivalents

Cash equivalents include investments with original maturities of three months or less at the time they are purchased.

Compensated Absences

Unused sick time may accumulate until retirement. Employees with a minimum of ten years of services are paid twenty-five percent accumulated sick time upon retirement with a maximum of 240 hours. A liability for these amounts is included in the Statement of Net Assets

Income Taxes

MCO is exempt from income taxes under Section 115 of the Internal Revenue Code.

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTE 2 – GASB STATEMENTS NO. 34 and 35

In fiscal 2002, MCO adopted GASB Statement No. 34, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments*, as amended by Statement No. 35, *Basic Financial Statements—and Management’s Discussion and Analysis—for Public Colleges and Universities* effective July 1, 2000. MCO now follows the “business-type” activities which provides for the following components of MCO’s financial reporting:

- Managements’ Discussion and Analysis,
- Basic financial statements including a Statement of Net Assets, Statement of Revenues, Expenses, and Changes in Net Assets, and Statement of Cash Flows for MCO as a whole, and
- Notes to the financial statements

GASB Statements No. 34 and 35 also require such items as reporting revenues net of discounts and allowances, deferral of certain summer tuition, depreciation of capital assets and Workers’ Compensation allocation liability (See Note 8). In addition, certain amounts previously reported as scholarship expenses are reported as an allowance against tuition and related revenues. The prior year fund balances were restated to reflect the net assets as follows:

Total of fund balances at July 1, 2000 as previously reported	\$363,327
Accumulated depreciation of capital assets	(159,881)
Deferred revenue for summer tuition	(1,216)
Allocation of State Unfunded Workers’ Compensation	<u>(5,288)</u>
Net assets at July 1, 2000 as restated	<u>\$196,942</u>

For fiscal 2001, student tuition and fees were restated from \$11,576 to \$14,858, and depreciation expense of \$17,331 was recorded for the first time in 2001.

NOTE 3 - STATE SUPPORT

MCO is a state-supported institution of higher education which receives a student-based subsidy and other subsidies from the State of Ohio (the State). These subsidies are determined biennially and released annually based upon allocations devised by the Ohio General Assembly and the Ohio Board of Regents.

In addition to subsidies, the State provides capital appropriations for construction of major plant facilities on the campus. The financing of construction is obtained by the State through issuance of State revenue bonds. State funds are pledged for repayment of the revenue bonds. In the event these funds are insufficient to retire the revenue bonds, a pledge exists to assess a special student fee to students of state assisted institutions of higher education. As a result of this financing arrangement, the outstanding debt relating to the revenue bonds is not included in MCO’s Statement of Net Assets.

State appropriations are recognized when received. Restricted appropriations are recognized as revenue only to the extent expended.

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 4 - RELATED ORGANIZATIONS

The Medical College of Ohio at Toledo Foundation (Foundation) is an Ohio not-for-profit corporation deemed to be exempt from income taxes under Section 501(C)(3) of the Internal Revenue Code. The Foundation is organized primarily for the purpose of supporting the activities of MCO and is directed by a separate Board of Trustees, unrelated to the MCO Board of Trustees. The assets of the Foundation were generated from gifts and grants made directly to the Foundation and not from any public funds of MCO; accordingly, the accounts of the Foundation are not included in the financial statements of MCO. For the years ended June 30, 2002 and 2001, respectively, the Foundation paid approximately \$180 and \$385 to MCO as reimbursement for personnel and payroll related costs, rent for use of MCO facilities, and other administrative costs.

GASB Statement No. 39, *Financial Reporting Entity—Affiliated Organizations* has been issued and is effective for periods beginning after June 15, 2003. This statement will require MCO to reflect the Foundation as a discretely presented component unit in the financial statements based on the significance of its relationship with MCO.

Associated Physicians of the Medical College of Ohio (APMCO) is a for profit entity, operating under a separate Board of Trustees, organized to provide physician services at the Medical College Hospitals. Amounts received from APMCO for the use of hospital facilities and support services are included in Other Hospital Revenues. MCO does not hold any ownership in APMCO; therefore, the assets and liabilities of APMCO are not recorded in the accompanying financial statements.

NOTE 5 - POOLED CASH AND INVESTMENTS

Cash and investments are accounted for on a pooled basis for making daily cash and investment transactions. Pooled cash and investments with maturity of three months or less are considered to be cash equivalents. GASB Statement No. 3, *Deposits with Financial Institutions Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*, requires cash and cash equivalents and investments held by the College to be categorized into the following risk categories:

- (1) Cash and Cash Equivalents
 - a. Insured or collateralized with securities held by MCO, or by its agent in MCO's name.
 - b. Collateralized with securities held by the pledging financial institution's trust department or agent in MCO's name.
 - c. Uncollateralized

- (2) Investments
 - a. Insured or registered, or securities held by MCO, or by its agent in MCO's name.
 - b. Uninsured and unregistered, with securities held by the counter party's trust department or agent in MCO's name.
 - c. Uninsured and unregistered, with securities held by the counter party or by its trust department or agent, but not in MCO's name.

The bank balance of cash deposits was \$1,804 at June 30, 2002. Of the balance, up to \$100 is insured by federal depository insurance (Category 1) and the remainder is uninsured but collateralized by pools of securities pledged by depository banks and held in the name of the respective banks (Category 2). Differences between bank balances and carrying values of cash result from checks issued but not presented to the bank for payment.

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

Investments are stated at market value at June 30, 2002 and 2001. Investments are not insured or registered in MCO's name but are held in safekeeping by MCO's custodial bank's trust department whose records identify MCO's ownership (Category 2).

	<u>June 30, 2002</u> Market and Carrying Value	<u>June 30, 2001</u> Market and Carrying Value
Cash:		
Cash Deposits	\$2,389	\$ 1,650
Bank Overdrafts	(5,398)	(1,707)
Cash in Escrow		
Linear Accelerator purchase	1,839	
Cash Equivalents:		
Money Market Funds	10,850	4,318
Investments:		
U.S. Government Obligations	8,918	5,789
Corporate Notes	19,857	23,504
Accrued Interest Receivable	<u>348</u>	<u>550</u>
Total Pooled Cash and Investments	<u>\$38,804</u>	<u>\$34,104</u>

Net unrealized gains on U.S. government obligations and corporate notes were \$1,143 and \$96, respectively, at June 30, 2002 and is included in investment income.

NOTE 6 – ACCOUNTS RECEIVABLE AND LOANS

Accounts receivable relate to several transactions including tuition and fees, patient services, auxiliary enterprise sales, grants and contracts, and miscellaneous sales and services.

Accounts receivable are recorded net of allowance for uncollectable accounts of \$2,614 and \$5,293 respectively for 2002 and 2001.

