

**STATE OF ILLINOIS
SIU PHYSICIANS & SURGEONS, INC.**

**FINANCIAL AUDIT
June 30, 2006
(With comparative totals for 2005)**

**Performed as Special Assistant Auditors
for the Auditor General, State of Illinois**

STATE OF ILLINOIS
SIU PHYSICIANS & SURGEONS, INC.

FINANCIAL AUDIT
June 30, 2006

CONTENTS

Agency Officials	1
Financial Statement Report	
Summary	2
Independent Auditors' Report	3
Management's Discussion and Analysis	5
Basic Financial Statements	
Statement of Net Assets	12
Statement of Revenues, Expenses, and Changes in Net Assets	13
Statement of Cash Flows	14
Notes to Basic Financial Statements	15
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i>	22

**STATE OF ILLINOIS
SIU PHYSICIANS & SURGEONS, INC.**

**FINANCIAL AUDIT
June 30, 2006**

AGENCY OFFICIALS

Chief Executive Officer

Mr. David Tkach

Chief Financial Officer

Mr. Peter R. Cadwell

Executive Director, Financial Affairs

Ms. M. Elizabeth Collier

Agency offices are located at:

800 North Rutledge Street
Springfield, Illinois 62794

**STATE OF ILLINOIS
SIU PHYSICIANS & SURGEONS, INC**

**FINANCIAL AUDIT
June 30, 2006**

FINANCIAL STATEMENT REPORT

SUMMARY

The audit of the accompanying basic financial statements SIU Physicians & Surgeons, Inc. was performed by Crowe Chizek and Company LLC.

Based on their audit, the auditors expressed an unqualified opinion on SIU Physicians & Surgeons, Inc.'s basic financial statements.



Crowe Chizek and Company LLC
Member Horwath International

INDEPENDENT AUDITORS' REPORT

Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited the accompanying basic financial statements of SIU Physicians & Surgeons, Inc. (SIU P&S), a component unit of Southern Illinois University, as of and for the year ended June 30, 2006, as listed in the Table of Contents. These financial statements are the responsibility of the SIU P&S's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the SIU P&S's 2005 financial statements. The financial statements of SIU P&S as of June 30, 2005 were audited by other Special Assistant Auditors for the Auditor General whose report dated October 5, 2005 expressed an unqualified opinion on those financial statements.

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 financial statements. An audit also includes assessing the accounting principles used and the 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, the financial statements referred to above present fairly, in all material respects, the financial position of the SIU Physicians & Surgeons, Inc. as of June 30, 2006, and the changes in financial position and cash flows, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 6, 2006, on our consideration of the SIU P&S's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal controls 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 audit.

The management's discussion and analysis on pages 5 through 11 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Crowe Chizek and Company LLC
Crowe Chizek and Company LLC

Springfield, Illinois
October 6, 2006

SIU PHYSICIANS & SURGEONS, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS
Fiscal Year Ending June 30, 2006
(Unaudited)

Introduction

The discussion and analysis of the financial statements of SIU Physicians & Surgeons, Inc., ("SIU P&S") provides an overview of the financial activities for the year ended June 30, 2006. Management has prepared the financial statements and the related footnote disclosure along with the discussion and analysis.

SIU P&S is reported as a component unit of Southern Illinois University ("the University"). As such, its financial information is also included in the financial activities of the University. Therefore SIU P&S must comply with accounting principles generally accepted in the United States of America ("GAAP") that are applicable to the University, including those pronouncements promulgated by the Governmental Accounting Standards Board ("GASB").

History and Background

SIU P&S, incorporated in 1997 as a 501(c)(3) tax-exempt organization, is the faculty practice plan for Southern Illinois University School of Medicine ("School of Medicine"). SIU P&S operates as a multi-specialty physician group which both aids in the training of medical students and residents and provides clinical services. The School of Medicine bills and collects the fees for the professional services performed by the physicians. The revenues received by SIU P&S are used to compensate its physician members, to support research and educational activities of the School of Medicine, and to pay for clinical operating costs.

