

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**Chicago, Illinois**

**FINANCIAL STATEMENTS**  
**June 30, 2005 and 2004**

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

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**WOLCOTT, WOOD AND TAYLOR, INC.  
FINANCIAL STATEMENT REPORT  
SUMMARY  
June 30, 2005**

The audit of the accompanying basic financial statements of Wolcott, Wood and Taylor, Inc. was performed by Clifton Gunderson LLP.

Based on their audit, the auditors expressed an unqualified opinion on the Agency's basic financial statements.

## Independent Auditor's Report

The Honorable William G. Holland  
Auditor General  
State of Illinois  
and  
The Board of Directors  
Wolcott, Wood and Taylor, Inc.

As Special Assistant Auditors for the Auditor General, we have audited the accompanying basic financial statements of Wolcott, Wood and Taylor, Inc. (WWT), a component unit of the University of Illinois, as of and for the years ended June 30, 2005 and 2004, as listed in the table of contents. These financial statements are the responsibility of WWT's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States 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 significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of Wolcott, Wood and Taylor, Inc. as of June 30, 2005 and 2004, and its changes in financial position and cash flows for the years 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 our report dated August 12, 2005 on our consideration of WWT'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 control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The accompanying management's discussion and analysis on pages 3 through 10 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 principally 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.

*Clifton Gunderson LLP*

Peoria, Illinois  
August 12, 2005

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**June 30, 2005 and 2004**

(Unaudited)

**Introduction**

The following discussion and analysis provides an overview of the financial position and activities of Wolcott, Wood and Taylor, Inc. (hereinafter referred to as WWT) for the years ended June 30, 2005 and 2004, with selected comparative information for the year ended June 30, 2003. This discussion has been prepared by management and should be read in conjunction with the financial statements and the notes which follow this section.

Wolcott, Wood and Taylor is a wholly owned subsidiary of the University of Illinois whose specified purpose is to provide billing and other management services on behalf of the Medical Service Plan of the College of Medicine of the University of Illinois at Chicago (MSP).

Incorporated in 1999, the initial charge to WWT was to transition the billing and collection operations on behalf of the 25 physician groups which comprise the MSP. Prior to the establishment of WWT, billing and collection services were provided by a number of billing entities, some internal but most independent of the University. Phase-in of the billing and collections operations from the many billing entities to WWT was substantially completed in 2004. There continue to be some areas of the practice which bill independently of WWT.

Gross billings on behalf of the University increased from \$148.0 million in 2003 to \$175.6 million in 2004 to \$190.6 million in 2005. Correspondingly, net collections grew from \$45.3 million posted in 2003 to \$55.3 million posted in 2004. Net collections decreased slightly from \$55.3 million posted in 2004 to \$54.9 million posted in 2005, primarily due to delayed payments from the Illinois Department of Public Aid.

Gross revenue from operations increased slightly from \$5.2 million in 2003 to \$5.9 million in 2004 to \$6.1 million in 2005. Net income totaled \$106,688, \$86,717, and \$687,356 for the years ended June 30, 2003, 2004, and 2005, respectively. Cash and investments grew from \$858,909 as of June 30, 2003 to \$1,136,247 as of June 30, 2004 to \$1,517,748 as of June 30, 2005. Operating staff increased from an average of 52.2 full time equivalents (FTEs) in 2003 to an average of 57.1 FTEs in 2004 to an average of 60.8 FTEs in 2005.

In the summer of 2001, WWT executed a five-year lease for approximately 13,000 square feet located in the downtown Chicago area. Due to a favorable real estate market, the lease was renegotiated in December 2004 decreasing annual rental cost by approximately \$75,000. The lease amendment also provides an opportunity for expansion, a right of first offer, and minimal security deposit requirements. The term of the lease was extended through December 2014.

Payroll and HR management services previously provided by Administaff were transitioned to ADP TotalSource effective December 1, 2004. Both Administaff and ADP TotalSource are recognized as leading providers of payroll and HR services. After evaluating proposals from both companies, it was decided ADP TotalSource provided a potential savings opportunity of \$40,000 to \$60,000 annually with no discernable reduction in service.

Management's focus during this past year has been on strengthening operations, recruiting and retaining qualified staff, and improving productivity.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**June 30, 2005 and 2004**

(Unaudited)

**Financial Highlights**

2005 represents the fourth full year of operations for WWT. Changes in net assets represent the operating activity of WWT which results from revenues, expenses, gains, and losses and are summarized below for the years ended June 30, 2005, 2004, and 2003.

