

Bell Memorial Hospital and Subsidiary

**Consolidated Financial Report
with Additional Information
June 30, 2008**

Bell Memorial Hospital and Subsidiary

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Independent Auditor's Report

To the Board of Directors
Bell Memorial Hospital and Subsidiary

We have audited the accompanying consolidated balance sheet of Bell Memorial Hospital and Subsidiary (the "Hospital") as of June 30, 2008 and 2007 and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Bell Memorial Hospital and Subsidiary at June 30, 2008 and 2007 and the consolidated results of their operations, changes in net assets, and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 10 to the consolidated financial statements, the Hospital adopted the provisions of FASB Statement No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans*, as of June 30, 2007.

Plante & Moran, PLLC

December 3, 2008

Bell Memorial Hospital and Subsidiary

Consolidated Balance Sheet

	<u>June 30, 2008</u>	<u>June 30, 2007</u>
Assets		
Current Assets		
Cash and cash equivalents	\$ 11,416,701	\$ 9,895,005
Accounts receivable (Note 2)	4,054,866	5,145,143
Estimated third-party payor settlements (Note 3)	1,232,904	300,000
Assets limited as to use (Note 5)	5,608,140	719,077
Inventory	1,490,920	1,247,542
Prepaid expenses and other	245,580	995,918
Total current assets	24,049,111	18,302,685
Property and Equipment - Net (Note 4)	38,583,944	11,859,631
Other Assets (Note 5)	12,664,306	34,149,976
Total assets	<u>\$ 75,297,361</u>	<u>\$ 64,312,292</u>
Liabilities and Net Assets		
Current Liabilities		
Current portion of long-term debt (Note 6)	\$ 930,385	\$ 190,190
Accounts payable	1,591,358	1,276,861
Estimated third-party payor settlements (Note 3)	-	578,094
Construction payables (Note 4)	5,608,140	656,449
Accrued liabilities	2,882,291	1,729,907
Total current liabilities	11,012,174	4,431,501
Long-term Debt - Net of current portion (Note 6)	35,203,610	34,559,488
Other Liabilities (Note 8)	2,659,393	941,213
Total liabilities	48,875,177	39,932,202
Net Assets		
Unrestricted	25,424,004	24,191,513
Temporarily restricted	998,180	188,577
Total net assets	26,422,184	24,380,090
Total liabilities and net assets	<u>\$ 75,297,361</u>	<u>\$ 64,312,292</u>

Bell Memorial Hospital and Subsidiary

Consolidated Statement of Operations

	Year Ended	
	June 30, 2008	June 30, 2007
Unrestricted Revenue, Gains, and Other Support		
Net patient service revenue	\$ 47,072,674	\$ 40,127,810
Other	<u>1,040,336</u>	967,400
Total unrestricted revenue, gains, and other support	48,113,010	41,095,210
Expenses		
Salaries and wages	20,264,900	17,792,486
Employee benefits	4,747,715	4,357,972
Supplies	5,751,469	4,626,231
Purchased services	3,396,602	2,956,190
Insurance	540,416	680,765
Other healthcare expenses	4,708,073	4,233,961
Depreciation and amortization (Note 4)	1,675,016	1,628,134
Provision for bad debts	3,263,024	2,663,628
Interest expense	<u>84,823</u>	92,221
Total expenses (Note 12)	<u>44,432,038</u>	39,031,588
Operating Income	3,680,972	2,063,622
Other (Loss) Income	<u>(447,299)</u>	656,732
Excess of Revenue Over Expenses Before Unusual Event	3,233,673	2,720,354
Unusual Event - Conditional asset retirement obligation (Note 13)	<u>(750,000)</u>	-
Excess of Revenue Over Expenses	2,483,673	5,440,708
Contributed Land (Note 4)	-	2,033,000
Change in Net Unrealized Gains and Losses on Investments (Note 5)	(278,841)	168,540
Pension-related Changes Other Than Net Periodic Pension Costs (Note 9)	(972,341)	-
Adjustment to Initially Apply FASB Statement No. 158 (Notes 9 and 10)	-	417,043
Minimum Pension Liability Adjustment (Note 9)	<u>-</u>	24,190
Increase in Unrestricted Net Assets	<u>\$ 1,232,491</u>	\$ 8,083,481

Bell Memorial Hospital and Subsidiary

Consolidated Statement of Changes in Net Assets

	Year Ended June 30	
	2008	2007
Unrestricted Net Assets		
Excess of revenue over expenses	\$ 2,483,673	\$ 5,440,708
Contributed land	-	2,033,000
Change in unrealized gains and losses on investments	(278,841)	168,540
Pension-related changes other than net periodic pension costs	(972,341)	-
Adjustment to initially apply FASB Statement No. 158	-	417,043
Minimum pension liability adjustment	-	24,190
Increase in Unrestricted Net Assets	1,232,491	8,083,481
Temporarily Restricted Net Assets - Change in interest of net assets of charitable foundation	809,603	188,577
Increase in Net Assets	2,042,094	8,272,058
Net Assets - Beginning of year	24,380,090	18,828,386
Net Assets - End of year	\$ 26,422,184	\$ 27,100,444

