

# Mid-State Health Network

**Financial Statements**  
*September 30, 2014*



Mid-State Health Network  
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September 30, 2014

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## Independent Auditor's Report

Mid-State Health Network  
Lansing, Michigan

### Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and each major fund of Mid-State Health Network (the Entity) as of and for the year ended September 30, 2014, and the related notes to the financial statements, which collectively comprise the Entity's basic financial statements as listed in the table of contents.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditor's Responsibility*

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

### *Opinions*

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the Entity, as of September 30, 2014, and the respective changes in financial position, for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### *Change in Accounting Principle*

As discussed in Note 4 to the financial statements, Mid-State Health Network early implemented GASB Statement No. 69, Government Combinations and Disposals of Government Operations in fiscal year 2014. Our opinion is not modified with respect to these matters.

## **Other Matters**

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### **Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated March 27, 2015, on our consideration of the Entity's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Entity's internal control over financial reporting and compliance.

*Roslund, Prestage & Company, P.C.*

Roslund, Prestage & Company, P.C.  
Certified Public Accountants

March 27, 2015

**MANAGEMENT'S DISCUSSION  
AND ANALYSIS**



## **MID-STATE HEALTH NETWORK Management's Discussion and Analysis**

The summary financial information contained in this analysis is presented for the twelve-month period of October 1, 2013 through September 30, 2014. This analysis will help provide a context for the reader and assist in understanding the financial position of Mid-State Health Network (MSHN).

During fiscal year 2014, MSHN concluded a period of organizational development in preparation for beginning operations as a Prepaid Inpatient Health Network (PIHP) on January 1, 2014. There are twelve (12) Community Mental Health Service Programs (CMHSPs) consisting of Bay-Arenac Behavioral Health, Clinton-Eaton-Ingham Community Mental Health Authority, Community Mental Health for Central Michigan, Gratiot Community Mental Health Authority, Tuscola County Community Mental Health Authority, Huron County Community Mental Health Authority, Ionia County Community Mental Health Authority, LifeWays Community Mental Health Authority, Montcalm County Community Mental Health Authority, Newaygo County Community Mental Health Authority, Saginaw County Community Mental Health Authority, and Shiawassee County Community Mental Health Authority covering twenty-one (21) counties in the MSHN region.

During the initial three month time period covered in this analysis, MSHN organizational development costs, considered pre-award costs by the Michigan Department of Community Health, were funded exclusively by Medicaid Savings transferred to MSHN from the prior PIHPs in the MSHN region (Bay-Arenac Behavioral Health, Clinton-Eaton-Ingham Community Mental Health Authority, Community Mental Health for Central Michigan, and LifeWays Community Mental Health Authority) and recorded in MSHN financial statements as a revenue recognized from reserves.

Beginning January 1, 2014, MSHN entered into a contract with the State of Michigan for Medicaid funding, and entered into subcontracts with the CMHSPs in its region for the provision of Mental Health, Substance Use Disorder, and Developmental Disabilities services.

In April 2014 MSHN began to manage resources under Medicaid expansion referred to as Healthy Michigan. This program expands Medicaid coverage to persons at 133% of federal poverty. With the exception of persons previously cover by the Adult Benefit Waiver or provided service through CMHSP general or local funds, this populations treatment needs were largely unknown.

### **Financial Highlights**

- Reserves consist primarily of reserves received from the prior PIHPs: Medicaid Savings \$11,549,724 and Medicaid Internal Service Funds \$20,716,948 inclusive of interest earned this fiscal year.
- Net position at the end of the year was \$20,718,270.
- Unrestricted net position at the end of the year was \$1,322. This amount is equal to the interest earned on operating funds during our initial nine months as a PIHP.
- Medicaid funding received from MDCH is remitted to the CMHSPs within our region, upon receipt, net of taxes and MSHN administrative costs. Therefore, MSHN anticipated future unrestricted net position to consist only of interest earned on operating funds.

### **Operational Highlights**

- MSHN was established on July 1, 2013
- The Board of Directors first met in the month of July 2013.
- MSHN began the year with five (5) staff. During the year three (3) additional staff were hired. The total number of staff for MSHN is currently eight (8)

# MID-STATE HEALTH NETWORK

## Management's Discussion and Analysis

### Overview of Financial Statements

MSHN's financial statements comprise three components:

1. Government-wide financial statements
2. Fund financial statements
3. Notes to the financial statements

#### Government-Wide Financial Statements

The *Government-Wide Financial Statements* are designed to provide readers with a broad overview MSHN's finances in a manner similar to a private-sector business. This is accomplished by reporting the Entity's assets and liabilities using the full accrual method of accounting. In essence, this method requires the Entity to disclose borrowings, and compensated absences for employees on its financial statements.

