

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

*Consolidated Financial Statements as of
and for the Years Ended June 30, 2005 and
2004, Supplemental Consolidating Schedules
as of and for the Year Ended June 30, 2005,
and Independent Auditors' Report*



**Auditor of State
Betty Montgomery**

Board of Directors
Ohio State University Physicians, Inc. and Subsidiaries
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. and Subsidiaries, Franklin County, prepared by Deloitte & Touche LLP, for the audit period July 1, 2004 through June 30, 2005. 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. and Subsidiaries is responsible for compliance with these laws and regulations.

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

BETTY MONTGOMERY
Auditor of State

March 1, 2006

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OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Ohio State University Physicians, Inc.:

We have audited the accompanying consolidated balance sheets of Ohio State University Physicians, Inc. (an Ohio not-for-profit corporation) and subsidiaries ("OSUP") as of June 30, 2005 and 2004, and the related consolidated statements of activities and changes in net assets and cash flows for the years 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 audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of OSUP's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements, 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, such consolidated financial statements referred to above present fairly, in all material respects, the financial position of OSUP as of June 30, 2005 and 2004, and the results of their operations, changes in net assets, and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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 17 and 18 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 21, 2005, on our consideration of OSUP's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.



December 21, 2005

OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS AS OF JUNE 30, 2005 and 2004

	2005	2004
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 13,446,575	\$ 10,041,076
Accounts receivable—patient care, net of allowance (\$37,779,638 in 2005 and \$36,090,972 in 2004)	22,502,999	19,344,225
Accounts receivable other—current, net of allowance (\$15,330 in 2005 and \$498,235 in 2004)	978,427	1,495,814
Due from affiliate	2,690,404	1,832,126
Inventories	74,880	135,660
Prepaid expenses	692,887	631,785
Notes receivable	43,160	26,307
	<u>40,429,332</u>	<u>33,506,993</u>
NONCURRENT ASSETS:		
Property, plant, furnitures, and equipment, net of accumulated depreciation of (\$6,453,516 in 2005 and \$5,342,916 in 2004)	6,535,733	5,061,488
Restricted beneficial interest in clinical enterprise assets		53,747
Other assets	1,032,360	135,229
	<u>7,568,093</u>	<u>5,250,464</u>
TOTAL	<u>\$ 47,997,425</u>	<u>\$ 38,757,457</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Accounts payable	\$ 3,199,598	\$ 4,484,954
Accrued expenses	995,926	1,450,040
Accrued salaries and wages	7,725,546	7,043,999
Due to affiliates—current portion	5,522,276	3,285,536
Notes payable and capital leases—current portion	4,481,652	4,855,050
Other postretirement benefits obligation	1,199,747	2,307,391
Other current liabilities	2,535,251	
	<u>25,659,996</u>	<u>23,426,970</u>
LONG-TERM LIABILITIES:		
Notes payable and capital leases—less current portion	5,999,653	8,064,632
Due to affiliates—long-term	4,641,028	1,345,634
Other long-term liabilities	1,174,732	
	<u>11,815,413</u>	<u>9,410,266</u>
NET ASSETS:		
Unrestricted	10,172,294	5,820,639
Temporarily restricted net assets	349,722	99,582
	<u>10,522,016</u>	<u>5,920,221</u>
TOTAL	<u>\$ 47,997,425</u>	<u>\$ 38,757,457</u>

See notes to consolidated financial statements.

OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	2005		2004	
	Unrestricted Net Assets	Temporarily Restricted Net Assets	Unrestricted Net Assets	Temporarily Restricted Net Assets
OPERATING REVENUES:				
Net patient care revenues (net of charity care of \$1,527,985 in 2005 and \$1,208,402 in 2004)	\$ 152,542,255	\$ -	\$ 94,528,384	\$ -
Contract services	30,686,868		18,754,198	
Other services	<u>5,642,425</u>	<u>250,140</u>	<u>5,066,819</u>	<u>99,582</u>
Total operating revenues	<u>188,871,548</u>	<u>250,140</u>	<u>118,349,401</u>	<u>99,582</u>
OPERATING EXPENSES:				
Provider salaries	68,787,484		42,384,737	
Employees salaries and wages	30,011,941		17,649,355	
Provision for bad debts	17,529,058		9,450,435	
Provider fringe benefits	11,892,002		7,023,698	
Professional liability insurance	9,112,417		5,334,189	
Employee fringe benefits	9,298,727		5,408,287	
Medical supplies	1,033,562		178,237	
Office and administrative other	6,763,154		3,710,042	
Purchased services and management fees	5,745,762		3,259,078	
Academic enrichment and strategic initiative	5,041,341		2,945,357	
Clinical drugs and medications	10,945,032		7,237,650	
Rent and other occupancy costs	2,750,569		1,917,231	
Other provider related expenses	1,127,356		1,299,211	
Supplies	2,223,370		1,021,086	
Depreciation and amortization	1,144,054		823,779	
Other clinical related expenses	528,122		698,034	
Office and administrative billing	591,174		441,747	
Interest expense	524,622		376,475	
Insurance	<u>128,989</u>		<u>72,564</u>	
Total operating expenses	<u>185,178,736</u>	<u>-</u>	<u>111,231,192</u>	<u>-</u>
OPERATING INCOME	<u>3,692,812</u>	<u>250,140</u>	<u>7,118,209</u>	<u>99,582</u>
NONOPERATING INCOME:				
Other nonoperating—net	538,028		212,739	
Investment income	117,948		6,650	
Gain on sale of assets	<u>2,867</u>		<u>625</u>	
Total non-operating income	<u>658,843</u>	<u>-</u>	<u>220,014</u>	<u>-</u>
INCREASE IN NET ASSETS	4,351,655	250,140	7,338,223	99,582
NET ASSETS—Beginning of year	<u>5,820,639</u>	<u>99,582</u>	<u>(1,517,584)</u>	
NET ASSETS—End of year	<u>\$ 10,172,294</u>	<u>\$349,722</u>	<u>\$ 5,820,639</u>	<u>\$99,582</u>

See notes to consolidated financial statements.

OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	\$ 4,601,795	\$ 7,437,805
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	1,144,054	823,779
Gain on sale of assets	(2,867)	(625)
(Increase) decrease in:		
Accounts receivable—patient care—net	(3,158,774)	(15,592,661)
Accounts receivable—other current—net	517,387	(1,994,049)
Due from affiliates	(858,278)	(999,342)
Note receivable—short-term	(16,853)	(26,307)
Inventories	60,780	(93,613)
Prepaid expenses	(61,102)	173,292
Other assets	(897,131)	(128,611)
Accounts payable	(1,285,356)	(548,104)
Due to affiliates	5,532,134	2,735,129
Accrued salaries and wages	681,547	3,956,933
Other post-retirement benefit obligation	(1,107,644)	2,155,035
Other accrued liabilities	(454,114)	1,351,886
Other liabilities	<u>3,734,870</u>	<u> </u>
Net cash used in operating activities	<u>8,430,448</u>	<u>(749,453)</u>
CASH FLOWS FROM INVESTING ACTIVITIES—		
Purchase of property, plant, furnitures, and equipment	<u>(2,586,572)</u>	<u>(2,266,317)</u>
Cash used in investing activities	<u>(2,586,572)</u>	<u>(2,266,317)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from notes payable	11,195,112	12,398,814
Payments on notes payable	(13,633,489)	(2,826,603)
Beneficial interest in clinical enterprise assets	<u> </u>	<u>202,423</u>
Net cash provided by financing activities	<u>(2,438,377)</u>	<u>9,774,634</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	3,405,499	6,758,864
CASH AND CASH EQUIVALENTS—Beginning of year	<u>10,041,076</u>	<u>3,282,212</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 13,446,575</u>	<u>\$ 10,041,076</u>
SUPPLEMENTAL DISCLOSURES OF CASH INFORMATION:		
Cash paid for interest	<u>\$ 518,375</u>	<u>\$ 355,304</u>
Property additions under capital lease agreements	<u>\$ 704,201</u>	<u>\$ 205,945</u>
Transfers of assets:		
Fair value of assets assumed	<u>\$ 1,898,810</u>	<u>\$ 3,786,850</u>
Liabilities assumed	<u>\$ (1,873,923)</u>	<u>\$ 3,786,850</u>

See notes to consolidated financial statements.

OHIO STATE UNIVERSITY PHYSICIANS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED JUNE 30, 2005 AND 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 16 limited liability companies (“LLCs”). As of June 30, 2005 only 12 of the limited liability companies are active and included in the accompanying supplemental consolidating schedules. Four of the limited liability companies (Anesthesiology, Orthopedics, Otolaryngology, and Radiation Medicine) have been created but have no business activity through June 30, 2005.

