

***Ohio State University
Physicians, Inc. and
Subsidiaries***

*Consolidated Financial Statements and
Supplemental Consolidating Schedules as
of and for the Year Ended June 30, 2004
and Independent Auditors' Report*



**Auditor of State
Betty Montgomery**

Board of Directors
Ohio State University Physicians, Inc.
2080 Blankenship Hall
901 Woody Hayes Drive
Columbus, Ohio 43210-4016

We have reviewed the Independent Auditor's Report of the Ohio State University Physicians, Inc., Franklin County, prepared by Deloitte & Touche LLP, for the audit period July 1, 2003 to June 30, 2004. 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 Ohio State University Physicians, Inc. is responsible for compliance with these laws and regulations.

A handwritten signature in cursive script that reads "Betty Montgomery".

BETTY MONTGOMERY
Auditor of State

January 10, 2005

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OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Ohio State University Physicians, Inc.

We have audited the accompanying consolidated balance sheet of Ohio State University Physicians, Inc. (an Ohio not-for-profit corporation) and subsidiaries ("OSUP") as of June 30, 2004 and the related consolidated statement of activities and changes in net assets and cash flows for the year then ended. These consolidated financial statements are the responsibility of OSUP's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the 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 consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such consolidated financial statements referred to above present fairly, in all material respects, the financial position of OSUP June 30, 2004, and the results of their operations, changes in net assets, and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The supplemental schedules listed on pages 15 and 16 are presented for the purpose of additional analysis of the basic consolidated financial statements rather than to present the financial position and results of the individual entities, and are not a required part of the basic consolidated financial statements. These schedules are the responsibility of Ohio State University Physicians, Inc. and its subsidiaries' management. Such schedules have been subjected to the auditing procedures applied in our audits of the basic consolidated financial statements and, in our opinion, are fairly stated in all material respects when considered in relation to the basic consolidated financial statements taken as a whole.

In accordance with Government Auditing Standards, we have also issued a report dated December 10, 2004, on our consideration of OSUP's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grants and other matters. 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.


December 10, 2004

OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

JUNE 30, 2004

ASSETS

CURRENT ASSETS:

Cash and cash equivalents	\$ 10,041,076
Accounts receivable—patient care, net of allowance of \$36,090,972	19,344,225
Accounts receivable other—current, net of allowance of \$498,235	1,495,814
Due from affiliate	1,832,126
Inventories	135,660
Prepaid expenses	631,785
Notes receivable	<u>26,307</u>
Total current assets	<u>33,506,993</u>

NON-CURRENT ASSETS:

Property, plant, furnitures and equipment, net of accumulated depreciation of \$5,342,916	5,061,488
Restricted beneficial interest in clinical enterprise assets	53,747
Other assets	<u>135,229</u>
Total non-current assets	<u>5,250,464</u>

TOTAL \$ 38,757,457

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES:

Accounts payable	\$ 4,484,954
Accrued expenses	1,450,040
Accrued salaries and wages	7,043,999
Due to affiliates—current portion	3,285,536
Notes payable and capital leases—current portion	4,855,050
Other post-retirement benefits obligation	<u>2,307,391</u>
Total current liabilities	<u>23,426,970</u>

LONG-TERM LIABILITIES:

Notes payable and capital leases—less current portion	8,064,632
Due to affiliates—long-term	<u>1,345,634</u>
Total long-term liabilities	<u>9,410,266</u>

NET ASSETS:

Unrestricted	5,820,639
Temporarily restricted net assets	<u>99,582</u>
Total net assets	<u>5,920,221</u>

TOTAL \$ 38,757,457

See notes to consolidated financial statements.

OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS YEAR ENDED JUNE 30, 2004

	Unrestricted Net Assets	Temporarily Restricted Net Assets
NET PATIENT CARE REVENUES	\$ 94,528,384	\$ -
CONTRACT SERVICES	18,754,198	
OTHER SERVICES	<u>5,066,819</u>	<u>99,582</u>
Total operating revenues	<u>118,349,401</u>	<u>99,582</u>
OPERATING EXPENSES:		
Provider salaries	42,384,737	
Employees salaries and wages	17,649,355	
Provision for bad debts	9,450,435	
Provider fringe benefits	7,023,698	
Professional liability insurance	5,334,189	
Employee fringe benefits	5,408,287	
Medical supplies	5,002,237	
Office and administrative other	3,710,042	
Purchased services and management fees	3,259,078	
Academic enrichment and strategic initiative	2,945,357	
Clinical drugs and medications	2,413,650	
Rent and other occupancy costs	1,917,231	
Other provider related expenses	1,299,211	
Supplies	1,021,086	
Depreciation and amortization	823,779	
Other clinical related expenses	698,034	
Office and administrative billing	441,747	
Interest expense	376,475	
Insurance	<u>72,564</u>	
Total operating expenses	<u>111,231,192</u>	<u>-</u>
OPERATING INCOME	<u>7,118,209</u>	<u>99,582</u>
NON-OPERATING INCOME:		
Other non-operating—net	212,739	
Investment income	6,650	
Gain on sale of assets	<u>625</u>	
Total non-operating income	<u>220,014</u>	<u>-</u>
INCREASE IN NET ASSETS	7,338,223	99,582
NET ASSETS—Beginning of year	<u>(1,517,584)</u>	
NET ASSETS—End of year	<u>\$ 5,820,639</u>	<u>\$ 99,582</u>

See notes to consolidated financial statements.

OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS YEAR ENDED JUNE 30, 2004

CASH FLOWS FROM OPERATING ACTIVITIES:

Change in net assets	\$ 7,437,805
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Depreciation and amortization	823,779
Gain on sale of assets	(625)
(Increase) decrease in:	
Accounts receivable—patient care, net	(15,592,661)
Accounts receivable—other current, net	(1,994,049)
Due from affiliates	(999,342)
Note receivable—short-term	(26,307)
Inventories	(93,613)
Prepays	173,292
Other assets	(128,611)
Accounts payable	(548,104)
Due to affiliates	2,735,129
Accrued salaries and wages	3,956,933
Accrued pension	2,155,035
Other accrued liabilities	<u>1,351,886</u>
Net cash used in operating activities	<u>(749,453)</u>

CASH FLOWS FROM INVESTING ACTIVITIES:

Purchase of property, plant, furnitures and equipment	<u>(2,266,317)</u>
Net cash used in investing activities	<u>(2,266,317)</u>

CASH FLOWS FROM FINANCING ACTIVITIES:

Proceeds from notes payable	12,398,814
Payments on notes payable	(2,826,603)
Beneficial interest in clinical enterprise assets	<u>202,423</u>
Net cash provided by financing activities	<u>9,774,634</u>

NET INCREASE IN CASH AND CASH EQUIVALENTS 6,758,864

CASH AND CASH EQUIVALENTS—Beginning of year 3,282,212

CASH AND CASH EQUIVALENTS—End of year \$ 10,041,076

SUPPLEMENTAL DISCLOSURES OF CASH INFORMATION—

Cash paid for interest	<u>\$ 355,304</u>
Property additions under capital lease agreements	<u>\$ 205,945</u>
Transfers of assets:	
Fair value of assets assumed	<u>\$ 3,786,850</u>
Liabilities assumed	<u>\$ 3,786,850</u>

See notes to consolidated financial statements.

OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS YEAR ENDED JUNE 30, 2004

1. DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization—Ohio State University Physicians, Inc., (“OSUP”) located in Columbus, Ohio, is a 501(c)(3) tax-exempt physician organization for the physicians providing medical care and supporting medical research and medical education at The Ohio State University (the “University”). It was incorporated in Ohio in 2002 and the physicians primarily serve communities within the Central Ohio region.

OSUP is the single member of fourteen limited liability companies (“LLCs”). As of June 30, 2004 only eleven of the limited liability companies are active and included in the accompanying supplemental consolidating schedules. Three of the limited liability companies (Anesthesiology, Orthopedics and Otolaryngology) have been created but have no business activity through June 30, 2004.

The following table outlines the reporting of OSUP’s financial statements as of June 30, 2004 and 2003:

Practice Plan	2004	2003
Family Medicine Foundation, LLC (“FM”)	X	X
OSU Anesthesiology, LLC (“Anesthesiology”)	X	
OSU Children’s Pediatrics, LLC	X	
OSU Emergency Medicine, LLC (“EM”)	X	
OSU GYN and OB Consultants, LLC (“OBGYN”)	X	
OSU Internal Medicine, LLC (“IM”)	X	X
OSU Neuroscience Center, LLC (“Neurology”)	X	
OSU Orthopedics, LLC (“Orthopedics”)	X	
OSU Otolaryngology-Head and Neck Surgery, LLC (“Otolaryngology”)	X	
OSU Pathology, LLC (“Pathology”)	X	
OSU Physical Medicine and Rehabilitation (“Phys Med”)	X	
OSU Psychiatry, LLC (“Psychiatry”)	X	
OSU Radiology, LLC (“Radiology”)	X	
OSU Surgery, LLC (“Surgery”)	X	

OSUP obtains certain unique benefits from its association with the University. The consolidated financial statements of OSUP may not necessarily be indicative of the conditions that would have existed or the results of operations if OSUP had been operated without its affiliation with the University.

Principles of Consolidation—The consolidated financial statements include the accounts of the Ohio State University Physicians, Inc. and its subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Cash and Cash Equivalents—Cash and cash equivalents includes investments with original maturities of three months or less, excluding assets whose use is limited.

Patient Care Accounts Receivable and Net Patient Care Revenues—Net patient service revenue represents amounts received and the estimated net realizable amounts due from patients and third-party payors for services rendered. OSUP provides care to patients under various reimbursable agreements, including Medicare and Medicaid. These arrangements provide for payment for covered services at agreed-upon rates and under certain fee schedules and various discounts from charges. Provisions have been made in the consolidated financial statements for estimated contractual adjustments, representing the difference between the customary charges for services rendered and related reimbursement.

OSUP utilizes the allowance method for providing for the possibility of uncollectible accounts. The allowance is provided based on management's estimate of the collectibility of the accounts receivable as of June 30, 2004. The estimates take into consideration historical trends, payment history and current economic conditions. Actual results could vary from the estimate. Accounts are charged against the allowance when management deems them to be uncollectible. Interest is not charged by OSUP on past due accounts.

Charity Care and Community Benefit—Care is provided to patients regardless of their ability to pay. A patient is classified as charity care in accordance with policies established by the OSU Health System and OSUP. Because collection of amounts determined to qualify as charity care, are not pursued, such amounts are written off as administrative adjustments and not reported as net patient service revenue. OSUP maintains records to identify and monitor the level of charity care provided, including the amount of charges foregone for services furnished.