Bell Memorial Hospital and Subsidiary

Consolidated Statement of Cash Flows

	Year Ended	
	June 30, 2008	June 30, 2007
Cash Flows from Operating Activities		
Increase in net assets	\$ 2,042,094	\$ 8,272,058
Adjustments to reconcile increase in net assets to net cash from operating activities:		
Depreciation	1,675,016	1,628,134
Net change in unrealized net gains and losses on investments	278,841	(168,540)
Realized loss (gain) on sales of investments	14,709	(94,527)
Change in beneficial interest in net assets of Bell Foundation	(809,603)	(188,577)
Contributed land	-	(2,033,000)
Pension-related changes other than net periodic pension costs	972,341	-
Adjustment to initially apply FASB No. 158	-	(417,043)
Minimum pension liability adjustment	-	(24,190)
Change in fair value of interest rate swap	939,936	-
Unusual event - Conditional asset retirement obligation	750,000	-
Provision for bad debts	3,263,024	2,663,628
Changes in assets and liabilities which provided (used) cash:		
Accounts receivable	(2,172,747)	(3,130,468)
Estimated third-party payor settlements	(932,904)	-
Inventory	(243,378)	(400,014)
Prepaid expenses and other	338	(61,654)
Accounts and construction payable	773,583	470,438
Estimated third-party payor settlements	(578,094)	552,043
Accrued expenses	402,384	(129,365)
Other liabilities	(194,097)	375,265
Net cash provided by operating activities	6,181,443	7,314,188
Cash Flows from Investing Activities		
Purchase of property and equipment	(23,929,214)	(1,463,619)
Proceeds from sale of property and equipment	22,490	-
Purchase of investments held by trustee under self-insurance arrangements	(1,590,823)	(1,003,728)
Proceeds from sales of investments held by trustee under self-insurance arrangements	1,509,398	831,754
Purchase of investments held by trustees under bond indenture	(2,688,624)	(31,459,512)
Proceeds from sales of investments held by trustee under bond indenture	19,979,245	-
Collection of note receivable from affiliate	743,099	-
Net cash used in investing activities	(5,954,429)	(33,095,105)
Cash Flows from Financing Activities		
Proceeds from the issuance of debt	3,680,000	32,048,341
Principal payments on long-term debt	(2,295,683)	(419,785)
Bond financing costs	(89,635)	(549,916)
Net cash provided by financing activities	1,294,682	31,078,640
Net Increase in Cash and Cash Equivalents	1,521,696	5,297,723
Cash and Cash Equivalents - Beginning of year	9,895,005	7,317,636
Cash and Cash Equivalents - End of year	<u>\$ 11,416,701</u>	<u>\$ 12,615,359</u>
Supplemental Cash Flow Information		
Cash paid for interest, including capitalized interest of \$1,117,416 and \$218,025 in 2008 and 2007, respectively	\$ 1,202,239	\$ 310,246
Estimated abatement future liability capitalized	750,000	-
Noncash investing activity - Contributed land	-	2,033,000
Noncash investing activity - Construction payable (property and equipment additions)	4,492,605	656,449

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies

Reporting Entity - Bell Memorial Hospital (the "Hospital"), located in Ishpeming, Michigan, is a not-for-profit hospital. The Hospital provides inpatient and outpatient health care to residents of Ishpeming, Michigan and the surrounding community. Admitting physicians are primarily practitioners in the local area. The Hospital's sole member is Superior Healthcare System, a Michigan nonprofit holding company. Bell Medical Center is a nonprofit corporation that operates physicians' offices providing services to patients and is located adjacent to Bell Memorial Hospital.

A significant portion of the Hospital's and Bell Medical Center's net patient service revenue is receivable under contractual arrangements with the Medicare, Medicaid, and Blue Cross/Blue Shield of Michigan programs.

Principles of Consolidation - The consolidated financial statements include the accounts of Bell Memorial Hospital and its wholly owned subsidiary, Bell Medical Center. Intercompany balances and transactions have been eliminated in consolidation.

Cash and Cash Equivalents - Cash and cash equivalents include temporary investments with a maturity of three months or less, excluding those amounts included in assets limited as to use.

Accounts Receivable - Accounts receivable for patients, insurance companies, and governmental agencies are based on gross charges. An allowance for uncollectible accounts is established on an aggregate basis by using historical loss rate factors applied to unpaid accounts based on aging. Loss rate factors are based on historical loss experience and adjusted for economic conditions and other trends affecting the Hospital's ability to collect outstanding amounts. Uncollectible amounts are written off against the allowance for uncollectible accounts in the period they are deemed to be uncollectible. The allowance for contractual adjustments is based on expected payment rates from payors based on current reimbursement methodologies. This amount also includes amounts received as interim payments against unpaid claims by certain payors.

Inventory - Inventory, which consists primarily of medical and pharmaceutical products, is stated at cost, determined on a first-in, first-out basis or market.

