

THE UNIVERSITY OF MICHIGAN
REGENTS COMMUNICATION

Approved by the Regents
June 18, 2009

REQUEST FOR ACTION

SUBJECT: Michigan Health Corporation (MHC) Annual Business Plan

ACTION REQUESTED: Approve the MHC FY2010 Annual Business Plan and Budget

BUSINESS PLAN:

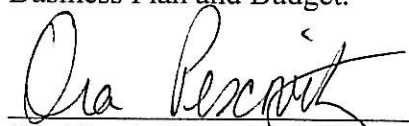
The Bylaws of MHC provide that MHC will annually submit a business plan to the Board of Regents for approval. MHC submitted its last business plan to the Board of Regents in June 2008. Since that time, MHC has focused on the operations of its existing subsidiaries and established the West Michigan Radiation Oncology joint venture with Metropolitan Hospital in Wyoming, Michigan.

In September 1996, the Regents approved the initial business plan and capitalization for MHC in the amount of \$30 million. As of June 30, 2009, MHC will have committed \$20.1 million to existing projects. MHC will begin its fourteenth year of operations in FY2010. The ventures in which MHC participates are expected to generate approximately \$107 million in net patient revenues in FY2010. MHC's share of these revenues, based on MHC's ownership interest in the ventures, is approximately \$27 million.

At the April Board meetings, the Board of MHC and the Sole Member Representative unanimously approved the FY2010 Business Plan for submission to the Board of Regents.

APPROVAL REQUESTED:

The Board of MHC recommends that the Board of Regents approve the MHC FY2010 Annual Business Plan and Budget.



Ora Hirsch Pescovitz, M.D.
Executive Vice President for Medical Affairs
Chair, Chief Executive Officer & Sole Member Representative, MHC

June 2009

MICHIGAN HEALTH CORPORATION
FISCAL YEAR 2010 ANNUAL BUSINESS PLAN



June 2009

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I. MHC OVERVIEW

A. Introduction

The Fiscal Year 2010 (FY2010) Business Plan for Michigan Health Corporation (MHC) provides an overview of the direction for MHC and its subsidiary organizations, as MHC begins its fourteenth year of operation.

The subsidiary organizations are grouped as to whether they are consolidated or unconsolidated on MHC's financial statements. Consolidated subsidiaries are organizations in which MHC maintains greater than fifty percent ownership. Unconsolidated subsidiaries are organizations in which MHC maintains ownership of fifty percent or less.

An overview of MHC, an operational and financial assessment, and the MHC Fiscal Year 2010 Budget are included in this business plan. In the Operational and Financial Assessment section, information is provided regarding capital allocation, management of MHC, future subsidiaries and capitalization, and subsidiary financial performance reviews. The MHC Fiscal Year 2010 Budget section highlights elements of the FY2010 budget and is followed by the MHC FY2010 budget statements.

B. Structure and Governance

MHC is a non-profit, non-stock membership corporation solely owned and operated by the University. MHC, the University of Michigan Medical School (UMMS), and the University of Michigan Hospitals and Health Centers (HHC) comprise the University of Michigan Health System (UMHS). The Executive Vice President for Medical Affairs is the Member Representative of MHC.

The MHC Board meets on a regular basis or as necessary to conduct business. The Board of Directors are: Ora Hirsch Pescovitz, M.D., Executive Vice President for Medical Affairs (Chair and Chief Executive Officer); Douglas Strong, Executive Director of the Hospitals and Health Centers (Vice Chair and Chief Operating Officer); Timothy Slottow, Chief Financial Officer of the University (Treasurer); James Woolliscroft, M.D., Dean of the Medical School (Secretary); and Glenna Schweitzer, Associate Vice Provost and Executive Director of the Office of Budget and Planning of the University.

All proposed activities that are presented to the MHC Board for approval are first reviewed and endorsed by the MHC Management Committee. The Committee is chaired by Thomas Campbell, the Associate Vice President for Strategic Planning and Business Development. Members of the Committee include Douglas Strong, the Chief Operating Officer of MHC, an Associate Professor of Internal Medicine from the Medical School, the Senior Finance Director and Revenue Cycle Officer of the HHC, the Administrative Director for MHC and representatives from the University Tax Office and the Office of General Counsel. The performance of each MHC subsidiary organization is reviewed annually by the MHC Management Committee. In this process, the goals of each subsidiary and its overall performance are reviewed, and goals for the coming year are assessed.