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Total revenue from operations	\$ 6,142,679	\$ 5,925,252	\$ 5,206,095
Total operating expenses	<u>5,288,191</u>	<u>5,607,871</u>	<u>4,809,340</u>
Operating income	854,488	317,381	396,755
Investment income	30,848	10,536	10,093
Interest expense	<u>(197,980)</u>	<u>(241,200)</u>	<u>(300,160)</u>
<b>Increase in net assets</b>	<u>\$ 687,356</u>	<u>\$ 86,717</u>	<u>\$ 106,688</u>

The slight increase in revenue from 2004 to 2005 reflects some additional activity and an increase to cover the cost of operations. Overall, revenue is established on operating budget and debt retirement requirements. Operating revenue increased by 3.7 percent while operating expenses decreased by 5.7 percent. The decrease in operating expense reflects a shift in a major subcontract from WWT to the University. Net income increased to \$687,356 in 2005 from the \$86,717 earned in 2004 in large part to provide funds for the repayment of debt.

The modest increase in revenue from 2003 to 2004 reflects the phase-in of additional activity through 2004 and a change in the methodology used by the University to pay WWT for services provided. Overall, revenue increased by 13.8 percent while operating expenses increased by 16.6 percent. Net income, while positive, declined by approximately \$20,000.

Funds necessary for start-up capital requirements and to cover early operating losses were provided as a loan by the University to WWT and guaranteed by MSP. Indebtedness to the University as of June 30, 2003 and 2004 totaled \$5,360,000. Principal repayment began in 2005 in the amount of \$400,000 leaving a balance due of \$4,960,000 as of June 30, 2005.

**Statements of Net Assets**

The statement of net assets presents the financial position at the end of the fiscal year and includes all assets and liabilities of WWT. Assets and liabilities are generally measured using current values except for capital assets, which are stated at historical cost less an allowance for depreciation. A summarized comparison of WWT's assets, liabilities, and net assets at June 30, 2005, 2004, and 2003 is as follows.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**June 30, 2005 and 2004**

(Unaudited)

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Assets:			
Current assets	\$ <u>1,690,283</u>	\$ <u>1,316,529</u>	\$ <u>1,045,301</u>
Capital assets	2,217,366	2,131,312	1,919,577
Less accumulated depreciation	<u>(1,842,653)</u>	<u>(1,585,439)</u>	<u>(1,250,739)</u>
Capital assets, net	<u>374,713</u>	<u>545,873</u>	<u>668,838</u>
Total assets	<u>2,064,996</u>	<u>1,862,402</u>	<u>1,714,139</u>
Liabilities:			
Current liabilities	640,361	1,590,088	263,577
Noncurrent liabilities	<u>4,560,000</u>	<u>4,095,035</u>	<u>5,360,000</u>
Total liabilities	<u>5,200,361</u>	<u>5,685,123</u>	<u>5,623,577</u>
Net assets:			
Invested in capital assets	374,713	545,873	668,838
Unrestricted	<u>(3,510,078)</u>	<u>(4,368,594)</u>	<u>(4,578,276)</u>
<b>Total net assets</b>	<u>\$ (3,135,365)</u>	<u>\$ (3,822,721)</u>	<u>\$ (3,909,438)</u>

A review of WWT's statement of assets at June 30, 2005, 2004, and 2003 highlights an overall moderate increase consisting of a steady increase in current assets and a mildly fluctuating value of capital assets.

Current assets consist of cash, operating investments, prepaid expense, and accounts receivables. Current assets have grown consistently from \$1,045,301 in 2003 to \$1,316,529 in 2004 to \$1,690,283 in 2005. The increase reflects a positive net income, reduction in purchases of capital assets, and a reduction in interest expense. Capital assets primarily consist of computer hardware, software, and furnishings. The increase in capital assets in 2005 reflects the replacement and/or upgrade of various computer and software assets.

Current liabilities consist of trade accounts, accrued compensation, and accrued interest. A major portion of current liabilities consists of the current portion of outstanding indebtedness to the University. In 2004, the financing agreement required the repayment of \$1,264,965 in principal and that amount is reflected in the 2004 current liabilities. Early in 2005, the financing agreement was amended such that only \$400,000 was to be repaid in 2005 and 2006. Current liabilities in 2005 reflects the \$400,000 to be repaid in 2006.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**June 30, 2005 and 2004**

(Unaudited)

