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CHASE BREXTON HEALTH SERVICES, INC.

**FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION**

JUNE 30, 2012 AND 2011

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To the Board of Directors
Chase Brexton Health Services, Inc.

Independent Auditor's Report

We have audited the accompanying statement of financial position of Chase Brexton Health Services, Inc. (a nonprofit organization) as of June 30, 2012, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the management of Chase Brexton Health Services, Inc. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Chase Brexton Health Services, Inc. as of and for the year ended June 30, 2011 were audited by other auditors whose report dated October 6, 2011, expressed an unqualified opinion on those statements.

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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Chase Brexton Health Services, Inc. as of June 30, 2012, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 5, 2012 on our consideration of Chase Brexton Health Services, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

To the Board of Directors
Chase Brexton Health Services, Inc.

Page Two

Independent Auditor's Report (Continued)

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

Gross, Mendelsohn & Associates, P.A.

Baltimore, Maryland
October 5, 2012

CHASE BREXTON HEALTH SERVICES, INC.
Statements of Financial Position
June 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Assets		
Current Assets		
Cash and cash equivalents	\$ 4,864,240	\$ 4,384,494
Cash and cash equivalents, reserved (IBNR)	716,615	610,785
Total Cash and Cash Equivalents	<u>5,580,855</u>	4,995,279
Certificate of deposit	500,677	500,000
Grants receivable	2,099,164	2,063,842
Accounts receivable, net of allowance for doubtful accounts	2,537,372	2,446,341
Investments, current portion	25,350,104	-0-
Inventory	535,198	377,077
Escrow receivable	609,000	-0-
Other receivables	57,479	319,697
Prepaid expenses	377,234	247,956
Total Current Assets	<u>37,647,083</u>	<u>10,950,192</u>
Property , net of accumulated depreciation		
Land, building and improvements	13,324,758	13,223,794
Medical equipment	652,968	652,968
Office furniture and equipment	3,957,860	3,192,450
Total	<u>17,935,586</u>	17,069,212
Accumulated depreciation	<u>(4,356,003)</u>	(4,114,404)
Net Property	<u>13,579,583</u>	<u>12,954,808</u>
Other Assets		
Board-designated cash	-0-	430,646
Investments, long-term portion	3,490	20,295,562
Security deposits	30,842	39,278
Total Other Assets	<u>34,332</u>	<u>20,765,486</u>
Total Assets	<u>\$ 51,260,998</u>	<u>\$ 44,670,486</u>

	<u>2012</u>	<u>2011</u>
Liabilities And Net Assets		
Current Liabilities		
Accounts payable and accrued expenses	\$ 3,924,377	\$ 2,685,314
Deferred revenue	281,334	257,526
Estimated claims incurred but not reported	716,615	610,785
Grant payable, CDBG	312,000	-0-
Security deposit	-0-	2,415
Total Current Liabilities	<u>5,234,326</u>	<u>3,556,040</u>
Commitments and Contingencies (Notes 3, 4, 5, 11 and 12)		
Net Assets		
Unrestricted		
Undesignated	45,612,219	19,653,047
Board-designated	-0-	20,716,866
Community development block grants	400,000	712,000
Total Unrestricted	<u>46,012,219</u>	<u>41,081,913</u>
Temporarily restricted	14,453	32,533
Total Net Assets	<u>46,026,672</u>	<u>41,114,446</u>
Total Liabilities and Net Assets	<u><u>\$ 51,260,998</u></u>	<u><u>\$ 44,670,486</u></u>

The accompanying notes are an integral part of these financial statements.

CHASE BREXTON HEALTH SERVICES, INC
Statements of Activities
Years Ended June 30, 2012 and 2011