The receivables are shown net of allowances for uncollectable accounts, as of June 30, as follows:

	<u>2002</u>	<u>2001</u>
Patient	\$35,158	\$33,207
Tuition, Fees and Student Loans	5,595	5,377
Auxiliary Services	55	94
Grants and Contracts	3,039	2,417
Capital	534	1,400
Accrued Interest	348	550
Miscellaneous College	1,489	3,114
Miscellaneous Hospital	<u>2,012</u>	<u>2,427</u>
	<u>\$48,230</u>	<u>\$48,586</u>

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 7 – CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2002 were as follows:

	July 1, 2001				June 30, 2002
	<u>Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>Reallocations</u>	<u>Balance</u>
Capital assets, not being depreciated:					
Land	\$ 2,687	\$ 1,064	\$ (144)	\$ (789)	\$ 2,818
Construction in Progress	17,510	14,093	(425)	(19,018)	12,160
Total capital assets not being depreciated	20,197	15,157	(569)	(19,807)	14,978
Capital assets being depreciated:					
Land improvements	655	9	-	4,000	4,664
Infrastructure	24,324	2	-	7,110	31,436
Building & Improvements	177,975	196	(81)	8,195	186,285
Equipment	105,837	3,833	(5710)	502	104,462
Total capital assets being depreciated	308,791	4,040	(5,791)	19,807	326,847
Less: accumulated depreciation	175,547	17,341	(4,632)	-	188,256
Total capital assets being depreciated, net	133,244	(13,301)	(1,159)	19,807	138,591
Total capital assets, Net	<u>\$153,441</u>	<u>\$ 1,856</u>	<u>\$(1,728)</u>	<u>\$ -</u>	<u>\$153,569</u>

Depreciation is recognized on a straight-line basis over the estimated useful life of the assets, as follows:

<u>Classification</u>	<u>Life Varies</u>
Infrastructure	2 – 40 years
Buildings	5 – 40 years
Equipment	3 – 20 years

NOTE 8 – WORKERS' COMPENSATION

The College participates in the State's self-insured workers' compensation plan (the Plan), which pays workers' compensation benefits to beneficiaries who have been injured on the job. Losses from asserted and unasserted claims for the participating State agencies and colleges in the Plan are accrued by the Ohio Bureau of Workers' Compensation (the Bureau) based on estimates that incorporate the past experience, as well as other considerations including the nature of each claim or incident and relevant trend factors. Participants in the State's Plan annually fund the workers' compensation liability based on rates set by the Bureau to collect the cash needed in subsequent fiscal years to pay the workers' compensation claims of participating State agencies and colleges. The Bureau has actuarially calculated estimated amounts for the State of \$727 million at June 30, 2002, \$559.3 million at June 30, 2001 and \$548.3 million at June 30, 2000 to be paid in future periods. The State determined the College's pro-rata share of the estimated liability on the basis of the College's share of actual cash payments (premiums and administrative costs) to the Bureau in the preceding fiscal year divided by such payments made by all participating entities. The College has restated its prior year fund balances for the estimated liability at June 30, 2000 of \$5,288. The estimated liability at June 30, 2002 and 2001 is \$4,880 and \$3,572, respectively. The increase of \$1,308 in 2002 and the decrease of \$1,716 in 2001 are included in operating expenses.

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

The decision to record this liability was a result of determinations made by the State of Ohio in its interpretations of the treatment of the unfunded pool obligation. Further, the recording of this liability is based on an allocation of the entire pool on a pro-rata basis to the participating state agencies and universities. Such amount could differ had a separate actuarial computation by participating state universities been performed.

NOTE 9 - RETIREMENT PLANS

MCO participates in the State Teachers Retirement System of Ohio (STRS) and the Public Employees Retirement System of Ohio (PERS) and alternative retirement plans (ARP) as defined by Ohio Revised Code, Section 3305 and Am. Sub. House Bill 586. These plans are statewide cost-sharing, multiple-employer public retirement systems administered and controlled by the State of Ohio. The State of Ohio issues annual plan financial reports, which can be obtained by contacting the appropriate state office.

Participating employees are entitled to retirement benefits payable for life, equal to 2.1% per year of credited service times the final average salary (the average of the three highest years of earnings) up to 30 years. The 31st year of earned service credit is calculated at 2.5%. An additional one-tenth of a percent is added to the calculation for every year over 31 years. Participating employees may retire at age 60 with at least five years of credited service, at age 55 with at least 25 years of credited service or at any age with at least 30 years of credited service. Participating employees retiring with less than 30 years of service or at less than age 65 receive reduced benefits. STRS limits the maximum annual benefit to the greater of 100% of the participant's final average salary or the participant's lifetime contribution plus interest at specified rates matched by an equal amount of employer contributed funds divided by an actuarially determined annuity factor. Retirement benefits vest with five years of credited service. STRS and PERS also provide health care, survivor and disability benefits.

State law provides for employer and employee contributions to STRS and PERS based on actuarially determined rates. The Ohio Retirement Study Council determines the ARP rates and the Ohio Department of Insurance approves ARP carriers. Senate Bill 346 established a revised PER's disability program. PER's members were given the opportunity to elect coverage under the original or revised disability program. Anyone hired after July 29, 1992, is automatically covered under the revised disability program. The revised program was designed to be cost neutral, therefore, does not affect PERS funding. There were no material changes in actuarial assumptions, benefit provisions, actuarial funding methods or other significant factors in fiscal years 2002, 2001, and 2000. The contribution rates for fiscal years 2002, 2001, and 2000, were as follows:

	Fiscal 2002/2001/2000 <u>STRS</u>	Fiscal 2002/2001/2000 <u>PERS</u>	Fiscal 2002/2001/2000 <u>ARP-STRS</u>	Fiscal 2002/2001/2000 <u>ARP-PERS</u>
Employer:	14.00%	13.31%	8%	7.31%
Employee:	9.30%	8.50%	9.3%	8.5%

Contributions made by employees are as follows:

	<u>2000</u>	<u>2001</u>	<u>2002</u>
STRS	\$2,412	\$2,270	\$2,319
ARP-STRS	373	535	574
PERS	7,098	7,153	7,585
ARP-PERS	652	713	669

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
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MCO Retirement costs funded as accrued are as follows:

	<u>2000</u>	<u>2001</u>	<u>2002</u>
STRS	\$ 3,573	\$ 3,417	\$ 3,491
ARP-STRS	321	460	494
PERS	11,028	8,844	11,867
ARP-PERS	561	614	575

PERS enacted a temporary employer rate rollback for calendar year 2000. For a period of six months, PERS reduced the contribution rate for employers to 10.84% and employees to 4.3%. The decision to roll back rates was based on the December 31, 1998 actuarial study, which indicated that actuarial assets exceed actuarial liabilities. The temporary rate rollback was 20%.