**Statements of Revenues, Expenses, and Changes in Net Assets**

The statement of revenues, expenses, and changes in net assets presents WWT's results of operations. A summarized comparison of WWT's revenues, expenses, and changes in net assets for the years ended June 30, 2005, 2004, and 2003 is as follows:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Revenue:			
Total operating revenues	\$ <u>6,142,679</u>	\$ <u>5,925,252</u>	\$ <u>5,206,095</u>
Expenses:			
Salaries and wages	3,781,571	3,547,328	3,030,834
Nonsalary expense	<u>1,249,406</u>	<u>1,725,843</u>	<u>1,266,231</u>
Subtotal	5,030,977	5,273,171	4,297,065
Depreciation	<u>257,214</u>	<u>334,700</u>	<u>512,275</u>
Total operating expense	<u>5,288,191</u>	<u>5,607,871</u>	<u>4,809,340</u>
Operating income	854,488	317,381	396,755
Nonoperating expense	<u>(167,132)</u>	<u>(230,664)</u>	<u>(290,067)</u>
<b>Increase in net assets</b>	<u>\$ 687,356</u>	<u>\$ 86,717</u>	<u>\$ 106,688</u>

Operating revenues represent payments made to WWT by the University for billing services provided on behalf of MSP together with funds necessary to meet debt retirement requirements. In 2003, the payment was calculated based on a percentage of gross charges billed and payments posted net of refunds. In 2004 and 2005, the payment methodology was revised such that the amount was set at a fixed value agreed upon prior to the start of the year and funds necessary to meet debt retirement requirements. Claims filed on behalf of MSP, gross charges billed, and net payments posted for 2005, 2004, and 2003 are as shown below:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Claims filed	463,048	473,780	472,467
Gross charges billed	\$ 190,604,632	\$ 175,572,508	\$ 148,088,678
Net payments posted	\$ 54,927,118	\$ 55,309,450	\$ 45,300,166

Growth in staffing and salary expense also grew annually from 2003 to 2005. Salary expense increased 6.6 percent over the previous year reflecting an increase in operating staff (FTEs), temporary staff provided to the University, and salary increases from 2004 to 2005. Salary expense increased 17.0 percent from 2003 to 2004 reflecting an increase in operating staff (FTEs), temporary staff provided to the University, and salary increases from 2003 to 2004.



**WOLCOTT, WOOD AND TAYLOR, INC.**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**June 30, 2005 and 2004**

(Unaudited)

Nonsalary expense decreased to \$1,704,600 in 2005 from \$2,301,743 in 2004 or 25.9 percent. Expense categories showing significant variation from 2004 to 2005 are as follows:

	<u>2005</u>	<u>2004</u>
Professional and other services	\$ 57,761	\$ 66,006
Recruitment	37,752	31,867
Software maintenance	264,149	214,147
Seminars and subscriptions	15,578	10,472
Third party claim processing	137,053	692,353
Rent	314,895	341,589
Utilities	15,231	4,823
Interest	197,980	241,200
Depreciation	257,214	334,700
Other	<u>406,987</u>	<u>364,586</u>
<b>Total nonsalary expense</b>	<b><u>\$ 1,704,600</u></b>	<b><u>\$ 2,301,743</u></b>

- The decrease in professional and other services reflects a decrease in consulting expense offset by an increase in bank charges. Prior to 2005, bank charges were paid for by the University.
- Given the labor market, certain positions with the company were filled with the assistance of a search firm resulting in an increase in recruitment expense.
- The increase in software maintenance expense reflects an increase in licensing cost imposed by Microsoft, Citrix, and other software vendors.
- Costs included under seminars and subscriptions reflect training expense associated with our billing software and the addition of new staff.
- The most significant change can be found under the third party claim processing. Early in 2005, the University decided to contract directly with the company responsible for third party claim processing rather than having WWT contract with the company.
- The decrease in rent payment reflects the reduction in rent costs achieved by renegotiating our facility lease.
- Utility costs in 2004 reflect the rebate of utility costs posted in 2003 and 2004.
- The interest rate charged WWT by the University is based on the rate earned by the University on its long term investments. As market rates have declined, the interest expense paid to the University has declined.
- The decline in depreciation expense reflects the rapid amortization of the computer hardware purchased early in the company's operations.