The following table outlines the reporting of OSUP’s financial statements as of June 30, 2005 and 2004:

Practice Plan	2005	2004
Family Medicine Foundation, LLC (“FM”)	X	X
OSU Anesthesiology, LLC (“Anesthesiology”)		
OSU Children’s Pediatrics, LLC	X	X
OSU Emergency Medicine, LLC (“EM”)	X	X
OSU Eye Physicians and Surgeons, LLC (“Eye”)	X	
OSU GYN and OB Consultants, LLC (“OBGYN”)	X	X
OSU Internal Medicine, LLC (“IM”)	X	X
OSU Neuroscience Center, LLC (“Neurology”)	X	X
OSU Orthopedics, LLC (“Orthopedics”)		
OSU Otolaryngology-Head and Neck Surgery, LLC (“Otolaryngology”)		
OSU Pathology, LLC (“Pathology”)	X	X
OSU Physical Medicine and Rehabilitation (“Phys Med”)	X	X
OSU Psychiatry, LLC (“Psychiatry”)	X	X
OSU Radiation Medicine, LLC (“Radiation Medicine”)		
OSU Radiology, LLC (“Radiology”)	X	X
OSU Surgery, LLC (“Surgery”)	X	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 include 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, 2005 and 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 nonoperating 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, 2005, 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, 2005 and 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, 2005 and 2004, the balance of temporarily restricted net assets is \$349,722 and \$99,582, respectively, and is available for health care services and physician’s expenses.

Federal Income Taxes—OSUP 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.

Reclassifications—Certain prior year amounts have been reclassified to conform to the current year presentation.

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 at June 30:

	2005	2004
Gross patient accounts receivable	\$ 60,282,637	\$ 55,435,197
Allowances for contractual and administrative adjustments and doubtful accounts	<u>(37,779,638)</u>	<u>(36,090,972)</u>
Total patient care accounts receivable—net	<u>\$ 22,502,999</u>	<u>\$ 19,344,225</u>

The mix of receivables from patients and third-party payors for 2005 and 2004 is as follows:

	2005	2004
Medicare	28 %	30 %
Medicaid	14	13
Commercial/other third-party payors	53	53
Patient	<u>5</u>	<u>4</u>
Total	<u>100 %</u>	<u>100 %</u>

4. BENEFICIAL INTEREST IN CLINICAL ENTERPRISES ASSET

Included in the composition of temporarily restricted net assets at June 30, 2004, was \$53,747, of beneficial interest in Clinical Enterprise. 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 as of June 30, 2005 and 2004, is as follows:

	2005	2004
Land and land improvements	\$ 923,159	\$ 738,299
Buildings	4,460,085	4,352,608
Equipment	6,400,163	4,871,846
Furniture and fixtures	1,199,835	441,651
CIP	6,007	
Total property, plant, furnitures, and equipment	<u>12,989,249</u>	<u>10,404,404</u>
Allowances for depreciation and amortization	<u>(6,453,516)</u>	<u>(5,342,916)</u>
Total property, plant, furnitures, and equipment—net	<u>\$ 6,535,733</u>	<u>\$ 5,061,488</u>

Depreciation and amortization expense for the years ended June 30, 2005 and 2004 amounted to \$1,144,054 and \$823,779, respectively.

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

Through June 30, 2005, 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	\$ 1,000,000	6/30/2006
OSU Children's Pediatrics, LLC		
OSU Emergency Medicine, LLC	1,000,000	10/31/2005
OSU Eye Physicians & Surgeons, LLC	800,000	6/30/2006
OSU GYN and OB Consultants, LLC	500,000	6/30/2006
OSU Internal Medicine, LLC	3,000,000	5/1/2006
OSU Neuroscience Center, LLC		
OSU Pathology, LLC	1,000,000	1/31/2006
OSU Physical Medicine and Rehabilitation	100,000	1/31/2006
OSU Psychiatry, LLC	50,000	1/31/2006
OSU Radiology, LLC	100,000	8/2/2006
OSU Surgery, LLC	1,000,000	12/31/2005

The agreements require monthly interest payments at the bank's prime rate less .75% (6.25% at June 30, 2005 and 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, 2005 and 2004, \$470,984 and \$300,000, respectively, was outstanding on these lines of credit.