During fiscal year 1993 and fiscal year 1996, MCO's Board of Trustees approved the adoption of the STRS Early Retirement Incentive Plan. The plan allows faculty members who meet certain eligibility requirements to elect early retirement and the College to purchase up to five years of service credit in the plan for the retiring employee. Accrued liabilities include \$536 at June 30, 2001, related to early retirement incentives. The liability will be paid in annual installments, with interest, through 2002. Educational and general fund balance was allocated for early retirement incentives, which will be transferred to unreserved fund balance as early retirement incentives are incurred. The change in allocated fund balance for fiscal 2002 and 2001, was as follows:

	<u>June 30, 2002</u>	<u>June 30, 2001</u>
Balance at beginning of year	\$(536)	\$(1,343)
Principal payments made for early retirement Incentives	<u>536</u>	<u>807</u>
Balance at end of year	<u>\$ -</u>	<u>\$ (536)</u>

NOTE 10 - LONG TERM DEBT AND LEASE COMMITMENTS

Capital lease activity for the year ended June 30, 2002 was as follows:

	Balance July 1, <u>2001</u>	<u>Additions</u>	<u>Reductions</u>	Balance June 30, <u>2002</u>	Current <u>Portion</u>
Master Lease Purchase Obligations	\$ -	\$4,977	\$ (51)	\$4,926	\$ 733
Other Lease Obligations	<u>1,230</u>	<u>1,140</u>	<u>(904)</u>	<u>1,466</u>	<u>796</u>
Total Long-Term Debt	<u>\$1,230</u>	<u>\$6,117</u>	<u>\$ (955)</u>	<u>\$6,392</u>	<u>\$1,529</u>

In 2002, MCO entered into a master equipment lease purchase agreement with a financial institution to finance a linear accelerator with monthly payments of \$48 beginning in July 2002 at 4.95% annual interest rate through 2009. At June 30, 2002, approximately \$1.9 million is included in capital assets; the remaining \$1.5 million is in an escrow account, which is included in restricted cash and cash equivalents.

In 2002, MCO entered into a master equipment lease purchase agreement with a financial institution to finance a water chiller unit with monthly payments of \$16 beginning in February 2002 at 3.79% annual interest rate through

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

2007. At June 30, 2002, approximately \$590 is included in capital assets, and \$298 of the remaining funds is in an escrow account, which is included in restricted cash and cash equivalents.

In 2002, MCO entered into a master equipment lease purchase agreement with a financial institution, which extends a \$3 million line of credit until June, 2007. Subsequently, MCO utilized the line of credit by entering into three capital lease agreements for \$560, \$77 and \$48. At June 30, 2002, \$685 is included in capital assets pertaining to these capital leases, related to equipment with monthly payments of \$13 at 4.8% interest rate through 2007.

MCO has other capital lease obligations of \$1,466 and \$1,229 at June 30, 2002 and 2001, respectively. The cost of the assets recorded under capital leases as of June 30, 2002, is \$3,399.

Minimum lease payments at June 30, 2002, by year and in the aggregate, under capital leases are as follows:

	Other Lease Obligations	Master Lease Purchase Obligations
2003	\$ 847	\$ 923
2004	569	923
2005	111	923
2006	10	923
2007	-	713
2008-2012	<u>-</u>	<u>1,159</u>
Net minimum lease payments	\$1,537	\$5,564
Less amounts representing interest	<u>(71)</u>	<u>(638)</u>
Present value of lease payments	<u>\$1,466</u>	<u>\$4,926</u>

Contracts have been entered into for capital construction projects in an amount approximating \$18,501. The estimated cost to complete construction in progress at June 30, 2002 is \$3,459, the majority of which will be funded by capital appropriations from the State of Ohio.

MCO leases certain facilities and data processing, patient care and other equipment under various noncancelable operating lease agreements. Total operating lease expense was \$1,032 in 2002 and \$699 in 2001. At June 30, 2002, MCO was committed to future minimum operating lease payments of \$544 in 2003, \$268 in 2004, and \$90 in 2005.

At the expiration of various patients care equipment leases, MCO has the option to make a termination payment, purchase the equipment at fair market value or extend the lease term. Future minimum operating lease payments include \$117 in termination payments related to these lease agreements.

NOTE 11 - MALPRACTICE MATTERS

MCO is self-insured for the first \$1,000 of loss per occurrence with an annual aggregate limit of \$3,000 for malpractice and general liability, and maintains umbrella insurance coverage that covers any excess liability on a claims made basis. Settlement amounts have not exceeded insurance coverage for each of the past three fiscal years.

In accordance with the terms of the insurance policy, MCO maintains a self-insurance trust. Investments held in trust are comprised of U.S. government securities and corporate bonds with a market value, which approximates cost at June 30, 2002. These investments are held in safekeeping by MCO's custodial bank's trust department. These securities are registered in the bank's name with internal bank records identifying MCO's ownership.

MEDICAL COLLEGE OF OHIO
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

At June 30, 2002 and 2001, MCO has accrued \$3,100 discounted at 6% and \$3,000 discounted at 6%, respectively, for asserted and unasserted claims, based on MCO's experience and studies performed by a consulting actuary. With respect to pending malpractice claims and legal action where MCO is a defendant, it is the opinion of management that any potential liability in such actions will not materially affect the financial position of MCO. Settlements have not exceeded insurance coverage in each of the past three years.

	<u>June 30, 2002</u>	<u>June 30, 2001</u>
Malpractice Liability at Beginning of Year	\$3,000	\$3,003
Provision for Incurred Claims	108	235
Payments for Claims	<u>(8)</u>	<u>(238)</u>
Malpractice Liability at End of Year	<u>\$3,100</u>	<u>\$3,000</u>

NOTE 12 – OPERATING EXPENSES

Operating expenses by functional category for the years ended June 30, 2002, and 2001 are as follows:

	<u>2002</u>	<u>2001</u>
Instruction	\$ 45,380	\$ 45,150
Research	15,207	14,588
Public Service	786	501
Academic Support	3,998	5,370
Student Services	1,628	1,559
Institutional Support	2,654	4,790
Operation and Maintenance of Plant	9,592	8,012
Auxillary Enterprises	1,094	972
Patient Services	2,964	3,966
Scholarships and Fellowships	158,973	148,304
Provision for Doubtful Accounts	3,250	6,668
State Unfunded Workers' Compensation	1,308	1,716
Depreciation	<u>17,341</u>	<u>17,331</u>
Total Operating Expenses	<u>\$264,175</u>	<u>\$255,495</u>

Medical College of Ohio
 Schedule of Expenditures of Federal Awards
 Year Ended June 30, 2002

