

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

FINANCIAL AUDIT
June 30, 2007
(With comparative totals for 2006)

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

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

FINANCIAL AUDIT
June 30, 2007

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>	23
Schedule of Findings and Recommendations	25

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

FINANCIAL AUDIT
June 30, 2007

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, 2007

FINANCIAL STATEMENT REPORT

SUMMARY

The audit of the accompanying basic financial statements of 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.

SUMMARY OF FINDINGS

The auditors identified a matter involving the Agency's internal control over financial reporting that they considered to be a significant deficiency. The significant deficiency is described in the accompanying Schedule of Findings on page 25 of this report, as finding 07-1, Fraud Prevention and Detection Program.

EXIT CONFERENCE

SIU Physicians & Surgeons, Inc. declined a formal exit conference to discuss the report. Responses to the recommendations were provided by Peter Cadwell, Chief Financial Officer, in a letter dated January 14, 2008.



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, 2007, 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 2006 financial statements and, in our report dated October 6, 2006, we 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, 2007, 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 January 22, 2008, 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
January 22, 2008

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Year Ending June 30, 2007
(UNAUDITED)

Introduction

The discussion and analysis of the financial statements of SIU Physicians & Surgeons, Inc., ("SIU P&S") provide an overview of the financial activities for the year ended June 30, 2007. 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 organizations, 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 support research and educational activities of the School of Medicine, pay for clinical operating costs, and compensate its physician members.

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

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Year Ending June 30, 2007
(UNAUDITED)

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.

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, 2007</u>	<u>June 30, 2006</u>	<u>Net Change</u>
Assets				
	Current Assets	\$35,403,765	\$39,203,819	\$(3,800,054)
	Noncurrent Assets	251,488	73,120	178,368
	Capital Assets, net	<u>976,939</u>	<u>779,975</u>	<u>196,964</u>
Total Assets		<u>36,632,192</u>	<u>40,056,914</u>	<u>(3,424,722)</u>
Liabilities				
	Current Liabilities	<u>7,317,760</u>	<u>8,828,121</u>	<u>(1,510,361)</u>
Total Liabilities		<u>7,317,760</u>	<u>8,828,121</u>	<u>(1,510,361)</u>
Net Assets				
	Invested in capital assets, net of debt	976,939	779,975	196,964
	Unrestricted, Designated	2,063,262	1,878,997	184,265
	Unrestricted, Undesignated	<u>26,274,231</u>	<u>28,569,821</u>	<u>(2,295,590)</u>
Total Net Assets		<u>\$29,314,432</u>	<u>\$31,228,793</u>	<u>\$(1,914,361)</u>

Current assets are largely comprised of realizable accounts receivables from patients (\$16,032,655). As of June 30, 2007 the gross accounts receivable balance was \$43,455,069 and the comparable amount from the prior fiscal year was \$45,157,060 a decrease of just under 4%. Accounts receivable have remained stable overall, but with a change in composition by Payer. The most noticeable change has been the reduction of Medicaid accounts receivable from the prior year end, decreasing to \$10,800,985 from \$18,258,975

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Year Ending June 30, 2007
(UNAUDITED)

or a 41% decrease. Medicaid accounts receivable has decreased from 6.3 months to 3 months. The overall accounts receivable for managed care has increased just slightly less than 3%.

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 the average daily charges for the period. The Days Charges Outstanding for all combined payers excluding Medicaid was 60 days at June 30, 2007 and 54 days at June 30, 2006

Comparative gross accounts receivable by payer are as follows:

