

CONSOLIDATED FINANCIAL STATEMENTS
AND DETAILS OF CONSOLIDATION

University of Wisconsin Medical Foundation, Inc.
and Subsidiary

Year ended June 30, 2004 and six months ended June 30, 2003

University of Wisconsin Medical Foundation, Inc.
and Subsidiary

Consolidated Financial Statements and Details of Consolidation

Year ended June 30, 2004 and six months ended June 30, 2003

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Report of Independent Auditors

The Board of Directors
University of Wisconsin Medical Foundation, Inc.

We have audited the accompanying consolidated balance sheets of University of Wisconsin Medical Foundation, Inc. and subsidiary (the Foundation) at June 30, 2004, and 2003, and the related consolidated statements of operations and changes in net assets and cash flows for the year ended June 30, 2004, and six months ended June 30, 2003. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of University of Wisconsin Medical Foundation, Inc. and subsidiary at June 30, 2004 and 2003, and the consolidated results of their operations and changes in net assets and their cash flows for the year ended June 30, 2004, and six months ended June 30, 2003, in conformity with accounting principles generally accepted in the United States.

Ernst & Young LLP

September 2, 2004

University of Wisconsin Medical Foundation, Inc.
and Subsidiary

Consolidated Balance Sheets

	June 30	
	2004	2003
Assets		
Current assets:		
Cash and cash equivalents	\$ 38,500,749	\$ 13,751,954
Accounts receivable, less allowances for contractual provisions and doubtful accounts of \$74,386,000 and \$93,202,000 in 2004 and 2003, respectively	63,396,385	60,655,043
Inventories	3,147,161	2,602,867
Prepaid expense and other current assets	7,976,297	6,214,188
Total current assets	113,020,592	83,224,052
Investments	22,076,577	21,071,802
Advances to, interests in net assets and investment in unconsolidated affiliates	8,025,174	5,793,142
Property, plant and equipment, net	63,873,840	64,662,469
Intangible assets, net	2,127,092	2,617,010
Other assets	2,056,598	2,384,764
Total assets	\$211,179,873	\$179,753,239
 Liabilities and net assets		
Current liabilities:		
Accounts payable and accrued expenses	\$ 52,536,605	\$ 35,324,613
Current maturities of long-term obligations	2,369,909	5,238,590
Amount due to Medical School Development Fund	7,353,419	5,710,629
Amount due to Research and Development Fund	327,269	873,002
Total current liabilities	62,587,202	47,146,834
Long-term obligations, less current portion	56,194,959	58,598,713
Total liabilities	118,782,161	105,745,547
Unrestricted net assets	92,397,712	74,007,692
Total liabilities and net assets	\$211,179,873	\$179,753,239

See accompanying notes to the consolidated financial statements.

University of Wisconsin Medical Foundation, Inc.
and Subsidiary

Consolidated Statements of Operations and Changes in Net Assets

	Year ended June 30 2004	Six months ended June 30 2003
Unrestricted revenue:		
Net patient service revenue	\$278,276,828	\$127,030,238
Premium revenue	97,118,736	44,157,003
Other revenue	21,795,415	8,051,358
Total revenues	397,190,979	179,238,599
Expenses:		
Compensation and benefits	238,358,466	103,731,809
Operating expenses paid through the University of Wisconsin, principally compensation and benefits	46,864,488	24,183,343
Other operating expenses	50,265,570	24,724,230
Purchased services	7,785,358	2,754,925
Medical School Development Fund	21,603,419	10,460,629
Research and Development Fund	9,840,491	6,068,073
University Community Clinics, Inc. support	-	706,632
University Health Care, Inc. support	861,930	410,088
Depreciation and amortization	8,138,151	3,759,921
Interest	1,463,864	830,312
Total expenses	385,181,737	177,629,962
Operating income	12,009,242	1,608,637
Other income (expenses):		
Equity in net earnings of unconsolidated affiliates	1,664,501	951,290
Investment income	1,066,517	653,237
Other	2,913,405	(19,960)
Other income, net	5,644,423	1,584,567
Revenue in excess of expenses before income taxes	17,653,665	3,193,204
Income tax (expense) benefit	(44,737)	53,999
Revenue in excess of expenses	17,608,928	3,247,203
Contribution of fixed assets	983,700	-
Change in unrealized losses on investments	(202,608)	(176,189)
Increase in unrestricted net assets	18,390,020	3,071,014
Unrestricted net assets at beginning of year	74,007,692	70,936,678
Unrestricted net assets at end of year	\$ 92,397,712	\$ 74,007,692