	AGENCY	CFDA #	FY2002
STUDENT FINANCIAL AID			
Federal Work Study	UDE	84.033	215,881
Federal Perkins Loan Program (Federal contribution)	UDE	84.038	93,701
			309,582
RESEARCH & DEVELOPMENT			
Bureau of Land Management	DOI	15.221	240,205
Department of Defense	DOD	12.420	78,842
Environmental Protection Agency	EPA	66.500	388,188
National Cancer Institute	DHHS	93.855	5,115
	DHHS	93.CN05109	36,236
	DHHS	93.CN05121	215,082
	DHHS	93.CN05123	87,533
	DHHS	93.CN15111	92,848
	DHHS	93.CN15121	40,934
	DHHS	93.CN15125	54,887
	DHHS	93.CN75108	(12,966)
	DHHS	93.CN85146	(90)
	DHHS	93.CN85147	15,114
	DHHS	93.CN85166	15,363
	DHHS	93.CN95118	13,857
National Institutes of Health	DHHS	93.113	47,105
	DHHS	93.121	34,048
	DHHS	93.173	149,868
	DHHS	93.173	(1,914)
	DHHS	93.279	81,132
	DHHS	93.279	78,682
	DHHS	93.279	2,487
	DHHS	93.279	232,350
	DHHS	93.361	41,545
	DHHS	93.361	18,647
	DHHS	93.361	63,781
	DHHS	93.361	48,875
	DHHS	93.393	114,347
	DHHS	93.394	259,934
	DHHS	93.394	71,982
	DHHS	93.394	140,185
	DHHS	93.395	312,006
	DHHS	93.395	117,401
	DHHS	93.396	223,690
	DHHS	93.396	90,788
	DHHS	93.396	382,920
	DHHS	93.398	165,561
	DHHS	93.399	26,038
	DHHS	93.821	3,337
	DHHS	93.837	169,443
	DHHS	93.837	277,391
	DHHS	93.837	251,448
	DHHS	93.837	327,146
	DHHS	93.837	498,233
	DHHS	93.837	276,641
	DHHS	93.837	58,735
	DHHS	93.837	888,118
	DHHS	93.838	(53)
	DHHS	93.846	55,376
	DHHS	93.847	35,072
	DHHS	93.847	306,870
	DHHS	93.847	51,960
	DHHS	93.847	145,642

Medical College of Ohio
 Schedule of Expenditures of Federal Awards
 Year Ended June 30, 2002

	AGENCY	CFDA #	FY2002
	DHHS	93.848	82,081
	DHHS	93.854	340,161
	DHHS	93.854	1,812
	DHHS	93.856	217,021
	DHHS	93.856	147,209
	DHHS	93.856	52,111
	DHHS	93.856	110,438
	DHHS	93.856	267,749
	DHHS	93.856	8,795
	DHHS	93.859	174,885
	DHHS	93.859	(64)
	DHHS	93.859	150,312
	DHHS	93.862	121,149
	DHHS	93.864	201,895
	DHHS	93.866	119,498
	DHHS	93.866	158,441
	DHHS	93.866	45,008
	DHHS	93.867	675
	DHHS	93.929	111,422
	DHHS	93.929	26,822
	DHHS	93.19277404	2,999
	DHHS	93.263005	14,876
	DHHS	93.DK02400	959,700
National Science Foundation	NSF	47.074	126,630
	NSF	47.074	114,907
	NSF	47.074	271
Pass through:			
Biocheck Labs	DHHS	93.855	4,123
Case Western University	DHHS	93.838	123,399
ECOG-Frontier Science	DHHS	93.395	130
Emory University	DHHS	93.853	9,146
Institute of Genomic Research	DHHS	93.856	77,518
Massachusetts Institute of Technology	DHHS	93.113	22,459
National Children's Cancer Institute	DHHS	93.395	7,303
National Medical Technology Testbed Inc	DOD	12.420	41,741
Statistics & Epidemiology	DHHS	93.HC55139	5,500
University of Rochester	DHHS	93.853	2,903
Ohio State University	DHHS	93.393	77,575
Southwest Oncology Group	DHHS	93.399	1,137
Toledo Community Hospital Oncology Program	DHHS	93.399	163
University of Alaska	DOC	11.430	8,203
University of Alaska	NSF	47.078	41,902
University of Cincinnati	DHHS	93.393	(209)
University of Iowa	DHHS	93.837	36,933
University of Michigan	DHHS	93.395	10,573
University of Michigan	NSF	47.074	39,653
University of Toledo	DHHS	93.837	6,319
University of Texas Health Center	DHHS	93.395	3,194
Veterans Medical Research Fdn	DHHS	93.856	192,224
Washington University	DHHS	93.121	359,989
Wayne State University	DHHS	93.173	74,511
			12,021,157
OTHER:			
Center for Disease Control	DHHS	93.263	51,674
Health Resources and Service Administration	DHHS	93.107	733,320
	DHHS	93.153	347,964
	DHHS	93.191	5,224
	DHHS	93.298	111,650
	DHHS	93.358	36,098
	DHHS	93.379	32,892

Medical College of Ohio
 Schedule of Expenditures of Federal Awards
 Year Ended June 30, 2002

	AGENCY	CFDA #	FY2002	
	DHHS	93.886	70,946	
	DHHS	93.896	(11,888)	
	DHHS	93.896	138,597	
	DHHS	93.918	171,825	
	DHHS	93.984	37,537	
	DHHS	93.984	138,806	
Health and Human Services	DHHS	93.558	13,200	
National Institutes of Health	DHHS	93.278	37,152	
	DHHS	93.278	33,352	
	DHHS	93.398	196,005	
National Science Foundation	NSF	47.074	3,981	
Pass through:				
Bowling Green State University	DHHS	93.44011285272	14,213	
City of Toledo	DHHS	93.940	12,237	
Ohio Department of Health	UDE	84.181	64,886	
	DHHS	93.917	(123)	
	DHHS	93.919	1,736	
	DHHS	93.958	140,765	
	DHHS	93.994	19,220	
	DHHS	93.994	150,803	
University of Illinois	DHHS	93.879	15	
			2,552,087	
Community Mental Health Services	DHHS	93.958	552,167	552,167
Total Expenditures of Federal Awards			15,434,993	

Agency Key:

DHHS Department of Health & Human Services
 DOC Department of Commerce
 DOD Department of Defense
 DOI Department of Interior
 EPA Environmental Protection Agency
 NSF National Science Foundation
 UDE Department of Education

MEDICAL COLLEGE OF OHIO

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2002

1. **Basis of Presentation**

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Medical College of Ohio and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

2. **Family Education Loan Program (CFDA No. 84.032)**

Medical College of Ohio acts as the intermediary for students obtaining Family Education loans from lending institutions. The lending institution is responsible for billings and collections of the loans. The Medical College of Ohio assists the lending institutions by processing the applications and forwarding checks from the lending institutions to the students. Loans advanced to students during the fiscal year ended June 30, 2002, totalled \$14,157,725.

3. **Health Professions Student Loan Program (CFDA No. 93.342)**

Revolving loan funds are established to maintain Health Professions Student Loans. Repayment of principal and interest are deposited back into the program for new loans. The Medical College of Ohio is responsible for administering the program, including the approving, disbursing, and collecting of the loans. Since July 1, 1993, Health Professions Student Loan funds have been awarded in the form of Primary Care Loans and Loans for Disadvantaged Students. As of June 30, 2002, outstanding loans under both programs totalled \$1,285,090.

4. **Federal Perkins Loan Program (CFDA No. 84.038)**

Revolving loan funds are also established to maintain Perkins loans. Repayments of principal and interest are deposited back into the program for new loans. The Medical College of Ohio is responsible for administering the program, including the approving, disbursing, and collecting of the loans. As of June 30, 2002, outstanding Perkins loans totalled \$4,008,001.