<u>Gross Accounts Receivable</u>				
<u>by Payer Class</u>				
As of	<u>June 30, 2007</u>		<u>June 30, 2006</u>	
Guarantor	\$12,066,134	27.76%	\$8,328,423	18.44%
Medicare	7,978,466	18.36%	6,164,314	13.65%
Medicaid	10,800,985	24.86%	18,258,975	40.43%
Indemnity	3,008,303	6.92%	2,876,449	6.37%
PPO Plans	5,564,569	12.80%	5,108,135	11.31%
HMO Plans	3,543,151	8.15%	3,781,062	8.37%
Workers Compensation	498,499	1.15%	706,576	1.56%
Unidentified remittances	<u>(5,038)</u>	-	<u>(66,874)</u>	(.13%)
Total Accounts Receivable, Prior to Uncollectibles	<u>\$43,455,069</u>		<u>\$45,157,060</u>	
Net Change	<u>\$(1,701,991)</u>	(3.77%)		

Overall the gross accounts receivable decreased 3.77% from the prior fiscal year. A large part of this was due to increased receipts from Medicaid.

The change in Current Liabilities decreased by \$1,510,361, or 17% from FY06 to FY07. This decrease consists of the amount due to the University for services rendered.

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.

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Year Ending June 30, 2007
(UNAUDITED)

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.

<u>Revenue, Expenses and Changes in</u>			
<u>Net Assets</u>			
<u>For the year ended</u>	<u>June 30, 2007</u>	<u>June 30, 2006</u>	<u>Net Change</u>
Operating Revenues			
Net patient service revenues	\$76,492,659	\$71,452,970	\$5,039,689
Other operating revenue	<u>654,167</u>	<u>979,884</u>	<u>(325,717)</u>
Total Operating Revenues	<u>77,146,826</u>	<u>72,432,854</u>	<u>4,713,972</u>
Operating Expenses	<u>79,737,734</u>	<u>70,133,073</u>	<u>9,604,661</u>
Operating Income (Loss)	<u>(2,590,908)</u>	<u>2,299,781</u>	<u>(4,890,689)</u>
Non-Operating Revenue	<u>676,547</u>	<u>341,358</u>	<u>335,189</u>
Increase (Decrease) in Net Assets	<u>(1,914,361)</u>	<u>2,641,139</u>	<u>(4,555,500)</u>
Net Assets Beginning of Year	<u>31,228,793</u>	<u>28,587,654</u>	<u>2,641,139</u>
Net Assets End of Year	<u>\$29,314,432</u>	<u>\$31,228,793</u>	<u>\$(1,914,361)</u>

Net patient service revenues reflect estimated collectible charges for professional services. There was an 11% increase in gross charges booked in FY07 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 modest increase in FY07, mostly resulting from Preferred Provider Organization plans. 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 PPO Plans and Medicaid, though the individual mix by Payer has remained relatively unchanged from the prior fiscal year. Comparative charges by payer class are:

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Year Ending June 30, 2007
(UNAUDITED)

<u>Total Charges by Payer Class</u>				
<u>For the year ended</u>	<u>June 30, 2007</u>		<u>June 30, 2006</u>	
Guarantor	\$20,504,430	8.57%	\$15,538,880	7.23%
Medicare	79,430,109	33.20%	73,409,684	34.15%
Medicaid	40,736,991	17.02%	34,704,920	16.14%
Indemnity	13,377,717	5.59%	12,753,394	5.93%
PPO Plans	50,284,725	21.02%	43,663,156	20.30%
HMO Plans	32,271,804	13.49%	32,304,034	15.03%
Workers Compensation	<u>2,653,692</u>	1.11%	<u>2,613,896</u>	1.22%
Total Charges	<u>\$239,259,468</u>		<u>\$214,987,964</u>	
Net Change	<u>\$24,271,504</u>	11.29%		

Additionally, as revenues increase, so do expenditures used to generate new revenues. Expenses increased 14% over the FY06 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 14% with the majority of this increase due to an expanded number of members and additional incentive payments owed at year-end. 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 and academic development expenses comprise 53% of total costs and increased over the two fiscal years by 10%. 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.

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

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Year Ending June 30, 2007
(UNAUDITED)

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.