A summary of long-term debt and capital lease obligations at June 30, 2005 and 2004, are as follows:

	2005	2004
Mortgage note payable—due in monthly installments of principal and interest (5.4% fixed rate), due in May 2008	\$ 2,647,920	\$ 2,852,558
Notes payable—due in monthly installments of principal and interest (2% fixed rate), due in September 2008	2,725,325	2,825,325
Notes payable—due in monthly installments of principal and interest (prime less 0.25% rate, due in February 2006	1,066,667	2,666,667
Notes payable—due in monthly installments of principal and interest (prime less 0.25% rate), due in December 2005	1,447,824	4,165,078
Notes payable—due in monthly installments of principal and interest (prime less .025% rate), due in June 2007	920,000	
Notes payable—due in monthly installments of principal and interest (4.53% fixed rate), due in November 2010	468,122	
Line of credit—due in monthly installments of interest (prime less 0.75%), due in October 2005	<u>470,984</u>	<u>300,000</u>
Total debt outstanding	9,746,842	12,809,628
Less current portion	<u>(4,317,140)</u>	<u>(4,754,143)</u>
Total debt outstanding	<u>\$ 5,429,702</u>	<u>\$ 8,055,485</u>

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

Year Ending June 30	Long-Term Debt
2006	\$4,317,140
2007	4,532,970
2008	328,918
2009	102,111
2010	<u>465,703</u>
Total	<u>\$9,746,842</u>

7. CAPITAL LEASE OBLIGATIONS

OSUP has \$652,045 in capital lease obligations that have varying maturity dates through 2007 and carry implicit interest rates ranging from 3.3% to 9.0%. Lease arrangements are being used to provide partial financing for certain movable equipment. Capital asset balances, net of depreciation, as of June 30, 2005 and 2004 that are financed under capital leases are \$727,125 and \$107,430, respectively.

The scheduled maturities of these leases as of June 30, 2005 are as follows:

Year Ending June 30	Capital Leases Obligations
2006	\$ 164,512
2007	177,116
2008	168,334
2009	178,212
2010	<u>46,289</u>
	734,463
Less amount representing interest under capital leases obligations	<u>(82,418)</u>
Total	<u>\$ 652,045</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 totaling \$1,898,810 and \$1,873,923, respectively, in 2005 from related parties. The assets and liabilities 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, 2005 and 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, 2005:

Practice Plan	Due From Health System
OSUP—Corporate	\$ 191,231
Family Medicine Foundation, LLC	248,574
OSU Emergency Medicine, LLC	39,380
OSU GYN and OB Consultants, LLC	51,639
OSU Internal Medicine, LLC	
OSU Neuroscience Center, LLC	
OSU Pathology, LLC	94,844
OSU Physical Medicine and Rehabilitation, LLC	
OSU Psychiatry, LLC	200,470
OSU Radiology, LLC	
OSU Surgery, LLC	<u>53,171</u>
 Total	 <u>\$ 879,309</u>

The Ohio State University and The Ohio State University College of Medicine and Public Health ("COMPH")—OSUP provides staffing, coding support, and medical directorships at The Ohio State University. The following are the balances due from the COMPH at June 30, 2005:

Practice Plan	Due From COMPH
OSUP—Corporate	\$ 169,555
Family Medicine Foundation, LLC	
OSU Emergency Medicine, LLC	
OSU GYN and OB Consultants, LLC	23,390
OSU Internal Medicine, LLC	132,713
OSU Neuroscience Center, LLC	
OSU Pathology, LLC	
OSU Physical Medicine and Rehabilitation, LLC	
OSU Psychiatry, LLC	
OSU Radiology, LLC	58,053
OSU Surgery, LLC	<u>1,427,384</u>
 Total	 <u>\$1,811,095</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, 2005:

Practice Plan	Due To Health System
OSUP—Corporate	\$ 241,772
Family Medicine Foundation, LLC	738,670
OSU Emergency Medicine, LLC	
OSU Eye Physicians & Surgeons, LLC	
OSU GYN and OB Consultants, LLC	536,205
OSU Internal Medicine, LLC	168,501
OSU Neuroscience Center, LLC	57,032
OSU Pathology, LLC	
OSU Physical Medicine and Rehabilitation, LLC	180,417
OSU Psychiatry, LLC	
OSU Radiology, LLC	
OSU Surgery, LLC	<u>4,456,141</u>
Total	<u>\$6,378,738</u>