Basic Financial Statements

The annual report consists of three basic financial statements. The Statement of Net Assets; the Statement of Revenues, Expenses and Changes in Net Assets; and the Statement of Cash Flows. These statements provide information on SIU P&S as a whole and present a long-term view of its finances. These statements include all assets and liabilities using the accrual basis of accounting. That is, revenues and assets are recognized when services are provided; expenses and liabilities are recognized when goods or services are received, regardless of when cash is received or paid. Each of these statements will be discussed.

Statement of Net Assets

The Statement of Net Assets reports what is owned (assets) and what is owed (liabilities) by SIU P&S. The net asset amount, the difference between what is owned and owed, is one way to measure the financial position of SIU P&S. And over time, the increase or decrease in net assets may indicate if that financial position is improving or not.

SIU PHYSICIANS & SURGEONS, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS
Fiscal Year Ending June 30, 2006
(Unaudited)

Net assets for SIU P&S are divided into three major categories, Invested in Capital Assets, Unrestricted Designated (which is a footnote designation) and Unrestricted Undesignated. The first category, Invested in Capital Assets, represents SIU P&S equity in property, plant and equipment, and is net of related debt and accumulated depreciation. The second category, Unrestricted Designated, represents balances internally designated to be used in support of academic development activities of the clinical departments. The third category, Unrestricted Undesignated, represents balances from operational activities that have not been restricted by parties external to SIU P&S and are available for general use.

<u>Net Asset Summary</u>				
	<u>For the year ended</u>	<u>June 30,</u> <u>2006</u>	<u>June 30,</u> <u>2005</u>	<u>Net Change</u>
Assets				
	Current Assets	\$ 39,203,819	\$ 33,852,509	\$ 5,351,310
	Noncurrent Assets	73,120		73,120
	Capital Assets, net	<u>779,975</u>	<u>593,226</u>	<u>186,749</u>
Total Assets		<u>40,056,914</u>	<u>34,445,735</u>	<u>5,611,179</u>
Liabilities				
	Current Liabilities	<u>8,828,121</u>	<u>5,858,081</u>	<u>2,970,040</u>
Total Liabilities		<u>8,828,121</u>	<u>5,858,081</u>	<u>2,970,040</u>
Net Assets				
	Invested in capital assets, net of debt	779,975	593,226	186,749
	Unrestricted, Designated	1,878,997	1,841,323	37,674
	Unrestricted, Undesignated	<u>28,569,821</u>	<u>26,153,105</u>	<u>2,416,716</u>
Total Net Assets		<u>\$ 31,228,793</u>	<u>\$ 28,587,654</u>	<u>\$ 2,641,139</u>

Current assets are largely comprised of realizable accounts receivables from patients (\$14,935,242). As of June 30, 2006 the gross accounts receivable balance was \$45,157,060 and the comparable amount from the prior fiscal year was \$44,695,642 an increase of just over 1%. Accounts receivable have remained stable, with a slight change in composition which saw an increase in PPO Plan receivables and a decrease in Medicaid receivables. Medicaid remains a delinquent payer though the historical accounts receivable growth experienced in prior fiscal years was not repeated in the current fiscal year. The outstanding accounts receivable is at \$18,258,975 which is approximately 6.3 months in arrears.

A measure of collection effort efficiency is a computation known as the Days Charges Outstanding. This calculation is made by dividing the gross outstanding accounts receivable by

SIU PHYSICIANS & SURGEONS, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS
Fiscal Year Ending June 30, 2006
(Unaudited)

the average daily charges for the period. The Days Charges Outstanding for all combined payers excluding Medicaid was 54 days at June 30, 2006 and 58 days at June 30, 2005.

Comparative gross accounts receivable by payer are as follows:

Gross Accounts Receivable by Payer Class				
<u>As of</u>	<u>June 30,</u> <u>2006</u>		<u>June 30,</u> <u>2005</u>	
Guarantor	\$ 8,328,423	18.44%	\$ 8,282,349	18.53%
Medicare	6,164,314	13.65%	6,015,619	13.46%
Medicaid	18,258,975	40.43%	19,081,337	42.69%
Indemnity	2,876,449	6.37%	2,811,241	6.29%
PPO Plans	5,108,135	11.31%	4,325,021	9.68%
HMO Plans	3,781,062	8.37%	3,647,956	8.16%
Workers Compensation	706,576	1.56%	653,339	1.46%
Unidentified remittances	<u>(66,874)</u>	(.13%)	<u>(120,920)</u>	(.27%)
Total Accounts Receivable, Prior to Uncollectibles	<u>\$ 45,157,060</u>		<u>\$ 44,695,942</u>	
Net Change	<u>\$ 461,118</u>	1.03%		

Overall, the gross accounts receivable increased by just over 1% from the prior fiscal year.

