

Superior Healthcare System and Affiliates

Ishpeming, Michigan

Consolidated Financial Statements and Supplementary Information

Years Ended June 30, 2012 and 2011

Superior Healthcare System and Affiliates

Consolidated Financial Statements and Supplementary Information

Years Ended June 30, 2012 and 2011

Table of Contents

Independent Auditor's Report	1
Financial Statements	
Consolidated Balance Sheets	2
Consolidated Statements of Operations.....	3
Consolidated Statements of Changes in Net Assets	4
Consolidated Statements of Cash Flows	5
Notes to Consolidated Financial Statements	7
Independent Auditor's Report on Supplementary Information	39
Supplementary Information	
Consolidating Balance Sheets	40
Consolidating Statements of Operations	44
Consolidating Statements of Changes in Net Assets.....	46



Independent Auditor's Report

Board of Directors
Superior Healthcare System
Ishpeming, Michigan

We have audited the accompanying consolidated balance sheet of Superior Healthcare System and Affiliates (the "Organization") as of June 30, 2012, and the related consolidated statements of operations, changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in 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 audit provides a reasonable basis for our opinion.

In our opinion, the 2012 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Superior Healthcare System and Affiliates as of June 30, 2012, and the results of their operations, changes in their net assets, and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States.

The June 30, 2011, consolidated financial statements were compiled by us; thus we did not audit or review the 2011 consolidated financial statements and, accordingly, express no opinion or other form of assurance on them.

Wipfli LLP

(report date), 2012
Green Bay, Wisconsin

Superior Healthcare System and Affiliates

Consolidated Balance Sheets

June 30, 2012 and 2011

<i>Assets</i>	2012	2011
Current assets:		
Cash and cash equivalents	\$ 9,980,376	\$ 10,518,318
Accounts receivable - Net	7,184,928	6,203,345
Inventories	1,430,671	1,563,414
Prepaid expenses and other	470,961	420,730
Amounts due from third-party reimbursement programs	1,099,217	3,027
Total current assets	20,166,153	18,708,834
Property and equipment - Net	40,602,107	43,120,875
Investments	62,225	49,714
Assets limited as to use	202,902	138,748
Other assets:		
Unamortized bond issue costs	237,204	251,877
Notes receivable	322,366	393,323
Investments in unconsolidated affiliates	1,048,443	933,888
Other	203,386	153,243
Total other assets	1,811,399	1,732,331
TOTAL ASSETS	\$ 62,844,786	\$ 63,750,502

<i>Liabilities and Net Assets</i>	2012	2011
Current liabilities:		
Current maturities of long-term debt	\$ 958,421	\$ 895,608
Current portion of obligations under capital leases	68,325	64,519
Current portion of deferred revenue	410,102	0
Accounts payable	1,094,545	1,351,112
Accrued and other liabilities	3,882,870	2,844,596
Total current liabilities	6,414,263	5,155,835
Long-term liabilities:		
Long-term debt - Less current maturities	31,436,615	32,380,149
Obligations under capital leases - Less current portion	75,554	143,879
Deferred revenue	410,102	0
Interest rate swap agreements	2,967,264	2,477,511
Pension liability	4,901,945	2,507,945
Other liabilities	425,436	1,300,000
Total long-term liabilities	40,216,916	38,809,484
Total liabilities	46,631,179	43,965,319
Net assets:		
Unrestricted	16,010,705	19,646,435
Temporarily restricted	202,902	138,748
Total net assets	16,213,607	19,785,183
TOTAL LIABILITIES AND NET ASSETS	\$ 62,844,786	\$ 63,750,502

Superior Healthcare System and Affiliates

Consolidated Statements of Operations

Years Ended June 30, 2012 and 2011

	2012	2011
Revenue:		
Patient service revenue	\$ 104,694,247	\$ 95,216,722
Revenue deductions	(54,334,660)	(46,199,141)
Net patient service revenue	50,359,587	49,017,581
Other revenue	7,240,758	5,223,756
Total revenue	57,600,345	54,241,337
Expenses:		
Salaries and wages	26,295,946	25,786,160
Employee benefits	6,604,235	6,093,725
Supplies	6,799,750	6,626,115
Purchased services	2,736,831	3,343,872
Insurance	382,637	568,517
Other health care expenses	6,855,248	5,502,796
Depreciation and amortization	3,065,986	3,129,721
Provision for bad debts	4,465,684	3,556,327
Interest	2,143,561	1,468,303
Total expenses	59,349,878	56,075,536
Loss from operations	(1,749,533)	(1,834,199)
Other income (deductions):		
Investment income	103,312	968,738
Contributions	48,106	40,539
Provision (credit) for income taxes	1,546	(160)
Gain (loss) on disposal of property and equipment	14,171	(91,932)
Change in net unrealized gains and losses on investments - Trading securities	81,995	(19,207)
Change in equity investments in unconsolidated affiliates	114,555	760,615
Change in fair value of interest rate swap agreements	(489,753)	357,265
Excess (deficiency) of revenue over expenses	(1,875,601)	181,659
Other changes in unrestricted net assets:		
Pension-related changes other than net periodic pension cost	(2,394,000)	1,447,680
Net assets released from restrictions	633,871	1,322,877
Increase (decrease) in unrestricted net assets	\$ (3,635,730)	\$ 2,952,216

See accompanying notes to consolidated financial statements.

Superior Healthcare System and Affiliates

Consolidated Statements of Changes in Net Assets

Years Ended June 30, 2012 and 2011

	2012	2011
Unrestricted net assets:		
Excess (deficiency) of revenue over expenses	\$ (1,875,601)	\$ 181,659
Pension-related changes other than net periodic pension cost	(2,394,000)	1,447,680
Net assets released from restrictions	633,871	1,322,877
Increase (decrease) in unrestricted net assets	(3,635,730)	2,952,216
Temporarily restricted net assets:		
Contributions	698,025	811,439
Net assets released from restrictions	(633,871)	(1,322,877)
Increase (decrease) in temporarily restricted net assets	64,154	(511,438)
Change in net assets	(3,571,576)	2,440,778
Net assets at beginning	19,785,183	17,344,405
Net assets at end	\$ 16,213,607	\$ 19,785,183

Superior Healthcare System and Affiliates

Consolidated Statements of Cash Flows

Years Ended June 30, 2012 and 2011

	2012	2011
Increase (decrease) in cash and cash equivalents:		
Change in net assets	\$ (3,571,576)	\$ 2,440,778
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	3,050,458	3,113,675
Amortization of bond issue discount	15,528	16,046
Change in net unrealized gains and losses on investments - Trading securities	(81,995)	19,207
Net realized gain on sales of investments	(2,602)	(408,553)
Pension-related changes other than net periodic pension cost	2,394,000	(1,447,680)
Change in fair value of interest rate swap agreements	489,753	(357,265)
Provision for bad debts	4,465,684	3,556,327
(Gain) loss on disposal of property and equipment	(14,171)	91,932
Change in equity investments in unconsolidated affiliates	(114,555)	(760,615)
Changes in operating assets and liabilities:		
Accounts receivable	(5,447,267)	(2,867,942)
Inventories	132,743	94,390
Prepaid expenses and other	(50,231)	(91,771)
Amounts due from third-party reimbursement programs	(1,096,190)	(3,027)
Other assets	(50,143)	(69,178)
Accounts payable	(256,567)	(687,916)
Amounts due to third-party reimbursement programs	0	(1,025,437)
Accrued and other liabilities	1,038,274	107,418
Deferred revenue	820,204	0
Other liabilities	(874,564)	(50,000)
Total adjustments	4,418,359	(770,389)
Net cash provided by operating activities	846,783	1,670,389