Inventory—OSUP's, inventory, which consists primarily of prescription drugs, is valued at cost on a first-in, first-out basis.

Property, Plant, Furnitures and Equipment—Property, plant, furnitures and equipment are stated at cost and include assets leased under capitalized lease obligations. Depreciation and amortization are calculated on the straight-line method. The depreciation and amortization methods are designed to amortize the assets over their estimated useful lives, ranging from 3 to 40 years. Capitalized lease amortization is included in depreciation expense.

Maintenance and repairs are charged to expense as incurred. Upon retirement of equipment, the cost is removed from the asset accounts and the related depreciation allowance is adjusted with the difference being charged or credited to non-operating gains (losses).

Professional and General Insurance—Because of the nature of its operations, OSUP is at all times subject to pending and threatened legal actions which arise in the normal course of its activities. Malpractice and general patient liability claims have been asserted against OSUP by various claimants. The claims are in various stages and some may ultimately be brought to trial.

OSUP maintains professional and general liability insurance, underwritten by the University Self-Insurance Fund ("USIF"). At June 30, 2004, management believes asserted and unasserted claims and assessments will not exceed the limits of insurance coverage. Coverage limits are \$4 million per incident with a \$25 million aggregate layer. Accordingly, no amounts have been accrued for malpractice and general patient liability claims at June 30, 2004.

There may be other claims asserted arising from services provided to patients, however, management has no basis to estimate the ultimate cost, if any, of the settlement of such potential claims and, accordingly, has not accrued for them.

Temporarily Restricted Net Assets—Temporarily restricted net assets are cash and other assets whose use by OSUP has been limited by donors. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying financial statements. As of June 30, 2004, the balance of temporarily restricted net assets is \$99,582 and is available for health care services and physician’s expenses.

Federal Income Taxes—Ohio State Physicians, Inc. is a not-for-profit corporation and has been recognized as tax-exempt pursuant to Sec. 501(c)(3) of the Internal Revenue Code. As such, no provision for income taxes has been included in the accompanying consolidated financial statements.

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

Fair Value of Financial Instruments—Cash and cash equivalents, accounts receivable and accounts payable are recorded at their approximate fair value.

Long-Lived Assets—OSUP continually evaluates whether circumstances have occurred that would indicate the remaining estimated useful life of long-lived assets may warrant revision or that the remaining balance of such assets may not be recoverable. When factors indicate that such assets should be evaluated for possible impairment, OSUP uses an estimate of the undiscounted cash flows over the remaining life of the asset in measuring whether the asset is recoverable. To date, no such impairments have been necessary.

Recently Issued Financial Accounting Standards—In May 2003, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards (“SFAS”) No. 150, *Accounting for Certain Financial Instruments With Characteristics of Both Liabilities and Equity*. SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. Under this statement, it requires a company to classify a financial instrument that is within its scope as a liability because the financial instrument embodies an obligation of a company. This statement is effective for OSUP beginning July 1, 2004. OSUP is currently evaluating the overall impact of SFAS No. 150 on its consolidated financial statements.

In December 2003, the FASB issued FASB Interpretation 46R, *Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51* (“FIN 46R”), to expand upon and strengthen existing accounting guidance that addresses when a company should include in its financial statements the assets, liabilities and activities of another entity. Until now, one company generally has included another entity in its consolidated financial statements only if it controlled the entity through voting interests. FIN 46R changes that by requiring a variable interest entity, as defined, to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity’s activities or entitled to receive a majority of the entity’s residual returns or both. FIN 46R also requires disclosures about variable interest entities that the company is not required to consolidate but in which it has significant variable interest. The consolidation requirements of FIN 46R apply immediately to variable interest entities created after December 31, 2003 and to older entities in the fiscal year beginning after December 31, 2004. Certain of the disclosure requirements, none of which appear to apply to OSUP at this time, are effective in all financial statements issued after December 31, 2003, regardless of when the variable interest entity was established. OSUP is currently evaluating the overall impact of FIN 46R on its consolidated financial statements.

2. CASH AND CASH EQUIVALENTS

OSUP maintains cash balances, which are in excess of those insured by the Federal Depository Insurance Corporation. However, to date, no losses have been experienced.

3. PATIENT ACCOUNTS RECEIVABLE AND CONCENTRATIONS OF CREDIT RISK

OSUP grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. Patient accounts receivable consists of the following:

Gross patient accounts receivable	\$ 55,435,197
Allowances for contractual and administrative adjustments and doubtful accounts	<u>(36,090,972)</u>
Total patient care accounts receivable—net	<u>\$ 19,344,225</u>

The mix of receivables from patients and third-party payors for 2004 is as follows:

Medicare	30 %
Medicaid	13
Commercial/other third-party payors	53
Patient	<u>4</u>
Total	<u>100 %</u>

4. BENEFICIAL INTEREST IN CLINICAL ENTERPRISES ASSET

Included in the composition of temporarily restricted net assets at June 30, 2004, is \$53,747 of beneficial interest in clinical enterprises. Investments are stated at fair value. This investment relates to the start-up costs of OSUP supported by the University through clinical enterprise.