The change in Current Liabilities increased by \$2,970,040 or 50% from FY05 to FY06. This increase consists of the amount due to the University for services rendered. It is anticipated that additional transfers to the University will occur in FY07 to reduce that amount due.

Statement of Revenues, Expenses and Changes in Net Assets

The change in total net assets as presented in the Statement of Net Assets is impacted by activity as reported in the Statement of Revenues, Expenses and Changes in Net Assets. This statement presents the operating, as well as the non-operating results of SIU P&S. Excess revenues over expenses result in increases in net assets; when expenses exceed revenues a decrease in net assets results.

The Statement is segregated by operating and non-operating activities. Operating revenues are those received for services provided in the normal course of business by SIU P&S. These primarily relate to patient care. Operating expenses are those expenses paid to acquire goods or services that are needed to provide patient care services.

SIU PHYSICIANS & SURGEONS, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS
Fiscal Year Ending June 30, 2006
(Unaudited)

Revenue, Expenses and Changes in Net Assets			
<u>For the year ended</u>	<u>June 30,</u> <u>2006</u>	<u>June 30,</u> <u>2005</u>	<u>Net Change</u>
Operating Revenues			
Net patient service revenues	\$ 71,452,970	\$ 68,934,176	\$ 2,518,794
Other operating revenue	<u>979,884</u>	<u>838,616</u>	<u>141,268</u>
Total Operating Revenues	72,432,854	69,772,792	2,660,062
Operating Expenses	<u>70,133,073</u>	<u>61,388,239</u>	<u>8,744,834</u>
Operating Income	2,299,781	8,384,553	(6,084,772)
Non-Operating Revenue	<u>341,358</u>	<u>191,330</u>	<u>150,028</u>
Increase in Net Assets	2,641,139	8,575,883	(5,934,744)
Net Assets Beginning of Year	<u>28,587,654</u>	<u>20,011,771</u>	<u>8,575,883</u>
Net Assets End of Year	<u>\$ 31,228,793</u>	<u>\$ 28,587,654</u>	<u>\$ 2,641,139</u>

Net patient service revenues reflect estimated collectible charges for professional services. There was a 12% increase in gross charges booked in FY06 largely due to recruitment of new clinical faculty and secondly to annual fee increases made during the year. SIU P&S currently operates in a market with a moderate level of managed care penetration. In terms of overall charges, the payer mix of managed care showed a slight increase in FY06. All of this activity is on a discounted fee-for-service basis as SIU P&S currently has no capitated managed care contracts. The most significant dollar increases by Payer Class were in Medicare (\$11,006,701), Medicaid (\$3,220,332) and Managed Care (\$9,584,647). Comparative charges by payer class are:

Total Charges by Payer Class				
<u>For the year ended</u>	<u>June 30, 2006</u>		<u>June 30, 2005</u>	
Guarantor	\$ 15,538,880	7.23%	\$ 16,874,416	8.76%
Medicare	73,409,684	34.15%	62,402,983	32.39%
Medicaid	34,704,920	16.14%	31,484,588	16.34%
Indemnity	12,753,394	5.93%	13,454,245	6.98%
PPO Plans	43,663,156	20.30%	39,685,676	20.59%
HMO Plans	32,304,034	15.03%	26,696,867	13.86%
Workers Compensation	<u>2,613,896</u>	1.22%	<u>2,075,337</u>	1.08%
Total Charges	<u>\$214,987,964</u>		<u>\$ 192,674,112</u>	
Net Change	<u>\$ 22,313,852</u>	11.59%		

SIU PHYSICIANS & SURGEONS, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS
Fiscal Year Ending June 30, 2006
(Unaudited)