The *Statement of Net Position* presents information on all of the Entity's assets and liabilities with the difference between the two reported as total net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Entity is improving or deteriorating.

The *Statement of Activities* presents information showing how the Entity's net position changed during the most recent fiscal year. All changes in the net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

#### Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources segregated for specific activities or objectives. The Entity, similar to state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the Entity may be divided into two categories: The Governmental Fund and the Internal Service Fund.

#### Governmental Funds

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financials, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirement.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The Entity adopts an annual budget for its General Fund. Budgetary comparison statements have been provided for the General Fund to demonstrate compliance with those budgets.

## MID-STATE HEALTH NETWORK Management's Discussion and Analysis

### Proprietary Funds – Internal Service Funds

Proprietary funds are used to account for the Entity's business-type activities. The Risk Reserve Funds are used to account for assets held as a reserve against potential liabilities relative to and as allowed by its contract with the Michigan Department of Community Health (MDCH). Pursuant to these contractual provisions, the Entity's risk management plan has been reviewed and approved by MDCH.

### Notes to Financial Statements

The notes provide additional information essential to a full understanding of the data provided in the government-wide and fund financial statements. The accompanying notes are an integral part of the financial statements and must be reviewed in conjunction with the information reported on the financial statements to provide a full understanding of the Entity's financial situation.

### Government-Wide Financial Analysis

#### Summary of Net Position

The following summarizes the assets, deferred outflows of resources, liabilities and net position on an agency-wide basis for the years ended September 30, 2014 and September 30, 2013.

<b>STATEMENT OF NET POSITION</b>		2014	2013
Cash and cash equivalents	\$18,179,827		
Restricted & other current assets	20,719,267		
Due from other governmental units	<u>19,139,492</u>		<u>\$118,524</u>
<b>Total Assets</b>	<b>58,038,586</b>		<b>118,524</b>
Payables	331,079		
Unearned Revenue	18,117,622		
Due to other governmental units	<u>18,871,614</u>		<u>118,524</u>
<b>Total Liabilities</b>	<b>37,320,315</b>		<b>118,524</b>
Restricted for risk management	20,716,948		
Unrestricted	<u>1,323</u>		
<b>Total Net Position</b>	<b><u>\$20,718,271</u></b>		<b><u>\$ 0</u></b>

Assets consist of Medicaid Savings, Medicaid Internal Service Funds and funds due from MDCH or the CMHSPs within our region. Liabilities consist of accruals for vendors and payroll, Medicaid Savings (unearned revenue), and funds due to the CMHSPs within our region.

#### Summary of Activities

The following summarizes the revenues, expenses and changes in net position on an agency-wide basis for the years ended September 30, 2014 and September 30, 2013.



**MID-STATE HEALTH NETWORK  
Management's Discussion and Analysis**

<b>CHANGES IN NET POSITION</b>		
	2014	2013
Interest	\$ 6,447	
Local Match Drawdown	2,951,151	
State Funding	<u>311,056,766</u>	<u>\$118,524</u>
Total Revenue	314,014,364	118,524
Taxes and Fees	21,387,408	
Local Match Drawdown	2,951,151	
Payments to CMHSP's	288,104,050	
PIHP Operations	<u>1,565,308</u>	<u>118,524</u>
Total Expenses	314,007,917	118,524
Medicaid ISF Transfer In	20,711,824	
Total Net Position	<u>\$ 20,718,271</u>	<u>\$ 0</u>

Revenue consists of Medicaid, DHS Incentive, Adult Benefit Waiver, and Local, and expense consists of PIHP operations, payments to member CMHSPs, taxes, and fees.

**Future Outlook**

In October 2014, MSHN became the Coordinating Agency for our region. The Entity began receiving Local Public Act 2 funds from the counties in our region for the provision of Substance Use Disorder (SUD) services, and received the Public Act 2 reserves from the prior Coordinating Agencies within our region. In addition, the Entity began receiving Community Grant funds from MDCH for the provision of SUD services.

MSHN has established risk and financial management strategies to assure ongoing stewardship and accountability. The expanded benefits and the additional responsibilities as the Coordinating Agency for SUD services create further uncertainty for MSHN.

**Contact Information**

As always, questions, comments, and suggestions are welcomed from interested parties and the general public. These can be directed to the Mid-State Health Network, Finance Department, 530 West Ionia, Suite F, Lansing, MI 48933.