MHC staff monitor the activities of the ventures on an ongoing basis. Financial statements from the ventures are reviewed monthly and various activities are tracked, including trend analyses. The MHC Administrative Director also attends board meetings for most of the subsidiary companies; actively participates in the MDS Finance and Operations Committee; and interfaces regularly with venture representatives to assist with problem solving and assuring that venture and MHC needs are being met. MHC staff also began attending the radiation oncology venture finance and operations committee meetings this past year.

C. Fiscal Year 2009 and 2010 Activities

During this past year, the MHC administrative staff focused on operational and financial reviews of the subsidiaries' performance and examined financial and cash flow relationships between MHC and UMHS and between MHC and its subsidiaries. As a result of this focus and the needs of the subsidiaries, MHC accomplished the following during fiscal year 2009 (FY2009):

- Established the West Michigan Radiation Oncology (WMRO) joint venture with Metropolitan Hospital in Wyoming, Michigan;
- Is expected to attain a favorable margin of revenue over expense in the amount of \$1,674,338;
- Received total cash distributions of \$1,028,625 from the radiation oncology ventures and earned an estimated \$378,000 from Great Lakes Lithotripsy, LLC;
- Worked closely with Renal Research Institute, LLC (RRI) and Michigan Dialysis Services, LLC (MDS) leadership to monitor and improve MDS financial and operational performance focusing on accounts receivable, supply costs and staffing;
- Completed an investment analysis with the Department of Radiation Oncology and implemented a new investment model with Radiation Oncology investing 25% in the MHC radiation oncology ventures;
- Began assessing the possibility of participating in the Particle Therapy Institute of Michigan (PTIM);
- Educated the non-profit venture boards regarding the Internal Revenue Service changes on the Form 990; and
- Oriented new Department of Radiation Oncology venture representatives to the venture issues and MHC requirements.

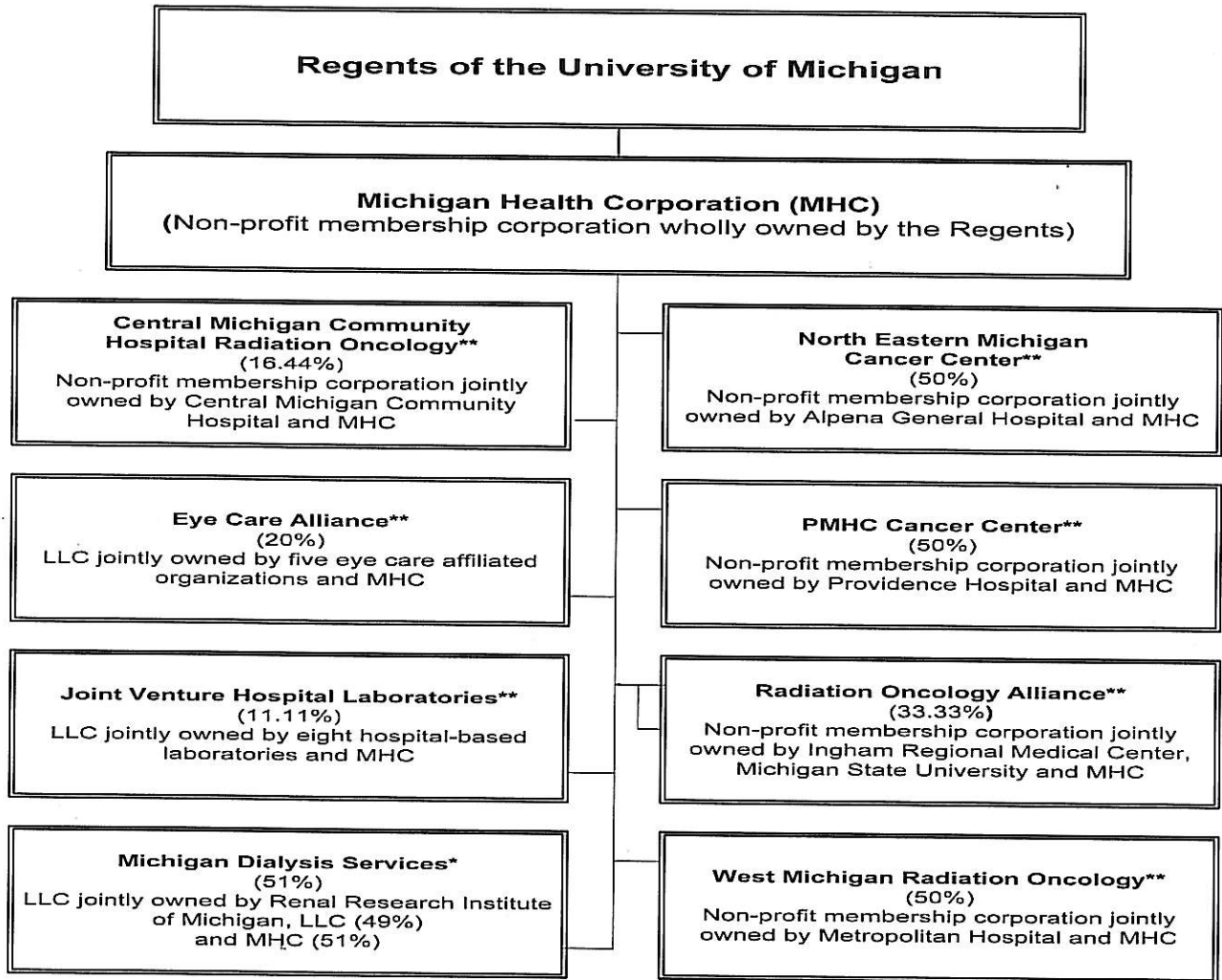
For FY2010, MHC administrative staff will focus on the following activities:

- Work with the project representatives in aggregate to reach overall target margins for MHC in support of MHC's FY2010 budgeted margin of \$2,069,475;
- Continue development of WMRO;
- Evaluate the potential for new projects relating to the advances in technology and new projects resulting from changes in the UMHS and health care environment, particularly in the area of radiation oncology and participation in PTIM (see note below);
- Analyze and evaluate MDS staffing levels and payment strategies and investigate alternatives to improve productivity and decrease the cost per treatment;
- Modify MDS agreements and policies to address Centers for Medicare and Medicaid Services changes;
- Evaluate additional growth opportunities for MDS;
- Monitor changes in Eye Care Alliance (ECA) to assure Delta Vision continues to fund all costs previously covered by the partners; and
- Continue to educate venture and MHC leadership on the new IRS reporting requirements, implement changes, institute additional policies and procedures as needed, and initiate data collection for new form requirements.

NOTE: PTIM is a collaboration between UMHS, Henry Ford Health System, St. John/Ascension, and the Karmanos Cancer Institute. These four organizations continue to make progress as a collaborative in evaluating and delivering a particle beam therapy service located at a neutral site for the citizens of the State of Michigan. PTIM will be providing a heavy ion (carbon) accelerator to deliver cancer treating therapies to patients. Carbon therapy, currently not available in the United States, has shown extraordinary results in effectively treating cancer in Japan and Germany. It is also much more effective in treating tumors than current radiation therapy or proton therapy. The collaborative approach ensures a broad patient base will be secured and more patients will benefit from this technology. This also expands the opportunities for collaboration around research and other clinical programs.

D. MHC Subsidiary Organizations

As MHC completes its thirteenth year of operation, the MHC Board has approved a total of eighteen (18) subsidiary organizations since its activation in 1996. Ten subsidiaries, or proposed subsidiaries, have been terminated and eight subsidiaries are operational. Participation in PTIM is being evaluated. The following chart shows each of the current subsidiary organizations under MHC. WMRO is a newly developed venture that has been added since last year's report. Michigan Healthcare Partners d/b/a Kids Care of Michigan was a venture that was dissolved in FY2009 and deleted from the chart below. The subsidiaries are identified as to whether they are consolidated or unconsolidated on MHC's financial statements. Consolidated subsidiaries are organizations where MHC maintains greater than a fifty percent ownership.



NOTES as of June 2009:

*Consolidated Venture on MHC's financial statement (e.g. greater than 50% ownership)

**Unconsolidated Ventures on MHC's financial statement (e.g. 50% or less ownership)

The percentages noted above indicate MHC's ownership interest in each venture.

MHC also owns Class B membership interest in Great Lakes Lithotripsy, LLC.

II. OPERATIONAL & FINANCIAL ASSESSMENT

A. Capital Allocation

Capitalization for MHC is provided predominantly by a loan under the Loan Agreement with HHC or equity transfers from HHC and clinical departments of the Medical School. Decisions to provide capitalization to MHC subsidiary organizations through a loan or through an equity transfer from MHC are made based on an evaluation of the needs of the system as a whole. This evaluation includes the prospects for a return on investment to MHC as well as to the Hospitals and Health Centers and/or the Faculty Group Practice of the Medical School.