Additionally, as revenues increase, so do expenditures used to generate new revenues. Expenses increased 14% over the FY05 level. The primary components of operating expenses are direct SIU P&S overhead, university overhead, academic development and member compensation (i.e. salaries and payroll tax expenses). Member salaries payable and related payroll taxes increased by 6% with the majority of this increase due to an expanded number of members. Member compensation (salaries expense plus payroll taxes) comprises 36% of operating expenses to pay member health care providers for services provided via patient care activities. These members are also faculty of the University and are compensated separately by the University for their academic responsibilities. The other major expense increases related to University overhead and academic development. University overhead expenses comprise 44% of total costs and increased over the two fiscal years by 24%. These overhead costs are for those expenses incurred by the School of Medicine in direct support of the clinical services being provided by the members. These operating costs are for support staff, supplies, rent and ongoing malpractice costs for the members and clinical faculty and are reimbursed by SIU P&S to the School of Medicine via an overhead charge. A significant part of the overhead increase related to transfers into the University for program costs for the Medicaid Intergovernmental Transfer (IGT) agreement relating to treatment of public aid patients. Another component of expense that increased from FY05 to FY06 by (34%) was academic development. Academic development funds are designated by SIU P&S to support continuation and expansion of medical school programs related to teaching, research and service.

Statement of Cash Flows

The Statement of Cash Flows provides relevant information about the cash receipts and cash payments during the year. It helps users assess the ability to generate future net cash flows, the ability to meet financial obligations as they come due, and the need for external financing.

For SIU P&S the statement is divided into four parts. The first shows net cash used by the operating activities of SIU P&S. The second reflects cash flows from non-capital and capital financing activities. Third, cash flows from investing activities, and finally, a reconciliation of net cash from operating activities to operating income as reflected on the Statement of Revenues, Expenses and Changes in Net Assets.

SIU PHYSICIANS & SURGEONS, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS
Fiscal Year Ending June 30, 2006
(Unaudited)

Cash Flows			
For the year ended	June 30,	June 30,	
	2006	2005	Net Change
Cash Provided (Used) by:			
Operating activities	\$ (552,865)	\$ 3,182,149	\$ (3,735,014)
Non-capital financing activities	(13,963)	(395,180)	381,217
Capital financing activities	(354,161)	(344,890)	(9,271)
Investing activities	<u>355,321</u>	<u>200,601</u>	<u>154,720</u>
Net Change in Cash	(565,668)	2,642,680	(3,208,348)
Cash, Beginning of Year	<u>2,701,540</u>	<u>58,860</u>	<u>2,642,680</u>
Cash, End of Year	<u>\$ 2,135,872</u>	<u>\$ 2,701,540</u>	<u>\$ (565,668)</u>

The year-end cash balance has decreased from FY05 to FY06 by \$(565,668). This decrease in cash is primarily due to the use of funds to grow operating activities. One factor mitigating cash flow concerns is the balance in the University agency account. The University collects and holds cash collections on behalf of SIU P&S until a distribution determination is made. The June 30, 2006 agency account balance was \$16 million, a \$ 5.7 million increase from year-end FY05. However, there is an offsetting amount of approximately \$3.3 million due the University.

Future Outlook

Overall, management remains optimistic about the short and long term viability and outlook of the health care sector of the economy and SIU P&S. There has been and continues to be a focused effort on expanding our clinical programs and faculty. Several examples include the Cancer Institute and the coordinated health programs with St John's hospital for women and children.

Management continues to review expenses and operating processes in an effort to control costs and improve operating efficiencies.

Management is aware of two potential issues that could have a negative impact on fiscal performance in the coming year. The State of Illinois has fallen well behind in keeping its obligations due SIU P&S and other health care providers in a current situation. In early FY2007 a significant amount of past claims were adjudicated and paid to us with a goal to maintain their payments to be within 60 days of billing. At the end of November 2006, our Days Charges Outstanding for this payer were at 3.1 months down from 6.3 months at the end of FY2006.