5. PROPERTY, PLANT, FURNITURES AND EQUIPMENT

The composition of property, plant, furnitures and equipment is as follows:

Land and land improvements	\$ 738,299
Buildings	4,352,608
Equipment	4,871,846
Furniture and fixtures	<u>441,651</u>
Total property, plant, furnitures and equipment	10,404,404
Allowances for depreciation and amortization	<u>(5,342,916)</u>
Total property, plant, furnitures and equipment—net	<u>\$ 5,061,488</u>

Depreciation and amortization expense for the year ended June 30, 2004 amounted to \$823,779.

6. NOTE PAYABLE—LINE OF CREDIT AND LONG-TERM DEBT

Through June 30, 2004, OSUP has available lines of credit agreements with a bank that provided for borrowings as follows:

Practice Plan	Line of Credit	Expiration Date
OSUP—Corporate Family Medicine Foundation, LLC	\$ -	
OSU Children’s Pediatrics, LLC		
OSU Emergency Medicine, LLC	1,000,000	June 30, 2005
OSU GYN and OB Consultants, LLC	300,000	September 30, 2004
OSU Internal Medicine, LLC	3,000,000	May 1, 2005
OSU Neuroscience Center, LLC		
OSU Pathology, LLC	1,000,000	July 16, 2004
OSU Physical Medicine and Rehabilitation		
OSU Psychiatry, LLC		
OSU Radiology, LLC		
OSU Surgery, LLC	500,000	June 30, 2005

The agreements require monthly interest payments at the bank’s prime rate less .75% (4.75% at June 30, 2004). The agreements were secured by accounts receivable, equipment and fixtures and were subject to certain restrictive and financial covenants. At June 30, 2004, \$300,000 was outstanding on these lines of credit.

A summary of long-term debt and capital lease obligations at June 30, 2004 follows:

	Balance
Mortgage note payable—due in monthly installments of principal and interest (5.4% fixed rate), due in May 2017	\$ 2,852,558
Notes payable—due in monthly installments of principal and interest (2% fixed rate), due in September 2008	2,825,325
Notes payable—due in monthly installments of principal and interest (4% fixed rate), due in February 2006	2,666,667
Notes payable—due in monthly installments of principal and interest (4% fixed rate), due in December 2005	4,165,078
Line of credit—due in monthly installments of interest (prime less 0.75%) due in September 2004	<u>300,000</u>
Total debt outstanding	12,809,628
Less: current portion	<u>(4,754,143)</u>
Total debt outstanding	<u>\$ 8,055,485</u>

Scheduled principal repayments on long-term debt are as follows:

Year Ending June 30	Long-Term Debt
2005	\$ 4,754,143
2006	2,805,393
2007	790,661
2008	790,661
2009	790,661
Thereafter	<u>2,878,109</u>
Total	<u>\$ 12,809,628</u>

7. CAPITAL LEASE OBLIGATIONS

OSUP has \$110,054 in capital lease obligations that have varying maturity dates through 2007 and carry implicit interest rates ranging from 3.28% to 4.25%. Lease arrangements are being used to provide partial financing for certain movable equipment. Capital asset balances, net of depreciation, as of June 30, 2004 that are financed under capital leases are \$107,430.

The scheduled maturities of these leases as of June 30, 2004 are as follows:

Year Ending June 30	Capital Leases Obligations
2005	\$ 100,907
2006	7,455
2007	<u>1,692</u>
	110,054
Less amount representing interest under capital leases obligations	<u>(4,516)</u>
	<u>\$ 105,538</u>

8. RELATED PARTY TRANSACTIONS AND INTERCOMPANY RECEIVABLES AND PAYABLES

OSUP is a supporting organization of the University.

Related Party Transactions

OSUP assumed assets and their related liabilities each totaling \$3,786,850 in 2004 from related parties. The assets were recorded at cost which approximated fair value.

Due From

University—OSUP received salary recovery money for research provided by its faculty from The Ohio State University Research Foundation (“OSURF”). Effective July 1, 2004 OSURF instituted a policy whereby they will only reimburse departments within the University, not OSUP. As of June 30, 2004, OSUP had been fully reimbursed by OSURF and there are no outstanding balances with OSUP.

The Ohio State University Health System (the "Health System")—OSUP provides staffing, coding support and medical directorships at The Ohio State University Hospital and The Ohio State University Hospital East. Also, the Health System is allocated costs for their share of OSUP administration and information services overhead and billed for physician billing services provided to Health System physicians by OSUP’s billing services. The following are the balances due from the Health System at June 30, 2004:

Practice Plan	Due From Health System
OSUP—Corporate	\$ 326,325
Family Medicine Foundation, LLC	625,367
OSU Emergency Medicine, LLC	13,222
OSU GYN and OB Consultants, LLC	125,101
OSU Internal Medicine, LLC	300
OSU Neuroscience Center, LLC	
OSU Pathology, LLC	264,332
OSU Physical Medicine and Rehabilitation, LLC	
OSU Psychiatry, LLC	234,440
OSU Radiology, LLC	70
OSU Surgery, LLC	<u>242,969</u>
Total	<u>\$ 1,832,126</u>

Due To

Health System—OSUP pays premiums for the USIF (malpractice) and health insurance to the OSU Office of the Treasurer. The following are the balances due to the Health System at June 30, 2004:

Practice Plan	Due To Health System
OSUP—Corporate	\$ 639,072
Family Medicine Foundation, LLC	585,000
OSU Emergency Medicine, LLC	
OSU GYN and OB Consultants, LLC	113,365
OSU Internal Medicine, LLC	246,284
OSU Neuroscience Center, LLC	367,178
OSU Pathology, LLC	
OSU Physical Medicine and Rehabilitation, LLC	4,366
OSU Psychiatry, LLC	32,371
OSU Radiology, LLC	
OSU Surgery, LLC	<u>911,680</u>
Total	<u>\$ 2,899,316</u>

The Ohio State University College of Medicine and Public Health (“COMPH”)—Under the College of Medicine Medical Practice Plan, OSUP is obligated to contribute to the OSU College of Medicine Academic Enrichment Fund, Teaching and Research Fund (“Academic Enrichment”) and Strategic Initiative Fund. Academic Enrichment covers the salaries, benefits and other operating expenses of the Department of Emergency Medicine. Academic Enrichment is paid to the Dean’s office for support of the Academic, Research and Clinical missions of the College. The Strategic Initiative fund is comprised of various funds established by the College to support resident education. All of these funds are paid on a quarterly basis.

Practice Plan	Due To COMPH
OSUP—Corporate	\$ -
Family Medicine Foundation, LLC	116,441
OSU Emergency Medicine, LLC	215,338
OSU GYN and OB Consultants, LLC	244,840
OSU Internal Medicine, LLC	
OSU Neuroscience Center, LLC	702,496
OSU Pathology, LLC	6,404
OSU Physical Medicine and Rehabilitation, LLC	32,371
OSU Psychiatry, LLC	4,366
OSU Radiology, LLC	73,913
OSU Surgery, LLC	<u>335,685</u>
Total	<u>\$1,731,854</u>

9. MEDICAL MALPRACTICE CLAIMS

OSUP purchases professional and general liability insurance to cover medical malpractice claims through The Ohio State University. The University has established a trusted self-insurance fund for professional liability claims. The University’s estimated liability and the related contributions to the University’s self insurance fund for professional liability claims is based upon an independent actuarial determination as of June 30, 2004. Premiums are assessed to OSUP based on the physician’s specialty and the types of surgery performed.

10. RETIREMENT AND HEALTH PLANS

Retirement benefits are provided for the employees of OSUP through a tax-sheltered 403(b) and 401(a) program administered by an insurance company. OSUP is required to make nondiscretionary contributions of no less than 7.5% under the Interim Retirement Plan; however, some LLCs make an additional discretionary contribution of up to 17.5%, for a range of total employer contributions of 7.5% to 25%. Employees are allowed, but not required to make contributions to the 403(b) plan. OSUP's share of the cost of these benefits was \$6,210,610 for the year ended June 30, 2004.

Practice Plan	401(a) Contributions
OSUP—Corporate	\$ 236,229
Family Medicine Foundation, LLC	380,518
OSU Children's Pediatrics, LLC	
OSU Emergency Medicine, LLC	534,022
OSU GYN and OB Consultants, LLC	374,085
OSU Internal Medicine, LLC	2,022,782
OSU Neuroscience Center, LLC	132,134
OSU Pathology, LLC	302,885
OSU Physical Medicine and Rehabilitation, LLC	28,708
OSU Psychiatry, LLC	
OSU Radiology, LLC	811,521
OSU Surgery, LLC	<u>1,144,581</u>
Total	<u>\$5,967,465</u>

OSUP participates in a health insurance plan covering substantially all non-physician employees. All physician employees and certain non-physician employees receive benefits through the health care plan sponsored by the University. Covered services under both plans include medical, dental and vision benefits, life insurance and long-term disability.

11. COMMITMENTS AND CONTINGENCIES

Operating Leases—OSUP leases various equipment and facilities under operating leases expiring at various dates through September 2009. Total rental expense in 2004 for all operating leases was approximately \$1.2 million.

The following is a schedule by year of future minimum lease payments under operating leases as of June 30, 2004, that have initial or remaining lease terms in excess of one year.

Year Ending June 30	Amount
2005	\$ 1,808,763
2006	1,318,360
2007	954,743
2008	737,345
2009	<u>398,243</u>
Total	<u>\$ 5,217,454</u>

Litigation—OSUP is involved in litigation arising in the course of business. After consultation with legal counsel, management does not believe that claims and lawsuits individually or in the aggregate will have a material adverse effect on OSUP’s future financial position or results from operations.

Healthcare Legislation and Regulation—The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements and reimbursement for patient services. Federal and state government activity has continued with respect to investigations and allegations concerning possible violation of billing regulations by healthcare providers. Violations of these regulations could result in the imposition of significant fines and penalties, as well as having a significant effect on reported net income or cash flow.

Management believes that OSUP is in compliance with applicable government laws and regulations. While no regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

12. FUNCTIONAL EXPENSES

OSUP’s physicians provide medical services to residents within its geographical location. Expenses related to providing these services for the year ended June 30, 2004 are as follows:

Health care services	\$ 70,272,002
General and administration	<u>40,959,190</u>
Total	<u><u>\$ 111,231,192</u></u>

13. SUBSEQUENT EVENTS

On July 1, 2004, University Pathology Services, Inc. and Associated Physiatriy of Central Ohio, Inc. completed their final merger into OSUP with their respective LLC being the surviving entity in the merger. Additionally, Eye Physicians and Surgeons, Inc. and Glaucoma Consultants, Inc. began their transition into OSU Eye Physicians and Surgeons, Inc. on July 1, 2004.