Superior Healthcare System and Affiliates

Consolidated Statements of Cash Flows (Continued)

Years Ended June 30, 2012 and 2011

	2012	2011
Cash flows from investing activities:		
Capital expenditures	\$ (533,646)	\$ (539,213)
Proceeds from property and equipment disposals	30,800	188,784
Purchase of investments	0	(303,085)
Proceeds from sales of investments	7,932	3,164,218
Issuance of note receivable	(31,759)	(449,088)
Collection of note receivable	102,716	57,431
Net cash provided by (used in) investing activities	(423,957)	2,119,047
Cash flows from financing activities:		
Principal payments on long-term debt	(896,249)	(1,034,476)
Principal payments on obligations under capital leases	(64,519)	(46,642)
Net cash used in financing activities	(960,768)	(1,081,118)
Net increase (decrease) in cash and cash equivalents	(537,942)	2,708,318
Cash and cash equivalents at beginning	10,518,318	7,810,000
Cash and cash equivalents at end	\$ 9,980,376	\$ 10,518,318
Supplemental cash flow information:		
Cash paid for interest	\$ 2,128,033	\$ 1,576,469
Noncash financing and investing activities:		
Acquisition of property and equipment under capital lease obligations	\$ 0	\$ 140,247

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 Summary of Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the assets, liabilities, net assets, and operating activities of Superior Healthcare System and the following related entities controlled by Superior Healthcare System (collectively the "Organization"):

- Bell Memorial Hospital (the "Hospital")
- Bell Medical Center
- Bell Foundation
- Superior Enterprises

All significant intercompany accounts and transactions have been eliminated in preparing the accompanying consolidated financial statements.

The Entities

Superior Healthcare System, a nonprofit, nonstock corporation serves as the parent corporation for the affiliated entities and supports the operations of its affiliates.

The Hospital is a nonprofit, nonstock corporation that operates a 25-bed acute care facility. The Hospital provides comprehensive inpatient, outpatient, and emergency services to residents of Ishpeming, Michigan, and the surrounding areas. The Hospital's sole member is Superior Healthcare System.

Bell Medical Center is a nonprofit, nonstock corporation that operates physicians' offices and provides physician clinic services. Bell Medical Center's sole member is Superior Healthcare System. The Hospital provides financial support for Bell Medical Center's operations and has the ability to determine direction and assign various health care-related functions to Bell Medical Center.

Bell Foundation is a nonprofit, nonstock corporation that raises funds for specific projects or needs, administers and invests funds, and disburses payments to and for the benefit of tax-exempt organizations at the discretion of its Board of Directors.

Superior Enterprises is a for-profit organization that provides therapy services to organizations in Ishpeming, Michigan, and surrounding areas.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies** (Continued)

Financial Statement Presentation

The Organization follows accounting standards contained in the Financial Accounting Standards Board Accounting Standards Codification (ASC). The ASC is the single source of authoritative accounting principles generally accepted in the United States (GAAP) to be applied to nongovernmental entities in the preparation of financial statements in conformity with GAAP.

Use of Estimates in Preparation of Financial Statements

The preparation of the accompanying consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that directly affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates may also affect the reported amounts of revenue and expenses during the reporting period. Actual results may differ from these estimates.

Cash Equivalents

The Organization considers all highly liquid debt instruments with an original maturity of three months or less to be cash equivalents, excluding amounts whose use is limited or restricted.

Accounts Receivable and Credit Policy

Accounts receivable are uncollateralized patient obligations that are stated at the amount management expects to collect from outstanding balances. These obligations are primarily from local residents, most of whom are insured under third-party payor agreements. The Organization bills third-party payors on the patients' behalf, or if a patient is uninsured, the patient is billed directly. Once claims are settled with the primary payor, any secondary insurance is billed, and patients are billed for copay and deductible amounts that are the patients' responsibility. Payments on accounts receivable are applied to the specific claim identified on the remittance advice or statement. The Organization does not have a policy to charge interest on past due accounts.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies** (Continued)

Accounts Receivable and Credit Policy (Continued)

The carrying amounts of accounts receivable are reduced by allowances that reflect management's best estimate of the amounts that will not be collected. Management provides for contractual adjustments under terms of third-party reimbursement agreements through a reduction of gross revenue and a credit to accounts receivable. In addition, management provides for probable uncollectible amounts, primarily uninsured patients and amounts patients are personally responsible for, through a charge to operations and a credit to a valuation allowance based upon its assessment of historical collection likelihood and the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable.

In evaluating the collectability of accounts receivable, the Organization analyzes past results and identifies trends for each major payor source of revenue for the purpose of estimating the appropriate amounts of the allowance for doubtful accounts and the provision for bad debts. Data in each major payor source is regularly reviewed to evaluate the adequacy of the allowance for doubtful accounts. Specifically, for receivables relating to services provided to patients having third-party coverage, an allowance for doubtful accounts and a corresponding provision for bad debts are established based on historical write-off percentages; for receivables relating to self-pay patients, a provision for bad debts is made in the period services are rendered based on experience indicating the inability or unwillingness of patients to pay amounts for which they are financially responsible.

Inventories

Inventories of supplies are valued at the lower of cost, determined on the first-in, first-out method, or market.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 Summary of Significant Accounting Policies (Continued)

Investments

Investments are measured at fair value in the accompanying consolidated balance sheets. Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in the excess (deficiency) of revenue over expenses unless the income is restricted by donor or law. Unrealized gains and losses on investments are excluded from the excess (deficiency) of revenue over expenses unless the investments are trading securities. Realized gains and losses are determined by specific identification and charged to operations.

Assets Limited as to Use

Assets limited as to use include cash and investments contributed for specific purposes by donors.

Investments in Unconsolidated Affiliates

Investments in unconsolidated affiliates are accounted for using the equity method.

Fair Value Measurements

The Organization measures fair value of its financial instruments using a three-tier hierarchy, which prioritizes the inputs used in measuring fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

- Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Organization has the ability to access.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 Summary of Significant Accounting Policies (Continued)

Fair Value Measurements (Continued)

Level 2 Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets.
- Quoted prices for identical or similar assets or liabilities in inactive markets.
- Inputs other than quoted prices that are observable for the asset or liability.
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 Summary of Significant Accounting Policies (Continued)

Property, Equipment, and Depreciation

Property and equipment acquisitions are recorded at cost or, if donated, at fair value at the date of donation. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Property and equipment under capital leases are amortized on the straight-line method over the shorter period of the lease term or the estimated economic life. Such amortization expense is included with depreciation expense. Estimated useful lives range from 10 to 20 years for land improvements, 5 to 40 years for buildings and improvements, and 3 to 20 years for equipment. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support and are excluded from the excess (deficiency) of revenue over expenses unless explicit donor stipulations specify how the 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.

Impairment

The Organization reviews its property and equipment periodically to determine potential impairment by comparing the carrying value of the property and equipment with the estimated future net discounted cash flows expected to result from the use of the assets, including cash flows from disposition. Should the sum of the expected future net cash flows be less than the carrying value, the Organization would recognize an impairment loss at that time. No impairment loss was recognized in 2012 or 2011.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Unamortized Bond Issue Costs

Bond issue costs related to issuance of long-term debt are being amortized over the life of the related debt using the straight-line method.

Asset Retirement Obligations

ASC Topic 410-20, *Asset Retirement Obligations*, clarifies when an entity is required to recognize a liability for a conditional asset retirement obligation. The Organization has considered ASC Topic 410-20, specifically as it relates to its legal obligation to perform asset retirement activities, such as asbestos removal, on its existing properties. During 2009, the Hospital entered into an agreement with a local developer to sell its old facility for \$1. In connection with this agreement, the Hospital is obligated for an amount not to exceed \$825,000 for the removal of asbestos within the old facility. At June 30, 2012 and 2011, the Hospital has a recorded liability of \$500,000 and \$700,000, respectively, which is the balance remaining under this agreement. The liability is included in accrued and other liabilities in 2012 and other liabilities in 2011 in the accompanying consolidated balance sheets.