SIU PHYSICIANS & SURGEONS, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS
Fiscal Year Ending June 30, 2006
(Unaudited)

The second area of concern is the level of reimbursement rates from Medicare. Under currently enacted legislation Medicare reimbursement rates are scheduled to decrease by approximately (5%) on January 1, 2007 unless legislative action is taken to avert these decreases. We have had these anticipated reimbursement reductions scheduled before but legislative initiatives have been implemented to negate these changes. We remain confident that the legislative branch will again act upon these planned reductions and make changes to the legislation to eliminate, reduce or even provide for a positive shift in the rates. In early December 2006, legislation was enacted at the federal level which avoided the 5% reduction and fees for 2007 will be frozen at current levels for the second year in a row.

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
STATEMENT OF NET ASSETS

June 30, 2006

(With comparative totals for June 30, 2005)

	2006	2005
ASSETS		
Current assets		
Cash	\$ 2,135,872	\$ 2,701,540
Deposits with SIU (Note 8)	16,013,380	10,262,961
Accounts receivable (Note 4)		
Patient, net of allowance and uncollectibles of		
\$30,221,818 for 2006 and \$28,940,177 for 2005	14,935,242	15,755,765
Estimated Illinois Department of Health and		
Family Services (Note 4)	5,798,502	5,132,243
Other receivables	320,823	-
Total current assets	39,203,819	33,852,509
Noncurrent assets		
Other receivables	73,120	-
Capital assets, net of accumulated		
depreciation (Note 5)	779,975	593,226
Total noncurrent assets	853,095	593,226
Total assets	40,056,914	34,445,735
LIABILITIES		
Current liabilities		
Accounts payable and accrued		
liabilities-SIU (Note 8)	5,058,324	1,793,437
Accounts payable-other	497,335	635,479
Employee salaries payable	2,653,624	2,806,390
Retirement contributions payable	148,260	225,199
Withholding taxes payable	395,373	333,929
Employer taxes payable	70,337	59,869
Other liabilities	4,868	3,778
Total liabilities	8,828,121	5,858,081
NET ASSETS		
Invested in capital assets, net of related debt	779,975	593,226
Net assets, unrestricted	30,448,818	27,994,428
Total net assets	\$ 31,228,793	\$ 28,587,654

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

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
STATEMENT OF REVENUES, EXPENSES, AND
CHANGES IN NET ASSETS

Year Ended June 30, 2006

(With comparative totals for the year ended June 30, 2005)

	2006	2005
Operating revenues		
Net patient service revenue	\$ 71,452,970	\$ 68,934,176
Other operating revenues	979,884	838,616
Total operating revenues	<u>72,432,854</u>	<u>69,772,792</u>
Operating expenses		
Salaries	24,264,831	22,968,895
Payroll taxes	1,142,421	1,041,861
General and administrative	466,190	425,106
Insurance	588,640	572,657
Professional services	672,754	808,437
Medical transcription	759,632	574,486
Software license fees	536,942	631,311
Clinical supplies	1,173,088	1,262,801
Equipment	64,596	64,952
Depreciation	167,412	118,096
Pharmaceutical	2,109,333	2,571,490
University overhead (Note 8)	30,591,351	24,664,328
Academic development (Note 8)	7,595,883	5,683,819
Total operating expenses	<u>70,133,073</u>	<u>61,388,239</u>
Operating income	<u>2,299,781</u>	<u>8,384,553</u>
Nonoperating revenues (expenses)		
Interest expense	-	(7,712)
Interest income (Note 3)	355,321	200,601
Contributions/donations	(13,963)	(1,559)
Total nonoperating revenues (expenses)	<u>341,358</u>	<u>191,330</u>
Increase in net assets	2,641,139	8,575,883
Net assets, beginning of year	<u>28,587,654</u>	<u>20,011,771</u>
Net assets, end of year	<u>\$ 31,228,793</u>	<u>\$ 28,587,654</u>

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
STATEMENT OF CASH FLOWS

Year Ended June 30, 2006

(With comparative totals for the year ended June 30, 2005)