Cash Flows	June 30, 2007	June 30, 2006	Net Change
For the year ended			
Cash Provided (Used) by:			
Operating activities	\$ (83,408)	\$ (552,865)	\$ 469,457
Non-capital financing activities	96,701	(13,963)	110,664
Capital financing activities	(410,961)	(354,161)	(56,800)
Investing activities	<u>(172,940)</u>	<u>355,321</u>	<u>(528,261)</u>
Net Change in Cash	(570,608)	(565,668)	(4,940)
Cash and cash equivalents, Beginning of Year	<u>2,135,872</u>	<u>2,701,540</u>	<u>(565,668)</u>
Cash and cash equivalents, End of Year	<u>\$1,565,264</u>	<u>\$2,135,872</u>	<u>\$(570,608)</u>

The year-end cash balance has decreased from FY06 to FY07 by \$570,608. 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, 2007 agency account balance was \$13 million. However, there is an offsetting amount of approximately \$2.2 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 SIUP&S. There has been and continues to be a focused effort on expanding our clinical programs and faculty. Several examples include the SimmonsCooper Cancer Institute and several coordinated health programs with St John's Hospital for Women and Children.

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Year Ending June 30, 2007
(UNAUDITED)

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 made a concerted effort to reduce the level of unpaid medical bills for Medicaid recipients as noted earlier, though there is no guarantee they will maintain this in the coming fiscal years.

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 (10%) on January 1, 2008 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.

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.
STATEMENT OF NET ASSETS
June 30, 2007

(With comparative totals for June 30, 2006)

	2007	2006
ASSETS		
Current assets		
Cash and Cash Equivalents (Note 3)	\$ 1,565,264	\$ 2,135,872
Investments (Note 3)	845,700	-
Deposits with SIU (Note 8)	12,932,988	16,013,380
Accounts receivable (Note 4)		
Patient, net of allowance and uncollectibles of \$27,422,414 for 2007 and \$30,221,818 for 2006	16,032,655	14,935,242
Estimated Illinois Department of Health and Family Services (Note 4)	3,977,617	5,798,502
Accrued Interest Receivable	4,586	-
Other receivables	44,955	320,823
Total current assets	35,403,765	39,203,819
Noncurrent assets		
Other receivables	251,488	73,120
Capital assets, net of accumulated depreciation (Note 5)	976,939	779,975
Total noncurrent assets	1,228,427	853,095
Total assets	36,632,192	40,056,914
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities-SIU (Note 8)	2,307,994	5,058,324
Accounts payable-other	733,569	497,335
Employee salaries payable	3,514,952	2,653,624
Retirement contributions payable	272,373	148,260
Withholding taxes payable	409,476	395,373
Employer taxes payable	74,012	70,337
Other liabilities	5,384	4,868
Total liabilities	7,317,760	8,828,121
NET ASSETS		
Invested in capital assets, net of related debt	976,939	779,975
Net assets, unrestricted	28,337,493	30,448,818
Total net assets	\$ 29,314,432	\$ 31,228,793

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, 2007

(With comparative totals for the year ended June 30, 2006)

	2007	2006
Operating revenues		
Net patient service revenue	\$ 76,492,659	\$ 71,452,970
Other operating revenues	654,167	979,884
Total operating revenues	<u>77,146,826</u>	<u>72,432,854</u>
Operating expenses		
Salaries	27,773,138	24,264,831
Payroll taxes	1,272,003	1,142,421
General and administrative	522,192	466,190
Insurance	423,539	588,640
Professional services	672,044	672,754
Medical transcription	785,542	759,632
Software license fees	546,494	536,942
Clinical supplies	1,609,856	1,173,088
Equipment	719,320	64,596
Depreciation (Note 5)	213,997	167,412
Pharmaceutical	3,333,295	2,109,333
University overhead (Note 8)	33,893,655	30,591,351
Academic development (Note 8)	7,972,659	7,595,883
Total operating expenses	<u>79,737,734</u>	<u>70,133,073</u>
Operating income (loss)	<u>(2,590,908)</u>	<u>2,299,781</u>
Nonoperating revenues (expenses)		
Net investment income (Note 3)	677,347	355,321
Contributions/donations	(800)	(13,963)
Total nonoperating revenues (expenses)	<u>676,547</u>	<u>341,358</u>
Increase (decrease) in net assets	(1,914,361)	2,641,139
Net assets, beginning of year	<u>31,228,793</u>	<u>28,587,654</u>
Net assets, end of year	<u>\$ 29,314,432</u>	<u>\$ 31,228,793</u>