* * * * *

SUPPLEMENTAL SCHEDULES

OHIO STATE UNIVERSITY PHYSICIANS INC., AND SUBSIDIARIES

**CONSOLIDATING BALANCE SHEET
JUNE 30, 2004**

ASSETS	OSUP - Corporate	FM	IM	EM	Surgery	Pathology	Radiology	Phys Med	OBGYN	Neurology	Psychiatry	Aggregated	EJE	Total
CURRENT ASSETS:														
Cash and cash equivalents	\$ 1,236,071	\$ 1,448,447	\$ 1,584,307	\$ 366,630	\$ 922,840	\$ 2,435,342	\$ 515,649	\$ -	\$ 1,210,495	\$ 264,284	\$ 53,427	\$ 10,037,492	\$ 3,584	\$ 10,041,076
Accounts receivable—patient care gross		46,823	13,246,361	2,944,789	12,989,298	4,330,109	8,558,592	626,060	6,317,395	6,041,253	334,517	55,435,197		55,435,197
Allowances		(21,550)	(7,544,059)	(2,170,961)	(8,456,196)	(2,942,696)	(5,997,340)	(313,031)	(4,048,916)	(4,462,650)	(133,573)	(36,090,972)		(36,090,972)
Accounts Receivable—patient, ne	-	25,273	5,702,302	773,828	4,533,102	1,387,413	2,561,252	313,029	2,268,479	1,578,603	200,944	19,344,225	-	19,344,225
Accounts receivable other—current	495,784	126,326	361,521	29,335	188,565	62,633	351,021	307,557	56,122	10,322	4,863	1,994,049		1,994,049
Due from affiliate	366,263	625,367	300	13,222	242,969	264,332	70		125,101		234,440	1,872,064	(39,938)	1,832,126
Allowance for uncollectible non-patient receivable	(498,235)											(498,235)		(498,235)
Inventories			135,660									135,660		135,660
Prepaid expenses	80,056	3,515	384,514	4,052	123,515	11,203	1,229		23,232		469	631,785		631,785
Notes receivable						26,307						26,307		26,307
Total current assets:	<u>1,679,939</u>	<u>2,228,928</u>	<u>8,168,604</u>	<u>1,187,067</u>	<u>6,010,991</u>	<u>4,187,230</u>	<u>3,429,221</u>	<u>620,586</u>	<u>3,683,429</u>	<u>1,853,209</u>	<u>494,143</u>	<u>33,543,347</u>	<u>(36,354)</u>	<u>33,506,993</u>
NONCURRENT ASSETS—														
Property, plant, furnitures and equipmen	865,746		8,252,742	138,697	352,878		21,586		708,586	64,169		10,404,404		10,404,404
Accumulated depreciator	(243,488)		(4,273,882)	(115,432)	(163,026)		(2,104)		(480,815)	(64,169)		(5,342,916)		(5,342,916)
Property, plant, furnitures and equipment—ne	622,258	-	3,978,860	23,265	189,852	-	19,482	-	227,771	-	-	5,061,488	-	5,061,488
Due from affiliate—long-term		16,476	116,992	40,897	90,456	30,935	57,232	10,337	30,543	21,100	17,674	432,642	(432,642)	
Restricted beneficial interest in clinical enterprise asse	53,747											53,747		53,747
Other assets	11,911		140,975		(17,657)							135,229		135,229
Total non-current asset:	<u>687,916</u>	<u>16,476</u>	<u>4,236,827</u>	<u>64,162</u>	<u>262,651</u>	<u>30,935</u>	<u>76,714</u>	<u>10,337</u>	<u>258,314</u>	<u>21,100</u>	<u>17,674</u>	<u>5,683,106</u>	<u>(432,642)</u>	<u>5,250,464</u>
TOTAL	<u>\$ 2,367,855</u>	<u>\$ 2,245,404</u>	<u>\$ 12,405,431</u>	<u>\$ 1,251,229</u>	<u>\$ 6,273,642</u>	<u>\$ 4,218,165</u>	<u>\$ 3,505,935</u>	<u>\$ 630,923</u>	<u>\$ 3,941,743</u>	<u>\$ 1,874,309</u>	<u>\$ 511,817</u>	<u>\$ 39,226,453</u>	<u>\$ (468,996)</u>	<u>\$ 38,757,457</u>
LIABILITIES AND NET ASSETS														
CURRENT LIABILITIES:														
Accounts payable	\$ 362,749	\$ 11,899	\$ 1,770,191	\$ 23,437	\$ 236,077	\$ 104,967	\$ 638,140	\$ 191,759	\$ 295,782	\$ 798,656	\$ 49,097	\$ 4,482,754	\$ 2,200	\$ 4,484,954
Accrued expense:	160,000	19,158	29,014	119,500	919,630	21,806	83,666	52,991	83,666	44,275		1,450,040		1,450,040
Accrued salaries and wage:	290,182	677,030	3,046,984	378,919	289,580	445,893	1,282,864	44,171	520,818	17,352	50,206	7,043,999		7,043,999
Due to affiliates—current portio	9,719	701,441	246,284	215,338	337,388	6,404	73,913	36,737	358,205	1,029,767	308,894	3,324,090	(38,554)	3,285,536
Notes payable and capital leases—current portio			315,050		2,640,000				1,900,000			4,855,050		4,855,050
Other postretirement benefits obligatio	18,603	50,087		700,817	591,477		567,888	9,106	333,902	35,511		2,307,391		2,307,391
Total current liabilities:	<u>841,253</u>	<u>1,459,615</u>	<u>5,407,523</u>	<u>1,438,011</u>	<u>5,014,152</u>	<u>579,070</u>	<u>2,562,805</u>	<u>334,764</u>	<u>3,492,373</u>	<u>1,925,561</u>	<u>408,197</u>	<u>23,463,324</u>	<u>(36,354)</u>	<u>23,426,970</u>
LONG-TERM LIABILITIES:														
Notes payable and capital leases—less current portio			5,473,246		1,524,719				1,066,667			8,064,632		8,064,632
Due to affiliates—long-term	736,735				911,680					129,861		1,778,276	(432,642)	1,345,634
Total long-term liability:	<u>736,735</u>	<u>-</u>	<u>5,473,246</u>	<u>-</u>	<u>2,436,399</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,066,667</u>	<u>129,861</u>	<u>-</u>	<u>9,842,908</u>	<u>(432,642)</u>	<u>9,410,266</u>
NET ASSETS:														
Unrestricted	789,867	686,207	1,524,662	(186,782)	(1,176,909)	3,639,095	943,130	296,159	(617,297)	(181,113)	103,620	5,820,639		5,820,639
Temporarily restricted net asset		99,582										99,582		99,582
Total net assets:	<u>789,867</u>	<u>785,789</u>	<u>1,524,662</u>	<u>(186,782)</u>	<u>(1,176,909)</u>	<u>3,639,095</u>	<u>943,130</u>	<u>296,159</u>	<u>(617,297)</u>	<u>(181,113)</u>	<u>103,620</u>	<u>5,920,221</u>	<u>-</u>	<u>5,920,221</u>
TOTAL	<u>\$ 2,367,855</u>	<u>\$ 2,245,404</u>	<u>\$ 12,405,431</u>	<u>\$ 1,251,229</u>	<u>\$ 6,273,642</u>	<u>\$ 4,218,165</u>	<u>\$ 3,505,935</u>	<u>\$ 630,923</u>	<u>\$ 3,941,743</u>	<u>\$ 1,874,309</u>	<u>\$ 511,817</u>	<u>\$ 39,226,453</u>	<u>\$ (468,996)</u>	<u>\$ 38,757,457</u>