REPORT OF INDEPENDENT AUDITORS ON
COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Board of Trustees
Medical College of Ohio

We have audited the financial statements of the Medical College of Ohio as of and for the year ended June 30, 2002, and have issued our report thereon dated September 27, 2002. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Medical College of Ohio's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be disclosed under Government Auditing Standards.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Medical College of Ohio's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Board of Trustees, management, federal awarding agencies, state agency, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



September 27, 2002

REPORT OF INDEPENDENT AUDITORS ON
COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH
MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH OMB CIRCULAR A-133

Board of Trustees
Medical College of Ohio

Compliance

We have audited the compliance of the Medical College of Ohio with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2002. The Medical College of Ohio's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Medical College of Ohio's management. Our responsibility is to express an opinion on the Medical College of Ohio's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Medical College of Ohio's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Medical College of Ohio's compliance with those requirements.

In our opinion, the Medical College of Ohio complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2002.

Internal Control Over Compliance

The management of the Medical College of Ohio is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Medical College of Ohio's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Board of Trustees, management, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

September 27, 2002

MEDICAL COLLEGE OF OHIO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

June 30, 2002

Part I - Summary of Auditor's Results

Financial Statement Section

- (i) Type of auditor's report issued: unqualified
- (ii) Internal control over financial reporting:
- Material weakness(es) identified? yes X no
- Reportable condition(s) identified not considered
to be material weakness(es)? yes X none
reported
- (iii) Noncompliance material to financial statements noted? yes X no

Federal and State Awards Section

- (viii) Dollar threshold used to determine Type A programs: \$1,046,574
- (ix) Auditee qualified as low-risk auditee? X yes no
- (v) Type of auditor's report on compliance for major programs: unqualified
- (iv) Internal control over compliance:
- Material weakness(es) identified? yes X no
- Were reportable condition(s) identified not considered
to be material weakness(es)? yes X none
reported
- (vi) Any audit findings disclosed that are required to be reported
in accordance with Circular A-133 (Section .510(a))? yes X no
- (vii) Identification of major programs:

CFDA Number(s)	Name of Federal Program or Cluster
Various 93.958 93.918	Research and Development Cluster Community Mental Health Services Ryan White Title III Program

Part II - Schedule of Financial Statement Findings

None

Part III - Schedule of Federal Award Findings and Questioned Costs

None

REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Medical College of Ohio

We have audited the accompanying balance sheets of the Medical College Hospitals (Hospital Funds of the Medical College of Ohio, a component unit of the State of Ohio, - see Note 1) as of June 30, 2002 and 2001, and the related statements of revenue and expenses and changes in fund balance and cash flows for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Hospital funds and are not intended to present fairly the financial position of the Medical College of Ohio, and the results of its operations in conformity with accounting principles generally accepted in the United States.

As discussed in Note 8, the Hospital changed its method of accounting for Workers' Compensation liability.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Medical College Hospitals as of June 30, 2002 and 2001, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.



September 27, 2002

MEDICAL COLLEGE HOSPITALS

**BALANCE SHEETS
(Dollars in Thousands)**

	<u>Year Ended June 30</u>	
	<u>2002</u>	<u>2001</u>
<u>ASSETS</u>		
Current Assets		
Cash and Cash Equivalents	\$ -	\$ 1,386
Investments	-	256
Accounts Receivable, Net	37,703	35,187
Estimated Receivables Under Third Party Reimbursement Programs	6,517	1,847
Accrued Interest Receivable	105	179
Inventories	3,171	2,985
Prepaid Expense	414	329
Total Current Assets	47,910	42,169
Property, Plant and Equipment		
Property, Plant and Equipment at Cost	177,503	171,795
Less Accumulated Depreciation	<u>(103,744)</u>	<u>(97,089)</u>
Net Property, Plant and Equipment	73,759	74,706
Other Assets		
Self-Insurance Trust Investments	2,053	1,916
Investments Held For Capital Expansion	<u>14,761</u>	<u>9,273</u>
Total Other Assets	16,814	11,189
Total Assets	<u>\$ 138,483</u>	<u>\$ 128,064</u>
<u>LIABILITIES AND FUND BALANCES</u>		
Current Liabilities		
Accounts Payable	\$ 12,274	\$ 8,393
Accrued Liabilities	15,553	9,509
Malpractice - Current Portion	100	800
Long-Term Debt - Current Portion	<u>1,529</u>	<u>630</u>
Total Current Liabilities	29,456	19,332
Noncurrent Liabilities		
Malpractice	3,000	2,200
Allocation of State Unfunded Workers' Compensation	4,234	3,071
Long-Term Debt	<u>4,863</u>	<u>600</u>
Total Noncurrent Liabilities	12,097	5,871
Total Liabilities	41,553	25,203
Fund Balance	<u>96,930</u>	<u>102,861</u>
Total Liabilities and Fund Balance	<u>\$ 138,483</u>	<u>\$ 128,064</u>

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

MEDICAL COLLEGE HOSPITALS
STATEMENTS OF REVENUE AND EXPENSES AND
CHANGES IN FUND BALANCE
(Dollars in Thousands)

	Year Ended June 30	
	2002	2001
Revenue		
Net Patient Service Revenue	\$ 155,870	\$ 149,740
Other Revenue	9,051	8,287
Investment Income	911	1,289
	165,832	159,316
Expenses		
Salaries and Benefits	85,523	77,318
Supplies	37,089	35,314
Allocated College Expenses	11,119	11,519
Outside Purchased Services	17,811	16,832
Depreciation and Amortization	9,981	9,765
Provision for Uncollectible Accounts	3,250	6,668
Information/Communication	1,285	1,316
Travel	266	377
Interest on Debt	94	-
State Unfunded Workers' Compensation	1,163	(1,695)
Other Expenses	2,631	1,179
	170,212	158,593
Revenue Less Than Expenses	(4,380)	723
Fund Balance at Beginning of Year	102,861	108,823
Restatement for State Unfunded Workers' Compensation (Note 8)	-	(4,766)
Fund Balance at Beginning of Year as Restated	102,861	104,057
Transfers:		
Transfer to Subsidized Programs	-	34
Transfer of Plant Assets Between College and Hospital	(1,855)	(4,134)
State Capital Appropriations	-	1,650
Net Realized and Unrealized Gain on Investments	304	531
	\$ 96,930	\$ 102,861

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

MEDICAL COLLEGE HOSPITALS

STATEMENTS OF CASH FLOWS
(Dollars in Thousands)

	Year Ended June 30	
	2002	2001
Operating Activities		
Revenue Less than Expenses	\$ (4,380)	\$ 723
Adjustments to Reconcile Revenue Less Than Expenses to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	9,981	9,765
Provision for Uncollectible Accounts	3,250	6,668
Changes in Assets and Liabilities Affecting Operating Activities:		
Receivables	(10,362)	(14,465)
Inventories	(186)	196
Prepaid Expense	(85)	(83)
Accounts Payable	3,881	(964)
Accrued Liabilities	7,307	(1,463)
Net Cash Provided by Operating Activities	9,406	377
Noncapital Financing Activities		
Subsidized Program Transfer	-	34
Net Cash Provided by in Noncapital Financing Activities	-	34
Capital and Related Financing Activities		
Acquisition of Property, Plant, and Equipment	(10,889)	(9,234)
Capital Expansion Funds	(5,488)	22
Capital Lease Obligations	236	(955)
Proceeds from Line of Credit	682	-
Proceeds from Capital Debt	4,310	-
Capital Debt Principle Payments	(66)	-
Net Cash Used in Capital and Related Financing Activities	(11,215)	(10,167)
Investing Activities		
Net Sales of Investments	560	9,036
Purchases of Self-Insurance Trust Investments	(137)	(166)
Net Cash Provided by Investing Activities	423	8,870
Decrease in Cash and Cash Equivalents	(1,386)	(886)
Cash and Cash Equivalents at Beginning of Year	1,386	2,272
Cash and Cash Equivalents at End of Year	-	\$ 1,386

Supplemental disclosure of cash flow information:

This amount represents a noncash capital and related financing activity and are not included in the Acquisition of Property, Plant and Equipment above. During fiscal 2002 and 2001, MCO entered into capital lease obligations of \$1,139 and \$427, respectively, for certain hospital equipment, which is also excluded from the statement of cash flows.