The Ohio State University and 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	\$ 910
Family Medicine Foundation, LLC	45,167
OSU Emergency Medicine, LLC	358,134
OSU Eye Physicians & Surgeons, LLC	323,405
OSU GYN and OB Consultants, LLC	977,638
OSU Internal Medicine, LLC	85,563
OSU Neuroscience Center, LLC	1,155,376
OSU Pathology, LLC	27,563
OSU Physical Medicine and Rehabilitation, LLC	88,422
OSU Psychiatry, LLC	303,598
OSU Radiology, LLC	219,710
OSU Surgery, LLC	<u>199,080</u>
Total	<u>\$3,784,566</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 trustee 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, 2005. Premiums are assessed to OSUP based on the physician's specialty and the types of surgery performed. Premiums paid for the year ended June 30, 2005 were \$9,327,507.

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 \$9,943,268 and \$6,210,610 for the years ended June 30, 2005 and 2004, respectively.

Practice Plan	401(a) Contributions	
	2005	2004
OSUP—Corporate	\$ 214,955	\$ 236,229
Family Medicine Foundation, LLC	468,568	380,518
OSU Children's Pediatrics, LLC		
OSU Emergency Medicine, LLC	520,964	534,022
OSU Eye Physicians & Surgeons, LLC	32,720	
OSU GYN and OB Consultants, LLC	1,024,017	374,085
OSU Internal Medicine, LLC	2,230,655	2,022,782
OSU Neuroscience Center, LLC	220,054	132,134
OSU Pathology, LLC	1,228,679	302,885
OSU Physical Medicine and Rehabilitation, LLC	96,082	28,708
OSU Psychiatry, LLC	6,495	
OSU Radiology, LLC	1,581,955	811,521
OSU Surgery, LLC	2,318,124	1,144,581
Total	<u>\$9,943,268</u>	<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 2005 and 2004 for all operating leases was approximately \$2.1 million and \$1.2 million, respectively.

The following is a schedule by year of future minimum lease payments under operating leases as of June 30, 2005, that have initial or remaining lease terms in excess of one year.

Year Ending June 30	Amount
2006	\$1,735,181
2007	1,240,447
2008	916,748
2009	435,624
2010	91,096
Thereafter	<u>530,740</u>
 Total	 <u>\$4,949,836</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 flows.

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 years ended June 30, 2005 and 2004, are as follows:

	2005	2004
Health care services	\$ 113,842,616	\$ 70,272,002
General and administration	<u>71,336,120</u>	<u>40,959,190</u>
Total	<u>\$ 185,178,736</u>	<u>\$ 111,231,192</u>

13. SUBSEQUENT EVENTS

On July 1, 2005, OSU Radiation Medicine, LLC became a separate entity from OSU Radiology, LLC. On November 1, 2005, OSU Otolaryngology—Head & Neck Surgeons, LLC joined OSUP.