Property and Equipment - Property and equipment amounts are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Interest cost incurred on borrowed funds during the period of construction of capital assets, net of income earned on those funds, is capitalized as a component of the cost of constructing those assets.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Assets Limited as to Use - Assets limited as to use labeled "held by trustee for payment of professional liability claims" are self-insurance funds restricted by the self-insurance trust agreement for funding professional liability claims of the Hospital. Assets limited as to use labeled "held by trustee under indenture agreement" are bond proceeds restricted by the indenture agreement for funding the replacement hospital facility (see Note 5).

Investments - Investments are stated at fair market value. Investment income or loss, including realized gains and losses on investments, interest, and dividends, is included in excess of revenue over expenses unless the income or loss is restricted by donor or law. Net change in unrealized gains or losses on investments is excluded from excess of revenue over expenses.

Interest in Net Assets of Charitable Foundation - Interest in net assets of Bell Foundation (the "Foundation") reflect the future beneficial interests to be received by Bell Memorial Hospital for the construction of the replacement hospital. This interest in the future contributions from the Foundation is recorded at the fair market value of the assets in the Foundation specifically designated for the benefit of Bell Memorial Hospital and Subsidiary.

Debt Issuance Costs - Debt issuance costs were incurred by the Hospital in connection with obtaining the Series 2007 and Series 2007B bonds. These costs are amortized over the term of the related debt, commencing with the first bond principal payment.

Interest Rate Swap - The Hospital entered into an interest rate swap agreement to reduce economic risks associated with variability in cash outflows for interest required under provisions of variable rate revenue bonds. Interest rate swaps are recognized as assets or liabilities at fair value. Realized gains and losses on interest rate swaps are classified as a component of operating income and are presented as part of interest expense in the consolidated statement of changes in net assets. Unrealized changes in the fair value of the interest rate swap are recognized as part of other income, separate from operating income (see Note 7). The Hospital does not use hedge accounting for these swaps.

Professional Liability Insurance - The Hospital accrues the estimated ultimate expense, including litigation and settlement expense, for any reported and unreported incidents of potential improper professional services during the year that are in excess of applicable insurance coverage or fall within the applicable deductible amounts (see Note 11).

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Temporarily Restricted Net Assets - Temporarily restricted net assets reflect assets contributed or pledged to the Bell Foundation on behalf of the Hospital and/or its subsidiary, the use of which is restricted by the donor. Temporarily restricted net assets are restricted for the replacement hospital facility project and related property and equipment purchases. Investment earnings on temporarily restricted investments are restricted by donors for specific purposes.

Net Patient Service Revenue - Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. Management believes that it is in compliance with all applicable laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

Charity Care - The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Charity care for the years ended June 30, 2008 and 2007 totaled approximately \$685,000 and \$292,000, respectively.

Employee Pension Plan - The Hospital maintains a defined contribution plan and a defined benefit plan. Eligibility separately for each plan is for qualified employees who meet certain requirements as to age and length of service as documented in each plan. Each employee's interest is vested as specified in the plans. For the defined contribution plan, pension expense is recognized as it is earned by the employees. For the defined benefit plan, pension expense is actuarially determined (see Note 9).

Operating and Nonoperating Activities - The Hospital's primary mission is to meet the healthcare needs of its local market area through a broad range of general and specialized healthcare services including inpatient acute care, outpatient services, and other healthcare services. Activities directly associated with the furtherance of this purpose are considered to be operating activities. Other activities that result in gains or losses unrelated to the Hospital's primary mission are considered to be nonoperating and are reported in other income, consisting of unrestricted donations, investment income, and change in the fair market value of the interest rate swap.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Excess of Revenue Over Expenses - The consolidated statement of operations includes excess of revenue over expenses. Changes in unrestricted net assets, which are excluded from excess of revenue over expenses, consistent with industry practice, include contributions of long-lived assets, unrealized gains and losses on investments, and pension liability adjustments.

Contributions - The Hospital reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

Gifts of long-lived assets such as land, buildings, and equipment are reported as unrestricted support unless explicit donor stipulations specify how donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service. Donated long-lived assets are recorded at fair market value at the time of contribution.

Tax Status - The Hospital and Bell Medical Center are tax exempt under Section 501(c)(3) of the Internal Revenue Code and, accordingly, no tax provision is reflected in the consolidated financial statements.

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

Reclassifications - Certain 2007 amounts have been reclassified to conform with the 2008 presentation.

Fair Value of Financial Instruments - The fair value of financial instruments, including cash, accounts receivable, accounts payable, and debt, approximate carrying values. Investments are recorded at fair value under generally accepted accounting principles. The fair value of debt approximates carrying value because of the variable rate nature of the instrument.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Accounting for Conditional Asset Retirement Obligations - Financial Accounting Standards Board Interpretation No. 47 (FIN 47), *Accounting for Conditional Asset Retirement Obligation*, clarified when an entity is required to recognize a liability for a conditional asset retirement obligation. Management has considered FIN 47, specifically as it related to its legal obligation to report asset retirement activities, such as asbestos removed, on its existing properties. The Hospital records these obligations once there is a determinate settlement date for the asset retirement obligations and incurs the related cost once there is a final settlement cost determined to be incurred by the Hospital.