See accompanying notes to the consolidated financial statements.

University of Wisconsin Medical Foundation, Inc.
and Subsidiary

Consolidated Statements of Cash Flows

	Year ended June 30 2004	Six months ended June 30 2003
Operating activities		
Increase in net assets	\$18,390,020	\$ 3,071,014
Adjustments to reconcile increase in net assets to net cash provided by (used in) operating activities:		
Depreciation and amortization	8,138,151	3,759,921
Equity in net earnings of unconsolidated affiliates	(1,664,501)	(951,290)
University Community Clinics (UCC) Contribution, less cash received of \$375,691	(1,969,343)	-
(Gain) loss on sale of assets	(109,309)	19,960
Change in unrealized losses on investments	202,608	176,189
Changes in assets and liabilities:		
Accounts receivable	(1,382,318)	1,334,405
Inventories	(544,294)	(234,023)
Accounts payable and accrued expenses	16,701,811	(3,658,976)
Amount due to Medical School Development Fund	1,642,790	(2,451,692)
Other	(2,378,096)	(2,628,329)
Net cash provided by (used in) operating activities	37,027,519	(1,562,821)
Investing activities		
Purchases of investments	(32,372,209)	(8,794,808)
Sales of investments	31,164,826	6,191,648
(Increase) decrease in advances to, interests in net assets and investment in unconsolidated affiliates	(567,531)	804,675
Additions to property, plant and equipment, net	(5,231,375)	(1,543,894)
Net cash used in investing activities	(7,006,289)	(3,342,379)
Financing activities		
Proceeds from long-term obligations, net of discounts	3,000,000	3,003,389
Payments on long-term obligations	(8,272,435)	(1,753,703)
Cash (used in) provided by financing activities	(5,272,435)	1,249,686
Net increase (decrease) in cash and cash equivalents	24,748,795	(3,655,514)
Cash and cash equivalents at beginning of period	13,751,954	17,407,468
Cash and cash equivalents at end of period	\$38,500,749	\$13,751,954
Supplementary information –		
Cash paid for interest	\$ 1,463,864	\$ 830,312

See accompanying notes to the consolidated financial statements.

University of Wisconsin Medical Foundation, Inc.
and Subsidiary

Notes to Consolidated Financial Statements

June 30, 2004

1. Business Description and Significant Accounting Policies

Business Description

The University of Wisconsin Medical Foundation, Inc. (the Foundation) is a nonstock, not-for-profit corporation. It was created on January 1, 1996, by organizing 14 separate Departmental Practice Plan Associations of the University of Wisconsin Medical School (DPPAs) into one entity. As a result, the Foundation performs all functions previously performed by the DPPAs.

An agreement with the Board of Regents of the University of Wisconsin System was entered into upon creation of the Foundation. The organization, operation and distributions of the Foundation are subject to the provisions of the agreement.

The Foundation was formed for the purposes of: (1) providing education to medical students, practicing physicians, health care providers and personnel, patients and the general public; (2) supporting medical research in the field of clinical medicine; and (3) promoting the delivery of patient care. Medical care is primarily provided in the southern half of Wisconsin. The Foundation operates exclusively for the benefit of, and to support the purposes and operations of, the University of Wisconsin Medical School (Medical School) and the University of Wisconsin – Madison (University). The Foundation also provides to, and receives support from, the University of Wisconsin Hospital and Clinics Authority (UWHCA), which has an affiliation agreement with the Board of Regents of the University.