* * * * *

SUPPLEMENTAL CONSOLIDATING SCHEDULES

OHIO STATE UNIVERSITY PHYSICIANS INC., AND SUBSIDIARIES

**CONSOLIDATING BALANCE SHEET
AS OF JUNE 30, 2005**

ASSETS	OSUP—Corporate	FM	IM	EM	Eye	Surgery	Pathology	Radiology	Phys Med	OBGYN	Neurology	Psychiatry	Aggregated	EJE	Total
CURRENT ASSETS:															
Cash and cash equivalents	\$1,837,082	\$1,804,001	\$ 2,231,424	\$ 29,343	\$ 424,381	\$ 789,678	\$ 4,316,129	\$ 419,594	\$ 49,772	\$ 568,457	\$ 847,411	\$ 116,684	\$ 13,433,956	\$ 12,619	\$ 13,446,575
Accounts receivable—patient:															
Accounts receivable—patient care gross		157,503	16,455,028	4,219,559	1,438,503	11,201,974	4,635,400	10,283,365	1,012,549	7,641,071	2,707,047	530,638	60,282,637		60,282,637
Allowances		(67,104)	(9,093,606)	(2,934,843)	(769,066)	(7,117,167)	(3,152,645)	(7,461,826)	(529,656)	(4,516,070)	(1,841,137)	(296,518)	(37,779,638)		(37,779,638)
Accounts receivable—patient—net	-	90,399	7,361,422	1,284,716	669,437	4,084,807	1,482,755	2,821,539	482,893	3,125,001	865,910	234,120	22,502,999	-	22,502,999
Accounts receivable other—current	96,239	9,792	75,806	67,399	67,617		33,529	271,697	191,857	159,454	8,584	11,783	993,757		993,757
Due from affiliate	521,328	203,338	133,411	39,380	9,897	1,480,555	128,456	58,053		75,029	960	200,470	2,850,877	(160,473)	2,690,404
Allowance for uncollectible non-patient receivables							(15,330)						(15,330)		(15,330)
Inventories			74,880										74,880		74,880
Prepaid expenses	88,688		422,151	8,945	1,785	114,615	14,153	25,624		16,926			692,887		692,887
Notes receivable							43,160						43,160		43,160
Total current assets	2,543,337	2,107,530	10,299,094	1,429,783	1,173,117	6,469,655	6,002,852	3,596,507	724,522	3,944,867	1,722,865	563,057	40,577,186	(147,854)	40,429,332
NONCURRENT ASSETS:															
Property, plant, furnitures, and equipment:															
Property, plant, furnitures, and equipment	997,888		9,487,848	163,390	1,091,988	288,812	9,393	29,551	131,833	724,377	64,169		12,989,249		12,989,249
Accumulated depreciation	(428,418)		(5,061,404)	(129,604)	(30,333)	(103,325)	(157)	(8,400)	(114,314)	(513,392)	(64,169)		(6,453,516)		(6,453,516)
Property, plant, furnitures, and equipment—net	569,470	-	4,426,444	33,786	1,061,655	185,487	9,236	21,151	17,519	210,985	-	-	6,535,733	-	6,535,733
Due from affiliate—long-term															
Restricted beneficial interest in clinical enterprise assets															
Other assets	100,411	777,881	116,991	40,897		294,644	50,760	57,230	10,337	30,543	21,100	17,674	1,518,468	(486,108)	1,032,360
Total noncurrent assets	669,881	777,881	4,543,435	74,683	1,061,655	480,131	59,996	78,381	27,856	241,528	21,100	17,674	8,054,201	(486,108)	7,568,093
TOTAL	\$3,213,218	\$2,885,411	\$14,842,529	\$ 1,504,466	\$ 2,234,772	\$ 6,949,786	\$ 6,062,848	\$ 3,674,888	\$ 752,378	\$ 4,186,395	\$ 1,743,965	\$ 580,731	\$ 48,631,387	\$ (633,962)	\$ 47,997,425
LIABILITIES AND NET ASSETS															
CURRENT LIABILITIES:															
Accounts payable	\$ 111,701	\$ 72,066	\$ 1,425,994	\$ 27,701	\$ 20,496	\$ 481,947	\$ 148,832	\$ 24,126	\$ 275,959	\$ 128,370	\$ 453,508	\$ 28,898	\$ 3,199,598	\$ -	\$ 3,199,598
Accrued expenses	199,999	5,980	19,428	25	17,197	342,196	13,663			368,240	29,198		995,926		995,926
Accrued salaries and wages	261,764	876,935	4,428,155	435,957	22,302	305,753	1,103,765	83,677	74,927	63,719	21,292	47,300	7,725,546		7,725,546
Due to affiliates—current portion	4,330	836,411	168,916	358,439	511,339	200,722	61,175	219,762	268,865	1,514,298	1,212,820	313,053	5,670,130	(147,854)	5,522,276
Notes payable and capital leases—current portion			1,289,780	470,984	206,397	1,447,824				1,066,667			4,481,652		4,481,652
Other postretirement benefits obligation	20,272	12,230	178,667	255,911	5,774	7,661		118,114		599,118	2,000		1,199,747		1,199,747
Other current liabilities	240,395		362,167	103,227	186,099	625,952	130,758	302,408	32,385	350,356	195,994	5,510	2,535,251		2,535,251
Total current liabilities	838,461	1,803,622	7,873,107	1,652,244	969,604	3,412,055	1,458,193	748,087	652,136	4,090,768	1,914,812	394,761	25,807,850	(147,854)	25,659,996
LONG-TERM LIABILITIES:															
Notes payable and capital leases—less current portion			4,817,927		1,181,726								5,999,653		5,999,653
Due to affiliates—long-term	670,995					4,456,141							5,127,136	(486,108)	4,641,028
Other long-term liabilities	65,741			6,610				1,102,381					1,174,732		1,174,732
Total long-term liabilities	736,736	-	4,817,927	6,610	1,181,726	4,456,141	-	1,102,381	-	-	-	-	12,301,521	(486,108)	11,815,413
NET ASSETS:															
Unrestricted	1,638,021	732,067	2,151,495	(154,388)	83,442	(918,410)	4,604,655	1,824,420	100,242	95,627	(170,847)	185,970	10,172,294		10,172,294
Temporarily restricted net assets		349,722											349,722		349,722
Total net assets	1,638,021	1,081,789	2,151,495	(154,388)	83,442	(918,410)	4,604,655	1,824,420	100,242	95,627	(170,847)	185,970	10,522,016	-	10,522,016
TOTAL	\$3,213,218	\$2,885,411	\$14,842,529	\$ 1,504,466	\$ 2,234,772	\$ 6,949,786	\$ 6,062,848	\$ 3,674,888	\$ 752,378	\$ 4,186,395	\$ 1,743,965	\$ 580,731	\$ 48,631,387	\$ (633,962)	\$ 47,997,425