Note 2 - Patient Accounts Receivable

Accounts receivable consist of the following:

	2008	2007
Patients, insurance companies, and governmental agencies	\$ 12,416,778	\$ 12,240,083
Less:		
Allowance for uncollectible accounts	(1,792,872)	(1,458,256)
Allowance for contractual adjustments and interim payment advances	(6,824,664)	(6,126,204)
Total patient accounts receivable	3,799,242	4,655,623
Other	255,624	489,520
Total accounts receivable	\$ 4,054,866	\$ 5,145,143

The Hospital and its subsidiary grant credit without collateral to patients, most of whom are local residents and are insured under third-party payor agreements. The composition of receivables from patients and third-party payors is as follows:

	Percent	
	2008	2007
Medicare	28	35
Blue Cross/Blue Shield of Michigan	20	17
Medicaid	11	12
Commercial insurance and HMOs	20	18
Patients	21	18
Total	100	100

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 3 - Patient Service Revenue

Approximately 86 percent of the Hospital's net patient service revenue is received from the Medicare, Medicaid, and Blue Cross/Blue Shield of Michigan programs. The Hospital and its subsidiary have agreements with third-party payors that provide for reimbursement at amounts different from established rates. A summary of the basis of reimbursement with these third-party payors is as follows:

- **Medicare** - The Hospital is reimbursed as a critical access hospital by the Medicare program. Critical access hospitals receive cost reimbursement for all acute-care inpatient and most outpatient services. Other outpatient services are reimbursed on an established fee-for-service methodology.
- **Medicaid** - Inpatient, acute-care services rendered to Medicaid program beneficiaries are also paid at prospectively determined rates per discharge. Inpatient capital costs relating to Medicaid patients are paid on a cost-reimbursement method. Outpatient and physician services are reimbursed on an established fee-for-service methodology or ambulatory payment classification system.
- **Blue Cross/Blue Shield of Michigan** - Services rendered to subscribers are reimbursed as a percentage of charges subject to a limitation on the annual rate of increase.
- **Health Maintenance Organizations** - Services rendered to HMO beneficiaries are paid at predetermined rates or at a percentage of hospital charges.

Cost report settlements result from the adjustment of interim payments to final reimbursement under the Medicare, Medicaid, and Blue Cross/Blue Shield of Michigan programs that are subject to audit by fiscal intermediaries. These audits may result in changes to these estimated cost report settlement balances and will be adjusted in future periods as final settlements are determined. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Final cost report settlements increased net patient service revenue by approximately \$1,200,000 for the year ended June 30, 2008, reflecting amount settlements received for prior years in excess of previously estimated amounts. There were no significant final cost report settlements impacting net patient service revenue for the year ended June 30, 2007.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 4 - Property and Equipment

Cost of property and equipment and depreciable lives are summarized as follows.

	<u>2008</u>	<u>2007</u>	<u>Depreciable Life - Years</u>
Land	\$ 2,470,402	\$ 2,490,402	-
Buildings	17,336,435	17,332,911	20-40
Equipment	15,283,652	13,706,706	3-5
Construction in progress	<u>28,535,221</u>	<u>1,754,229</u>	-
Total cost	63,625,710	35,284,248	
Less accumulated depreciation	<u>(25,041,766)</u>	<u>(23,424,617)</u>	
Net carrying amount	<u>\$ 38,583,944</u>	<u>\$ 11,859,631</u>	

Construction in progress relates to the construction of a replacement hospital facility. The project has an estimated construction cost of \$34,000,000, which is being financed primarily through the Series 2007 and 2007B tax-exempt bonds issued by the Economic Development Corporation of the County of Marquette, Michigan (see Note 6). The replacement hospital facility was opened for operations in September 2008. The balance to finish the project was approximately \$5,000,000 at June 30, 2008. Outstanding payment on construction billings approximated \$5,600,000 and \$700,000 at June 30, 2008 and 2007, respectively.

In connection with the construction of the replacement hospital facility, the Hospital reduced its estimate of the useful lives of certain buildings and equipment that will no longer be utilized. This change had the effect of increasing depreciation expense by approximately \$450,000 for the years ended June 30, 2008 and 2007.

During 2007, the Hospital received a contribution of land valued at \$2,033,000.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 5 - Other Assets

Other assets consist of the following:

	2008	2007
Assets limited as to use:		
Funds held by trustee for payment of professional liability claims	\$ 2,123,417	\$ 2,292,849
Funds held by trustees under bond indenture	14,247,917	31,581,231
Total assets limited as to use	16,371,334	33,874,080
Less amount for payment of current liabilities	(5,608,140)	(719,077)
Total assets limited as to use - Long term	10,763,194	33,155,003
Beneficial interest in net assets of Bell Foundation	998,180	188,577
Bond issue costs	639,551	549,916
Other	263,381	256,480
Total other assets	<u>\$ 12,664,306</u>	<u>\$ 34,149,976</u>

Assets whose use is limited consist of the following investment types:

	2008	2007
Money market investments	\$ 2,882,757	\$ 15,307,049
Corporate bonds	600,342	850,110
U.S. government obligations	8,680,696	16,342,770
Municipal government obligations	2,750,000	-
Common and preferred stocks	1,457,539	1,374,151
Total investments	<u>\$ 16,371,334</u>	<u>\$ 33,874,080</u>

Investment income and change in net unrealized gains and losses on investments are reported in the consolidated statements of operations and changes in net assets as follows:

	2008	2007
Other income - Interest and dividends	\$ 488,649	\$ 491,756
Other income - Realized (losses) gains on sales of investments	(14,709)	94,527
Total	<u>\$ 473,940</u>	<u>\$ 586,283</u>
Other changes in unrestricted net assets - Change in net unrealized gains and losses on investments	<u>\$ (278,841)</u>	<u>\$ 168,540</u>

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 6 - Long-term Debt

Long-term debt at June 30, 2008 and 2007 is as follows:

	<u>2008</u>	<u>2007</u>
Notes payable to Michigan State Hospital Finance Authority	\$ 442,923	\$ 2,701,224
Adjustable Rate Demand Limited Obligation Revenue Bonds, Series 2007	32,285,000	32,285,000
Adjustable Rate Demand Limited Obligation Revenue Bonds, Series 2007B	3,700,000	-
Other	<u>16,637</u>	<u>54,019</u>
Total	36,444,560	35,040,243
Less original issue discount	310,565	290,565
Less current portion	<u>930,385</u>	<u>190,190</u>
Long-term portion	<u>\$ 35,203,610</u>	<u>\$ 34,559,488</u>

The notes payable to Michigan State Hospital Finance Authority (MSHFA) consist of three notes issued in connection with the Hospital Equipment Loan Program. The first two notes were collateralized by an irrevocable bank letter of credit, which in turn was collateralized by a second irrevocable bank letter of credit. The second irrevocable bank letter of credit was collateralized by a real estate mortgage and equipment. These notes were due in monthly installments of approximately \$24,000 through September 2014, plus interest at a variable rate of 1.20 percent. The letters of credit expire in September 2014. These two notes were paid off with the proceeds of the Series 2007B bonds during the year ended June 30, 2008.

The third note is collateralized by an irrevocable bank letter of credit. This note is due in monthly installments of approximately \$11,000 through September 2011, plus interest due at a variable rate of 2.95 percent at June 30, 2008 (3.85 percent at June 30, 2007). The letter of credit expires in September 2011.

The Adjustable Rate Demand Limited Obligation Revenue Bonds, Series 2007 and Series 2007B, issued by the Economic Development Corporation of the County of Marquette, Michigan, were issued for the purpose of constructing a replacement hospital facility, installing water and sewer connections, and to pay off the remaining balance on the notes payable to MSHFA.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 6 - Long-term Debt (Continued)

The Series 2007 bonds mature on March 1, 2033 and have a variable interest rate established by the bank on a weekly basis using the weekly London Interbank Offering Rate (LIBOR) times .67, for an effective rate of 1.65 percent at June 30, 2008 (3.56 percent at June 30, 2007). The bonds require monthly interest-only payments for the period from May 1, 2007 through February 27, 2009. The bonds require annual payments ranging from \$710,000 to \$2,125,000 beginning March 1, 2009 through March 1, 2033.

The Series 2007B bonds mature on August 1, 2032 and have a variable interest rate established by the bank on a weekly basis using the weekly LIBOR times .67, for an effective rate of 1.65 percent at June 30, 2008. The bonds require monthly interest-only payments for the period from August 1, 2007 through July 31, 2008. The bonds require annual payments ranging from \$80,000 to \$250,000 beginning August 1, 2008 through August 1, 2032.

The bonds are secured by irrevocable direct-pay letters of credit, which expire on March 15, 2010 for the 2007 Series, and on August 15, 2010 for the 2007B Series. The bonds are subject to mandatory redemption upon the expiration or termination of the letters of credit unless the existing letters of credit have been extended or an alternate letter of credit has been issued. The Series 2007 and Series 2007B bonds are also guaranteed by the Hospital's sole member, Superior Healthcare System.

The variable rate Series 2007 and Series 2007B Bonds described above are remarketed on a weekly basis. Should the remarketing agent be unable to remarket the bonds and notes based on its best efforts, the bonds and notes would be "put" back to the trustee, who would draw down on the letters of credit to pay down the Series 2007 and Series 2007B Bonds.

In connection with the above note payables to the MSHFA, the Hospital has agreed to certain financial covenants relating to debt service coverage, additional indebtedness, minimum cash requirements, minimum unrestricted net asset balance, and various other operational covenants.