**GOVERNMENT-WIDE  
FINANCIAL STATEMENTS**



Mid-State Health Network  
Statement of Net Position - Governmental Activities  
September 30, 2014

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**Assets**

Cash and cash equivalents - unrestricted	\$ 18,179,827
Due from other governmental units	19,139,492
Cash and cash equivalents - restricted	14,719,026
Investments - restricted	5,997,875
Other current assets	<u>2,366</u>

Total assets 58,038,586

**Liabilities**

Accounts payable	253,224
Due to other governmental units	18,871,614
Accrued payroll	77,855
Unearned revenue	<u>18,117,622</u>

Total liabilities 37,320,315

**Net position**

Restricted for risk management	20,716,948
Unrestricted	<u>1,323</u>

Total net position \$ 20,718,271

Mid-State Health Network  
Statement of Activities - Governmental Activities  
For the Year Ending September 30, 2014

	<u>Expenses</u>	<u>Program Revenues</u>		<u>Net (Expense) Revenue and Changes Net Position</u>
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	
<b>Functions</b>				
Governmental activities				
Health & welfare - mental health	<u>\$314,007,917</u>	<u>\$ -</u>	<u>\$314,007,917</u>	\$ -
General revenues				
Unrestricted investment revenue and net gains (losses)				1,323
Restricted investment revenue and net gains (losses)				<u>5,124</u>
Total general revenues				<u>6,447</u>
<b>Special items</b>				
Medicaid ISF transfer from Bay-Arenac Behavioral Health				6,696,604
Medicaid ISF transfer from Community Mental Health for Central Michigan				5,639,321
Medicaid ISF transfer from CMHA of Clinton, Eaton, & Ingham Counties				1,649,034
Medicaid ISF transfer from LifeWays Community Mental Health Authority				3,313,486
Medicaid ISF transfer from Saginaw County Community Mental Health Authority				<u>3,413,379</u>
Total special items				<u>20,711,824</u>
<b>Change in net position</b>				20,718,271
<b>Net position, beginning of year</b>				<u>-</u>
<b>Net position, end of year</b>				<u><u>\$ 20,718,271</u></u>

## FUND FINANCIAL STATEMENTS



Mid-State Health Network  
Governmental Funds Balance Sheet - General Fund  
September 30, 2014

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**Assets**

Cash and cash equivalents	\$ 18,179,827
Due from other governmental units	19,139,445
Other current assets	<u>2,366</u>
Total assets	<u><u>\$ 37,321,638</u></u>

**Liabilities**

Accounts payable	\$ 253,224
Due to other governmental units	18,871,614
Accrued payroll	77,855
Unearned revenue	<u>18,117,622</u>
Total liabilities	37,320,315

**Fund balance**

Unassigned	<u>1,323</u>
Total fund balance	<u><u>1,323</u></u>
Total liabilities and fund balances	<u><u>\$ 37,321,638</u></u>

There are no reconciling items from fund balance on the governmental funds balance sheet to net position on the statement of net position.

Mid-State Health Network  
Statement of Revenues, Expenditures and Changes in Fund Balances - General Fund  
Health & Welfare - Mental Health  
For the Year Ending September 30, 2014

**Revenues**

State funding	
Medicaid	\$ 290,989,522
Healthy Michigan	17,449,319
Autism	646,930
DHS Incentive	637,300
Adult Benefit Waiver	1,333,695
Total State funding	311,056,766
Contributions - Local match drawdown	2,951,151
Interest income	1,323
	314,009,240

**Expenditures**

Operating expenditures	
Salaries and wages	403,849
Fringe benefits	204,044
Legal and professional	16,086
Printing expense	36,500
Meeting expense	10,279
Other operating expense	64,657
Telephone expense	10,230
Board per diem	6,300
Consulting services	110,127
Rent expense	23,482
Insurance	38,644
Membership and dues	2,935
Supplies	8,443
Travel and conferences	40,985
Utilities	5,936
Total operating expenditures	982,497
Contract expenditures	
Use tax	13,075,472
HICA tax	2,709,678
Local match	2,951,151
HRA expense	5,598,965
Payments to affiliate members	288,104,050
Contractual services	586,104
Total contract expenditures	313,025,420
Total expenditures	314,007,917

**Excess of revenues over expenditures**

1,323

**Fund balance, beginning of year**

-

**Fund balance, end of year**

\$ 1,323

There are no reconciling items from the net change in fund balance on the statement of revenues, expenditures and changes in fund balances to the change in net position on the statement of activities.