OHIO STATE UNIVERSITY PHYSICIANS INC., AND SUBSIDIARIES

**CONSOLIDATING STATEMENT OF OPERATIONS
FOR THE YEAR ENDED JUNE 30, 2005**

	OSUP	FM	IM	EM	Eye	Surgery	Pathology	Radiology	Phys Med	OBGYN	Neurology	Psychiatry	Aggregated	EJE	Total
OPERATING REVENUES:															
Patient care revenues:															
Gross patient care revenue	\$ -	\$ 301,265	\$ 112,669,044	\$ 19,984,210	\$ 4,125,822	\$ 60,782,038	\$ 32,898,327	\$ 56,460,257	\$ 5,712,304	\$ 34,958,047	\$ 16,203,917	\$ 2,484,605	\$ 346,579,836	\$ -	\$ 346,579,836
Provision for contractual and administrative		(123,186)	(57,751,394)	(9,083,526)	(2,085,509)	(35,557,534)	(21,613,951)	(36,119,476)	(2,758,802)	(18,633,742)	(9,657,247)	(653,214)	(194,037,581)		(194,037,581)
Net patient care revenues	-	178,079	54,917,650	10,900,684	2,040,313	25,224,504	11,284,376	20,340,781	2,953,502	16,324,305	6,546,670	1,831,391	152,542,255		152,542,255
Contract services	2,140,140	10,515,176		1,287,147	67,195	5,346,011	5,855,568	231,900	882,668	2,737,637	13,934	1,871,364	30,948,740	(261,872)	30,686,868
Other services	4,083,582	370,882	986,031	444,094	6,429	1,790,421	424,347		38,664	172,685	284,160		8,601,295	(2,708,730)	5,892,565
Total operating revenues	6,223,722	11,064,137	55,903,681	12,631,925	2,113,937	32,360,936	17,564,291	20,572,681	3,874,834	19,234,627	6,844,764	3,702,755	192,092,290	(2,970,602)	189,121,688
OPERATING EXPENSES:															
Provider salaries	150,000	5,776,297	22,867,272	4,804,114	531,905	11,656,457	4,661,915	9,568,208	1,312,917	4,416,346	1,650,672	1,391,381	68,787,484		68,787,484
Employees salaries and wages	2,396,994	2,416,819	9,944,500	605,503	562,320	4,576,111	4,059,649	1,204,002	345,687	2,483,670	950,744	465,942	30,011,941		30,011,941
Provision for bad debts	29,927		3,822,925	4,085,569	174,306	2,646,616	976,064	3,396,595	158,047	1,389,095	715,271	134,643	17,529,058		17,529,058
Provider fringe benefits	13,689	737,664	2,549,102	833,278	42,829	2,582,369	1,375,841	1,915,451	172,240	983,616	358,128	327,795	11,892,002		11,892,002
Professional liability insurance		641,022	1,951,569	605,113	225,397	3,672,726	139,965	507,048	147,395	871,987	264,075	86,120	9,112,417		9,112,417
Employee fringe benefits	642,317	702,117	2,952,535	167,477	155,378	1,494,502	1,268,969	446,397	102,827	908,167	300,294	157,762	9,298,742	(15)	9,298,727
Medical supplies			605,250		22,272	215,769	23,308		13,780	113,618	39,565		1,033,562		1,033,562
Office and administrative other	948,334	53,283	1,439,275	172,141	63,352	1,842,988	1,105,199	378,777	56,378	477,615	160,095	67,275	6,764,712	(1,558)	6,763,154
Purchased services and management fees	391,930	55,074	475,148	61,600	20,804	662,435	1,052,607	149,663	276,101	2,166,187	(7,744)	515,395	5,819,200	(73,438)	5,745,762
Academic enrichment and strategic initiative		184,945	977,960	679,689	104,133	723,095	524,549		63,396	301,516	105,286	86,841	5,041,341		5,041,341
Clinical drugs and medications			5,185,677		24,498				1,026,918	2,963,636	1,742,823	1,480	10,945,032		10,945,032
Rent and other occupancy costs	217,246		1,107,894	43,064	42,392	500,686	44,078	58,378	1,945	501,227	87,396	146,263	2,750,569		2,750,569