In connection with the issuance of the irrevocable direct-pay letter of credit and related Series 2007 and 2007B Bonds, the Hospital has agreed to certain financial covenants relating to debt service coverage, days cash on hand, aging of accounts receivable, and various other operational covenants.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 6 - Long-term Debt (Continued)

Minimum principal payments on long-term debt to maturity for the next five years are as follows:

2009	\$ 930,385
2010	973,820
2011	1,030,355
2012	895,000
2013	945,000
Thereafter	<u>31,670,000</u>
Total	<u>\$ 36,444,560</u>

Note 7 - Interest Rate Swap Agreement

The Hospital has entered into interest rate swaps of its Adjustable Rate Demand Limited Obligation Revenue Bonds, Series 2007 and 2007B. The Series 2007 Bonds' interest rate swap is in the notional amounts as detailed in the table noted below. The Series 2007B Bonds' interest rate swap is in the amount of the outstanding issuance. The Hospital has entered into these interest rate swaps to reduce the impact of changes in the interest rate on its variable rate long-term debt.

The effective date of the swap is June 1, 2007, and the swap agreement matures on March 1, 2017 for the Series 2007 Bonds. The effective date on the swap is September 1, 2007, and the swap agreement matures on August 1, 2018 for the 2007B Bonds. The effect of the swaps was to effectively change the Hospital's variable interest rate on bonds to a synthetic fixed rate of 3.5 percent and 3.665 percent for the Series 2007 and 2007B, respectively. Due to decreasing interest rates, at June 30, 2008, the swaps had a negative fair value of approximately \$940,000 (see Note 8). The swap's counterparty is rated "Aa2" by Moody's, "A+" by Standard and Poor's, and "AA-" by Fitch. The Hospital or counterparty may terminate the interest rate swap agreement if either party fails to perform under the terms of a standard ISDA Master Agreement as amended. If terminated, the Hospital has the option to enter into a new interest rate swap agreement with another counterparty or to convert its variable rate bonds into fixed rate bonds. However, the Hospital does not anticipate nonperformance by the counterparties.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 7 - Interest Rate Swap Agreement (Continued)

The notional amounts for each year for the Series 2007 Bonds, for which the fixed rate will apply under the interest rate swap agreement, are as follows:

	Notional Amounts
Effective date	\$ 21,213,750
March 1, 2009 - February 28, 2010	20,681,250
March 1, 2010 - February 28, 2011	20,126,250
March 1, 2011 - February 28, 2012	19,545,000
March 1, 2012 - February 28, 2013	18,941,250
March 1, 2013 - February 28, 2014	18,303,750
March 1, 2014 - February 28, 2015	17,640,000
March 1, 2015 - February 28, 2016	16,942,500
March 1, 2016 - March 1, 2017	16,215,000

Note 8 - Other Liabilities

The detail of other liabilities is as follows:

	2008	2007
Accrued pension cost (Note 9)	\$ 980,985	\$ 141,548
Accrued professional liability claims (Note 11)	738,472	799,665
Fair market value of interest rate swap agreement	939,936	-
Total other liabilities	<u>\$ 2,659,393</u>	<u>\$ 941,213</u>

Note 9 - Pension and Other Postretirement Benefit Plans

The Hospital has two noncontributory defined benefit pension plans that together cover substantially all employees who meet minimum service and age requirements.

Union employees are covered under a defined contribution plan that is administered under a collective bargaining arrangement. Under the defined contribution plan, the Hospital has no liability for current or prior service costs other than to pay fixed amounts per hour worked by eligible employees.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 9 - Pension and Other Postretirement Benefit Plans (Continued)

Effective November 1, 2005, nonunion employees are covered under a defined contribution plan. For those nonunion employees who were not eligible for the defined benefit plan, the plan allows for employee contributions and requires a matching contribution equal to employee deferrals, up to 5.5 percent. For those nonunion employees who were eligible for the defined benefit plan, the plan allows for employee contributions and requires nonelective, monthly deferrals ranging from 7.0 percent to 10.0 percent, based on the employee's period of service as of November 1, 2005. The Hospital has two noncontributory defined benefit pension plans that together cover substantially all employees who meet minimum service and age requirements.

Pension expense under the defined contribution plans was approximately \$974,000 and \$912,000 for the years ended June 30, 2008 and 2007, respectively.

Non-union employees are covered under a defined benefit plan that pays benefits based on, among other things, an employee's years of service and level of compensation. Effective November 1, 2005, this plan was frozen by the Hospital and participants no longer are accruing benefits under this plan. The funding policy of the Hospital is to contribute annually an amount in compliance with the requirements of the Employee Retirement Income Security Act of 1974 (ERISA). Contributions were intended to provide not only for benefits attributed to services to date, but also for those expected to be earned in the future.

Obligations and Funded Status

At June 30	Pension Benefits	
	2008	2007
Change in Benefit Obligation		
Benefit obligation at beginning of year	\$ 8,390,597	\$ 8,010,737
Interest cost	515,100	491,626
Actuarial (gain) loss	(264,868)	137,882
Benefits paid	<u>(268,709)</u>	<u>(249,648)</u>
Benefit obligation at end of year	8,372,120	8,390,597
Change in Plan Assets		
Fair value of plan assets at beginning of year	8,249,049	7,343,667
Actual return on plan assets	(589,205)	1,155,030
Benefits paid	<u>(268,709)</u>	<u>(249,648)</u>
Fair value of plan assets at end of year	<u>7,391,135</u>	<u>8,249,049</u>
Funded status at end of year	<u>\$ (980,985)</u>	<u>\$ (141,548)</u>

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 9 - Pension and Other Postretirement Benefit Plans (Continued)

Amounts recognized in the balance sheet consist of the following:

	Pension Benefits	
	2008	2007
Noncurrent liabilities (Note 8)	\$ (980,985)	\$ (141,548)

The accumulated benefit obligation for all defined benefit pension plans was \$8,372,120 and \$8,390,597 at June 30, 2008 and 2007, respectively.