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

MEDICAL COLLEGE HOSPITALS
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Medical College Hospitals (the Hospital) is a nonprofit teaching hospital located in Toledo, Ohio. The Hospital is licensed to operate a 258-bed acute and ambulatory care facility, a 25-bed child and adolescent psychiatric facility and a 36-bed rehabilitation facility.

The Hospital is operated as part of the Medical College of Ohio (MCO), a nonprofit, state-supported medical school, which is a component unit of the State of Ohio.

Accounting and reporting principles

The accounting and reporting principles followed by the Hospital include those established by the American Institute of Certified Public Accountants (AICPA). The financial statements have been prepared based on the provisions of the AICPA Audit and Accounting Guide entitled "Health Care Organizations," and does not reflect the GASB reporting requirements.

Patient accounts receivable and revenue

Patient accounts receivable and revenue are recorded at net realizable value when patient services are performed. MCO has agreements with third-party payors that provide for payments to MCO at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows.

- **Medicare and Medicaid**

MCO is a provider of services under the Medicare and Medicaid programs. MCO is paid a prospectively determined fixed price for each Medicare and Medicaid inpatient. The price varies depending on the type of illness or the patient's diagnostic related group classification. Capital costs, certain Medicare outpatient services, and Medicaid outpatient services are also reimbursed on a prospectively determined fixed price. Graduate medical education is reimbursed on a per resident basis under the Medicare program. MCO receives payment for other Medicare outpatient services and certain inpatient costs on a reasonable cost basis.

- **Other Payors**

MCO has also entered into payment agreements with certain commercial carriers to provide health care services. The basis for payment to MCO under these agreements is based on prospectively determined fixed prices, fee screens, or on a percentage of billed charges.

Provision is made in the financial statements for the differences between MCO's standard rates charged for services rendered and third-party reimbursements and for estimated settlements based on third-party reimbursement contracts. Retroactive settlements resulting from third-party audits of filed cost reports are reflected in the financial statements in the year of settlement. These provisions and settlements are included in deductions from patient service revenue. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

MEDICAL COLLEGE HOSPITALS
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

Charity care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. These amounts qualify as charity care and are not reported as revenue.

Inventories

Inventories include pharmaceuticals and medical and surgical supplies. Inventories are stated at the lower of cost or market. Cost is determined on the average cost basis.

Investments

Investments are made in accordance with policies of the Board of Trustees of the Medical College of Ohio. The types of investments that may be purchased by the institution include United States treasury obligations, certificates of deposit, bankers acceptances, corporate notes and bonds, money market funds, government agency securities and commercial paper. Investments qualifying as "derivatives" may not be purchased. As MCO does not present a classified balance sheet, the investments held in the pooled investment fund are classified as current assets on the Hospital balance sheet.

Certain cash and investments are board designated for self-insurance and capital expansion. These assets are presented in the noncurrent section of the Hospital's balance sheets.

State capital appropriations

The State of Ohio provides funding for construction of major plant facilities. State capital appropriations are not reflected on MCO's financial statements until expended by the State. When expended, state appropriations are recognized as additions to property, plant, and equipment and fund balance.

Property, plant and equipment

Property, plant and equipment are recorded at cost or, if acquired by donation, at appraised values. Depreciation and amortization of assets acquired under capital leases is computed using the straight-line method over the lesser of the assets' estimated useful lives or terms of the leases. Amortization of assets under capital leases is included with depreciation expense.

Income taxes

MCO is exempt from income taxes under Section 115 of the Internal Revenue Code.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

MEDICAL COLLEGE HOSPITALS
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 2 - NET PATIENT SERVICE REVENUE

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Net patient service revenue is comprised of the following:

	<u>Year Ended June 30, 2002</u>	<u>Year Ended June 30, 2001</u>
Gross patient charges	\$272,790	\$262,373
Less provision for third-party contractual allowances and adjustments:		
Medicare	(39,666)	(42,322)
Medicaid	(5,132)	(8,142)
Other	(62,421)	(54,428)
Less charity care services	<u>(9,701)</u>	<u>(7,740)</u>
Net Patient Service Revenue	<u>\$155,870</u>	<u>\$149,740</u>

Approximately 50% of the Hospital's revenue is derived under prospectively determined rate provisions of third-party programs (primarily Medicare and Medicaid). Revenue received under these third-party agreements (primarily the Medicare and Medicaid programs) are subject to examination and retroactive adjustments. Prior year settlements recognized in 2002 and 2001 increased net patient service revenue by approximately \$1,300 and \$200, respectively. Net patient service revenue for 2002 and 2001 includes \$5,506 and \$4,689, respectively, from the Ohio Hospital Care Assurance Program. It is the opinion of management that it is at least reasonably possible that the estimated settlements recorded will not change by material amounts in the near term.

NOTE 3 - CHARITY AND UNCOMPENSATED CARE

Charity care includes services provided to persons who cannot afford healthcare because of inadequate resources or who are uninsured or underinsured. In addition to charity care, services are provided under Medicaid and other Welfare programs. Certain payments received under these programs are less than the cost of providing the service.

A summary of charity and uncompensated care, at cost, is as follows:

	<u>Year Ended June 30, 2002</u>	<u>Year Ended June 30, 2001</u>
Traditional charity care	\$5,864	\$4,777
Unpaid costs of traditional Medicaid programs	1,042	1,569
Unpaid costs of Other Welfare programs	<u>3,913</u>	<u>2,967</u>
Total Charity and Uncompensated Care	<u>\$10,819</u>	<u>\$9,313</u>

Charity and uncompensated care approximated 6.42% of total Hospital expenses for the year ended June 30, 2002 and 5.81% for the year ended June 30, 2001, and do not include provision for uncollectible accounts.

MEDICAL COLLEGE HOSPITALS
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 4 - CASH AND INVESTMENTS

In 1998, MCO adopted Governmental Accounting Standards Board Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, which requires that investments in equity securities with readily determinable fair values and all investments in debt securities be measured at fair value. Fair value is determined based on quoted market prices.