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

Year Ended June 30, 2007

(With comparative totals for the year ended June 30, 2006)

	2007	2006
Cash flows from operating activities		
Cash receipts from patient services	\$ 80,296,523	\$ 65,462,871
Payments to employees	(28,041,405)	(25,563,955)
Payments for goods and services	(8,376,049)	(6,509,318)
Payments to University	(44,616,644)	(34,919,673)
Payments to Foundation	-	(2,674)
Other cash receipts	654,167	979,884
Net cash provided by (used in) operating activities	<u>(83,408)</u>	<u>(552,865)</u>
Cash flows from noncapital financing activities		
Contributions/donations paid	(800)	(13,963)
Proceeds from loan repayments	97,501	-
Net cash provided by (used in) noncapital financing activities	<u>96,701</u>	<u>(13,963)</u>
Cash flows from capital financing activities		
Purchase of capital assets	(410,961)	(354,161)
Net cash provided by (used in) capital financing activities	<u>(410,961)</u>	<u>(354,161)</u>
Cash flows from investing activities		
Purchase of investments	(1,419,906)	-
Proceeds from sales of investments and maturities	600,000	-
Interest income	646,966	355,321
Net cash provided by (used in) investing activities	<u>(172,940)</u>	<u>355,321</u>
Net increase (decrease) in cash	(570,608)	(565,668)
Cash and cash equivalents at beginning of year	2,135,872	2,701,540
Cash and cash equivalents at end of year	<u>\$ 1,565,264</u>	<u>\$ 2,135,872</u>
Reconciliation of operating income (loss) to net cash used in operating activities		
Operating income (loss)	\$ (2,590,908)	\$ 2,299,781
Adjustments to reconcile operating income (loss) to net cash used in operating activities		
Depreciation expense	213,997	167,412
Changes in assets and liabilities		
Deposits with SIU	3,080,392	(5,750,419)
Receivables (net) and capital assets (net)	723,472	(239,679)
Accounts payable and other liabilities	(1,510,361)	2,970,040
Net cash provided by (used in) operating activities	<u>\$ (83,408)</u>	<u>\$ (552,865)</u>

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, 2007

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 goods 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, 2007

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.

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, 2007:

Government programs	
Medicare	33%
Medicaid	17
Commercial insurance	41
Self-pay and other	9
	<hr/>
	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, 2007

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 \$2,063,262 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, 2006, 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, 2007

NOTE 3 - CASH AND INVESTMENTS

Investment Policy: It is the policy of SIU P&S to invest funds in a manner which will provide investment returns and security consistent with good business practices, while meeting the daily cash flow demands. The SIU P&S Investment Policy authorizes SIU P&S to invest in securities of the U.S. Government or its agencies; interest bearing savings accounts, certificates of deposit, interest bearing time deposits, and other direct obligations; and money market mutual funds provided they comply with the previous restriction.

The three basic objectives of SIU P&S's investment policy are safety of invested funds; maintenance of sufficient liquidity to meet cash flow needs; and attainment of the maximum investment returns possible consistent with the first two objectives. SIU P&S insures the safety of its invested funds by limiting credit and interest rate risks. SIU P&S's portfolio is structured to ensure that securities mature at the same time as cash is needed to meet anticipated demands. Additionally, since all possible cash demands cannot be anticipated, the portfolio consists largely of securities with active secondary or resale markets. The investment returns on the SIU P&S portfolio is a priority after the safety and liquidity objectives have been met. Investments are limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed.