Temporarily Restricted Net Assets

Temporarily restricted net assets are those whose use by the Organization has been limited by donors to a specific time period or purpose.

Interest Rate Swap Agreements

The Organization entered into interest rate swap agreements 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 on the accompanying consolidated statements of operations. Unrealized changes in the fair value of the interest rate swaps are recognized as part of other income, separate from operating income. The Organization does not use hedge accounting for these interest rate swap agreements.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 Summary of Significant Accounting Policies (Continued)

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 are adjusted in future periods as final settlements are determined.

Excess (Deficiency) of Revenue Over Expenses

The accompanying consolidated statements of operations and changes in net assets include excess (deficiency) of revenue over expenses, which is considered the operating indicator. Changes in unrestricted net assets that are excluded from the operating indicator include unrealized gains and losses on investments other than trading securities, contributions of long-lived assets, including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets, pension-related changes other than net periodic cost, and transfers to (from) related organizations other than for goods and services.

Charity Care

The Organization provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Organization does not pursue collection of amounts determined to qualify as charity care, they are not included in net patient service revenue in the accompanying consolidated statements of operations.

The estimated cost of providing care to patients under the Organization's charity care policy is calculated by multiplying the Organization's ratio of cost to gross charges by the gross uncompensated charges associated with providing charity care.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Donor-Restricted Gifts

Unconditional promises to give cash and other assets to the Organization are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is deemed unconditional. The gifts are reported as either temporarily or permanently 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 as unrestricted net assets and reported in the accompanying consolidated statements of operations and changes in net assets 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 statements of operations.

Advertising Costs

The Organization expenses advertising costs as incurred.

Unemployment Compensation

The Organization has elected the reimbursement method to finance the cost of unemployment compensation benefits. Unemployment compensation expense is charged to operating expense when paid or when the amount of the claims can be estimated. The Organization contributes to a state unemployment trust held by a third party.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 **Summary of Significant Accounting Policies (Continued)**

Income Taxes

The Hospital, Bell Medical Center, and Bell Foundation are nonprofit corporations as described in Section 501(c)(3) of the Internal Revenue Code (the "Code") and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. These entities are also exempt from state income taxes on related income.

Superior Enterprises is a for-profit entity. The accompanying consolidated statements of operations include a provision/credit for income taxes. Deferred tax assets and liabilities related to these entities are not significant.

In order to account for any uncertain tax positions, the Organization determines whether it is more likely than not that a tax position will be sustained upon examination of the technical merits of the position, assuming the taxing authority has full knowledge of all information. If the tax position does not meet the more-likely-than-not recognition threshold, the benefit of that position is not recognized in the consolidated financial statements.

The Organization recorded no assets or liabilities for uncertain tax positions or unrecognized tax benefits in 2012 and 2011. Federal income tax returns for the years ended 2009 and beyond remain subject to examination by the Internal Revenue Service.

Electronic Health Record Incentive Funding

The American Recovery and Reinvestment Act of 2009 (ARRA) provides for incentive payments under the Medicare and Medicaid programs for certain hospitals and physician practices that demonstrate meaningful use of certified electronic health record (EHR) technology. The ARRA provisions, collectively referred to as the Health Information Technology for Economic and Clinical Health Act, are intended to promote the adoption and meaningful use of health information technology and qualified EHR technology.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 Summary of Significant Accounting Policies (Continued)

Electronic Health Record Incentive Funding (Continued)

The Hospital recognizes revenue for EHR incentive payments when there is reasonable assurance that the Hospital will meet the conditions of the program, primarily demonstrating meaningful use of certified EHR technology for the applicable period. The demonstration of meaningful use is based on meeting a series of objectives. Meeting the series of objectives in order to demonstrate meaningful use becomes progressively more stringent as its implementation is phased in through stages as outlined by the Centers for Medicare & Medicaid Services (CMS).

Amounts recognized under the Medicare and Medicaid EHR incentive programs are based, in part, on management's best estimates of cost report data, which is subject to audit by fiscal intermediaries and, accordingly, amounts recognized are subject to change. In addition, the Hospital's attestation of its compliance with the meaningful use criteria is subject to audit by the federal government or its designee.

The Hospital has deferred recognition of the payment received under the Medicare EHR program. The deferred revenue is being amortized and recognized as revenue over three years, which is the period the software would have been depreciated and cost reimbursed through the cost report.

For the year ended June 30, 2012, the Hospital amortized \$410,102 of deferred revenue from the Medicare EHR incentive program, which is included in other revenue in the accompanying consolidated statement of operations. As of June 30, 2012, deferred revenue from the Medicare EHR incentive program totaled \$820,204.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 1 Summary of Significant Accounting Policies (Continued)

New Accounting Pronouncements

In July 2011, the FASB issued Accounting Standards Update (ASU) No. 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and Allowance for Doubtful Accounts for Certain Health Care Entities*. This ASU amends ASC Topic 954 and requires health care entities to change the presentation of their statement of operations by reclassifying the provision for bad debts associated with patient service revenue from an operating expense to a deduction from patient service revenue. Entities are also required to enhance disclosures about their policies for recognizing revenue and assessing bad debts. In addition, this guidance requires disclosure of qualitative and quantitative information about changes in the allowance for doubtful accounts. The guidance in this ASU is effective for the Organization's year ending June 30, 2013, with early adoption permitted.

In August 2010, the FASB issued ASU No. 2010-23, *Measuring Charity Care for Disclosure*. This ASU amends ASC Topic 954 and requires entities to use cost as the measurement basis for charity care disclosures, including both direct and indirect costs. Entities are also required to disclose the method used to determine these costs, such as directly from a costing system or through an estimation process. The guidance in this ASU was adopted by the Organization for the year ended June 30, 2012.

Subsequent Events

Subsequent events have been evaluated through (report date), 2012, which is the date the consolidated financial statements were issued. See Note 9 for specific subsequent events related to the Series 2007A Limited Obligation Revenue Bonds.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 2 Reimbursement Arrangements With Third-Party Payors

The Organization has agreements with third-party payors that provide for reimbursement at amounts that vary from its established rates. A summary of the basis of reimbursement with major third-party payors follows:

- *Medicare* - The Hospital is certified as a critical access hospital with reimbursement based on cost for inpatient, outpatient, and rural health clinic services. Professional services provided by physicians and other clinicians are reimbursed based on prospectively determined fee schedules.
- *Medicaid* - Inpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based upon clinical, diagnostic, and other factors. In addition, capital-related costs related to inpatient services are reimbursed under a cost methodology. Outpatient services are paid based upon a prospectively determined fee schedule for each type of service. Professional services provided by physicians and other clinicians are reimbursed based upon one of the following methods: a prospectively determined fee schedule or a cost-reimbursement methodology depending on the type of professional services provided.
- *Blue Cross Blue Shield of Michigan ("Blue Cross")* - Inpatient and outpatient services rendered to Blue Cross subscribers are reimbursed on a controlled-charge basis. Professional services provided by physicians and other clinicians are reimbursed on a prospectively determined fee schedule.
- *Other* - The Organization also has entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment to the Organization under these agreements includes prospectively determined rates and discounts from established charges.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 2 Reimbursement Arrangements With Third-Party Payors (Continued)

- *Accounting for Contractual Arrangements* - The Hospital is reimbursed for cost reimbursable items at an interim rate, and final settlements are determined after audit of the Hospital's related annual cost reports by the respective Medicare, Medicaid, and Blue Cross fiscal intermediaries. Estimated provisions to approximate the full expected settlements after review by the intermediaries are included in the accompanying consolidated financial statements. The Hospital's cost reports have been audited by the Medicare, Medicaid, and Blue Cross fiscal intermediaries through June 30, 2009, June 30, 2009, and June 30, 2011, respectively.