Expenses consist primarily of direct and indirect costs related to the operation of patient care clinics and to provide support in accordance with the purposes for which the Foundation was formed.

In 2002, the Foundation elected to change its fiscal year-end to June 30 effective June 30, 2003.

In July 2003, University Healthcare, Inc. contributed its clinic operation known as University Community Clinics (UCC) to the Foundation. The assets, liabilities and net assets of UCC, which were assumed by the Foundation in July 2003, were \$2,792,520, \$447,486 and \$2,345,034, respectively. The Foundation has assimilated UCC into its operations.

University of Wisconsin Medical Foundation, Inc.
and Subsidiary

Notes to Consolidated Financial Statements (continued)

1. Business Description and Significant Accounting Policies (continued)

Basis of Accounting and Use of Estimates

The accompanying financial statements have been prepared on the accrual basis of accounting. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with an original maturity of three months or less. The majority of cash and cash equivalents are invested in three financial institutions and exceed depository insurance limits.

Inventories

Inventories are stated at the lower of cost or market. Cost is determined principally by the first-in, first-out method.

Investments

Debt and equity securities with readily determinable fair values, based on quoted market prices, are stated at fair value with realized and change in unrealized gains and losses reported in the consolidated statements of operations and changes in net assets.

Deferred Financing Expenses

Costs of issuing long-term debt are being amortized over the respective terms of the loans.

Intangible Assets

Intangible assets represent the excess of the purchase price over the fair value of tangible net assets of acquired businesses and are amortized using the straight-line method over 3 to 40 years. Accumulated amortization on intangible assets totaled \$3,144,900 and \$3,732,900 as of June 30, 2004 and 2003, respectively.

University of Wisconsin Medical Foundation, Inc.
and Subsidiary

Notes to Consolidated Financial Statements (continued)

1. Business Description and Significant Accounting Policies (continued)

Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is provided by a combination of straight-line and accelerated methods over the estimated useful lives, which range from 3 to 40 years.

Revenue in Excess of Expenses

The consolidated statements of operations and changes in net assets include revenue in excess of expenses. Operating revenue includes revenue generated from direct patient care and related support services. Gains or losses not directly related to the ongoing operations of the Foundation or that occur infrequently are reported as other income (expense). Other income (expense) primarily consists of investment income, contributions and equity in net earnings of unconsolidated affiliates. Other changes in unrestricted net assets, which are excluded from revenue in excess of expenses, consistent with industry practice, primarily include changes in unrealized gains and losses on investments.

Principles of Consolidation

The consolidated financial statements include the accounts and balances of the Foundation and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Fair Value of Financial Instruments

Except as otherwise noted, the carrying value of all financial instruments of the Foundation approximates fair value.

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

2. Net Patient Service and Premium Revenue

The Foundation has agreements with third-party payors that provide for payments to the Foundation at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, discounted charges and per diem payments. Net patient service revenue is reported at the estimated realizable amounts from patients, third-party payors and others for services rendered. Provisions for estimated third-party adjustments are estimated in the period the related services are rendered and are adjusted in future periods as actual payments are determined. Premium revenue consists of net capitation payments from the following:

	Year ended June 30 2004	Six months ended June 30 2003
Physicians Plus Insurance Corporation (PPIC)	\$45,905,268	\$19,706,825
University Healthcare, Inc.	33,760,260	15,974,866
Group Health Cooperative (GHC)	17,453,208	8,475,312
	\$97,118,736	\$44,157,003

As of June 30, 2004 and 2003, approximately 13% and 11%, respectively, of net patient receivables are due from Medicare and Medicaid.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to varying interpretation. During the last few years, as a result of nationwide investigations by governmental agencies, various health care organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which in some instances have resulted in organizations entering into significant settlement agreements. 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 potential exclusion from the Medicare and Medicaid programs. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

3. Income Taxes

The Foundation recognized an income tax benefit of \$0 and \$95,000 at June 30, 2004 and 2003, respectively.