	2012		
	Unrestricted	Temporarily Restricted	Total
Support and Revenue			
Pharmacy	\$ 32,278,523	\$ -0-	\$ 32,278,523
Fees for service	11,332,787	-0-	11,332,787
Grants and contracts from governmental agencies	6,455,524	-0-	6,455,524
Managed care capitation	3,227,045	-0-	3,227,045
Other grants and contributions	685,282	200	685,482
Special events, net	65,002	-0-	65,002
	<u>54,044,163</u>	<u>200</u>	<u>54,044,363</u>
Less contractual, other adjustments and free services	(5,018,213)	-0-	(5,018,213)
Support and Revenue, net	<u>49,025,950</u>	<u>200</u>	<u>49,026,150</u>
Net assets released from restrictions:			
Satisfaction of program restrictions	18,280	(18,280)	-0-
Total Support and Revenue	<u>49,044,230</u>	<u>(18,080)</u>	<u>49,026,150</u>
Expenses			
Program services			
Pharmacy	22,025,480	-0-	22,025,480
Primary care services	10,014,964	-0-	10,014,964
Mental health services	2,076,470	-0-	2,076,470
Case management	2,461,558	-0-	2,461,558
Dental	1,237,391	-0-	1,237,391
Total Program Services	<u>37,815,863</u>	<u>-0-</u>	<u>37,815,863</u>
Supporting services			
Management and general	6,619,987	-0-	6,619,987
Fundraising	1,095,883	-0-	1,095,883
Total supporting services	<u>7,715,870</u>	<u>-0-</u>	<u>7,715,870</u>
Total Expenses	<u>45,531,733</u>	<u>-0-</u>	<u>45,531,733</u>
Income from Operations Before Other Revenue	<u>3,512,497</u>	<u>(18,080)</u>	<u>3,494,417</u>
Other Income (Expense)			
Investment income (loss), net	(75,891)	-0-	(75,891)
Partnership income	899,410	-0-	899,410
Rental income, net	28,850	-0-	28,850
Gain on sale of property	596,633	-0-	596,633
Other income	280,807	-0-	280,807
Grant forfeiture	(312,000)	-0-	(312,000)
Total Other Income, Net	<u>1,417,809</u>	<u>-0-</u>	<u>1,417,809</u>
Change in Net Assets	<u>4,930,306</u>	<u>(18,080)</u>	<u>4,912,226</u>
Net Assets at Beginning of Year	<u>41,081,913</u>	<u>32,533</u>	<u>41,114,446</u>
Net Assets at End of Year	<u>\$ 46,012,219</u>	<u>\$ 14,453</u>	<u>\$ 46,026,672</u>

2011		
Unrestricted	Temporarily Restricted	Total
\$ 28,999,020	\$ -0-	\$ 28,999,020
10,411,929	-0-	10,411,929
6,406,748	-0-	6,406,748
4,036,522	-0-	4,036,522
561,689	7,541	569,230
58,700	-0-	58,700
50,474,608	7,541	50,482,149
(4,813,010)	-0-	(4,813,010)
45,661,598	7,541	45,669,139
1,400	(1,400)	-0-
45,662,998	6,141	45,669,139
20,108,844	-0-	20,108,844
9,395,925	-0-	9,395,925
1,913,856	-0-	1,913,856
2,061,584	-0-	2,061,584
1,206,853	-0-	1,206,853
34,687,062	-0-	34,687,062
4,709,633	-0-	4,709,633
750,358	-0-	750,358
5,459,991	-0-	5,459,991
40,147,053	-0-	40,147,053
5,515,945	6,141	5,522,086
2,899,142	-0-	2,899,142
885,161	-0-	885,161
45,974	-0-	45,974
-0-	-0-	-0-
17,536	-0-	17,536
-0-	-0-	-0-
3,847,813	-0-	3,847,813
9,363,758	6,141	9,369,899
31,718,155	26,392	31,744,547
<u>\$ 41,081,913</u>	<u>\$ 32,533</u>	<u>\$ 41,114,446</u>

The accompanying notes are an integral part of these financial statements.

CHASE BREXTON HEALTH SERVICES, INC.
Statements Of Cash Flows
Years Ended June 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Cash Flows From Operating Activities		
Change in net assets	\$ 4,912,226	\$ 9,369,899
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	694,098	660,861
Net realized and unrealized losses (gains) on investments	408,864	(2,461,493)
Provision for bad debts	(313,598)	168,694
Gain on sale of property	(596,633)	-0-
Changes in operating assets and liabilities:		
Grants receivable	(35,322)	(226,214)
Accounts receivable	222,567	(259,174)
Inventory	(158,121)	(89,251)
Other receivables	262,218	(319,697)
Prepaid expenses	(129,278)	(124,597)
Accounts payable and accrued expenses	1,239,063	5,385
Deferred revenue	23,808	73,571
Estimated claims incurred but not reported	105,830	(23,308)
Grant payable	312,000	-0-
Security deposits, net	6,021	4
Net Cash Provided by Operating Activities	<u>6,953,743</u>	<u>6,774,680</u>
Cash Flows From Investing Activities		
Purchases of property	(2,216,905)	(8,762,937)
Proceeds from sale of property	1,494,665	-0-
Escrow deposits paid	(609,000)	-0-
Release of board designated cash	430,646	(155)
Change in certificate of deposit	(677)	(50,000)
Decrease in cash surrender value of life insurance	-0-	8,463
Change in investment in partnership	(945)	1,558
Proceeds from sale of investments	9,651,209	6,519,178
Purchases of investments	(15,117,160)	(5,150,343)
Net Cash Used in Investing Activities	<u>(6,368,167)</u>	<u>(7,434,236)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	585,576	(659,556)
Cash and Cash Equivalents at Beginning of Year	<u>4,995,279</u>	<u>5,654,835</u>
Cash and Cash Equivalents at End of Year	<u>\$ 5,580,855</u>	<u>\$ 4,995,279</u>