	2006	2005
Cash flows from operating activities		
Cash receipts from patient services	\$ 65,462,871	\$ 62,766,555
Payments to employees	(25,563,955)	(23,441,485)
Payments for goods and services	(6,509,318)	(6,616,153)
Payments to University	(34,919,673)	(30,117,783)
Payments to Foundation	(2,674)	(247,601)
Other cash receipts	979,884	838,616
Net cash provided by (used in) operating activities	(552,865)	3,182,149
Cash flows from noncapital financing activities		
Contributions/donations paid	(13,963)	(1,559)
Payments of long-term debt	-	(393,621)
Net cash provided by (used in) noncapital financing activities	(13,963)	(395,180)
Cash flows from capital financing activities		
Purchase of capital assets	(354,161)	(344,890)
Net cash provided by (used in) capital financing activities	(354,161)	(344,890)
Cash flows from investing activities		
Interest income	355,321	200,601
Net cash provided by (used in) investing activities	355,321	200,601
Net increase (decrease) in cash	(565,668)	2,642,680
Cash at beginning of year	2,701,540	58,860
Cash at end of year	\$ 2,135,872	\$ 2,701,540
Reconciliation of operating income (loss) to net cash used in operating activities		
Operating income	\$ 2,299,781	\$ 8,384,553
Adjustments to reconcile operating income (loss) to net cash used in operating activities		
Depreciation expense	167,412	118,096
Changes in assets and liabilities		
Deposits with SIU	(5,750,419)	(1,364,269)
Receivables (net)	(239,679)	(4,803,353)
Accounts payable and other liabilities	2,970,040	847,122
Net cash provided by (used in) operating activities	\$ (552,865)	\$ 3,182,149

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

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2006

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of SIU Physicians & Surgeons, Inc. (“SIU P&S”) have been prepared in accordance with accounting principles generally accepted in the United States of America, as prescribed by the Governmental Accounting Standards Board (GASB). To facilitate the understanding of data included in the financial statements, summarized below are the significant accounting policies.

Financial Reporting Entity: SIU P&S is organized exclusively for charitable, educational and scientific purposes and to benefit and support the teaching, research and service missions of Southern Illinois University School of Medicine (“School of Medicine”).

Due to the significance of the financial relationship with Southern Illinois University (“University”), in accordance with Governmental Accounting Standards Board Statement No. 14, *The Financial Reporting Entity*, SIU P&S is included as a component unit of the University for financial reporting purposes. The financial activities included in these financial statements are reported in a separate column in the University’s financial statements to emphasize that SIU P&S is an Illinois not-for-profit organization legally separate from the University.

These financial statements include all financial activities over which SIU P&S exercises direct responsibility.

Basis of Presentation: SIU P&S is a special-purpose government entity engaged only in business-type activities, which are financed in whole or in part by fees charged to external parties. Accordingly, the overall activity of SIU P&S is reported through the government-wide statement of net assets, statement of revenue, expenses and changes in net assets and statement of cash flows.

Operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of SIU P&S. Exchange transactions are those in which each party receives and gives up essentially equal values. Non-operating revenues, such as investment earnings, result from non-exchange transactions or ancillary activities.

Operating expenses are those expenses paid to acquire good or services that are needed to provide patient care services. Non-operating expenses are primarily limited to investment activities and contributions/donations.

Basis of Accounting: The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred regardless of when the related cash flow takes place.

(Continued)

STATE OF ILLINOIS
 SIU Physicians & Surgeons, Inc.
 NOTES TO BASIC FINANCIAL STATEMENTS
 June 30, 2006

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, are generally followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. SIU P&S has the option of following subsequent private-sector guidance, subject to this same limitation. SIU P&S has elected not to follow subsequent private-sector guidance as it relates to its operations.

Cash and Cash Equivalents: By policy, SIU P&S treats all deposits in financial institutions and short-term investments with original maturities of 90 days or less as cash and cash equivalents. At June 30, 2006, no cash equivalents were carried by SIU P&S.

Patient Accounts Receivable and Net Patient Service Revenue: SIU P&S has agreements with certain third-party payors, including Medicare and Medicaid that provide for payments at amounts different from established rates. Patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered.

The allowance for doubtful accounts represents the expected losses to be realized upon ultimate collection of patient accounts receivable, which are not subject to third-party payor agreements. Allowance estimates are based on historical experience and other relevant factors. Accounts determined to be uncollectible are charged to operations in the year in which they are determined to be uncollectible.