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

4. Charity Care

Charity care represents patient care services rendered at reduced or no fees due to the inability of the patient to pay for services. The estimated amount of charity care provided, measured as foregone charges, totaled approximately \$2,836,400 and \$7,306,300 for the six months ended June 30, 2003, and year ended June 30, 2004, respectively. In addition to providing charity care, the Foundation provides other programs and services for the general community. These programs and services consist of health promotion and education, health clinics, screenings and counseling.

5. Investments

The composition of investments at June 30, 2004 and 2003, is set forth in the following table:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2004:				
Cash and short-term investments	\$ 3,912,225	\$ 9,819	\$ -	\$ 3,922,044
U.S. Treasury obligations	4,088,047	-	(90,387)	3,997,660
U.S. government and agency securities	7,501,125	71,078	(98,328)	7,473,875
U.S. corporate obligations	6,783,690	-	(100,692)	6,682,998
Total investments	<u>\$22,285,087</u>	<u>\$ 80,897</u>	<u>\$(289,407)</u>	<u>\$22,076,577</u>
June 30, 2003:				
U.S. Treasury obligations	\$ 8,329,297	\$ 1,094	(176,321)	8,154,070
U.S. government and agency securities	1,163,262	5,596	(7,446)	1,161,412
U.S. corporate obligations	11,585,145	180,682	(9,507)	11,756,320
Total investments	<u>\$21,077,704</u>	<u>\$187,372</u>	<u>\$(193,274)</u>	<u>\$21,071,802</u>

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

5. Investments (continued)

The amortized cost and fair value of debt securities at June 30, 2004, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations.

	Amortized Cost	Fair Value
Available for sale:		
Due in one year or less	\$ 6,522,449	\$ 6,461,149
Due after one through five years	15,762,638	15,615,428
	\$22,285,087	\$22,076,577

The following table summarizes the unrealized losses on investments held at June 30, 2004:

	Less than Twelve Months		Twelve Months or Longer	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2004:				
Cash and short-term investments	\$ 3,922,044	\$ -	\$ -	\$ -
U.S. Treasury obligations	3,997,660	(90,387)	-	-
U.S. government and agency securities	7,473,875	(98,328)	-	-
U.S. corporate obligations	6,682,998	(100,692)	-	-
Total investments	\$22,076,577	\$(289,407)	\$ -	\$ -

6. Advances to, Interests in Net Assets and Investment in Unconsolidated Affiliates

Advances to, interests in net assets and investment in unconsolidated affiliates consisted of the following at June 30:

	2004	2003
Madison Medical Center (MMC)	\$3,528,989	\$3,407,374
Physicians Plus Surgery Center (PPSC)	3,161,989	2,198,777
University Healthcare, Inc. (UHC)	1,094,354	-
Other	239,842	186,991
	\$8,025,174	\$5,793,142

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

6. Advances to, Interests in Net Assets and Investments in Unconsolidated Affiliates (continued)

The MMC investment represents a 38% interest in a limited liability partnership accounted for under the equity method of accounting. The interest in net assets of PPSC represents a 50% interest in the net assets of a 501(c)3 organization accounted for using a method of accounting similar to the equity method. The UHC advance was made to facilitate the pending transaction described in Note 14.

Summarized financial information for MMC and PPSC is as follows at June 30, 2004:

Assets	\$10,296,015
Liabilities	<u>501,669</u>
Net assets	<u><u>\$ 9,794,346</u></u>

7. Property, Plant and Equipment

Property, plant and equipment are summarized as follows at June 30:

	2004	2003
Land	\$ 5,867,568	\$ 5,855,566
Buildings and leasehold improvements	60,264,863	59,949,104
Medical and office equipment	43,629,727	46,389,863
	109,762,158	112,194,533
Less accumulated depreciation	(45,888,318)	(47,532,064)
	\$63,873,840	\$ 64,662,469

8. Estimated Medical Claims Payable

The Foundation has a provider agreement with Physicians Plus Insurance Corporation (PPIC), requiring the Foundation to provide medical services to the members of PPIC in exchange for a per member, per month payment. PPIC withholds from the Foundation's capitation payment amounts paid to other providers on behalf of the Foundation. At June 30, 2004 and 2003, liabilities for estimated claims incurred but not reported by other health care providers were \$1,487,500 and \$1,318,800, respectively, and are included in accrued expenses in the consolidated balance sheets.