Compliance

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations, particularly those relating to the Medicare and Medicaid programs, can be subject to government review and interpretation, as well as regulatory actions unknown and unasserted at this time. Federal government activity has increased with respect to investigations and allegations concerning possible violations by health care providers of regulations, which could result in the imposition of significant fines and penalties, as well as significant repayments of previously billed and collected revenue from patients' services. Management believes the Organization is in substantial compliance with current laws and regulations.

CMS uses recovery audit contractors (RACs) as part of its further efforts to ensure accurate payments. RACs search for potentially inaccurate Medicare payments that may have been made to health care providers and not detected through existing CMS program integrity efforts. Once a RAC identifies a claim it believes is inaccurate, CMS makes a deduction from or addition to the provider's Medicare reimbursement in an amount estimated to equal the overpayment or underpayment. RAC reviews of the Organization's activities are anticipated; however, the outcome of any potential reviews is unknown and cannot be reasonably estimated as of June 30, 2012.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 3 Accounts Receivable

Accounts receivable consisted of the following at June 30:

	2012	2011
Patient accounts receivable	\$ 21,434,786	\$ 14,412,416
Less:		
Contractual adjustments	10,937,684	6,082,114
Allowance for doubtful accounts	3,668,002	2,487,522
Net patient accounts receivable	6,829,100	5,842,780
Other receivables	355,828	360,565
Accounts receivable - Net	\$ 7,184,928	\$ 6,203,345

Note 4 Charity Care

The estimated cost of providing care to patients under the Hospital's charity care policy was approximately \$651,000 and \$848,000 in 2012 and 2011, respectively.

Note 5 Investments, Assets Limited as to Use, and Investment Income

Investments

Investments, stated at fair value, consisted of the following at June 30:

	2012	2011
Cash	\$ 12,488	\$ 5,189
Certificates of deposit	26,881	6,257
Mutual funds	3,797	3,304
Equity securities	19,059	34,964
Total investments	\$ 62,225	\$ 49,714

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 5 Investments, Assets Limited as to Use, and Investment Income (Continued)

Assets Limited as to Use

Assets limited as to use, stated at fair value, consisted of the following at June 30:

	2012	2011
Certificates of deposit	\$ 0	\$ 20,162
Equity securities	202,902	118,586
Total assets limited as to use	\$ 202,902	\$ 138,748

Investment Income

Investment income and gains and losses on assets limited as to use, cash equivalents, and other investments included the following:

	2012	2011
Investment income:		
Interest and dividend income	\$ 100,710	\$ 560,185
Net realized gain on sales of investments	2,602	408,553
Total investment income	\$ 103,312	\$ 968,738
Change in net unrealized gains and losses on investments - Trading securities	\$ 81,995	\$ (19,207)

Investments, in general, are exposed to various risks such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investments, it is reasonably possible that changes in the value of certain investments will occur in the near term and such changes could materially affect the amounts reported in the consolidated financial statements.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 6 Investments in Unconsolidated Affiliates

The Organization has a 5.12% interest in Upper Peninsula Managed Care, LLC and Upper Peninsula Health Plan, Inc. (the "Corporations").

Detail by investment for the years ended June 30, 2012 and 2011, is as follows:

	2012		2011	
	Investments	Change	Investments	Change
Corporations	\$ 1,048,443	\$ 114,555	\$ 933,888	\$ 760,615

The following is a summary of the financial position of the Corporations' investments accounted for under the equity method as of June 30:

	Unaudited	
	2012	2011
Assets	\$ 34,525,790	\$ 38,891,284
Liabilities	\$ 14,048,378	\$ 20,651,289
Equity	\$ 20,477,412	\$ 18,239,995

Note 7 Fair Value Measurements

Following is a description of the valuation methodologies used for assets measured at fair value:

- Mutual funds are valued at quoted market prices which represent the net asset value (NAV) of shares held by the Organization.
- Equity securities are valued at quoted market prices.
- The interest rate swap agreements are recorded at the amount at which they could be settled, based on estimates by a third-party valuation service, which uses a discounted cash flow analysis using observable market-based inputs, including forward interest rate curves.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 7 Fair Value Measurements (Continued)

The following tables set forth by level, within the fair value hierarchy, the Organization's assets and liabilities as of June 30:

2012	Fair Value Measurements Using			Total Assets/ Liabilities at Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Equity securities:				
Basic materials	\$ 27,424	\$ 0	\$ 0	\$ 27,424
Technology	193,304	0	0	193,304
Financial	1,233	0	0	1,233
Growth and income mutual fund	3,797	0	0	3,797
Total assets	\$ 225,758	\$ 0	\$ 0	\$ 225,758
Liabilities - Interest rate swap agreements				
	\$ 0	\$ (2,967,264)	\$ 0	\$ (2,967,264)
2011				
Assets:				
Equity securities:				
Basic materials	\$ 15,316	\$ 0	\$ 0	\$ 15,316
Technology	126,965	0	0	126,965
Financial	1,343	0	0	1,343
Health care	9,926	0	0	9,926
Growth and income mutual fund	3,304	0	0	3,304
Total assets	\$ 156,854	\$ 0	\$ 0	\$ 156,854
Liabilities - Interest rate swap agreements				
	\$ 0	\$ (2,477,511)	\$ 0	\$ (2,477,511)

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 8 Property and Equipment

Property and equipment consisted of the following at June 30:

	2012	2011
Land and land improvements	\$ 2,246,545	\$ 2,246,545
Buildings and building improvements	39,564,401	39,564,401
Equipment	18,067,139	18,113,150
Vehicles	109,201	109,201
Total property and equipment	59,987,286	60,033,297
Less - Accumulated depreciation	19,387,334	16,912,422
Net depreciated value	40,599,952	43,120,875
Construction in progress	2,155	0
Property and equipment - Net	\$ 40,602,107	\$ 43,120,875

Depreciation expense on property and equipment totaled \$3,035,785 and \$3,099,003 for the years ended June 30, 2012 and 2011, respectively.

Note 9 Long-Term Debt

Long-term debt consisted of the following at June 30:

	2012	2011
Limited Obligation Revenue Bonds, Series 2007A, dated March 1, 2007, monthly interest payments at a variable rate of LIBOR times 0.67% (0.30% at June 30, 2012), maturing in varying amounts through March 1, 2033	\$ 29,255,000	\$ 30,060,000
Limited Obligation Revenue Bonds, Series 2007B, dated August 1, 2007, monthly interest payments at a variable rate of LIBOR times 0.67% (0.29% June 30, 2012), maturing in varying amounts through August 1, 2032	3,360,000	3,450,000

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 9 Long-Term Debt (Continued)

	2012	2011
Note payable dated September 9, 2009, bearing interest at 6.49%, interest and principal payments due monthly, due September 2012	\$ 1,355	\$ 6,566
Note payable dated November 24, 2010, bearing interest at 5.99%, interest and principal payments due monthly, due December 2013	5,824	9,426
Note payable dated November 13, 2009, bearing interest at 6.00%, interest and principal payments due monthly, due November 2012	1,967	5,733
Note payable dated November 25, 2009, bearing interest at 5.95%, interest and principal payments due monthly, due December 2012	6,402	10,600
Totals	32,630,548	33,542,325
Less:		
Original issue discounts	235,512	266,568
Current maturities	958,421	895,608
Long-term portion	\$ 31,436,615	\$ 32,380,149