Mid-State Health Network  
Statement of Net Position  
Proprietary Funds - Internal Service Fund  
September 30, 2014

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**Assets**

Cash and cash equivalents	\$ 14,719,026
Investments	5,997,875
Accounts receivable	47
Total assets	<u>20,716,948</u>

**Net position**

Restricted for risk management	<u>\$ 20,716,948</u>
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Mid-State Health Network  
Statement of Revenues, Expenses and Changes in Net Position  
Proprietary Funds - Internal Service Fund  
For the Year Ending September 30, 2014

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**Non-operating revenue**

Interest income \$ 5,124

**Special items**

Medicaid ISF transfer from Bay-Arenac Behavioral Health	6,696,604
Medicaid ISF transfer from Community Mental Health for Central Michigan	5,639,321
Medicaid ISF transfer from CMHA of Clinton, Eaton, & Ingham Counties	1,649,034
Medicaid ISF transfer from LifeWays Community Mental Health Authority	3,313,486
Medicaid ISF transfer from Saginaw County Community Mental Health Authority	3,413,379
Total special items	<u>20,711,824</u>

**Change in net position**

20,716,948

**Net position, beginning of year**

-

**Net position, end of year**

\$ 20,716,948

Mid-State Health Network  
Statement of Cash Flows  
Proprietary Funds - Internal Service Fund  
For the Year Ending September 30, 2014

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<b>Cash flows from investing activities</b>	
Revenue and net gains (losses) from investments	\$ 5,124
<b>Cash flows from special items</b>	
Special items - Medicaid ISF	20,711,824
<b>Net increase (decrease) in cash and cash equivalents</b>	<u>20,716,948</u>
<b>Cash and cash equivalents, beginning of year</b>	<u>-</u>
<b>Cash and cash equivalents, end of year</b>	<u><u>\$ 20,716,948</u></u>

**NOTES TO THE FINANCIAL STATEMENTS**



## **NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies of Mid-State Health Network (the Entity) conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The following is a summary of the significant accounting policies used by the Entity.

### **Reporting Entity**

Mid-State Health Network was formed by the CMHSP Participants to serve as the prepaid inpatient health plan (“PIHP”) for the twenty-one counties designated by the Michigan Department of Community Health as Region 5. The CMHSP Participants include Bay-Arenac Behavioral Health, Clinton-Eaton-Ingham Community Mental Health Authority, Community Mental Health for Central Michigan, Gratiot Community Mental Health Authority, Tuscola Community Mental Health Authority, Huron County Community Mental Health Authority, Ionia County Community Mental Health Authority, LifeWays Community Mental Health Authority, Montcalm County Community Mental Health Authority, Newaygo County Community Mental Health Authority, Saginaw County Community Mental Health Authority, and Shiawassee County Community Mental Health Authority.

Mid-State Health Network is a regional entity, which was formed pursuant to 1974 P.A. 258, as amended, MCL §330.1204b, as a public governmental entity separate from the CMHSP Participants that established it.

The accompanying financial statements have been prepared in accordance with criteria established by the Governmental Accounting Standards Board for determining the various governmental organizations to be included in the reporting entity. These criteria include significant operational financial relationships that determine which of the governmental organizations are a part of the Entity’s reporting entity, and which organizations are legally separate, component units of the Entity. Based on the application of the criteria, the Entity does not contain any component units.

### **Government-wide and Fund Financial Statements**

The government-wide financial statements (i.e. the statement of net position and the statement of activities) report information on all of the non-fiduciary activities of the Entity.

*Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include charges to consumers who purchase, use or directly benefit from services provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues.

Net position is restricted when constraints placed on it are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net position. When both restricted and unrestricted resources are available for use, generally it is the Entity’s policy to use restricted resources first, and then unrestricted resources as they are needed.

Major individual governmental funds are reported as separate columns in the fund financial statements.

### **Measurement Focus, Basis of Accounting and Financial Statement Presentation**

Government-wide Financial Statements – The government-wide financial statements (statement of net position and statement of activities) are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

**Governmental Fund Financial Statements** - The governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Entity generally considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

Intergovernmental revenue, charges for services and other revenues associated with the current fiscal period are all considered susceptible to accrual and have been recognized as revenue of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

**Proprietary Fund Financial Statements** – The financial statements of the proprietary funds are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide statements described above. Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The Entity reports the following major governmental funds:

**Governmental Funds**

*General Fund* – This fund is the Entity's primary operating fund. It accounts for all financial resources of the Entity, except those required to be accounted for in other funds.

**Proprietary Funds**

*Internal Service Fund* - This fund represents amounts set aside to fund the net uninsured exposure of potential shortfalls of contract revenues.

**Estimates**

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 expenditures during the reporting period. Actual results could differ from those estimates.

**Budgetary Data**

The Entity adopts an annual budget for the general fund. The budget is adopted and prepared on the modified accrual basis of accounting. The budget is also adopted at the function level. The budgeted revenues and expenditures for governmental fund types, as presented in this report, include any authorized amendments to the original budget as adopted.