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

9. Long-Term Obligations

Long-term obligations as of June 30, are as follows:

	2004	2003
Wisconsin Health and Educational Facilities Authority Variable Rate Demand Revenue Bonds, Series 2000, variable interest at 1.04% as of June 30, 2004 (1.03% as of June 30, 2003), due in a balloon payment in 2030	\$47,500,000	\$48,400,000
Wisconsin Health and Educational Facilities Authority Variable Rate Demand Revenue Bonds, Series 2002C, variable interest at 1.23% as of June 30, 2004 (1.13% as of June 30, 2003), due in annual principal payments of \$150,000 through the year 2017	1,950,000	2,100,000
Revolver notes, interest at 4.20% at June 30, 2003	–	3,000,000
MMC obligation under capital lease, annual payments of \$1,269,800 to \$1,562,000 including interest at 12.76%, due in monthly installments through 2010	6,264,868	6,722,057
Note payable, quarterly principal payments of \$190,000, variable interest at 3.8125% as of June 30, 2004, (2.31% as of June 30, 2003), due January 2008	2,850,000	3,610,000
Other unsecured notes payable to former PPMG shareholders, monthly payments of \$2,656, through August 2003, including interest at 7.5% as of June 30, 2003	–	5,246
	58,564,868	63,837,303
Less current maturities	(2,369,909)	(5,238,590)
	\$56,194,959	\$58,598,713

The owners of the Series 2002C and 2000 Bonds may elect to have their Bonds purchased on any business day at a price equal to the purchase price. Pursuant to a remarketing agreement between the Foundation and a remarketing agent, the remarketing agent has agreed to offer for sale and use its best efforts to sell the Series 2002C and 2000 Bonds if optionally or mandatorily tendered for purchase.

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

9. Long-Term Obligations (continued)

The Foundation has transferable irrevocable direct pay letters of credit with banks, under the terms of which the banks agree to loan to the Foundation the amount necessary to purchase the Series 2002C and 2000 Bonds if not remarketed. The maximum amount of the liquidity loans would be the principal (\$1,950,000 and \$47,500,000 for the Series 2002C and 2000 Bonds, respectively, at June 30, 2004, plus accrued interest). The transferable irrevocable direct pay letters expire January 15, 2007 and May 15, 2008, for the Series 2002C and 2000 Bonds, respectively. These letters of credit are collateralized with real estate owned by the Foundation.

In conjunction with the issuance of the Series 2000 Bonds, the Foundation paid \$255,000 to enter into an interest rate cap agreement with a third party. The interest rate cap agreement will limit the Foundation's exposure to increases in interest rates on the 2000 Bonds to a maximum annual interest rate of 7%. The term of the interest rate cap agreement is the shorter of 30 years or the termination of the bonds. The fair value of the interest rate cap agreement approximates \$0 and \$200 at June 30, 2004 and 2003, respectively, and is recorded as an other noncurrent asset in the consolidated balance sheets.

The Foundation has revolver notes from a local bank under which it may borrow up to \$25,000,000 at variable interest rates based on prime or LIBOR plus 100 basis points. Borrowings under this agreement in 2004 and 2003 totaled \$3,000,000 and \$8,000,000, respectively, of which \$0 and \$3,000,000, respectively, are outstanding at June 30, 2004 and 2003.

The Foundation leases certain office space from MMC, which is treated as a capital lease. Total principal and interest payments made to MMC in 2004 and 2003 were approximately \$1,288,800 and \$633,400, respectively. The Foundation is also subject to contingent rentals based on the amount of MMC total rental and general administrative expenses over \$540,000. The amount of these contingent rental expenses was \$464,100 and \$212,500 in 2004 and 2003, respectively.