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 \$615,075.

Cash and Investments: Cash and cash equivalents of SIU P&S include bank accounts and investments with original maturities of ninety days or less at the time of purchase, primarily U.S. Treasury Bills and money market funds.

Investments are reported at fair value. The fair value is determined to be the amount, usually quoted market prices, at which financial instruments could be exchanged in a current transaction between willing partners.

The calculation of realized gains is independent of the calculation of the net increase in the fair value of investments. Realized gains and losses on investments that had been held in more than one fiscal year and sold in the current year may have been recognized as an increase or decrease in the fair value of investments reported in the prior year.

(Continued)

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2007

NOTE 3 - CASH AND INVESTMENTS (Continued)

Investment income net of realized and unrealized gains and losses on investments for the year ended June 30, 2007 are reflected below.

Interest earnings	\$651,552
Realized gain on investment	7,667
Unrealized gain on investments	<u>18,128</u>
Net Investment income	<u>\$677,347</u>

Credit Risk: Credit risk is the risk of loss due to the failure of the security issuer or backer to meet promised interest or principal payments on required dates. Credit risk is mitigated by limiting investments to those instruments of less than one year maturity; and pre-qualifying the financial institutions with which we will do business.

Concentration of Credit Risk: The SIU P&S investment policy states that the portfolio should consist of a mix of various types of securities, issues and maturities

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 minimized custodial credit risk through its investment policy. At June 30, 2007, SIU maintained \$1,138,207 in bank deposits, of which \$1,038,207 was uninsured and uncollateralized.

Interest Rate Risk: Interest rate risk is the risk that the market value of portfolio securities will fall or rise due to changes in general interest rates. Interest rate risk is mitigated by maintaining significant balances in cash equivalent and other short maturity investments and by establishing an asset allocation policy that is consistent with the expected cash flows of SIU P&S. National City Bank manages the SIU P&S portfolio. Interest rate risk is disclosed below using the segmented time distribution method. As of June 30, 2007, SIU P&S had the following cash and investment balances:

Investment Type	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1-5	6-10	No Maturity
U.S. Treasuries	\$ 298,845	\$ 298,845	\$ -	\$ -	\$ -
U.S. Agencies	<u>546,855</u>	<u>546,855</u>	-	-	-
Total Investments	<u>845,700</u>	<u>\$ 845,700</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Cash and Cash Equivalents	<u>1,565,264</u>				
Total Cash & Investments	<u>\$2,410,964</u>				

(Continued)

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2007

NOTE 3 - CASH AND INVESTMENTS (Continued)

This disclosure provides time horizons of investment maturities. It is not a classification of investments as current or noncurrent as presented in the Statement of Net Assets.

NOTE 4 - ACCOUNTS RECEIVABLE

Following is a summary of patients' accounts receivable at June 30, 2007 by type of payor:

Government programs	
Medicare	\$ 7,978,466
Medicaid	10,800,985
Commercial insurance	12,614,522
Self-pay and other	<u>12,061,096</u>
	43,455,069
Less	
Allowance for assignment losses	22,054,063
Allowance for doubtful accounts	<u>5,368,351</u>
Net patients' accounts receivable	<u>\$ 16,032,655</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, 2007 were \$3,977,617.

(Continued)

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2007

NOTE 5 - CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2007, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>Ending Balance</u>
Equipment	\$ 1,353,163	\$ 410,961	\$ -	\$ 1,764,124
Office furniture	<u>13,777</u>	<u>-</u>	<u>-</u>	<u>13,777</u>
	<u>1,366,940</u>	<u>410,961</u>	<u>-</u>	<u>1,777,901</u>
Less accumulated depreciation for				
Equipment	573,188	213,997	-	787,185
Office furniture	<u>13,777</u>	<u>-</u>	<u>-</u>	<u>13,777</u>
	<u>586,965</u>	<u>213,997</u>	<u>-</u>	<u>800,962</u>
Capital assets, net	<u>\$ 779,975</u>	<u>\$ 196,964</u>	<u>\$ -</u>	<u>\$ 976,939</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, 2007, \$2,520,516 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, 2007, was valued at \$29,505,400.