The Series 2007A and Series 2007B Limited Obligation Revenue Bonds are secured by irrevocable direct-pay letters of credit, which expire on March 15, 2013 and August 15, 2013, respectively, and are secured by substantially all of the Hospital's and Bell Medical Center's assets, including property, equipment, accounts receivable, and inventories. 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 2007A and Series 2007B Limited Obligation Revenue Bonds are also guaranteed by the Organization. Letters of credit fees are 3.75% on the Series 2007A and 2.75% on the Series 2007B Limited Obligation Revenue Bonds through March 15, 2013 and August 15, 2013, respectively.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 9 Long-Term Debt (Continued)

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

In connection with the issuance of the letters of credit and related Series 2007A and Series 2007B Limited Obligation Revenue Bonds, the Organization has agreed to certain financial covenants relating to debt service coverage, days cash on hand, aging of accounts receivable, and various other operational covenants. At June 30, 2010, the Organization was in violation of these financial covenants. Amendment No. 2 to the Reimbursement Agreement waived these financial covenants through June 30, 2011, and established new monthly covenants for the period from January 1, 2011 through June 30, 2011, including modifications to certain financial covenants. At June 30, 2011, the Organization was in violation with one of the new covenants, resulting in the bank hiring an independent consultant for the purpose of reviewing the financial reporting and system processes of the Organization.

Effective January 26, 2012, the Organization entered into a Forbearance Agreement and Amendment No. 3 to the Reimbursement Agreement related to the Series 2007A Limited Obligation Revenue Bonds. The agreements stipulate additional covenants that the Organization must comply with related to the bonds. With these agreements in place, the Organization's letter of credit related to the Series 2007A Limited Obligation Revenue Bonds was extended through March 15, 2015. Based on the extension of the letter of credit, the Organization classified the related debt as long-term on the accompanying consolidated balance sheets at June 30, 2012.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 9 Long-Term Debt (Continued)

Scheduled payments of principal on long-term debt at June 30, 2012, including current maturities, are summarized as follows:

2013	\$ 958,421
2014	987,127
2015	1,035,000
2016	1,080,000
2017	1,135,000
Thereafter	27,435,000
<hr/>	
Total	\$ 32,630,548

Note 10 Interest Rate Swap Agreements

In conjunction with the issuance of the Series 2007A and Series 2007B Limited Obligation Revenue Bonds (Note 9), the Organization entered into two interest rate swap agreements for the purpose of mitigating the floating interest rate risk on the variable rate bonds. The notional amount of the swap agreements was \$22,301,250 and \$23,576,250 at June 30, 2012 and 2011, respectively. The Organization pays a fixed rate of 3.500% and 3.665% for the Series 2007A and Series 2007B Limited Obligation Revenue Bonds, respectively, and receives a variable rate of 0.67% times LIBOR.

The interest rate swap agreements were recorded as liabilities of \$2,967,264 and \$2,477,511 as of June 30, 2012 and 2011, respectively. The Organization recognized interest income of \$91,266 and expense of \$357,265 during the years ended June 30, 2012 and 2011, respectively, related to these interest rate swap agreements included in other income (deductions) in the accompanying consolidated statements of operations.

The Organization is exposed to credit loss in the event of nonperformance by the counterparty to the interest rate swap agreements. However, the Organization does not anticipate nonperformance by the counterparty.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 11 Leases

The Hospital leases various equipment under capital lease obligations. Capital assets included the following amounts at June 30 for leases that have been capitalized:

	2012	2011
Equipment	\$ 281,762	\$ 281,762
Less - Accumulated amortization	91,261	41,667
Net book value	\$ 190,501	\$ 240,095

Future minimum payments, by year and in the aggregate, under capital leases with initial or remaining terms in excess of one year consisted of the following:

2013	\$ 75,263
2014	61,678
2015	16,224
2016	1,279
Total minimum lease payments	154,444
Amount representing interest	10,565
Present value of net minimum lease payments	143,879
Less - Current portion	68,325
Long-term obligations under capital leases	\$ 75,554

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 12 Net Patient Service Revenue

Net patient service revenue consisted of the following:

	2012	2011
Gross patient service revenue:		
Inpatient services	\$ 22,033,556	\$ 21,532,023
Outpatient services	82,660,691	73,684,699
Total gross patient service revenue	104,694,247	95,216,722
Less - Contractual adjustments and other discounts	54,334,660	46,199,141
Net patient service revenue	<u>\$ 50,359,587</u>	<u>\$ 49,017,581</u>

The Hospital's mix of gross revenue from patients and third-party payors at June 30 is as follows:

	2012	2011
Medicare	44%	44%
Medicaid	12%	13%
Blue Cross	34%	31%
Other commercial payors	7%	9%
Patients	3%	3%
Totals	<u>100%</u>	<u>100%</u>

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 13 Malpractice Insurance

The Organization's professional liability insurance for claim losses of less than \$1 million per claim and \$3 million per year covers professional liability claims reported during a policy year ("claims made" coverage). The professional liability insurance policy is renewable annually and has been renewed by the insurance carrier for the annual period extending through April 2013.

Under a claims-made policy, the risk for claims and incidents not asserted within the policy period remains with the Organization. The Organization has included a provision of \$425,000 and \$700,000 at June 30, 2012 and 2011, respectively, in accrued and other liabilities for potential claims from services provided to patients which have not yet been asserted as of June 30, 2012 and 2011.

Note 14 Retirement Plans

The Organization has two noncontributory pension plans that together cover substantially all employees who meet service and age requirements.

Union employees are covered under a defined contribution plan that is administered under a collective bargaining arrangement.

The Hospital's plan provides for either profit sharing or matching contributions to be made by the plan sponsor to eligible participants. Employees who were eligible for the Bell Memorial Hospital Non-Union Pension Plan prior to it being frozen on November 1, 2005, are eligible to receive employer profit sharing contributions. The amount of profit sharing contributions received by an eligible participant is based on a specified percentage of the participant's annual pay as specified in the plan documents. Nonunion, noncontingent participants who are not eligible to receive the employer profit sharing contributions are instead eligible to receive employer matching contributions. Employer matching contributions are based on 100% of the pretax contributions made by the participant, up to a maximum of 5.5% of the employee's pay. Amounts contributed to the plan from other qualified plans are not matched.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 14 Retirement Plans (Continued)

Expenses under the defined contribution plans for the years ended June 30, 2012 and 2011, were approximately \$1,745,000 and \$1,207,000, respectively.

The Organization also sponsors a defined benefit pension plan. The Organization's Board of Directors voted to freeze the future accrual of benefits under the defined benefit pension plan effective November 1, 2005.

The following table sets forth the defined benefit pension plan's funded status and amounts recognized in the accompanying consolidated balance sheets for the defined benefit pension plan at June 30:

	2012	2011
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 10,158,870	\$ 10,301,342
Interest cost	548,317	531,873
Actuarial (gain) loss	2,121,486	(348,104)
Benefits paid	(318,258)	(326,241)
Benefit obligation at end of year	12,510,415	10,158,870
Change in plan assets:		
Fair value of plan assets at beginning of year	7,650,925	6,345,717
Actual return on plan assets	11,171	1,620,562
Employer contributions	264,632	10,887
Benefits paid	(318,258)	(326,241)
Fair value of plan assets at end of year	7,608,470	7,650,925
Funded status at end of year	\$ (4,901,945)	\$ (2,507,945)

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 14 Retirement Plans (Continued)

Pension expense for the years ended June 30 was comprised of the following:

	2012	2011
Pension expense:		
Interest cost	\$ 548,317	\$ 531,873
Expected return on assets	(539,107)	(433,820)
Amortization of unrecognized loss	23,692	79,075
Total pension expense	\$ 32,902	\$ 177,128

Amounts recognized in the accompanying consolidated balance sheets consisted of the following at June 30:

	2012	2011
Pension liability	\$ 4,901,945	\$ 2,507,945
Net assets:		
Net (gain) loss	\$ (2,370,308)	\$ 1,526,755
Amortization recognized	(23,692)	(79,075)
Total amount recognized in net assets	\$ (2,394,000)	\$ 1,447,680

Weighted average assumptions used as of June 30, the measurement date, in developing the net periodic benefit cost were as follows:

	2012	2011
Discount rate	5.50%	5.25%
Expected return on plan assets	7.00%	7.00%

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 14 Retirement Plans (Continued)

To develop the expected long-term rate of return on asset assumptions, the Organization considered the historical returns and future expectations for returns in each asset class, as well as targeted asset allocation percentages within the pension portfolio.