As of June 30, 2009, \$20.1 million of the initial capitalization is expected to be committed to MHC and its subsidiaries, of which \$16.2 million is expected to have been invested (See Table 1 below).

Table 1. MHC Capital Allocation for Board Approved Subsidiaries

	MHC Approved Commitment	Net Changes	MHC Approved Commitment	MHC Investment	Net Changes	MHC Investment
	6/30/08		6/30/09	6/30/08		6/30/09
MHC Current Subsidiaries						
Central Michigan Community Hospital Radiation Oncology	\$917,800	(\$82,200)	\$835,600	\$917,800	(\$128,625)	\$789,175
Eye Care Alliance	\$333,800		\$333,800	\$321,800		\$321,800
Joint Venture Hospital Laboratories	\$15,000		\$15,000	\$15,000		\$15,000
Michigan Dialysis Services	\$4,389,743		\$4,389,743	\$3,046,381		\$3,046,381
North Eastern Michigan Cancer Center	\$1,880,127	(\$500,000)	\$1,380,127	\$1,880,127	(\$500,000)	\$1,380,127
PMHC Cancer Center	\$4,185,685	(\$400,000)	\$3,785,685	\$4,185,685	(\$ 400,000)	\$3,785,685
Radiation Oncology Alliance	\$-0-		\$-0-	(\$3,000)		(\$3,000)
West Michigan Radiation Oncology	\$400,000		\$400,000	\$-0-	\$400,000	\$400,000
Subtotal	\$ 12,122,155	(\$982,200)	\$11,139,955	\$10,363,793	(\$628,625)	\$9,735,168
Closed and Non-Active Ventures	\$727,789		\$727,789	(\$1,757,852)		(\$1,757,852)
MHC Administrative Operations*	\$7,787,825	\$450,000	\$8,237,825	\$7,737,825	\$500,000	\$8,237,825
Totals	\$20,637,769	(\$532,200)	\$20,105,569	\$16,343,766	(\$128,625)	\$16,215,141

* Includes a \$210,000 investment in mobile Lithotripsy.

B. Management

The operation and management of MHC is provided through a Management Agreement with the University. As a result, the business, administrative and management services are provided by employees of UMHS. MHC has 2.90 full time equivalents dedicated to the operations, management and financial reporting of MHC.

PricewaterhouseCoopers, LLP, MHC's auditors, performed procedures testing of MHC's activities for the fiscal year ending June 30, 2008.

C. Future Capitalization and Development

The sole member representative of MHC, together with the Board of MHC, will allocate any additional capitalization for MHC for development of new MHC projects and subsidiary organizations up to the initially approved capitalization of \$30,000,000. The initial approval in September 1996 made financing available through a combination of equity transfers and loan agreements between MHC and the Regents. The HHC was identified as the primary source of financing. Some funding is provided by clinical departments in the Medical School in support of their ventures. Future capitalization for MHC is considered as part of the UMHS capital planning and allocation process.

The Board of MHC will continue to meet as necessary to review the status of its current subsidiaries and develop and approve new projects, based on the needs of UMHS and the changing health care environment. MHC will also continue to perform the necessary legal and financial due diligence for every new project it considers. All projects approved by MHC will remain consistent with and supportive of the University's missions and the purpose and intent of MHC. Future projects that MHC participates in during the term of this business plan will be reported to the Board of Regents as necessary.

D. Financial Performance of Subsidiaries

Most MHC subsidiaries are past their development and start-up stages and are now in ongoing operations. The exception to this is WMRO, which began treating patients in November 2008. Participation in the Particle Therapy Institute of Michigan is a potential future MHC activity. MHC will continue to focus on operational and financial performance reviews and address what management and funding actions to take if subsidiaries do not meet their activity and financial goals. The most significant changes that occurred in FY2009 were the start up of WMRO; an investment analysis of the radiation oncology ventures and changing the funding model of these ventures; orientation of new administrative staff in the Department of Radiation Oncology to their multiple ventures in MHC; and analyzing and modifying MDS operations to improve its financial performance.

Although MHC operates with a July 1 to June 30 fiscal year, many of MHC's subsidiaries operate with a different fiscal year. This creates timing difficulties in developing and reporting budgets and projections to MHC and particularly in developing the MHC Annual Business Plan. Currently, the subsidiaries are held accountable for the annual budgets approved during the year by MHC as part of the venture budgeting process, not necessarily the revenue and expense reflected in the July to June period of the MHC Annual Business Plan.