**WOLCOTT, WOOD AND TAYLOR, INC.  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
June 30, 2005 and 2004**

(Unaudited)

Nonsalary expense grew to \$2,301,743 in 2004 from \$2,078,666 in 2003 or 10.7 percent. Expense categories showing significant variation from 2003 to 2004 are as follows:

	<u>2004</u>	<u>2003</u>
Professional and other services	\$ 66,006	\$ 37,954
Supplies	58,373	78,712
Software maintenance	214,147	165,914
Third party claim processing	692,353	322,237
General services	228,129	195,853
Interest	241,200	300,160
Depreciation	334,700	512,275
Other	<u>466,835</u>	<u>465,561</u>
<b>Total nonsalary expense</b>	<b><u>\$ 2,301,743</u></b>	<b><u>\$ 2,078,666</u></b>

- The increase in professional and other services primarily reflects a new contract with a vendor providing automated telephone services for patients who have not responded to written communications.
- Supply expense has declined as the number of new staff has declined.
- Software maintenance expense is based on the number of claims processed. This calculation is generally made in October. Claims processed through October 2003 totaled 479,899 as compared to 381,913 processed the prior year.
- Increases in third party claim processing expense reflects an increase in covered lives adjudicated by the third party claim processing vendor and a broadening of the vendor's scope of services to include utilization management.
- The majority of the increase categorized under general service expense reflects increases in postage and printing costs for claims and patient statements. In addition, WWT contracted with two new companies; one to shred paper with sensitive information and one to provide offsite storage of billing records.
- Interest rates vary from year to year and are established based on the University's short term investment rate. The decline from 2003 to 2004 reflects the decrease in interest rates.
- The decline in depreciation expense reflects the rapid amortization of the computer hardware purchased early in the company's operations.
- Other expenses reflect the cost of general operations.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**June 30, 2005 and 2004**

(Unaudited)

**Statements of Cash Flows**

The statement of cash flows provides additional information of WWT's financial results by reporting major sources and uses of cash. A comparative summary of the statements of cash flows for the years ended June 30, 2005, 2004, and 2003 is as follows:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Cash received from operations	\$ 6,197,771	\$ 5,942,983	\$ 5,300,115
Cash expended for operations	<u>(5,102,784)</u>	<u>(5,208,506)</u>	<u>(4,221,607)</u>
Net cash provided by operating activities	1,094,987	734,477	1,078,508
Net cash used in capital and related financing activities	(86,054)	(211,735)	(277,852)
Net cash used in noncapital financing activities	(658,280)	(255,940)	(317,580)
Net cash used in investing activities	<u>(350,653)</u>	<u>(266,802)</u>	<u>(483,076)</u>
Net increase in cash and cash equivalents	-	-	-
Cash and cash equivalents, beginning of year	<u>5,000</u>	<u>5,000</u>	<u>5,000</u>
<b>Cash and cash equivalents, end of year</b>	<u><u>\$ 5,000</u></u>	<u><u>\$ 5,000</u></u>	<u><u>\$ 5,000</u></u>

The increase in funds derived from operations from 2004 to 2005 was in large part applied to retirement of long-term debt. The balance was used to pay interest, purchase equipment, and be invested in short-term instruments.

From 2003 to 2004, the decrease in funds derived from operations was partially offset by decreases in capital acquisitions and payments of interest expense to the University. The remaining funds totaling \$266,802 were invested in short-term instruments as are other liquid assets.

**Economic Factors that will Affect Future**

Management believes that opportunities exist for continued improvement of operations. This coupled with greater experience is expected to result in lower costs per claim processed and improved collections.

**WOLCOTT, WOOD AND TAYLOR, INC.  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
June 30, 2005 and 2004**

(Unaudited)

Nevertheless, insurance companies, governmental payors, and other third party payors continue to ratchet down the amount paid for services provided. Historical reductions in reimbursement coupled with those proposed may reduce payments from some payors by as much as five percent over a two year period. These reductions and other pressures on the Medical Center, including increased malpractice insurance and reduced State support, may ultimately impact WWT operations.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**STATEMENTS OF NET ASSETS**  
**June 30, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash	\$ 5,000	\$ 5,000
Bank repurchase agreement	1,458,748	1,031,247
Certificate of deposit	54,000	100,000
Accounts receivable	36,111	91,203
Prepaid expenses	<u>136,424</u>	<u>89,079</u>
Total current assets	1,690,283	1,316,529
 <b>CAPITAL ASSETS, net</b>	 <u>374,713</u>	 <u>545,873</u>
 <b>TOTAL ASSETS</b>	 <u>\$ 2,064,996</u>	 <u>\$ 1,862,402</u>
 <b>LIABILITIES AND NET ASSETS</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 17,677	\$ 78,420
Accrued expenses	191,434	186,403
Accrued interest	-	60,300
Current installment of long-term debt	400,000	1,264,965
Accrued rent	<u>31,250</u>	<u>-</u>
Total current liabilities	640,361	1,590,088
 <b>LONG-TERM DEBT, net of current installment included above</b>	 <u>4,560,000</u>	 <u>4,095,035</u>
Total liabilities	<u>5,200,361</u>	<u>5,685,123</u>
 <b>NET ASSETS</b>		
Invested in capital assets	374,713	545,873
Unrestricted	<u>(3,510,078)</u>	<u>(4,368,594)</u>
Total net assets	<u>(3,135,365)</u>	<u>(3,822,721)</u>
 <b>TOTAL LIABILITIES AND NET ASSETS</b>	 <u>\$ 2,064,996</u>	 <u>\$ 1,862,402</u>