SIU P&S acts as the Plan Administrator, all contributions are from members rather than the organization.

(Continued)

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2007

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 \$12,932,988 are classified as deposits with SIU in the accompanying statement 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, 2007, the University earned \$33,893,655 for services provided to SIU P&S, of which \$2,268,041 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, 2007, SIU P&S contributed to the University \$7,972,659 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 \$1,808,000 in the year ended June 30, 2006 to \$3,500,000 in the year ended June 30, 2007. Contributing to this increase in costs, was the addition of new physicians during the period and a charge of \$495,000 for an excess commercial medical liability coverage policy put in place by the University's Risk Management.

NOTE 10 - 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, 2007. 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.



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 basic 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, 2007, and have issued our report thereon dated January 22, 2008. 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 for the purpose of expressing an opinion on the effectiveness of SIU P&S's internal control over financial reporting. Accordingly, we do not express an opinion the effectiveness of SIU P&S's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency described in the accompanying schedule of findings as item 07-01 to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that result in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we do not believe that the significant deficiency described above is a material weakness.

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*. We are currently conducting a State compliance examination of SIU P&S as required by the Illinois State Auditing Act. The results of the examination will be reported to management of SIU P&S under separate cover.

SIU P&S's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Recommendations. We did not audit SIU P&S's response and, accordingly, we express no opinion on it.

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


Crowe Chizek and Company LLC

Springfield, Illinois
January 22, 2008

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

June 30, 2007

SCHEDULE OF FINDINGS AND RECOMMENDATIONS

FINDING 07-1 Fraud Prevention and Detection Program

Physicians & Surgeons Inc. (SIU P&S) does not have a fraud risk assessment program in place. According to SIU P&S management, SIU P&S has established internal controls in order to prevent and detect fraud as well as errors that may occur, however, these controls and associated risks are not monitored on an on-going basis within a structured fraud prevention and detection program.

SIU P&S relies on current internal controls that have been put in place to prevent and detect fraud. Additionally, SIU P&S management has relied on the internal and external audits for identification of control weaknesses.

Accounting industry trends have increased organization's awareness of the prevalence of fraud. Many organizations rely in part on their auditors to uncover internal fraud, but audits, even those of the highest quality, are not a substitute for management establishing good internal control.

SIU P&S is responsible for the development of internal controls and the monitoring of their operating effectiveness. Additionally, it is management's responsibility to prevent and detect fraud. Therefore, SIU P&S should implement a formal policy regarding evaluation of fraud risk and a system of internal controls to help prevent and detect fraudulent activity within its organization. Preparing a written policy will serve to document SIU P&S's awareness and responsibility for fraud prevention and detection.

SIU P&S does not have a Fraud Prevention and Detection program which could result in fraud risks facing the organization not to be recognized and addressed by SIU P&S management. (Finding Code No. 07-1)

Recommendation:

We recommend that management establish a continuous fraud prevention, deterrence and detection program. This program should include evaluating whether appropriate internal controls have been implemented in any areas identified as posing a higher risk of fraudulent activity, as well as controls over the financial reporting process. In addition, the Board of Directors should evaluate management's identification of fraud risks and implementation of anti-fraud measures.

STATE OF ILLINOIS
SIU Physicians & Surgeons, Inc.

June 30, 2007

SIU P&S Response:

SIU P&S understands this finding is the result of the passage of Statement on Auditing Standards 112 (SAS 112) - *Communicating Internal Control Related Matters Identified in an Audit*. SIU P&S will review the requirements of a formal fraud prevention and detection program and study the best way to implement such a program as necessary. Management believes it may need the involvement of the external auditors in helping to ensure it addresses this matter appropriately.