The defined benefit pension plan's asset allocations at June 30 were as follows:

	2012	2011
Cash, cash equivalents, and receivables	3.41%	1.48%
Mutual funds - Equity	69.81%	72.15%
Mutual funds - Fixed income	26.78%	26.37%
Totals	100.00%	100.00%

Following is a description of the valuation methodologies used for pension assets measured at fair value. There have been no changes in the methodologies used at June 30, 2012 and 2011. Money market funds are valued at historical cost, which approximates fair value. Mutual funds are valued at quoted market prices, which represent the NAV of shares held by the plan at year-end.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the plan believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 14 Retirement Plans (Continued)

The following tables set forth by level, within the fair value hierarchy, the Organization's assets within the defined benefit pension plan at fair value as of June 30:

	Assets at Fair Value as of June 30, 2012			
	Level 1	Level 2	Level 3	Total
Money market fund	\$ 250,212	\$ 0	\$ 0	\$ 250,212
Mutual funds:				
Growth funds	2,781,939	0	0	2,781,939
Intermediate-term bond funds	2,034,471	0	0	2,034,471
International funds	794,463	0	0	794,463
Value funds	1,747,385	0	0	1,747,385
Total mutual funds	7,358,258	0	0	7,358,258
Total assets at fair value	\$ 7,608,470	\$ 0	\$ 0	\$ 7,608,470

	Assets at Fair Value as of June 30, 2011			
	Level 1	Level 2	Level 3	Total
Money market fund	\$ 111,185	\$ 0	\$ 0	\$ 111,185
Mutual funds:				
Growth funds	3,112,569	0	0	3,112,569
Intermediate-term bond funds	2,019,382	0	0	2,019,382
International funds	825,650	0	0	825,650
Value funds	1,582,139	0	0	1,582,139
Total mutual funds	7,539,740	0	0	7,539,740
Total assets at fair value	\$ 7,650,925	\$ 0	\$ 0	\$ 7,650,925

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 14 Retirement Plans (Continued)

Estimated Future Benefit Payments

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

2013	\$ 377,172
2014	439,236
2015	467,542
2016	508,218
2017	584,082
Succeeding five years	3,424,561

Superior Enterprises' employees are covered by a defined contribution plan that is administered by a third-party administrator as part of an overall benefits program. The plan provides for matching contributions to be made by Superior Enterprises for employees meeting eligibility requirements. The contributions are based upon 100% of an employee's salary up to a maximum of 3% of the employee's salary. The plan was established as a Simple IRA and amounts contributed to the plan from other plans are not subject to the match. All assets in the plan are deemed to be vested immediately.

Note 15 Self-Funded Health Insurance

The Organization sponsors a self-funded health insurance plan covering substantially all of its employees and their dependents, of which some services are provided by the Organization. The health insurance expense is based upon actual claims paid, administration fees, and provisions for unpaid and unreported claims at year-end. Health insurance expense was approximately \$2,100,000 and \$2,300,000 for the years ended June 30, 2012 and 2011, respectively.

A provision of approximately \$300,000 for unpaid and unasserted claims at June 30, 2012 and 2011, was included in accrued and other liabilities in the accompanying consolidated balance sheets. Management believes this provision is sufficient to cover estimated claims, including claims incurred but not yet reported.

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 16 Functional Expenses

The Organization is a general acute care facility that provides inpatient and outpatient health care services and clinic services to patients in Ishpeming, Michigan, and the surrounding area. Expenses related to providing these services were as follows:

	2012	2011
Health care services	\$ 46,775,703	\$ 44,056,788
General and administrative	12,430,375	11,888,300
Fundraising	143,800	130,448
Total	\$ 59,349,878	\$ 56,075,536

Note 17 Concentration of Credit Risk

Financial instruments that potentially subject the Organization to credit risk consist principally of accounts receivable, interest rate swap agreements, and cash deposits in excess of insured limits in financial institutions.

Accounts receivable consist of amounts due from patients, their insurers, or governmental agencies (primarily Medicare and Medicaid) for health care provided to the patients. The majority of the Hospital's patients are from Ishpeming, Michigan, and the surrounding areas. The mix of receivables from patients and third-party payors was as follows at June 30:

	2012	2011
Medicare	24%	30%
Medicaid	8%	7%
Other third-party payors	53%	42%
Patients	15%	21%
Totals	100%	100%

Superior Healthcare System and Affiliates

Notes to Consolidated Financial Statements

Note 17 **Concentration of Credit Risk (Continued)**

The Organization maintains depository relationships with area financial institutions insured by the Federal Deposit Insurance Corporation (FDIC). On November 9, 2010, the FDIC issued a final rule implementing Section 343 of the Dodd-Frank Wall Street Reform and Consumer Protection Act that provides for unlimited insurance coverage of non-interest-bearing transaction accounts through December 31, 2012. The Organization maintains cash in interest-bearing accounts at these institutions that are insured by the FDIC up to \$250,000. At June 30, 2012, the Organization's bank balances in excess of FDIC-insured limits were approximately \$8,582,000. In addition, other investments held by financial institutions are uninsured.

Note 18 **Reclassifications**

Certain reclassifications have been made to the 2011 consolidated financial statements to conform to the 2012 classifications.

Supplementary Information



Independent Auditor's Report on Supplementary Information

Board of Directors
Superior Healthcare System
Ishpeming, Michigan

We have audited the consolidated financial statements of Superior Healthcare System and Affiliates as of and for the year ended June 30, 2012, and our report thereon dated (report date), 2012, which expressed an unqualified opinion on those financial statements, appears on page 1. Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information appearing on pages 40 through 47 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

The June 30, 2011, consolidated financial statements were compiled by us, thus we did not audit or review the 2011 consolidated financial statements and, accordingly, express no opinion or other form of assurance on them.