OHIO STATE UNIVERSITY PHYSICIANS INC., AND SUBSIDIARIES

**CONSOLIDATING STATEMENT OF OPERATIONS
YEAR ENDED JUNE 30, 2004**

	OSUP	FM	IM	EM	Surgery	Pathology	Radiology	Phys Med	OBGYN	Neurology	Psychiatry	Aggregated	EJE	Total
PATIENT CARE REVENUES:														
Gross patient care revenue	\$ -	\$ 110,374	\$ 92,906,308	\$ 13,344,315	\$ 31,098,177	\$ 15,987,531	\$ 27,793,232	\$2,528,576	\$ 12,825,109	\$ 7,339,389	\$ 601,723	\$ 204,534,734	\$ -	\$ 204,534,734
Provision for contractual and administrative		(47,051)	(44,619,280)	(5,858,240)	(17,941,550)	(10,472,738)	(18,560,018)	(1,213,518)	(6,518,206)	(4,605,019)	(170,730)	(110,006,350)		(110,006,350)
Net patient care revenue:	-	63,323	48,287,028	7,486,075	13,156,627	5,514,793	9,233,214	1,315,058	6,306,903	2,734,370	430,993	94,528,384		94,528,384
CONTRACT SERVICES	2,162,160	8,484,413	447,127	2,102,212	1,923,437	1,605,050	113,400	58,193	1,419,924	17,333	463,366	18,796,615	(42,417)	18,754,198
OTHER SERVICES	2,985,194	153,431	1,281,776	274,921	722,964	248,501		344,802	280,122	34,781	22,324	6,348,816	(1,182,415)	5,166,401
TOTAL OPERATING REVENUES	<u>5,147,354</u>	<u>8,701,167</u>	<u>50,015,931</u>	<u>9,863,208</u>	<u>15,803,028</u>	<u>7,368,344</u>	<u>9,346,614</u>	<u>1,718,053</u>	<u>8,006,949</u>	<u>2,786,484</u>	<u>916,683</u>	<u>119,673,815</u>	<u>(1,224,832)</u>	<u>118,448,983</u>
OPERATING EXPENSES:														
Provider salaries	21,000	4,115,573	20,103,740	4,263,933	4,715,448	1,454,086	4,885,123	374,589	1,536,912	602,656	311,677	42,384,737		42,384,737
Employees salaries and wage:	2,122,615	1,725,161	8,598,873	456,947	2,213,805	246,210	456,821	130,277	996,618	560,831	141,197	17,649,355		17,649,355
Provision for bad debt:	282,873		3,335,862	2,370,963	1,334,450	466,339	831,648	65,742	439,579	306,052	16,927	9,450,435		9,450,435
Provider fringe benefit	3,491	624,284	2,450,835	691,109	1,168,419	302,568	1,060,557	58,144	423,443	172,658	68,190	7,023,698		7,023,698
Professional liability insurance		711,762	1,512,991	399,643	2,116,264		114,761	52,991	248,191	145,660	31,926	5,334,189		5,334,189
Employee fringe benefit	557,847	552,127	2,649,098	121,018	709,061	107,245	150,843	40,410	316,012	164,939	39,687	5,408,287		5,408,287
Medical supplies			4,824,000		82,485	9,021		1,002	54,746	30,983		5,002,237		5,002,237
Office and administrative other	864,096	100,311	1,465,966	93,333	604,691	112,755	171,712	15,147	169,584	91,881	16,493	3,705,969		3,705,969
Purchased services and management fee	900,644	196,370	302,509	129,658	381,887	407,711	78,801	128,479	491,882	147,305	99,442	3,264,688	(5,610)	3,259,078
Academic enrichment and strategic initiative		141,087	910,795	699,801	362,497	156,404	450,778	20,939	127,793	66,072	9,191	2,945,357		2,945,357
Clinical drugs and medication:								446,111	1,297,505	670,034		2,413,650		2,413,650
Rent and other occupancy cost	191,457		1,004,535	42,869	237,901	13,423	34,853	2,866	281,450	77,467	30,410	1,917,231		1,917,231
Other provider related expense		48,099	361,478	320,198	239,553	73,483	80,279	25,346	91,569	34,645	24,561	1,299,211		1,299,211
Supplies	88,893	372	379,328	55,906	227,287	48,558	9,681	50,088	50,587	94,682	15,704	1,021,086		1,021,086
Depreciation and amortization	142,090		636,860	4,137	20,117		2,104		18,471			823,779		823,779