The following is a breakdown of gross patient service revenues, by payor, for the year ended June 30, 2006:

Government programs	
Medicare	34%
Medicaid	16
Commercial insurance	42
Self-pay and other	8
	100%

Capital Assets: Capital assets are reported at cost. Contributed assets are reported at estimated fair value at the time received. Capital assets that exceed \$5,000 are capitalized and depreciated using the straight-line method. Estimated useful lives of capital assets are as follows:

Scientific/medical equipment	7 years
Office equipment	7 years
Office furniture	7 years
EDP equipment	5 years

(Continued)

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2006

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

Net Assets: In the accompanying financial statements, equity is displayed as in three components as follows:

Invested in Capital Assets, Net of Related Debt – Consists of capital assets, net of accumulated depreciation, less the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. There is currently no related debt associated with capital assets.

Restricted – Consists of net assets that are legally restricted by outside parties or by law through constitutional provisions or enabling legislation. When both restricted and unrestricted resources are available for use, generally it is SIU P&S's policy to use restricted resources first, then unrestricted resources when they are needed. SIU P&S currently has no restricted net assets.

Unrestricted – Consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt." The Board of Directors has designated a portion of unrestricted assets totaling \$1,878,997 to use for academic development purposes.

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 certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Financial Information: The financial statements include certain prior-year summarized comparative information in total. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the SIU P&S financial statements for the year ended June 30, 2005, from which the summarized financial information was derived.

NOTE 2 – TAX STATUS

The U.S. Treasury Department issued a determination letter, dated June 9, 1997, indicating SIU P&S is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

(Continued)

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2006

NOTE 3 – CASH AND INVESTMENTS

Deposits with SIU: SIU P&S deposits most of its cash receipts in the University's pooled cash investment accounts. The University, acting as agent for SIU P&S, makes all distributions as directed. Pooled cash and investments, which consist principally of cash and certificates of deposit, are stated at cost which approximates fair value. SIU P&S's pooled cash and investments are not classified with investments since specific investment securities of the pooled fund maintained by the University are not purchased on behalf of, and/or separately allocated to, the participants of the fund. Interest on pooled cash and investments allocated from the University was \$355,321.

Custodial Credit Risk Related to Deposits: Custodial credit risk is the risk that, in the event of a bank failure, SIU P&S's deposits might not be recovered. SIU P&S does not have a deposit policy for custodial credit risk.

At June 30, 2006, \$2,779,314 of SIU P&S's bank balance of \$2,879,314 was uninsured and uncollateralized.

NOTE 4 – ACCOUNTS RECEIVABLE

Following is a summary of patients' accounts receivable at June 30, 2006 by type of payor:

Government programs	
Medicare	\$ 6,164,314
Medicaid	18,258,975
Commercial insurance	12,472,222
Self-pay and other	<u>8,261,549</u>
	45,157,060
Less	
Allowance for assignment losses	26,304,637
Allowance for doubtful accounts	<u>3,917,181</u>
Net patients' accounts receivable	<u>\$ 14,935,242</u>

SIU P&S has an agreement with the Illinois Department of Healthcare and Family Services. Under such agreement, SIU P&S receives additional reimbursement based upon a cost reimbursement methodology. SIU P&S is reimbursed at defined rates with additional reimbursement being received after submission of an annual cost settlement. Estimated settlements at June 30, 2006 were \$5,798,502.

(Continued)

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2006

NOTE 5 – CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2006, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>Ending Balance</u>
Equipment	\$ 999,002	\$ 354,161	\$ -	\$ 1,353,163
Office furniture	<u>13,777</u>	<u>-</u>	<u>-</u>	<u>13,777</u>
	<u>1,012,779</u>	<u>354,161</u>	<u>-</u>	<u>1,366,940</u>
Less accumulated depreciation for				
Equipment	405,776	167,412	-	573,188
Office furniture	<u>13,777</u>	<u>-</u>	<u>-</u>	<u>13,777</u>
	<u>419,553</u>	<u>167,412</u>	<u>-</u>	<u>586,965</u>
Capital assets, net	<u>\$ 593,226</u>	<u>\$ 186,749</u>	<u>\$ -</u>	<u>\$ 779,975</u>

NOTE 6 – CHARITY CARE

SIU P&S has a policy to provide charitable medical care to individuals unable to pay for such services. During the year ended June 30, 2006, \$2,568,502 was foregone for charitable medical care and supplies furnished.