These financial statements should be read only in connection with  
the accompanying notes to financial statements.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS**  
**For the Years Ended June 30, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
<b>OPERATING REVENUES</b>	\$ 6,142,679	\$ 5,925,252
<b>OPERATING EXPENSES</b>		
Salaries and wages	3,781,571	3,547,328
General services	235,360	228,129
Recruitment	37,752	31,867
Travel	17,763	16,185
Insurance	14,652	14,619
Telecommunications	35,496	33,853
Software maintenance	264,149	214,147
Professional and other contractual services	57,761	66,006
Leased equipment	5,270	3,879
Supplies	56,332	58,373
Third party claim processing	137,053	692,353
Seminars and subscriptions	15,578	10,472
Maintenance and repairs	10,337	6,329
Rent	314,895	341,589
Utilities	15,231	4,823
Other	31,777	3,219
Depreciation	<u>257,214</u>	<u>334,700</u>
Total operating expenses	<u>5,288,191</u>	<u>5,607,871</u>
Operating income	<u>854,488</u>	<u>317,381</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Investment income	30,848	10,536
Interest expense	<u>(197,980)</u>	<u>(241,200)</u>
Total nonoperating revenues and expenses	<u>(167,132)</u>	<u>(230,664)</u>
<b>INCREASE IN NET ASSETS</b>	687,356	86,717
<b>NET ASSETS, BEGINNING OF YEAR</b>	<u>(3,822,721)</u>	<u>(3,909,438)</u>
<b>NET ASSETS, END OF YEAR</b>	<u>\$ (3,135,365)</u>	<u>\$ (3,822,721)</u>

These financial statements should be read only in connection with  
the accompanying notes to financial statements.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**STATEMENTS OF CASH FLOWS**  
**For the Years Ended June 30, 2005 and 2004**

	<u>2005</u>	<u>2004</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Fees collected	\$ 6,197,771	\$ 5,942,983
Payments to suppliers	(1,326,244)	(1,707,954)
Payments to employees	<u>(3,776,540)</u>	<u>(3,500,552)</u>
Net cash provided by operating activities	<u>1,094,987</u>	<u>734,477</u>
 <b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Purchases of capital assets	<u>(86,054)</u>	<u>(211,735)</u>
 <b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>		
Interest paid	(258,280)	(255,940)
Payments on long-term debt	<u>(400,000)</u>	<u>-</u>
Net cash used in noncapital financing activities	<u>(658,280)</u>	<u>(255,940)</u>
 <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Interest received on investments	30,848	10,536
Purchase of investments	(427,501)	(346,338)
Redemption of certificate of deposit	<u>46,000</u>	<u>69,000</u>
Net cash used in investing activities	<u>(350,653)</u>	<u>(266,802)</u>
 <b>NET INCREASE IN CASH</b>	 -	 -
 <b>CASH, BEGINNING OF YEAR</b>	 <u>5,000</u>	 <u>5,000</u>
 <b>CASH, END OF YEAR</b>	 <u>\$ 5,000</u>	 <u>\$ 5,000</u>
 <b>RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
Operating income	\$ 854,488	\$ 317,381
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	257,214	334,700
Effects of changes in:		
Accounts receivable	55,092	17,731
Prepaid expenses	(47,345)	(11,621)
Accounts payable and accrued expenses	(55,712)	76,286
Accrued rent	<u>31,250</u>	<u>-</u>
 <b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	 <u>\$ 1,094,987</u>	 <u>\$ 734,477</u>

These financial statements should be read only in connection with the accompanying notes to financial statements.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2005 and 2004**

**NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations**

Wolcott, Wood and Taylor, Inc. (WWT) is an Illinois not-for-profit corporation with offices located in Chicago, Illinois. The articles of incorporation authorize WWT to provide practice management support services and operate as a billing/collection entity under the laws of the State of Illinois.