Other clinical related expense			85,136		88,242	286,563			235,892	2,201		698,034		698,034
Other office and administrative billing	351,265	3,392	349,468	53,186	105,932	40,314	98,071	10,065	70,821	25,065	21,428	1,129,007	(687,260)	441,747
Interest expense			227,549	1,334	94,978		246		51,872	496		376,475		376,475
Insurance	25,064	142	31,675		13,864	1,819						72,564		72,564
Taxes	50								2,221			2,271		2,271
Allocated overhead		43,320	237,136	35,054	87,623	26,335	35,567	10,035	31,265	23,525	3,904	533,764	(531,962)	1,802
TOTAL OPERATING EXPENSE	<u>5,551,385</u>	<u>8,262,000</u>	<u>49,467,834</u>	<u>9,739,089</u>	<u>14,804,504</u>	<u>3,752,834</u>	<u>8,461,845</u>	<u>1,432,231</u>	<u>6,936,413</u>	<u>3,217,152</u>	<u>830,737</u>	<u>112,456,024</u>	<u>(1,224,832)</u>	<u>111,231,192</u>
OPERATING INCOME (LOSS)	<u>(404,031)</u>	<u>439,167</u>	<u>548,097</u>	<u>124,119</u>	<u>998,524</u>	<u>3,615,510</u>	<u>884,769</u>	<u>285,822</u>	<u>1,070,536</u>	<u>(430,668)</u>	<u>85,946</u>	<u>7,217,791</u>	<u>-</u>	<u>7,217,791</u>
NONOPERATING INCOME (EXPENSE):														
Other nonoperating income	4,330	6,179	366,987	(3,433)	(200,635)	(7,350)	(100)		(5,991)	52,752		212,739		212,739
Investment income (loss)	6,650											6,650		6,650
Gain (loss) sale of asset			625									625		625
TOTAL NONOPERATING INCOME (LOSS)	<u>10,980</u>	<u>6,179</u>	<u>367,612</u>	<u>(3,433)</u>	<u>(200,635)</u>	<u>(7,350)</u>	<u>(100)</u>	<u>-</u>	<u>(5,991)</u>	<u>52,752</u>	<u>-</u>	<u>220,014</u>	<u>-</u>	<u>220,014</u>
INCREASE (DECREASE) IN NET ASSETS	<u>\$ (393,051)</u>	<u>\$ 445,346</u>	<u>\$ 915,709</u>	<u>\$ 120,686</u>	<u>\$ 797,889</u>	<u>\$ 3,608,160</u>	<u>\$ 884,669</u>	<u>\$ 285,822</u>	<u>\$ 1,064,545</u>	<u>\$ (377,916)</u>	<u>\$ 85,946</u>	<u>\$ 7,437,805</u>	<u>\$ -</u>	<u>\$ 7,437,805</u>

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND COMPLIANCE AND OTHER MATTERS BASED UPON THE AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Board Of Directors
Ohio State University Physicians, Inc.
Columbus, Ohio

We have audited the financial statements of Ohio State University Physicians, Inc. ("OSUP"), as of and for the year ended June 30, 2004, and have issued our report thereon dated December 10, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered OSUP'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 an opinion 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 caused by error or fraud 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. However, we noted other matters involving the internal control over financial reporting that we have reported to the management of OSUP in a separate letter dated December 10, 2004.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether OSUP's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Directors, management of OSUP and the Auditor of the State of Ohio and is not intended to be and should not be used by anyone other than these specified parties.



December 10, 2004



**Auditor of State
Betty Montgomery**

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OHIO STATE UNIVERSITY PHYSICIANS, INC.

FRANKLIN 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
FEBRUARY 10, 2005**