NOTE 7 – RETIREMENT PLAN

SIU P&S employees may elect to participate in the SIU P&S Retirement Plan (the "Plan"), a defined contribution plan. Participants may contribute up to 25% (but not less than 10%) of taxable compensation through a one-time irrevocable election. If the participant makes no election, an assumption is made that 15% will be contributed each pay period.

Quorum Consulting Services (the "Trustee") maintains an investment portfolio for the Plan contributions with Smith Barney, Citigroup. Contributions are deposited into the participants' accounts, and they may direct the investments among a collection of mutual funds selected by the Plan Administrator. Investment earnings are allocated to the participants' accounts based on the investment return of the mutual funds(s). The combined participants' investment portfolio at June 30, 2006, was valued at \$22,391,892.

SIU P&S acts as the Plan Administrator, but does not own any Plan assets and has no responsibility for the Plan obligations.

(Continued)

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2006

NOTE 8 – RELATED PARTY

SIU P&S entered into a master contract with the Board of Trustees of SIU, which specifies the relationship between the two organizations in accordance with the Legislative Audit Commission's University Guidelines, as amended in 1997. The contract states, among other provisions, that the University shall employ members of SIU P&S as full-time faculty of the School of Medicine for the performance of duties related to its teaching, research and service missions and that SIU P&S shall provide separate and concurrent employment to members of SIU P&S for the performance of duties related to patient care and service to the community. The University, in return, supports SIU P&S by continuing operation of outpatient clinics, maintenance of records and accounting systems, billing and collection services, custody and handling of funds, procurement of goods and services and other related activities as agreed upon by both parties. Funds collected by the University and not yet remitted to SIU P&S, totaling \$16,013,380 are classified as deposits with SIU in the accompanying statements of net assets.

The University receives a portion of SIU P&S's professional income for providing support services in accordance with the master agreement. For the year ended June 30, 2006, the University earned \$30,591,351 for services provided to SIU P&S, of which \$5,023,583 is included in the amount due to SIU.

The University and SIU Foundation at Carbondale also receive from SIU P&S, after providing for support services, funds for Academic Development that are to be used for medical, educational, and research development for the School of Medicine. For the year ended June 30, 2006, SIU P&S contributed to the University \$7,593,209 and the Foundation \$2,674 for such Academic Development services. In September of 2005, the SIU P&S Board of Directors approved the Academic Development funds previously contributed to the SIU Foundation be retained and designated the funds to be used for the purposes stated previously.

NOTE 9 – PROFESSIONAL LIABILITY

All professional liability is assumed by the University and coverage is included as part of the University's overall self-insurance program. The medical professional liability assessment for the self-insurance fund increased from \$1,244,000 in the year ended June 30, 2005 to \$1,808,000 in the year ended June 30, 2006. Contributing to this increase in costs, was the addition of 20 new physicians during the period and a charge of \$240,000 for an excess commercial medical liability coverage policy put in place by the University's Risk Management.

NOTE 10 – LEASE COMMITMENTS

SIU P&S entered into a five-year operating lease for surgical equipment expiring June 30, 2006. Rent expense for the equipment for the year ended June 30, 2006, was \$17,822.

(Continued)

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2006

NOTE 11 – LINE OF CREDIT

SIU P&S has a \$3,000,000 line of credit with National City Bank of Michigan/Illinois, all which was unused at June 30, 2006. Advances on the line of credit are payable on demand and carry an interest rate equal to the 30-day London Interbank Offered Rate. The line of credit is secured by a security interest in accounts receivable.

(Continued)



Crowe Chizek and Company LLC
Member Horwath International

**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**

Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited the financial statements of the SIU Physicians & Surgeons, Inc. (SIU P&S), a component unit of Southern Illinois University, as of and for the year ended June 30, 2006, and have issued our report thereon dated October 6, 2006. 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 SIU P&S'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 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 SIU P&S'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*.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor and agency management and is not intended to be and should not be used by anyone other than these specified parties.

Crowe Chizek and Company LLC
Crowe Chizek and Company LLC

Springfield, Illinois
October 6, 2006