MCO's cash and investments are accounted for on a pooled basis. MCO employs the shared method of accounting for pooled cash and investments and for proportionate distribution of income to each fund with equity in the pool. The Hospital's portion of the bank balance of cash deposits at June 30, 2002, was \$569. Of the bank balance, up to \$100 is insured by federal depository insurance and the remainder is uninsured but collateralized by pools of securities pledged by the depository bank and held in the name of the bank.

Investments are stated at market value at June 30, 2002 and 2001. Investments are held in safekeeping by MCO's custodial bank's trust department, whose records identify MCO's ownership. For purposes of the statement of cash flows, the Hospital considers all highly liquid debt instruments with an original maturity of three months or less to be cash equivalents.

	<u>June 30, 2002</u> Market and Carrying Value	<u>June 30, 2001</u> Market and Carrying Value
Cash Equivalents:		
Money Market Funds	\$ -	\$ <u>1,386</u>
Total Cash and Cash Equivalents	<u>\$ -</u>	<u>\$ 1,386</u>
Investments:		
Corporate Notes	\$ 2,696	\$ 1,883
Bonds	<u>6,004</u>	<u>7,646</u>
Total Investments	<u>\$ 8,701</u>	<u>\$ 9,529</u>
Investments included in Current Assets	(6,060)	\$ 256
Investments included in Capital Expansion Funds	<u>14,761</u>	<u>9,273</u>
Total Investments	<u>\$ 8,701</u>	<u>\$ 9,529</u>

MEDICAL COLLEGE HOSPITALS
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 5 - ACCOUNTS RECEIVABLE

A summary of accounts receivable, net is as follows:

	<u>June 30</u>	
	<u>2002</u>	<u>2001</u>
Patient accounts:		
Inpatient	\$29,568	\$30,548
Outpatient	8,957	12,082
Other	<u>15,812</u>	<u>10,507</u>
	54,337	59,137
Less:		
Allowance for uncollectible accounts	(2,598)	(5,278)
Contractual and other adjustments	<u>(14,036)</u>	<u>(18,672)</u>
Net Accounts Receivable	<u>\$37,703</u>	<u>\$35,187</u>

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors for 2002 and 2001 was as follows:

	<u>2002</u>	<u>2001</u>
Medicare	30%	39%
Commercial	24	22
Traditional Medicaid	11	11
Medical Mutual of Ohio	7	7
Blue Cross	8	4
Other Third-Party Payors	19	15
Patients	<u>1</u>	<u>2</u>
	<u>100%</u>	<u>100%</u>

NOTE 6 - SETTLEMENTS UNDER THIRD-PARTY REIMBURSEMENT CONTRACTS

The reimbursement for Medicare and Medicaid patients is subject to final determination by the respective agencies. Final determinations have been made through 1999 for Medicare and 1997 for Medicaid. Tentative settlements have been made through 2001 for both Medicare and Medicaid.

MEDICAL COLLEGE HOSPITALS
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 7- PROPERTY, PLANT AND EQUIPMENT

A summary of property, plant and equipment is as follows:

	<u>June 30</u>	
	<u>2002</u>	<u>2001</u>
Land and improvements	\$ 3,188	\$ 565
Building and fixtures	111,138	97,300
Equipment	57,098	58,505
Construction in progress (estimated cost to complete \$5,178)	<u>6,079</u>	<u>15,425</u>
	177,503	171,795
Less: Accumulated depreciation	<u>(103,744)</u>	<u>(97,089)</u>
Net Property, Plant and Equipment	<u>\$ 73,759</u>	<u>\$ 74,706</u>

NOTE 8 – WORKERS’ COMPENSATION

The College participates in the State’s self-insured workers’ compensation plan (the Plan), which pays workers’ compensation benefits to beneficiaries who have been injured on the job. Losses from asserted and unasserted claims for the participating State agencies and colleges in the Plan are accrued by the Ohio Bureau of Workers’ Compensation (the Bureau) based on estimates that incorporate the past experience, as well as other considerations including the nature of each claim or incident and relevant trend factors. Participants in the State’s Plan annually fund the workers’ compensation liability based on rates set by the Bureau to collect the cash needed in subsequent fiscal years to pay the workers’ compensation claims of participating State agencies and colleges. The Bureau has actuarially calculated estimated amounts for the State of \$727 million at June 30, 2002, \$559.3 million at June 30, 2001 and \$548.3 million at June 30, 2000 to be paid in future periods. The State determined the Hospital’s pro-rata share of the estimated liability on the basis of the Hospital’s share of actual cash payments (premiums and administrative costs) to the Bureau in the preceding fiscal year divided by such payments made by all participating entities. The Hospital has restated its prior year fund balances for the estimated liability at June 30, 2000 of \$4,766. The estimated liability at June 30, 2002 and June 30, 2001 is \$4,234 and \$3,071 respectively. The increase of \$1,163 in 2002 and the decrease \$1,695 in 2001 are included in operating expenses.

The decision to record this liability was a result of determinations made by the State of Ohio in its interpretations of the treatment of the unfunded pool obligation. Further, the recording of this liability is based on an allocation of the entire pool on a pro-rata basis to the participating state agencies and universities. Such amount could differ had a separate actuarial computation by participating state universities been performed.

MEDICAL COLLEGE HOSPITALS
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 9 – LONG TERM DEBT AND LEASE COMMITMENTS

Capital lease activity for the year ended June 30, 2002 was as follows:

	Balance July 1, <u>2001</u>	<u>Additions</u>	<u>Payments</u>	Balance June 30, <u>2002</u>	Current <u>Portion</u>
Master Lease Purchase Obligations	\$ -	\$4,977	\$ (51)	\$4,926	\$ 733
Other Lease Obligations	<u>1,230</u>	<u>1,140</u>	<u>(904)</u>	<u>1,466</u>	<u>796</u>
Total Long-Term Debt	<u>\$1,230</u>	<u>\$6,117</u>	<u>\$ (955)</u>	<u>\$6,392</u>	<u>\$1,529</u>

In 2002, MCO entered into a master equipment lease purchase agreement with a financial institution to finance a linear accelerator with monthly payments of \$48 beginning in July 2002 at 4.95% annual interest rate through 2009. At June 30, 2002, approximately \$1.9 million is included in capital assets; the remaining \$1.5 million is in an escrow account, which is included in restricted cash and cash equivalents.

In 2002, MCO entered into a master equipment lease purchase agreement with a financial institution to finance a water chiller unit with monthly payments of \$16 beginning in February 2002 at 3.79% annual interest rate through 2007. At June 30, 2002, approximately \$590 is included in capital assets, and \$298 of the remaining funds is in an escrow account, which is included in restricted cash and cash equivalents.

In 2002, MCO entered into a master equipment lease purchase agreement with a financial institution, which extends a \$3 million line of credit until June, 2007. Subsequently, MCO utilized the line of credit by entering into three capital lease agreements for \$560, \$77 and \$48. At June 30, 2002, \$685 is included in capital assets pertaining to these capital leases, related to equipment with monthly payments of \$13 at 4.8% interest rate through 2007.