WWT was created by the Board of Trustees of the University of Illinois (University) effective July 8, 1999 to provide billing and collection services and practice management support services for the Medical Service Plan of the College of Medicine of the University of Illinois at Chicago (MSP). WWT is recognized by the University of Illinois as a University related organization, and is incorporated within the University's financial report as a component unit.

**Basis of Presentation**

WWT prepared its financial statements as a Business Type Activity, as defined by GASB Statement No. 34, using the economic resources measurement focus and the accrual basis of accounting. Business Type Activities are those financed in whole or in part by fees charged to external parties for goods and services. Pursuant to GASB Statement No. 20, the Company has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989, and do not conflict with or contradict GASB pronouncements. WWT has elected not to apply FASB pronouncements issued after November 30, 1989.

**Cash and Cash Equivalents**

The Company considers all liquid investments with original maturities of three months or less to be cash equivalents.

**Accounts Receivable**

Accounts receivable have been adjusted for all known uncollectible accounts. No allowance for doubtful accounts has been provided since, in management's judgment, it is believed that the amount of such allowance would not be significant.

**Capital Assets**

Assets with an original cost greater than \$1,000 and a useful life of more than one year are capitalized. Capital assets are depreciated on an accelerated or straight-line basis over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful life. The following estimated useful lives are being used by WWT:



**WOLCOTT, WOOD AND TAYLOR, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2005 and 2004**

**NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Capital Assets** (Continued)

Data processing equipment	5 years
Computer software	3 years
Furniture and fixtures	7 years
Leasehold improvements	5 years

**Revenue Recognition**

Revenue is recognized by WWT as services are provided.

**Classification of Revenues**

The Company has classified its revenues as either operating or nonoperating revenues according to the following criteria:

Operating revenues - Operating revenues include activities that have the characteristics of exchange transactions, such as billing and collection and practice management support services.

Nonoperating revenues - Nonoperating revenues include activities that have the characteristics of nonexchange transactions and other revenue sources that are defined as nonoperating revenues by GASB No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Government Entities That Use Proprietary Fund Accounting*, and GASB No. 34, such as investment income.

**Use of Estimates**

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

**Income Taxes**

Although WWT is an Illinois not-for-profit corporation, it is subject to federal income taxes under the U.S. Internal Revenue Code.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2005 and 2004**

**NOTE 2 - DEPOSITS AND INVESTMENTS**

**Deposits**

At June 30, 2005, WWT has a bank balance of \$59,000, consisting of a checking account with a carrying amount of \$5,000 and a certificate of deposit with a carrying amount of \$54,000. The balance is insured (FDIC) for \$59,000.

At June 30, 2004, WWT has a bank balance of \$105,000, consisting of a checking account with a carrying amount of \$5,000 and a certificate of deposit with a carrying amount of \$100,000. The balance is insured (FDIC) for \$100,000. The remaining \$5,000 is uncollateralized and uninsured.

**Investments**

As of June 30, 2005, WWT had the following investments and maturities:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Less Than 1 Year</u>
Repurchase agreement	<u>\$1,458,748</u>	<u>\$1,458,748</u>

As of June 30, 2004, WWT had the following investments and maturities:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Less Than 1 Year</u>
Repurchase agreement	<u>\$1,031,247</u>	<u>\$1,031,247</u>

Custodial Credit Risk. For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, WWT will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. WWT does not have a deposit policy for custodial credit risk.

Interest Rate Risk. WWT does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2005 and 2004**

**NOTE 3 - CAPITAL ASSETS**

Capital asset activity for the year ended June 30, 2005 was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>Ending Balance</u>
Data processing equipment	\$ 587,757	\$ 37,490	\$ -	\$ 625,247
Computer software	1,180,625	48,564	-	1,229,189
Furniture and fixtures	280,794	-	-	280,794
Leasehold improvements	<u>82,136</u>	<u>-</u>	<u>-</u>	<u>82,136</u>
Total	<u>2,131,312</u>	<u>86,054</u>	<u>-</u>	<u>2,217,366</u>
Less accumulated depreciation:				
Data processing equipment	425,548	85,054	-	510,602
Computer software	970,117	117,830	-	1,087,947
Furniture and fixtures	148,055	37,915	-	185,970
Leasehold improvements	<u>41,719</u>	<u>16,415</u>	<u>-</u>	<u>58,134</u>
Total accumulated depreciation	<u>1,585,439</u>	<u>257,214</u>	<u>-</u>	<u>1,842,653</u>
<b>Capital assets, net</b>	<u>\$ 545,873</u>	<u>\$ (171,160)</u>	<u>\$ -</u>	<u>\$ 374,713</u>