Components of Net Periodic Benefit Cost and Other Amounts Recognized in Other Comprehensive Income

	2008	2007
Net Periodic Benefit Cost		
Interest cost	\$ 515,100	\$ 491,626
Expected return on plan assets	(648,004)	(575,915)
Total net periodic benefit cost	\$ (132,904)	\$ (84,289)

Amounts Recognized in Other Comprehensive Income

Total recognized in net periodic benefit cost and other comprehensive income	\$ 972,341	\$ (441,233)
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Assumptions

Weighted Average Assumptions Used to Determine Benefit Obligations at June 30

	Pension Benefits	
	2008	2007
Discount rate	6.50 %	6.25 %

Weighted Average Assumptions Used to Determine Net Periodic Benefit Cost for Years Ended June 30

	Pension Benefits	
	2008	2007
Discount rate	6.25 %	6.25 %
Expected long-term return on plan assets	8.00	8.00

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 9 - Pension and Other Postretirement Benefit Plans (Continued)

In selecting the expected long-term rate of return on assets, the Hospital considered the average rate of earnings expected on the funds invested or to be invested to provide for the benefits of the plan. This included considering the allocation of trust assets and the expected returns likely to be earned over the life of the plan. The Hospital's historical rate of return on a fiscal year basis averaged approximately 8.00 percent per annum for the 10-year period ended June 30, 2008.

Plan Assets

Asset Category	June 30	
	2008	2007
Equity securities	69 %	60 %
Debt securities	28	37
Other	3	3
Total	100 %	100 %

The goals of the investment program are to fully fund the obligation to pay retirement benefits in accordance with the plan documents. Pension funds will be invested in growth-oriented securities up to 65 percent of equities.

Contributions

No contributions are required for 2008 and also were not required for 2007 under the minimum funding requirements of ERISA, as the plan is frozen.

Estimated Future Benefit Payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	Pension Benefits
2009	\$ 294,163
2010	314,705
2011	330,621
2012	350,554
2013	384,089
2014-2018	2,685,343

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 10 - Change in Accounting Principle - Adoption of FAS 158

During the year ended June 30, 2007, the Hospital adopted the provisions of FASB Statement No. 158 (FAS 158), *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, an amendment of FASB Statements Nos. 87, 88, 106, and 132(R). FAS 158 changes the accounting for defined benefit pension and postretirement plans by requiring that the full over- or underfunded status of a defined benefit plan be recognized as an asset or liability. For defined benefit pension plans, the funded status of the plan is the difference between the projected benefit obligation (PBO) and the fair value of plan assets.

The adoption of FAS 158 as of June 30, 2007 resulted in an increase to unrestricted net assets in the amount of \$417,043.

The incremental effect of applying FAS 158 on individual line items in the consolidated balance sheet as of June 30, 2007 is as follows:

	Before Application of FAS 158	Adjustments	After Application of FAS 158
Liability for pension benefits	\$ 558,591	\$ (417,043)	\$ 141,548
Unrestricted net assets	23,774,470	417,043	24,191,513

Note 11 - Professional Liability Insurance

The Hospital is insured against potential professional liability claims under a claims-made policy, whereby only the claims reported to the insurance carrier during the policy period are covered regardless of when the incident giving rise to the claim occurred. Under the terms of the policy, the Hospital bears the risk of the ultimate costs of any individual and aggregate claims exceeding the policy limits for claims asserted in the policy year. The Hospital has accrued the estimated outstanding claims as of June 30, 2008 and 2007 (see Note 8).

Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during the claims-made term, but reported subsequently, will be uninsured.

Bell Memorial Hospital and Subsidiary

Notes to Consolidated Financial Statements June 30, 2008 and 2007

Note 12 - Functional Expenses

The Hospital is a general acute care facility that provides inpatient and outpatient health-care services to patients in Ishpeming, Michigan and surrounding communities. Expenses related to providing these services for the years ended June 30, 2008 and 2007 are as follows:

	<u>2008</u>	<u>2007</u>
Healthcare services	\$ 36,213,963	\$ 32,328,404
General and administrative	<u>8,218,075</u>	<u>6,703,184</u>
Total	<u>\$ 44,432,038</u>	<u>\$ 39,031,588</u>

Note 13 - Conditional Asset Retirement Obligations

The Hospital has an obligation related to the removal of asbestos within the Hospital's floor tiles and pipe insulation upon demolition or abandonment of the Hospital's current facility, which was vacated in September 2008. As of June 30, 2008, the Hospital has not determined whether the current facility will be sold or donated to an outside party, or who will be responsible for the cost of the abatement. The Hospital has determined to record the estimated cost of the abatement based on a 2006 survey as a conditional liability. The Hospital has recorded a liability of \$750,000 related to the potential costs associated with the asbestos abatement.