**Cash and Cash Equivalents**

The Entity's cash and cash equivalents are considered to be cash on hand, money market funds, demand deposits and certificates of deposit.

**Receivables**

Due from other governmental units consist primarily of amounts due from the CMHSP Participants and due from MDCH.

**Inventories**

The Entity does not recognize as an asset inventories of supplies. The cost of these supplies is considered immaterial to the financial statements and the quantities are not prone to wide fluctuation from year to year. The costs of such supplies are expensed when purchased.

### **Unearned Revenue**

Unearned revenues arise when resources are received by the Entity before it has a legal claim to them. In subsequent periods, when the revenue recognition criterion is met, or when the Entity has a legal claim to the resources, the liability for unearned revenue is removed from the fund financial statements and government-wide financial statements, and revenue is recognized.

### **Deferred Outflows/Inflows of Resources**

In addition to assets, the financial statements will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. The Entity has no items that qualify for reporting in this category.

In addition to liabilities, the financial statements will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Entity has no items that qualify for reporting in this category.

### **Net Position and Fund Balances**

Restricted net position shown in the government-wide financial statements will generally be different from amounts reported as reserved/assigned fund balances in the governmental fund financial statements. This occurs because of differences in the measurement focus and basis of accounting used in the government-wide and fund financial statements and because of the use of funds to imply that restrictions exist.

#### Fund Balances

The Entity has implemented GASB Statement No. 54, "Fund Balance Reporting and Governmental Fund Type Definitions." This Statement provides more clearly defined fund balance categories to make the nature and extent of the constraints placed on a government's fund balances more transparent. The following classifications describe the relative strength of the spending constraints:

- *Nonspendable fund balance* - amounts that are in nonspendable form (such as inventory or prepaid expenditures) or are either legally or contractually required to be maintained intact.
- *Restricted fund balance* - amounts constrained to specific purposes by their providers (such as taxpayers, grantors, bondholders, and higher levels of government), through constitutional provisions, or by enabling legislation. The Entity would typically use restricted fund balance first, followed by committed resources, and then assigned resources as appropriate opportunities arise, but reserves the right to selectively spend unassigned resources first to defer the use of these classified funds.
- *Committed fund balance* - amounts constrained to specific purposes by the Entity itself, using its highest level of decision-making Entity (Entity's Board). To be reported as committed, amounts cannot be used for any other purpose unless the Entity takes the same highest level action to remove or change the constraint.
- *Assigned fund balance* - amounts the Entity intends to use for a specific purpose. Intent can be expressed by the Entity's Board or by an official or body to which the Board delegates the Entity.
- *Unassigned fund balance* - amounts that are available for any purpose. Positive amounts are reported only in the general fund.

#### Net Position - Restrictions

Net position in the government-wide financial statements are reported as restricted when constraints placed on net position use is either:

- Externally imposed by creditors, grantors, contributors, or laws or regulations of other governments, or
- Imposed by law through constitutional provisions or enabling legislation.

### **MDCH Revenue**

Mid-State Health Network serves as the Pre-Paid Inpatient Health Plan for the area that includes Arenac, Bay, Clare, Clinton, Eaton, Gladwin, Gratiot, Hillsdale, Huron, Ingham, Ionia, Isabella, Jackson, Mecosta, Midland, Montcalm, Newaygo, Osceola, Saginaw, Shiawassee, and Tuscola Counties. Mid-State Health Network contracts directly with the MDCH to administer mental health and substance abuse revenues for covered services provided to eligible residents of these counties.

**NOTE 2. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY**

**Budgetary Information**

Annual budgets are adopted at the functional level and on a basis consistent with generally accepted accounting principles for all governmental funds. All annual appropriations lapse at fiscal year-end. The Entity does not maintain a formalized encumbrance accounting system. The budgeted revenues and expenditures, as presented in this report, include any authorized amendments to the original budget as adopted.

**Excess of Expenditures over Appropriations**

P.A. 621 of 1978, Section 18(1), as amended, provides that a local unit shall not incur expenditures in excess of the amount appropriated.

During the current year, the Entity incurred expenditures in excess of the amounts appropriated as shown on the schedule in the back of this report.

**NOTE 3. DETAIL NOTES**

**Cash and Cash Equivalents**

At September 30<sup>th</sup> the carrying amount of the Entity's cash and investments was as follows:

Cash and Cash Equivalents	Amount
Petty Cash	\$ 200
Checking, Savings, & Money Market Accounts – unrestricted	18,179,627
Checking, Savings, & Money Market Accounts – restricted	14,719,026
Totals	\$ 32,898,853

**Restricted Cash and Investments**

- Cash and investments have been restricted in the Internal Service Fund in the amount of \$14,719,026 for the expected future risk corridor requirements of the MDCH contract.