Wipfli LLP

(report date), 2012
Green Bay, Wisconsin

Superior Healthcare System and Affiliates

Consolidating Balance Sheet

June 30, 2012

<i>Assets</i>	Bell Memorial Hospital	Bell Medical Center	Bell Foundation	Superior Enterprises	Eliminations	Consolidated Total
Current assets:						
Cash and cash equivalents	\$ 9,250,049	\$ 213,579	\$ 326,483	\$ 190,265	\$ 0	\$ 9,980,376
Accounts receivable - Net	6,144,751	854,980	0	243,302	(58,105)	7,184,928
Inventories	1,428,171	0	0	2,500	0	1,430,671
Prepaid expenses and other	420,061	46,221	0	4,679	0	470,961
Amounts due from third-party reimbursement programs	1,099,217	0	0	0	0	1,099,217
Total current assets	18,342,249	1,114,780	326,483	440,746	(58,105)	20,166,153
Property and equipment - Net	40,364,134	226,033	0	11,940	0	40,602,107
Investments	0	0	62,225	0	0	62,225
Assets limited as to use	0	0	202,902	0	0	202,902
Beneficial interest in net assets of Bell Foundation	388,708	0	0	0	(388,708)	0
Other assets:						
Unamortized bond issue costs	237,204	0	0	0	0	237,204
Notes receivable	25,000	297,366	0	0	0	322,366
Investments in unconsolidated affiliates	1,048,443	0	0	0	0	1,048,443
Other	197,179	6,207	0	0	0	203,386
Total other assets	1,507,826	303,573	0	0	0	1,811,399
TOTAL ASSETS	\$ 60,602,917	\$ 1,644,386	\$ 591,610	\$ 452,686	\$ (446,813)	\$ 62,844,786

Superior Healthcare System and Affiliates

Consolidating Balance Sheet (Continued) June 30, 2012

<i>Liabilities and Net Assets</i>	Bell Memorial Hospital	Bell Medical Center	Bell Foundation	Superior Enterprises	Eliminations	Consolidated Total
Current liabilities:						
Current maturities of long-term debt	\$ 945,000	\$ 0	\$ 0	\$ 13,421	\$ 0	\$ 958,421
Current portion of obligations under capital leases	68,325	0	0	0	0	68,325
Current portion of deferred revenue	410,102	0	0	0	0	410,102
Accounts payable	1,065,755	64,619	0	22,276	(58,105)	1,094,545
Accrued and other liabilities	3,117,720	658,109	0	107,041	0	3,882,870
Total current liabilities	5,606,902	722,728	0	142,738	(58,105)	6,414,263
Long-term liabilities:						
Long-term debt - Less current maturities	31,434,488	0	0	2,127	0	31,436,615
Obligations under capital leases - Less current portion	75,554	0	0	0	0	75,554
Deferred revenue	410,102	0	0	0	0	410,102
Interest rate swap agreements	2,967,264	0	0	0	0	2,967,264
Pension liability	4,901,945	0	0	0	0	4,901,945
Other liabilities	425,436	0	0	0	0	425,436
Total long-term liabilities	40,214,789	0	0	2,127	0	40,216,916
Total liabilities	45,821,691	722,728	0	144,865	(58,105)	46,631,179
Net assets:						
Unrestricted	14,392,518	921,658	388,708	307,821	0	16,010,705
Temporarily restricted	388,708	0	202,902	0	(388,708)	202,902
Total net assets	14,781,226	921,658	591,610	307,821	(388,708)	16,213,607
TOTAL LIABILITIES AND NET ASSETS	\$ 60,602,917	\$ 1,644,386	\$ 591,610	\$ 452,686	\$ (446,813)	\$ 62,844,786

See Independent Auditor's Report on Supplementary Information.

Superior Healthcare System and Affiliates

Consolidating Balance Sheet

June 30, 2011

<i>Assets</i>		Bell Memorial Hospital	Bell Medical Center	Bell Foundation	Superior Enterprises	Eliminations	Consolidated Total						
Current assets:													
Cash and cash equivalents	\$	10,270,679	\$	52,287	\$	111,783	\$	83,569	\$	0	\$	10,518,318	
Accounts receivable - Net		4,481,493		1,480,911		0		273,283		(32,342)		6,203,345	
Inventories		1,560,414		0		0		3,000		0		1,563,414	
Prepaid expenses and other		381,269		34,024		0		5,437		0		420,730	
Amounts receivable from third-party reimbursement programs		3,027		0		0		0		0		3,027	
Total current assets		16,696,882		1,567,222		111,783		365,289		(32,342)		18,708,834	
Property and equipment - Net		42,698,696		400,833		0		21,346		0		43,120,875	
Investments		0		0		49,714		0		0		49,714	
Assets limited as to use		0		0		138,748		0		0		138,748	
Beneficial interest in net assets of Bell Foundation		152,068		0		0		0		(152,068)		0	
Other assets:													
Unamortized bond issue costs		251,877		0		0		0		0		251,877	
Notes receivable		0		393,323		0		0		0		393,323	
Investments in unconsolidated affiliates		933,888		0		0		0		0		933,888	
Other		147,036		6,207		0		0		0		153,243	
Total other assets		1,332,801		399,530		0		0		0		1,732,331	
TOTAL ASSETS		\$	60,880,447	\$	2,367,585	\$	300,245	\$	386,635	\$	(184,410)	\$	63,750,502

Superior Healthcare System and Affiliates

Consolidating Balance Sheet (Continued)

June 30, 2011

<i>Liabilities and Net Assets</i>	Bell Memorial Hospital	Bell Medical Center	Bell Foundation	Superior Enterprises	Eliminations	Consolidated Total
Current liabilities:						
Current maturities of long-term debt	\$ 879,472	\$ 0	\$ 0	\$ 16,136	\$ 0	\$ 895,608
Current portion of obligations under capital leases	64,519	0	0	0	0	64,519
Accounts payable	1,277,781	102,880	0	2,793	(32,342)	1,351,112
Accrued and other liabilities	2,219,297	540,890	0	84,409	0	2,844,596
Total current liabilities	4,441,069	643,770	0	103,338	(32,342)	5,155,835
Long-term liabilities:						
Long-term debt - Less current maturities	32,363,960	0	0	16,189	0	32,380,149
Obligations under capital leases - Less current portion	143,879	0	0	0	0	143,879
Interest rate swap agreements	2,477,511	0	0	0	0	2,477,511
Pension liability	2,507,945	0	0	0	0	2,507,945
Other liabilities	1,300,000	0	0	0	0	1,300,000
Total long-term liabilities	38,793,295	0	0	16,189	0	38,809,484
Total liabilities	43,234,364	643,770	0	119,527	(32,342)	43,965,319
Net assets:						
Unrestricted	17,494,015	1,723,815	161,497	267,108	0	19,646,435
Temporarily restricted	152,068	0	138,748	0	(152,068)	138,748
Total net assets	17,646,083	1,723,815	300,245	267,108	(152,068)	19,785,183
TOTAL LIABILITIES AND NET ASSETS	\$ 60,880,447	\$ 2,367,585	\$ 300,245	\$ 386,635	\$ (184,410)	\$ 63,750,502

See Independent Auditor's Report on Supplementary Information.

Superior Healthcare System and Affiliates

Consolidating Statement of Operations Year Ended June 30, 2012

	BellMemorial Hospital	BellMedical Center	Bell Foundation	Superior Enterprises	Eliminations	Consolidated Total
Revenue:						
Patient service revenue	\$ 88,537,802	\$ 16,156,445	\$	0	0	\$ 104,694,247
Revenue deductions	(46,112,760)	(8,221,900)		0	0	(54,334,660)
Net patient service revenue	42,425,042	7,934,545		0	0	50,359,587
Other revenue	4,094,514	1,476,218		2,141,398	(471,372)	7,240,758
Total revenue	46,519,556	9,410,763		2,141,398	(471,372)	57,600,345
Expenses:						
Salaries and wages	16,563,376	8,091,096	74,041	1,567,433	0	26,295,946
Employee benefits	4,943,920	1,266,219	22,682	371,414	0	6,604,235
Supplies	6,242,949	549,525	3,341	3,935	0	6,799,750
Purchased services	1,607,163	1,063,619	20,705	45,344	0	2,736,831
Insurance	261,655	120,982	0	0	0	382,637
Other health care expenses	6,536,643	687,787	22,638	79,552	(471,372)	6,855,248
Depreciation and amortization	2,733,302	321,372	393	10,919	0	3,065,986
Provision for bad debts	3,963,508	484,789	0	17,387	0	4,465,684
Interest	1,923,250	217,965	0	2,346	0	2,143,561
Total expenses	44,775,766	12,803,354	143,800	2,098,330	(471,372)	59,349,878
Income (loss) from operations	1,743,790	(3,392,591)	(143,800)	43,068	0	(1,749,533)
Other income (deductions):						
Investment income	100,174	0	7,039	249	(4,150)	103,312
Contributions	0	0	48,106	0	0	48,106
Provision (credit) for income taxes	0	0	0	1,546	0	1,546
Gain (loss) on disposal of property and equipment	(8,072)	22,243	0	0	0	14,171
Change in net unrealized gains and losses on investments -						
Trading securities	0	0	81,995	0	0	81,995
Change in equity investments in unconsolidated affiliates	114,555	0	0	0	0	114,555
Change in fair value of interest rate swap agreements	(489,753)	0	0	0	0	(489,753)
Excess (deficiency) of revenue over expenses	1,460,694	(3,370,348)	(6,660)	44,863	(4,150)	(1,875,601)
Other changes in unrestricted net assets:						
Transfer (to) from affiliates	(2,168,191)	2,568,191	(400,000)	0	0	0
Pension-related changes other than net periodic pension cost	(2,394,000)	0	0	0	0	(2,394,000)
Dividend	0	0	0	(4,150)	4,150	0
Net assets released from restrictions	0	0	633,871	0	0	633,871
Increase (decrease) in unrestricted net assets	\$ (3,101,497)	\$ (802,157)	\$ 227,211	\$ 40,713	\$ 0	\$ (3,635,730)