The Consolidated Statement of Operations on page ten summarizes the projected net gain or loss for MHC as a whole and by venture. In FY2009, MHC is projected to have a favorable margin of \$1,674,338 that compares unfavorably to the budgeted margin of \$2,924,586 for FY2009. This difference is primarily the result of PMHC Cancer Center having a projected unfavorable variance of (\$1,505,695) due to decreased intensity-modulated radiation therapy procedures, implant cases, and fewer prostate cases and more head and neck cases.

III. MHC FISCAL YEAR 2010 BUDGET

The MHC Fiscal Year 2010 Budget was developed from each subsidiary's financial plan, MHC's financial statements, projected results of the subsidiary's operations, and known/planned changes for the coming fiscal year.

MHC's consolidated financial statements are displayed beginning on page nine. Highlights of those financial statements are identified below.

A. Schedule of Investments Summary

The Schedule of Investments displayed on page nine outlines the expected changes in approved capitalization for each subsidiary and MHC Administration from FY2009 to FY2010.

Currently, the MHC Board has approved commitments in the amount of \$20.1 million, including \$11.9 million to projects and \$8.2 million to MHC Administration. Of this approved commitment, \$8.0 million is approved to be transferred to the subsidiaries and \$8.2 million to MHC Administration as of June 30, 2009. The \$8.2 million for MHC Administration includes \$5.6 million for interest costs paid to HHC.

Assuming the MHC Board approves all of the anticipated capital requests from its subsidiaries in FY2010, the total commitment level that the MHC Board will have approved for its subsidiaries and Administration will be \$20.2 million. Of this approved amount, MHC is projecting to have transferred funds totaling \$16.3 million as of June 30, 2010. With \$20.2 million of the original \$30 million capitalization designated for investment in current subsidiaries and MHC Administration, \$9.8 million will be available for other projects or venture needs as of June 30, 2010.

B. Consolidated Statement of Operations Summary

The statement on page ten summarizes the FY2009 projected net margin and the FY2010 budget for MHC as a whole and by venture. This summary identifies the direct results of operations of the subsidiaries, but does not reflect ancillary benefits to the Health System such as increased research funding and professional net income or expanded patient care service opportunities for the Hospitals and Health Centers and the Medical School Faculty Group Practice.

MHC is budgeting an overall favorable net margin of \$2,069,475 for FY2010 compared to a projected margin of \$1,674,338 for FY2009. In FY2010, all ventures are expected to have a positive net margin

except CMCHRO. While CMCHRO has improved its margin over prior years, it is still struggling to build volume and will continue to work to generate a positive operating margin.

C. MHC Consolidated Financial Statements

MHC consolidated financial statements follow on pages nine and ten.