Capital asset activity for the year ended June 30, 2004 was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>Ending Balance</u>
Data processing equipment	\$ 522,404	\$ 65,353	\$ -	\$ 587,757
Computer software	1,034,243	146,382	-	1,180,625
Furniture and fixtures	280,794	-	-	280,794
Leasehold improvements	<u>82,136</u>	<u>-</u>	<u>-</u>	<u>82,136</u>
Total	<u>1,919,577</u>	<u>211,735</u>	<u>-</u>	<u>2,131,312</u>
Less accumulated depreciation:				
Data processing equipment	339,193	86,355	-	425,548
Computer software	791,303	178,814	-	970,117
Furniture and fixtures	94,963	53,092	-	148,055
Leasehold improvements	<u>25,280</u>	<u>16,439</u>	<u>-</u>	<u>41,719</u>
Total accumulated depreciation	<u>1,250,739</u>	<u>334,700</u>	<u>-</u>	<u>1,585,439</u>
<b>Capital assets, net</b>	<u>\$ 668,838</u>	<u>\$ (122,965)</u>	<u>\$ -</u>	<u>\$ 545,873</u>

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2005 and 2004**

**NOTE 4 - LONG-TERM DEBT**

A note between WWT and the University of Illinois has been authorized effective January 31, 2000 in an amount not to exceed \$5,500,000 to provide capital to cover initial startup costs of WWT. As of June 30, 2005 and 2004, \$4,960,000 and \$5,360,000, respectively, of the authorized note was outstanding. The terms of the note provide for interest to be accrued and billed quarterly based on the University's investment money market intermediate rate of return. The effective interest rate as of June 30, 2005 and 2004 was 3.8 and 4.5 percent, respectively. Interest rates will be reviewed annually and adjusted at the beginning of the fiscal year should the University's investment money market intermediate term rate of return differ by at least 1 percent from the rate currently being charged. The note has been guaranteed by the University's Medical Service Plan (MSP).

Debt service requirements as of June 30, 2005, computed using the then prevailing interest rate, were as follows:

<b>Year Ending <u>June 30,</u></b>	<b>Total to be <u>Paid</u></b>	<b><u>Principal</u></b>	<b><u>Interest</u></b>
2006	\$ 583,143	\$ 400,000	\$ 183,143
2007	1,920,926	1,772,434	148,492
2008	1,920,701	1,840,752	79,949
2009	<u>960,349</u>	<u>946,814</u>	<u>13,535</u>
	<u>\$ 5,385,119</u>	<u>\$ 4,960,000</u>	<u>\$ 425,119</u>

**NOTE 5 - RELATED PARTIES**

The President is an employee of WWT and the University of Illinois. The Directors and Officers are employees of the University of Illinois. In accordance with the University's policy on "Conflicts of Commitment and Interest," all such individuals have received approval from their supervisors within the University. Additionally, as the directed purpose of WWT is to provide medical practice management support services for the University's MSP, the activities of these individuals have been judged to not represent conflicts of commitment or interest as defined within the University's policy.

**NOTE 6 - RETIREMENT AND POSTEMPLOYMENT BENEFITS**

Employees of WWT who have appointments within the University of Illinois of greater than 50 percent participate in the State Universities Retirement System of Illinois (SURS), a cost-sharing multiple-employer defined-benefit pension plan. The University contributes to the plan with a special funding situation whereby the State of Illinois makes substantially all actuarially determined required contributions on behalf of the participating employers. The University contributions include payments for WWT employees covered under the plan.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2005 and 2004**

**NOTE 6 - RETIREMENT AND POSTEMPLOYMENT BENEFITS (CONTINUED)**

SURS was established July 21, 1941 to provide retirement annuities and other benefits for staff members and employees of the State universities, certain affiliated organizations, and certain other State educational and scientific agencies and for survivors, dependents, and other beneficiaries of such employees. SURS is considered a component unit of the State of Illinois' financial reporting entity and is included in the State's financial reports as a pension trust fund. SURS is governed by Section 5/15, Chapter 40, of the *Illinois Compiled Statutes*. SURS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to SURS, 1901 Fox Drive, Champaign, IL 61820 or by calling 1-800-275-7877.

Eligible employees must participate upon initial employment. Employees are ineligible to participate if (a) employed after having attained age 68; (b) employed less than 50 percent of full-time; or (c) employed less than full-time and attending classes with an employer. Of those University employees ineligible to participate, the majority are students at the University.