See Independent Auditor's Report on Supplementary Information.

Superior Healthcare System and Affiliates

Consolidating Statement of Operations

Year Ended June 30, 2011

	Bell Memorial Hospital	Bell Medical Center	Bell Foundation	Superior Enterprises	Eliminations	Consolidated Total
Revenue:						
Patient service revenue	\$ 80,115,805	\$ 15,100,917	\$	0	\$	0
Revenue deductions	(39,190,805)	(7,008,336)		0	0	0
Net patient service revenue	40,925,000	8,092,581		0	0	0
Other revenue	2,314,019	1,304,051	22,875	2,001,596	(418,785)	5,223,756
Total revenue	43,239,019	9,396,632	22,875	2,001,596	(418,785)	54,241,337
Expenses:						
Salaries and wages	16,611,480	7,676,359	64,899	1,433,422	0	25,786,160
Employee benefits	4,196,002	1,484,729	28,081	384,913	0	6,093,725
Supplies	5,928,917	687,127	3,849	6,222	0	6,626,115
Purchased services	1,711,510	1,566,394	3,552	62,416	0	3,343,872
Insurance	425,341	143,176	0	0	0	568,517
Other health care expenses	5,216,096	600,803	29,624	75,058	(418,785)	5,502,796
Depreciation and amortization	2,701,071	404,327	443	23,880	0	3,129,721
Provision for bad debts	2,990,942	565,285	0	100	0	3,556,327
Interest	1,317,797	147,849	0	2,657	0	1,468,303
Total expenses	41,099,156	13,276,049	130,448	1,988,668	(418,785)	56,075,536
Income (loss) from operations	2,139,863	(3,879,417)	(107,573)	12,928	0	(1,834,199)
Other income (deductions):						
Investment income	955,875	0	12,379	484	0	968,738
Contributions	4,182	0	36,357	0	0	40,539
Provision (credit) for incomes taxes	0	0	0	(160)	0	(160)
Loss on disposal of property and equipment	(91,932)	0	0	0	0	(91,932)
Change in net unrealized gains and losses on investments - Trading securities	(46,275)	0	27,068	0	0	(19,207)
Change in equity investments in unconsolidated affiliates	760,615	0	0	0	0	760,615
Change in fair value of interest rate swap agreements	357,265	0	0	0	0	357,265
Excess (deficiency) of revenue over expenses	4,079,593	(3,879,417)	(31,769)	13,252	0	181,659
Other changes in unrestricted net assets:						
Transfers (to) from affiliates	(1,556,913)	3,896,013	(2,339,100)	0	0	0
Pension-related changes other than net periodic pension cost	1,447,680	0	0	0	0	1,447,680
Net assets released from restrictions	0	0	1,322,877	0	0	1,322,877
Increase (decrease) in unrestricted net assets	\$ 3,970,360	\$ 16,596	\$ (1,047,992)	\$ 13,252	\$	\$ 2,952,216

See Independent Auditor's Report on Supplementary Information.

Superior Healthcare System and Affiliates

Consolidating Statement of Changes in Net Assets

Year Ended June 30, 2012

	Bell Memorial Hospital	Bell Medical Center	Bell Foundation	Superior Enterprises	Eliminations	Consolidated Total
Unrestricted net assets:						
Excess (deficiency) of revenue over expenses	\$ 1,460,694	\$ (3,370,348)	\$ (6,660)	\$ 44,863	\$ (4,150)	\$ (1,875,601)
Transfer (to) from affiliates	(2,168,191)	2,568,191	(400,000)	0	0	0
Pension-related changes other than net periodic pension cost	(2,394,000)	0	0	0	0	(2,394,000)
Dividend	0	0	0	(4,150)	4,150	0
Net assets released from restrictions	0	0	633,871	0	0	633,871
Increase (decrease) in unrestricted net assets	(3,101,497)	(802,157)	227,211	40,713	0	(3,635,730)
Temporarily restricted net assets:						
Contributions	0	0	698,025	0	0	698,025
Change in beneficial interest in net assets of Bell Foundation	236,640	0	0	0	(236,640)	0
Net assets released from restrictions	0	0	(633,871)	0	0	(633,871)
Increase (decrease) in temporarily restricted net assets	236,640	0	64,154	0	(236,640)	64,154
Change in net assets	(2,864,857)	(802,157)	291,365	40,713	(236,640)	(3,571,576)
Net assets at beginning	17,646,083	1,723,815	300,245	267,108	(152,068)	19,785,183
Net assets at end	\$ 14,781,226	\$ 921,658	\$ 591,610	\$ 307,821	\$ (388,708)	\$ 16,213,607

See Independent Auditor's Report on Supplementary Information.

Superior Healthcare System and Affiliates

Consolidating Statement of Changes in Net Assets

Year Ended June 30, 2011

	Bell Memorial Hospital	Bell Medical Center	Bell Foundation	Superior Enterprises	Eliminations	Consolidated Total
Unrestricted net assets:						
Excess (deficiency) of revenue over expenses	\$ 4,079,593	\$ (3,879,417)	\$ (31,769)	\$ 13,252	\$ 0	\$ 181,659
Transfers (to) from affiliates	(1,556,913)	3,896,013	(2,339,100)	0	0	0
Pension-related changes other than net periodic pension cost	1,447,680	0	0	0	0	1,447,680
Net assets released from restrictions	0	0	1,322,877	0	0	1,322,877
Increase (decrease) in unrestricted net assets	3,970,360	16,596	(1,047,992)	13,252	0	2,952,216
Temporarily restricted net assets:						
Contributions	0	0	811,439	0	0	811,439
Change in beneficial interest in net assets of Bell Foundation	(1,673,468)	0	0	0	1,673,468	0
Net assets released from restrictions	0	0	(1,322,877)	0	0	(1,322,877)
Increase (decrease) in temporarily restricted net assets	(1,673,468)	0	(511,438)	0	1,673,468	(511,438)
Change in net assets	2,296,892	16,596	(1,559,430)	13,252	1,673,468	2,440,778
Net assets at beginning	15,349,191	1,707,219	1,859,675	253,856	(1,825,536)	17,344,405
Net assets at end	\$ 17,646,083	\$ 1,723,815	\$ 300,245	\$ 267,108	\$ (152,068)	\$ 19,785,183

See Independent Auditor's Report on Supplementary Information.