Michigan Health Corporation
Schedule of Investments
Budget for June 30, 2010

June 2009

	MHC Approved Commitment as of FY2009	Expected Changes in Commitment	MHC Expected Commitment as of FY2010	MHC Total Investment as of FY2009	Expected Changes in Investment	MHC Total Expected Investment as of FY2010
Consolidated Joint Ventures (A)						
Michigan Dialysis Services	\$ 4,389,743	\$ 0	\$ 4,389,743	\$ 3,046,381	\$ 0	\$ 3,046,381
Total Consolidated Joint Ventures	\$ 4,389,743	\$ 0	\$ 4,389,743	\$ 3,046,381	\$ 0	\$ 3,046,381
Unconsolidated Joint Ventures (B)						
Central Michigan Community Hospital Radiation Oncology	\$ 835,600	\$ (146,425)	\$ 689,175	\$ 789,175	\$ (100,000)	\$ 689,175
Eye Care Alliance	333,800		333,800	321,800		321,800
Joint Venture Hospital Laboratories	15,000		15,000	15,000		15,000
North Eastern Michigan Cancer Center	1,380,127	(200,000)	1,180,127	1,380,127	(200,000)	1,180,127
PMHC Cancer Center	3,785,685		3,785,685	3,785,685		3,785,685
Radiation Oncology Alliance	0		0	(3,000)		(3,000)
West Michigan Radiation Oncology	400,000	0	400,000	400,000	0	400,000
Total Unconsolidated Joint Ventures	\$ 6,750,212	\$ (346,425)	\$ 6,403,787	\$ 6,688,787	\$ (300,000)	\$ 6,388,787
Closed and Terminated Ventures						
Kids Care of Michigan (Michigan Healthcare Partners)	\$ 0	\$ 0	\$ 0	\$ (67,565)	\$ 0	\$ (67,565)
Michigan Health Management Corporation	550,000		550,000	550,000		550,000
Michigan Provider Network	0		0	0		0
Michigan Visiting Nurses - Consolidated	0		0	(2,418,076)		(2,418,076)
South Central Practice Association (Foote) (Jackson)	177,789	0	177,789	177,789	0	177,789
Closed and Terminated Ventures	\$ 727,789	\$ 0	\$ 727,789	\$ (1,757,852)	\$ 0	\$ (1,757,852)
Subtotal for All Ventures	\$ 11,867,744	\$ (346,425)	\$ 11,521,319	\$ 7,977,316	\$ (300,000)	\$ 7,677,316
Michigan Health Corporation - Administrative Activity	8,027,825	430,000 (C)	8,457,825	8,027,825	430,000 (C)	8,457,825
Mobile Lithotripsy	210,000		210,000	210,000		210,000
Funds Available to be Committed by the MHC Board	\$ 9,894,431	\$ (83,575)	\$ 9,810,856			
Regental Approved Limit on Capital Investment	\$ 30,000,000		\$ 30,000,000			
Remaining Funds Not Currently Invested				\$ 13,784,859	\$ (130,000)	\$ 13,654,859
Regental Approved Limit on Capital Investment				\$ 30,000,000		\$ 30,000,000

Notes:

- (A) Consolidated joint ventures are entities where MHC has an ownership percentage greater than 50%.
- (B) Unconsolidated joint ventures are entities where MHC has an ownership percentage up to 50%.
- (C) MHC-Admin's additional \$430,000 is approved with approval of the business plan.

Michigan Health Corporation
 Consolidated Statement of Operations
 ProForma Summary of Net Gain / (Loss) by Joint Venture
 as of June 30, 2010

	FY2008 Actual	FY2009 Budget	FY2009 Projection	FY2010 Budget
<u>Consolidated Joint Ventures</u>				
Michigan Dialysis Services (51.00%)	\$ 30,048	\$ 339,431	\$ 18,426	\$ 28,271
Michigan Health Management Corporation (100.00%)	6,476	0	0	0
Net Gain / (Loss) in Consolidated Joint Ventures	\$ 36,524	\$ 339,431	\$ 18,426	\$ 28,271
<u>Unconsolidated Equity in Joint Ventures</u>				
Central Michigan Community Hospital Radiation Oncology (16.44%)	\$ (53,101)	\$ (23,846)	\$ (27,070)	\$ (837)
Eye Care Alliance (20.00%)	(586)	(139)	0	0
Joint Venture Hospital Laboratories (11.11%)	0	0	0	0
NEMCC (50.00%)	108,878	158,758	326,464	337,369
PMHC Cancer Center (50.00%)	2,070,969	2,541,177	1,035,482	1,121,943
Radiation Oncology Alliance (33.33%)	48,209	(3,489)	176,337	210,333
West Michigan Radiation Oncology (50.00%)	0	0	180,685	386,112
Equity in Net Gain / (Loss) in Unconsolidated Joint Ventures	\$ 2,174,369	\$ 2,672,462	\$ 1,691,897	\$ 2,054,919
Michigan Health Corporation - Administrative Activity	(155,621)	(87,306)	(35,985)	(13,715)
Total Excess Revenue / (Expenses)	\$ 2,055,273	\$ 2,924,586	\$ 1,674,338	\$ 2,069,475

Notes:

- MHC ownership interest shown in parenthesis after venture name.
- MHC's Partnership Health Program ended May 31, 2006. Final expenses shown in FY2008.
- ECA is anticipating no cash call in FY2010; any financial needs to be covered by Delta Vision.
- PMHC did better than anticipated in FY2008 due to IMRT procedures. This has dropped in FY2009 due to IMRT being down, implant cases being down, prostate cases are down while head and neck cases are up and due to changes in procedures, treatment aids are down.
- MHC Administration interest expense changes due to changes in the rate provided by the University Treasurer's Office on the HHC master loan as well as significant payments on the loan in FY2008 and FY2009. Interest rates were 4.535% in FY2008, 3.064% in FY2009 and are estimated at 1.65% for FY2010.