MCO has other capital lease obligations of \$1,466 and \$1,229 at June 30, 2002 and 2001, respectively. The cost of the assets recorded under capital leases as of June 30, 2002, is \$3,399.

Minimum lease payments at June 30, 2002, by year and in the aggregate, under capital leases are as follows:

	<u>Other Lease Obligations</u>	<u>Master Lease Purchase Obligations</u>
2003	\$ 847	\$ 923
2004	569	923
2005	111	923
2006	10	923
2007	-	713
2008-2012	<u>-</u>	<u>1,159</u>
Net minimum lease payments	\$1,537	\$5,564
Less amounts representing interest	<u>(71)</u>	<u>(638)</u>
Present value of lease payments	<u>\$1,466</u>	<u>\$4,926</u>

MEDICAL COLLEGE HOSPITALS
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

The Hospital leases certain patient care equipment under various noncancelable operating lease agreements. Total operating lease expense was \$847 in 2002 and \$647 in 2001. At June 30, 2002, the Hospital was committed to future minimum operating lease payments of \$240 in 2003, \$68 in 2004, \$0 in 2005, and \$0 in 2006.

At the expiration of various leases, the Hospital has the option to make a termination payment, purchase the equipment at fair market value or extend the lease term. Future minimum operating lease payments include \$117 in termination payments related to these lease agreements.

NOTE 10 - RETIREMENT PLANS

The Hospital participates in the Public Employees Retirement System of Ohio (PERS) and alternative retirement plans (ARP) as defined by Ohio Revised Code, Section 3305 and Am. Sub. House Bill 586. These plans are statewide cost-sharing multiple-employer public retirement system administered and controlled by the State of Ohio. The State of Ohio issues an annual plan financial report which can be obtained by contacting the appropriate state office.

Participating employees are entitled to retirement benefits payable for life, equal to 2.1% per year of credited service times the final average salary (the average of the three highest years of earnings). Participants are entitled to retirement benefits equal to 2.5% of their final average salary for each year of service over 30 years. Participating employees may retire at age 60 with at least five years of credited service, at age 55 with at least 25 years of credited service or at any age with at least 30 years of credited service. Participating employees retiring with less than 30 years of service or at less than age 65 receive reduced benefits. Retirement benefits vest with five years of credited service. PERS also provides health care, survivor and disability benefits.

State law provides for employer and employee contributions to PERS based on actuarially determined rates. The Ohio Retirement Study Council determines the ARP rates and the Ohio Department of Insurance approves ARP carriers. Senate Bill 346 established a revised PERS disability program. PERS members were given the opportunity to elect coverage under the original or revised disability program. Anyone hired after July 29, 1992, is automatically covered under the revised disability program. The revised program was designed to be cost neutral, therefore, does not affect PERS funding. There were no material changes in actuarial assumptions, benefit provisions, actuarial funding methods or other significant factors for fiscal years 2002, 2001, and 2000. The employee and employer contribution rates for PERS were 4.3% and 10.84%, respectively, for fiscal year 2001, and 8.5% and 13.31%, respectively, for fiscal years 2000, and 2002. The employee and employer contribution rates for ARP were 8.5% and 7.31%, respectively, for fiscal year 2002.

The Hospital paid the required employee retirement plan contribution on behalf of contract personnel in fiscal 2002, fiscal 2001 and fiscal 2000. The payment of employee contributions by the Hospital becomes a part of the employees' final average salary calculation for the year. Contributions made by employees or on behalf of employees for PERS amounted to \$4,942 in fiscal 2002, \$4,656 in fiscal 2001 and \$4,455 in fiscal 2000. Contributions made by employees or on behalf of employees for ARP amounted to \$14 for fiscal year 2002. The Hospital's retirement costs for PERS are funded as accrued and amounted to \$7,737 in fiscal 2002, \$5,775 in fiscal 2001 and \$6,915 in fiscal 2000. The Hospital's retirement costs for ARP are funded as accrued and amounted to \$12 for fiscal 2002.

MCO also provides termination benefits upon retirement resulting from unused sick days. During fiscal year 2002 and 2001, MCO calculated its liability in accordance with the provisions of GASB Statement No. 16 "Accounting for Compensated Absences."

MEDICAL COLLEGE HOSPITALS
NOTES TO FINANCIAL STATEMENTS
Year Ended June 30, 2002
(Dollars in Thousands)

NOTE 11 - MALPRACTICE MATTERS

MCO is self-insured for the first \$1,000 of loss per occurrence with an annual aggregate limit of \$3,000 for malpractice and general liability and maintains umbrella insurance coverage that covers any excess liability on a claims made basis. Settlement amounts have not exceeded insurance coverage for each of the past three fiscal years.

In accordance with the terms of the insurance policy, MCO maintains a self-insurance trust. Investments held in trust are comprised of U.S. government securities and corporate bonds recorded at market value at June 30, 2002 and 2001. These investments are held in safekeeping by MCO's custodial bank's trust department. These securities are registered in the bank's name with internal bank records identifying MCO's ownership.

At June 30, 2002 and 2001, the Hospital has accrued \$3,100 discounted at 6% and \$3,000 discounted at 6%, respectively, for asserted and unasserted claims, based on MCO's experience and studies performed by a consulting actuary. With respect to pending malpractice claims and legal action where MCO is a defendant, it is the opinion of management that any potential liability in such actions will not materially affect the financial position of the Hospital.

	<u>June 30, 2002</u>	<u>June 30, 2001</u>
Malpractice Liability at Beginning of Year	\$3,000	\$3,003
Provision for Incurred Claims	107	235
Payments for Claims	<u>(7)</u>	<u>(238)</u>
Malpractice Liability at End of Year	<u>\$ 3,100</u>	<u>\$3,000</u>

NOTE 12 - TRANSACTIONS WITH THE COLLEGE AND RELATED ORGANIZATIONS

During fiscal 2002 and 2001, the Hospital made nonmandatory fund balance transfers of \$0 from other funds and \$33 thousand to other funds for coverage of fund balance deficits.

The Medical College of Ohio Foundation (the Foundation) is a nonprofit entity, operating under a separate Board, organized primarily for the purpose of supporting the activities of MCO. The assets of the Foundation are not included in the financial statements of the Hospital. Amounts received from the Foundation are included in private gifts, grants and contracts in the accompanying financial statements.

Associated Physicians of the Medical College of Ohio (APMCO) is a for profit entity, operating under a separate Board, organized to provide physician services at the Medical College Hospitals. Amounts received from APMCO for the use of hospital facilities and support services are included in Other Hospital Revenues. MCO does not hold any ownership in APMCO and, therefore, the assets and liabilities of APMCO are not recorded in the accompanying financial statements.

GASB Statement No. 39, *Financial Reporting Entity—Affiliated Organizations* has been issued and is effective for periods beginning after June 15, 2003. This statement will require MCO to reflect the Foundation as a discretely presented component unit in the financial statements based on the significance of its relationship with MCO.



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OFFICE OF THE AUDITOR

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MEDICAL COLLEGE OF OHIO

LUCAS COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

CERTIFIED
DECEMBER 26, 2002