Other provider related expenses		84,438	(759,216)	254,889	33,148	506,806	176,313	260,385	157,390	294,693	79,875	38,635	1,127,356		1,127,356
Supplies	71,004	51	232,764	72,091	23,271	283,595	979,934	113,635	53,232	100,947	246,920	45,960	2,223,404	(34)	2,223,370
Depreciation and amortization	184,934		815,770	14,172	32,517	51,133	157	8,396	4,403	32,572			1,144,054		1,144,054
Other clinical related expenses			90,056	10,065	6,156	232,455	14,874	304	2,079	170,906	1,227		528,122		528,122
Office and administrative billing	374,217	6,815	512,112	100,260	30,653	280,452	110,736	255,152	29,076	167,536	271,661	127,553	2,266,223	(1,675,049)	591,174
Interest expense	416		268,437	20,030	5	141,889	1,823	262	550	91,210			524,622		524,622
Insurance	51,408	1,650	33,192		100	31,684	5,624	2,253	2,223	166	689		128,989		128,989
Allocated overhead		101,448	361,752	68,052	20,421	239,292	102,468	130,323	22,920	103,020	43,452	27,360	1,220,508	(1,220,508)	
Total operating expenses	5,472,416	10,761,623	55,433,974	12,597,107	2,115,857	32,341,060	16,624,073	19,685,160	3,949,504	18,537,730	7,010,429	3,620,405	188,149,338	(2,970,602)	185,178,736
OPERATING INCOME (LOSS)	751,306	302,514	469,707	34,818	(1,920)	19,876	940,218	887,521	(74,670)	696,897	(165,665)	82,350	3,942,952	-	3,942,952
NONOPERATING REVENUE (EXPENSE):															
Other nonoperating income	13,232	(6,514)	161,882	(2,424)	85,362	238,623	(6,317)	(500)	(121,247)		175,931		538,028		538,028
Investment income (loss)	83,616						31,659			2,673			117,948		117,948
Gain (loss) sale of assets			(4,756)					(5,731)		13,354			2,867		2,867
Total nonoperating revenue (expense)	96,848	(6,514)	157,126	(2,424)	85,362	238,623	25,342	(6,231)	(121,247)	16,027	175,931	-	658,843	-	658,843
INCREASE (DECREASE) IN NET ASSETS	\$ 848,154	\$ 296,000	\$ 626,833	\$ 32,394	\$ 83,442	\$ 258,499	\$ 965,560	\$ 881,290	\$ (195,917)	\$ 712,924	\$ 10,266	\$ 82,350	\$ 4,601,795	\$ -	\$ 4,601,795

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

To the Board of Directors of
Ohio State University Physicians, Inc.
Columbus, Ohio

We have audited the consolidated financial statements of Ohio State University Physicians, Inc. ("OSUP"), as of and for the year ended June 30, 2005, and have issued our report thereon dated December 21, 2005. 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.

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 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 reportable 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.

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 or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we have reported to management of OSUP in a separate letter dated December 21, 2005.

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.

Deloitte + Touche LLP

December 21, 2005



**Auditor of State
Betty Montgomery**

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**OHIO STATE UNIVERSITY PHYSICIANS, INC., AND SUBSIDIARIES
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
MARCH 14, 2006**