SURS provides retirement, disability, and death benefits. Members are eligible for normal retirement at any age after 35 years of service, at age 60 after 8 years of service, or at age 62 after 5 years of service. There are also provisions for early retirement. Retirement benefits are based on certain formulas that generally are a function of years of service and the average salary based on the highest earnings of any four consecutive years. Disability benefits are paid to disabled members with two years of covered service, generally at 50 percent of basic compensation until the total benefits paid equal 50 percent of the total earnings in covered service. Death benefits are payable to survivors of an active member with one and one-half years of covered service or of a former member with ten years of covered service. These benefits are payable until children attain the age of 18, to a spouse after age 50, and to a dependent parent after age 55. Benefits are equal to the retirement contributions and interest, a lump sum payment of \$1,000, and a monthly annuity equal to a portion of the accrued normal retirement benefit based on specified formulas.

Plan members are required to contribute 8.0 percent of their annual covered salary and substantially all employer contributions are made by the State of Illinois on behalf of the individual employers at an actuarially determined rate. The current rate is 11.12 percent of annual covered payroll. The contribution requirements of plan members and employers are established and may be amended by the Illinois General Assembly. The University's contributions to SURS for the years ended June 30, 2005, 2004, and 2003 were \$145,751,517, \$755,398,000, and \$139,955,000, respectively, equal to the required contributions for each year.

Company employees hired prior to April 1, 1986 are exempt from contributions required under the Federal Insurance Contribution Act. Employees hired after March 31, 1986 are required to contribute 1.45 percent of their gross salary for Medicare. The Company is required to match this contribution.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2005 and 2004**

**NOTE 6 - RETIREMENT AND POSTEMPLOYMENT BENEFITS (CONTINUED)**

University employees may also elect to participate in certain tax-sheltered retirement plans. These voluntary plans permit employees to designate a part of their earnings into tax-sheltered investments and thus defer federal and state income taxes on their contributions and the accumulated earnings under the plans. Participation and the level of employee contributions are voluntary. The employer is not required to make contributions to these plans.

In addition to providing pension benefits, the State provides certain health, dental, and life insurance benefits to annuitants who are former State employees. This includes annuitants of WWT. Substantially all State employees, including the employees of WWT, may become eligible for postemployment benefits if they eventually become annuitants. Health and dental benefits include basic benefits for annuitants under the State's self-insurance plan and insurance contracts currently in force. Life insurance benefits for annuitants under age 60 are equal to their annual salary at the time of retirement; life insurance benefits for annuitants age 60 and older are limited to \$5,000 per annuitant.

Currently, the State does not segregate payments made to annuitants from those made to current employees for health, dental, and life insurance benefits. The cost of health, dental, and life insurance benefits is recognized by the State on a pay-as-you-go basis. These costs are funded by the State and are not an obligation of WWT or the University.

WWT has established a 401(k) plan for its employees who are at least 21 years of age and have completed 1,000 hours of service within a consecutive 12 month period. WWT does not make any contributions to the 401(k) plan.

**NOTE 7 - OPERATING LEASE**

WWT has a noncancellable operating lease for office space at 200 West Adams, Suite 225, Chicago, Illinois, that expires December 31, 2014.

Future minimum lease payments under this operating lease at June 30, 2005 are:

2006	\$ 124,016
2007	120,731
2008	127,257
2009	133,783
2010	140,309
2011 through 2015	<u>711,334</u>
	<u>\$ 1,357,430</u>

WWT maintains a certificate of deposit for \$54,000 at June 30, 2005 as a security deposit on the building lease.

**WOLCOTT, WOOD AND TAYLOR, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2005 and 2004**

**NOTE 8 - INCOME TAX**

As of June 30, 2005, WWT had tax net operating loss carryforwards approximating \$3,500,000. Timing differences relate to accounting for capital assets and the capitalization of certain start-up costs for tax reporting purposes. The loss carryforwards expire in varying amounts through the year 2020. Management believes that the likelihood of WWT utilizing the tax loss carryforwards in the near future is remote and thus has recorded a full valuation allowance with respect to the future benefits due to the uncertainty of their ultimate realization.

This information is an integral part of the accompanying financial statements.

**Independent Auditor's 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  
and  
The Board of Directors  
Wolcott, Wood and Taylor, Inc.

As Special Assistant Auditors for the Auditor General, we have audited the basic financial statements of Wolcott, Wood and Taylor, Inc. (WWT) as of and for the years ended June 30, 2005 and 2004, and have issued our report thereon dated August 12, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered WWT'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 WWT'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, the Board of Directors, and management of WWT, and is not intended to be and should not be used by anyone other than these specified parties.

*Clifton Henderson LLP*

Peoria, Illinois  
August 12, 2005