Certain of the Foundation's operating facilities and equipment are leased under capital leases. Included in property, plant and equipment at June 30, 2004 and 2003, are approximately \$4,041,601 and \$4,651,650 of such assets, net of \$3,958,399 and \$3,348,300 of accumulated depreciation.

The Foundation also has a bank term loan with credit available up to \$5,890,000 at variable interest rates based on prime or LIBOR. As of June 30, 2004 and 2003, \$2,850,000 and \$3,610,000, respectively, is outstanding on the term loan.

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

9. Long-Term Obligations (continued)

Certain loan agreements require maintenance of certain debt service coverage ratios, cash balances and compliance with various other restrictive covenants.

At June 30, 2004, the Foundation also has an unused letter of credit of \$200,000, which expires May 1, 2005.

Scheduled principal payments on long-term obligations for the next five years and thereafter are as follows:

2005	\$ 3,137,458
2006	3,277,284
2007	3,318,321
2008	3,270,549
2009	2,744,065
Thereafter	<u>45,921,607</u>
Subtotal	61,669,284
Less amount representing interest on obligations under capital leases	(3,104,416)
Less current portion	<u>(2,369,909)</u>
	<u><u>\$56,194,959</u></u>

The estimated fair value of long-term obligations, based on discounted cash flows at management's estimated current borrowing rates, approximates \$60,815,000 and \$67,764,000 at June 30, 2004 and 2003, respectively.

10. Related Parties

The Foundation reimburses the Medical School and University for operating supplies and for salaries paid to administrative and professional staff who also work for the Foundation. Total operating expenses pursuant to this arrangement are \$46,864,488 and \$24,183,343 in 2004 and 2003, respectively. Included in accounts payable and accrued expenses at June 30, 2004 and 2003, are \$1,275,000 and \$1,851,600, respectively, owed to the Medical School and to the University. In addition, support is provided to the Medical School and University annually (see Note 12).

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

10. Related Parties (continued)

The Foundation entered into a letter of understanding with University Health Care, Inc. (UHC), a not-for-profit corporation, to allow UHC to enter into managed care contracts on behalf of the Foundation, subject to the Foundation President's approval of Foundation reimbursement. Such an arrangement has been entered into for the benefit of providing physician services for Unity enrollees, and the Foundation shares the losses related to the purchased services risk pool. In 2004 and 2003, the Foundation incurred gains of \$2,396,400 and \$1,278,400, respectively, on the risk-sharing agreement. In addition, the Foundation provided funding support to UHC of \$861,930 and \$410,088 in 2004 and 2003, respectively, for certain administrative operations.

The Foundation has a \$1,154,000 interest-bearing note receivable from Physicians Plus Investment Group, LLP, which is owned by certain Foundation physician employees. The entire principal balance of this note is due on February 1, 2008, unless accelerated pursuant to the terms of the note agreement and is included in other assets in the consolidated balance sheets.

In 2003, the Foundation provided funding support of \$706,632, to University Community Clinics, Inc. (UCC) for funding support of certain clinical operations.

The Foundation also received support of \$5,069,800 and \$786,200 for personal services provided by staff to the hospital and support of regional activities from UWHCA in 2004 and 2003, respectively.

11. Retirement Plans and Profit-Sharing Plan

The Foundation has a Money Purchase Pension Plan (the Plan), covering substantially all Foundation physicians. Physician employees contribute a percentage of their salaries, up to defined limits, to the Plan.

The Foundation has a qualified defined-contribution retirement plan and a profit-sharing plan for substantially all full-time nonphysician employees upon completion of one year of service. Contributions are based on a percentage of participants' salaries and wages. Total defined-contribution retirement plan and profit-sharing expense was approximately \$5,513,200 and \$2,431,400 in 2004 and 2003, respectively.

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

12. Commitments and Contingencies

The Foundation is subject to various legal proceedings and claims, which are incidental to its normal business activities. In the opinion of the Foundation, the ultimate liability with respect to these actions will not materially affect the operations or net assets of the Foundation.