Additional Information



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To the Board of Directors
Bell Memorial Hospital and Subsidiary

We have audited the consolidated financial statements of Bell Memorial Hospital and Subsidiary as of June 30, 2008 and 2007. Our audits were made for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The accompanying consolidating balance sheet and statement of operations information is presented for the purpose of additional analysis of the consolidated financial statements rather than to present the financial position, results of operations, and cash flows of the individual entities and is not a required part of the basic consolidated financial statements. The consolidating information has been subjected to the procedures applied in the audits of the consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

Plante & Moran, PLLC

December 3, 2008

Bell Memorial Hospital and Subsidiary

Consolidating Balance Sheet June 30, 2008

	Bell Memorial Hospital	Bell Medical Center	Eliminating Entries	Total
Assets				
Current Assets				
Cash and cash equivalents	\$ 11,416,701	\$ -	\$ -	\$ 11,416,701
Accounts receivable	2,778,179	1,276,687	-	4,054,866
Estimated third-party payor settlements	1,232,904	-	-	1,232,904
Assets limited as to use	5,608,140	-	-	5,608,140
Inventory	1,458,103	32,817	-	1,490,920
Prepaid expenses and other	221,475	24,105	-	245,580
Total current assets	22,715,502	1,333,609	-	24,049,111
Property and Equipment - Net	38,287,151	296,793	-	38,583,944
Other Assets	12,658,099	6,207	-	12,664,306
Total assets	<u>\$ 73,660,752</u>	<u>\$ 1,636,609</u>	<u>\$ -</u>	<u>\$ 75,297,361</u>
Liabilities and Net Assets				
Current Liabilities				
Current portion of long-term debt	\$ 913,861	\$ 16,524	\$ -	\$ 930,385
Accounts payable	1,387,522	203,836	-	1,591,358
Construction payables	5,608,140	-	-	5,608,140
Accrued liabilities	2,305,718	576,573	-	2,882,291
Total current liabilities	10,215,241	796,933	-	11,012,174
Long-term Debt - Net of current portion	35,203,610	-	-	35,203,610
Other Liabilities	2,659,393	-	-	2,659,393
Total liabilities	48,078,244	796,933	-	48,875,177
Net Assets				
Unrestricted	24,584,328	839,676	-	25,424,004
Temporarily restricted	998,180	-	-	998,180
Total liabilities and net assets	<u>\$ 73,660,752</u>	<u>\$ 1,636,609</u>	<u>\$ -</u>	<u>\$ 75,297,361</u>

Bell Memorial Hospital and Subsidiary

Consolidating Statement of Operations Year Ended June 30, 2008

	Bell Memorial Hospital	Bell Medical Center	Eliminating Entries	Total
Unrestricted Revenue, Gains, and Other Support				
Net patient service revenue	\$ 38,436,901	\$ 8,635,773	\$ -	\$ 47,072,674
Other	1,001,118	39,218	-	1,040,336
Total unrestricted revenue, gains, and other support	39,438,019	8,674,991	-	48,113,010
Expenses				
Salaries and wages	13,158,042	7,106,858	-	20,264,900
Employee benefits	3,871,140	876,575	-	4,747,715
Supplies	5,208,561	542,908	-	5,751,469
Purchased services	1,848,896	1,547,706	-	3,396,602
Insurance	383,488	156,928	-	540,416
Other healthcare expenses	4,270,568	437,505	-	4,708,073
Depreciation and amortization	1,459,400	215,616	-	1,675,016
Provision for bad debts	2,582,899	680,125	-	3,263,024
Interest expense	44,296	40,527	-	84,823
Total expenses	32,827,290	11,604,748	-	44,432,038
Operating Income (Loss)	6,610,729	(2,929,757)	-	3,680,972
Other Income (Loss)				
Investment income	488,649	-	-	488,649
Contributions	10,406	8,291	-	18,697
Realized loss on sales of investments	(14,709)	-	-	(14,709)
Change in fair value of interest swap agreements	(939,936)	-	-	(939,936)
Total other income (loss)	(455,590)	8,291	-	(447,299)
Excess of Revenue Over (Under) Expenses Before Unusual Event	6,155,139	(2,921,466)	-	3,233,673
Unusual Event - Conditional asset retirement obligation	(750,000)	-	-	(750,000)
Excess of Revenue Over (Under) Expenses	5,405,139	(2,921,466)	-	2,483,673
Transfer (to) from Affiliate	(3,068,498)	3,068,498	-	-
Change in Net Unrealized Gains and Losses on Investments	(278,841)	-	-	(278,841)
Pension-related Changes Other Than Net Periodic Pension Costs	(972,341)	-	-	(972,341)
Increase in Unrestricted Net Assets	<u>\$ 1,085,459</u>	<u>\$ 147,032</u>	<u>\$ -</u>	<u>\$ 1,232,491</u>