Custodial Credit Risk – Deposits

Custodial credit risk is the risk that, in the event of a bank failure, the Entity's deposits might not be recovered. The Entity does not have a policy for custodial risk over deposits.

As of the end of the current fiscal year, \$32,652,070 of the Entity's \$32,902,070 bank balance was exposed to custodial credit risk because it was uninsured and uncollateralized. Deposits which exceed FDIC insurance coverage limits are held at local banks. The Entity believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the Entity evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution. Only those institutions with an acceptable estimated risk level are used as depositories.

Investments

At September 30<sup>th</sup>, the investments of the Entity were as follows:

Cash and Cash Equivalents	Amount
U.S. Agencies	\$5,997,875
Totals	\$ 5,997,875

State statutes authorize the Entity to invest in obligations and certain repurchase agreements of the United States Treasury and related governmental agencies, commercial paper, banker's acceptances of the United States banks, obligations of the State of Michigan or any of its political subdivisions, and mutual funds composed entirely of the above investments. See above for a listing of the Entity's investments.

The Entity's investment policy complies with the state statutes and has no additional investment policies that

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would limit its investment choices.

Credit Risk – Investments

State statutes limit investments in commercial paper to be rated at the time of purchase within the three highest classifications established by not less than two standard rating services. Investments in obligations of the State of Michigan or its political subdivisions must be rated as investment grade by not less than one rating service. Investments in bonds, obligations, or repurchase agreements must be made with the U.S. Treasury and banker's acceptances with United States banks. The Entity's investment policy limits investments to be made with prudent judgment as to the safety of the invested capital and probable outcome of income.

U.S. agency securities and local government bonds were rated as follows:

Investment Type	Rating	Amount
U.S. Agencies		
Federal Farm Credit Bank	AA+	\$997,818
Federal Home Loan Bank	AA+	4,002,586
Federal Home Loan Mtg Corp	AA+	997,471
Total Value		\$ 5,997,875

Concentration of Credit Risk

The Entity places no limit on the amount it may invest in any one issuer. At September 30<sup>th</sup>, concentrations in securities of any one issuer greater than 5% of investment fair value were as follows:

Investment Type	Issuer	% of Portfolio
U.S. Agencies	Federal Farm Credit Bank	16.6%
U.S. Agencies	Federal Home Loan Bank	66.7%
U.S. Agencies	Federal Home Loan Mtg Corp	16.6%

Custodial Credit Risk – Investments

Custodial credit risk is the risk that, in the event of a failure of the counterparty, the Entity will not be able to recover the value of its investments that are in the possession of an outside party. The Entity requires all security transactions, including collateral for repurchase agreements, to be made on a cash basis or a delivery vs. payment basis. Securities may be held by a third party custodian and must be evidenced by safekeeping receipts. The Entity does not have any additional policies for custodial credit risk over investments.

Interest Rate Risk – Investments

Under state statutes, investment in commercial paper is limited to maturities of not more than 270 days after the date of purchase. The Entity's investment policy does not place any further limitations on investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

At September 30<sup>th</sup>, maturities of investments in debt securities were as follows:

Investment Type	1-5 years	6-10 years	11-15 years	15+ years	Total
U.S. Agencies	\$5,997,875	\$ -	\$ -	\$ -	\$5,997,875
Total	\$5,997,875	\$ -	\$ -	\$ -	\$5,997,875



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**Due from Other Governmental Units**

Due from other governmental units as of September 30<sup>th</sup>, consists of the following:

Due From	Amount
Due from MDCH	\$ 2,912,617
Due from Bay-Arenac Behavioral Health	4,943,097
Due from Gratiot County Community Mental Health	18,852
Due from Huron Behavioral Health	624,048
Due from CMHA of Clinton, Eaton, & Ingham Counties	2,421,814
Due from Ionia County Community Mental Health	834,592
Due from Community Mental Health for Central Michigan	2,329,696
Due from LifeWays Community Mental Health Authority	374,842
Due from Montcalm Center for Behavioral Health	520,666
Due from Newaygo County Mental Health	476,232
Due from Saginaw County Community Mental Health Authority	2,851,007
Due from Shiawassee County Community Mental Health Authority	342,983
Due from Tuscola Behavioral Health Systems	489,046
<b>Total</b>	<b>19,139,492</b>

**Due to Other Governmental Units**

Due to other governmental units as of September 30<sup>th</sup>, consists of the following:

Due to	Amount
Due to State Use Tax Accrual	\$ 2,711,644
Due to the State HRA	1,860,508
Due to State HICA Accrual	915,984
Due to CEI CA	893,014
Due to NMSAS CA	363,237
Due to Riverhaven CA	339,797
Due to Saginaw CA	162,420
Due to Bay-Arenac Behavioral Health	941,028
Due to Gratiot County Community Mental Health	273,343
Due to Huron Behavioral Health	244,178
Due to CMHA of Clinton, Eaton, & Ingham Counties	2,870,157
Due to Ionia County Community Mental Health	297,343
Due to Community Mental Health for Central Michigan	1,569,451
Due to LifeWays Community Mental Health Authority	2,156,703
Due to Montcalm Center for Behavioral Health	453,891
Due to Newaygo County Mental Health	308,515
Due to Saginaw County Community Mental Health Authority	1,763,072
Due to Shiawassee County Community Mental Health Authority	373,479
Due to Tuscola Behavioral Health Systems	377,143
<b>Totals</b>	<b>\$ 18,874,907</b>

**Accrued Wages and Other Payroll Liabilities**

This liability represents amounts paid to employees during October that was earned during September. Also included are employer payroll taxes.

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Notes to the Financial Statements  
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**Unearned Revenue**

Unearned revenue represents amounts received in advance of the period in which they were earned as follows:

Unearned Revenue	Amount
Healthy Michigan Carryforward	\$ 6,408,311
Medicaid Savings	11,189,774
Other	317,068
Total	\$ 17,915,153

**Restrictions on Net Position**

A portion of the net position has been restricted equal to the net amount available in the Internal Service Fund (risk management) which has been set aside to fund the net uninsured exposure of potential shortfalls of contract revenues. As of September 30th, this amount was \$20,716,948.

In the fund financial statements a portion of the fund balance at September 30th is considered un-spensible equal to the amount of prepaid expenses, since prepaid expenses do not constitute "available spendable resources."

**NOTE 4. OTHER INFORMATION**

**Compliance Audits**

The Entity participates in various federal, state, and local grants for mental health programs. Certain provisions and allowable levels of participation and expenditures not qualifying for participation are subject to interpretation and adjustment by appropriate governmental agencies. State grants are subject to audit by responsible state agencies. Although these audits may result in some changes, they are not expected to have a material effect on the financial statements.

**Internal Service Fund**

The Entity authorized the establishment of an internal service fund. This fund is used to cover the risk of overspending the Managed Care Specialty Services Program Contract within the established risk corridor. This contract provides for the use of Department of Community Health funding for the establishment of Internal Service Funds.

Expenditures from this fund will occur when, in any one fiscal year, the Entity finds it necessary to expend more to provide services to carry out the contract requirements than revenue provided by the contract.

**Economic Dependency**

Revenues paid either directly or indirectly by the Michigan Department of Community Health represent 100% of the Entity's total revenues.

**Change in Accounting Principle**

In January 2013, the GASB issued Statement No. 69, Government Combinations and Disposals of Government Operations. This Statement establishes accounting and financial reporting standards related to government combinations, transfers of operations and disposals of government operations. The requirements of this Statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013. The Entity has decided that early implementation of GASB 69 would best serve the readers of these financial statements.

**Transfer of Operations**

Facts and assumptions

On January 1, 2014, Mid-State Health Network (MSHN) assumed the role as the prepaid inpatient health plan ("PIHP") for the twenty-one counties designated by the Michigan Department of Community Health as Region 5. This region had previously been served by the following 5 PIHPs: Bay-Arenac Behavioral Health, Clinton-Eaton-Ingham Community Mental Health Authority, Community Mental Health for Central Michigan, LifeWays Community Mental Health Authority, and Saginaw County Community Mental Health Authority. As a part of this change, the 5 PIHPs were required to transfer all assets and liabilities related to the Medicaid contract to MSHN.

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September 30, 2014

The transfers from the PIHPs consisted of cash or cash equivalents, unearned revenue (Medicaid Savings) and net position restricted for Medicaid Risk Reserve (Medicaid ISF). No significant capital assets or debt was assumed with the transfer of operations. Also, there are no deferred outflows of resources or deferred inflows of resources associated with the transfer.

Accounting at the transfer date

The assets and liabilities transferred to the MSHN represent a set of assets, liabilities and net position for the purpose of serving as a prepaid inpatient health plan, thus meeting the definition of an operation. There is no consideration given in the transaction.