Under the terms of an agreement (the Medical School Development Fund Agreement) between the Foundation and the University of Wisconsin Medical School, the Foundation will contribute to the Medical School Development Fund (MSDF). Total MSDF expenses pursuant to these arrangements are \$21,603,419 and \$10,460,629 in 2004 and 2003, of which \$7,353,419 and \$5,710,629 are due to the MSDF at June 30, 2004 and 2003, respectively. In 2004 and 2003, the Foundation was required to contribute the greater of 8.1% of professional receipts or the lesser of \$19,000,000 or 9% of professional receipts in any given fiscal year. The Medical School Development Fund Agreement can be renegotiated under certain circumstances as defined in the Medical School Development Fund Agreement.

The Foundation is required under the Agreement to make contributions to a Departmental Research and Development Fund. A minimum of 2.5% of net departmental professional receipts must be transferred to special accounts at the University of Wisconsin Foundation (UWF). The funds in the special accounts are to be used to support departmental research as determined by the Medical School's Departmental Executive Committee. Total fund expenses pursuant to this arrangement are \$9,840,491 and \$6,068,073 in 2004 and 2003, of which \$327,269 and \$873,002 are due to the University of Wisconsin Foundation (UWF) as of June 30, 2004 and 2003, respectively.

The Foundation rents certain equipment, office and clinical space under noncancelable lease agreements. Total rental expense was approximately \$4,118,400 and \$1,472,500 in 2004 and 2003, respectively.

A schedule of future minimum rental payments for the next five years is as follows:

2005	\$ 3,055,527
2006	2,646,164
2007	2,076,480
2008	1,546,344
2009	723,501
Thereafter	1,963,913
	<u>\$12,011,929</u>

University of Wisconsin Medical Foundation, Inc.
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Notes to Consolidated Financial Statements (continued)

13. Professional Liability Insurance

The Foundation has professional liability insurance covering nonphysician employees for claim losses up to \$1,000,000 per occurrence and \$3,000,000 per policy year. Losses in excess of this coverage are covered by a \$10,000,000 excess liability policy. All Foundation employed physicians are state of Wisconsin employees; as such, they have professional liability coverage through the State of Wisconsin Self-Funded Liability Program. Accrued expenses include a reporting endorsement of \$274,650 at June 30, 2004.

As a result of the Foundation's purchase of Physicians Plus Medical Group (PPMG), the former PPMG physicians also became state of Wisconsin employees with corresponding professional liability coverage through the State of Wisconsin Self-Funded Liability Program. For claims pertaining to services provided prior to February 1, 1998, the Foundation is liable up to its deductibles, which are not greater than \$200,000. Losses in excess of the deductibles up to \$1,000,000 are covered by an insurance company. Losses in excess of \$1,000,000 are covered by the patient's compensation fund. Accrued expenses include \$285,000 at June 30, 2004 and 2003, respectively, for the estimated deductibles to be paid on prior claims.

14. Subsequent Event

The Foundation is a member of UHC, a 501(c)(3) not-for-profit, nonstock corporation. UHC intends to exercise its direct option to purchase back its interest in Unity Health Insurance (Unity) from Blue Cross Blue Shield of Wisconsin (BCBS-Wi) and through its membership in Community Health Systems, LLC (CHS), exercise CHS's option to buy back the CHS interests in Unity from BCBS-Wi.

By virtue of its interest in CHS and through a previous transaction, UHC possesses an option to acquire Unity at book value. UHC has notified BCBS-Wi of its intent to exercise each option, and the transaction is expected to close in December 2004.

UWMF and UWHCA, both members of UHC, intend to provide the equity necessary for UHC to purchase Unity. These members previously provided certain advances to UHC in order to allow UHC to purchase all of the remaining voting membership interests in CHS. At the time the transaction closes, the remaining equity necessary for the purchase of Unity at book value is estimated to be \$40,000,000. UWMF intends to provide 40% of the remaining necessary equity.