MSHN recognizes the carrying values of assets and liabilities of the 5 PIHP's transferred operations as of January 1, 2014 and special items of \$20.7 million representing the inflow of resources for the net position received. The values are listed below:

Description	Carrying Values
<i>Transferred Assets</i>	
Cash and cash equivalents	\$ 32,261,548
<i>Transferred Liabilities</i>	
Unearned revenue (Medicaid Savings) received from:	
Bay-Arenac Behavioral Health	2,750,299*
Community Mental Health for Central Michigan	4,470,055
Clinton-Eaton-Ingham CMHA	1,531,232
LifeWays CMHA	1,308,638
Saginaw County CMHA	<u>1,489,500</u>
Total unearned revenue received	11,549,724
<i>Transferred Net Position</i>	
Net position restricted for Medicaid Risk Reserve received from:	
Bay-Arenac Behavioral Health	6,696,604
Community Mental Health for Central Michigan	5,639,321
Clinton-Eaton-Ingham CMHA	1,649,034
LifeWays CMHA	3,313,486
Saginaw County CMHA	<u>3,413,379</u>
Total net position received	<u>\$ 20,711,824</u>

\* - Bay-Arenac Behavioral Health reported a transfer to Mid-State Health Network out of their General Fund in the amount of \$4,873,912, which includes \$2,750,177 of Medicaid Savings, \$1,662,883 of Public Act 2 funds and \$460,852 of prior cost settlements between Bay-Arenac and Montcalm Center for Behavioral Health. Public Act 2 funds will be reported as transfers in to MSHN in the fiscal year ending September 30, 2015 when MSHN assumes the substance abuse operations for the region. Prior cost settlements between Bay-Arenac and Montcalm Center for Behavioral Health relate to periods before MSHN was created. Management does not believe that MSHN is entitled to these funds.

**REQUIRED SUPPLEMENTAL INFORMATION**

**BUDGETARY COMPARISON SCHEDULES**



Mid-State Health Network  
Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual  
Health & Welfare - Mental Health  
September 30, 2014

	Budgeted Amounts		General Fund	Variances with Final Budget
	Original	Final	Actual	
<b>Revenues</b>				
State funding				
Medicaid	\$ 278,666,260	\$ 313,393,937	\$ 309,723,071	\$ (3,670,866)
Adult Benefit Waiver	1,333,695	1,333,695	1,333,695	-
Total State funding	279,999,955	314,727,632	311,056,766	(3,670,866)
Contributions - Local match drawdown	-	3,270,795	2,951,151	(319,644)
Interest income	-	12,600	1,323	(11,277)
Total revenues	279,999,955	318,011,027	314,009,240	(4,001,787)
<b>Expenditures</b>				
Operating expenditures				
Salaries and wages	476,366	456,281	403,849	52,432
Fringe benefits	124,849	143,837	204,044	(60,207)
Legal and professional	162,500	42,000	16,086	25,914
Printing expense	50,000	40,000	36,500	3,500
Meeting expense	-	10,000	10,279	(279)
Other operating expense	265,000	197,727	64,657	133,070
Telephone expense	-	15,000	10,230	4,770
Board per diem	-	7,000	6,300	700
Consulting services	80,000	164,000	110,127	53,873
Rent expense	78,762	27,100	23,482	3,618
Insurance	63,333	38,644	38,644	-
Membership and dues	-	5,000	2,935	2,065
Supplies	-	73,500	8,443	65,057
Travel and conferences	-	74,721	40,985	33,736
Utilities	-	6,000	5,936	64
Total operating expenditures	1,300,810	1,300,810	982,497	318,313
Contract expenditures				
Use tax	-	9,737,248	13,075,472	(3,338,224)
HICA tax	2,747,282	2,736,327	2,709,678	26,649
Local match	-	3,270,795	2,951,151	319,644
HRA expense	5,815,396	5,586,574	5,598,965	(12,391)
Payments to affiliate members	269,209,386	294,402,192	288,104,050	6,298,142
Contractual services	927,081	977,081	586,104	390,977
Total contract expenditures	278,699,145	316,710,217	313,025,420	3,684,797
Total expenditures	279,999,955	318,011,027	314,007,917	4,003,110
<b>Excess of revenues over expenditures</b>	-	-	1,323	1,323
<b>Fund balance, beginning of year</b>	-	-	-	-
<b>Fund balance, end of year</b>	\$ -	\$ -	\$ 1,323	\$ 1,323



INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Mid-State Health Network  
Lansing, Michigan

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities and each major fund of Mid-State Health Network (the Entity), as of and for the year ended September 30, 2014, and the related notes to the financial statements, which collectively comprise the Entity's basic financial statements, and have issued our report thereon dated March 27, 2015.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Entity's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Entity's internal control. Accordingly, we do not express an opinion on the effectiveness of the Entity's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Entity's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Roslund, Prestage &amp; Company, P.C." The signature is written in a cursive, flowing style.

Roslund, Prestage & Company, P.C.  
March 27, 2015



**Mid-State Health Network  
Financial Statements  
September 30, 2014**