The accompanying notes are an integral part of these financial statements.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 1: Summary of Significant Accounting Policies

Chase Brexton Health Services, Inc. (the Center) is a community health care center with locations in Baltimore City, Baltimore County, Howard County, and Talbot County, Maryland, which are Federally Qualified Health Centers (FQHSs). The Center also provides medical consultation services at satellite locations throughout Maryland. Services provided include primary medical care, pharmaceuticals, mental health services, dental services, nutritional services and case management. The Center is the State's largest community-based provider of primary HIV medical and consultative care and is nationally recognized as an AIDS service provider. The Center was incorporated under the laws of Maryland in June 1989.

The Center has a proven record for effectively identifying and addressing health care issues to meet the needs of underserved, high-risk clients through research, as well as through client service. Clients can receive comprehensive medical care, pharmacy services, mental health services, addictions counseling, dental services, nutritional counseling, and case management. An integrated, client-oriented system of care guides and tracks clients through their on-site medical, mental health, and social services as well as through outpatient care.

The accounting and reporting policies of the Center conform to accounting principles generally accepted in the United States of America. Following is a description of the most significant of those policies:

Financial Statement Presentation: The Center reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. The Center currently does not have any permanently restricted net assets.

Use of Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Cash and Cash Equivalents: The Center classifies all investments which are readily convertible to cash and which have a maturity of three months or less when purchased as cash equivalents.

Accounts and Grants Receivables: Receivables are carried at original invoice amount less an estimate made for doubtful receivables. Management determines the allowance for doubtful accounts by reviewing its outstanding receivable balances and its historical collection experience with individual accounts and payor sources. Receivables are written off by management when, in their determination, all collection efforts have been exhausted. Recoveries of these receivables previously written off are recorded when received. The Center has established an allowance for doubtful accounts of \$1,428,763 and \$1,742,361 at June 30, 2012 and 2011, respectively, related to its accounts receivable. The Center's management has determined that the grants receivable are fully collectible, and therefore, no allowance has been established related to those receivables.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 1: Summary of Significant Accounting Policies (Continued)

Investments in Marketable Securities: Investments with readily determined fair market values are reported at fair value in the statements of financial position. Investments whose fair market values are not readily determinable are recorded at cost. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Realized and unrealized gains and losses on investments for the year are reported in the statements of activities as part of investment income (loss), net.

The Center invests primarily in a professionally managed portfolio that contains mutual funds. Such investments are exposed to various risks such as interest rate, market and credit. Due to the level of risk associated with such investments and the level of uncertainty related to changes in the value of such investments, it is a least reasonable possible that changes in risks in the near term could materially affect investment balances and the amounts reported in the financial statements.

Other Investments: Other investments are composed of an investment in a closely held corporation and a limited liability limited partnership. These investments are recorded at cost since the Center owns less than 20% of each of these investments. In addition, the Center holds a certificate of deposit that is recorded at cost, which approximates fair value.

Inventory: Inventory, which consists of pharmaceuticals, is stated at the lower of cost, determined on the first-in, first-out (FIFO) method, or market.

Property and Depreciation: Property is stated at cost or, if donated, at fair market value at the date of gift, less accumulated depreciation. It is the Center's policy to capitalize all property acquisitions in excess of \$5,000 having useful lives of longer than one year. Depreciation is computed on a straight-line basis and is charged to expense over the estimated useful lives of the assets as follows:

Building and improvements	5 - 40 years
Medical equipment	5 - 7 years
Office furniture and equipment	3 - 7 years

Depreciation expense for the years ended June 30, 2012 and 2011 was \$694,098 and \$660,861, respectively.

Patient Service Revenue: Patient service revenue, which consists of fees for service, pharmacy and managed care capitation, is recorded at established billing rates or at the amount realizable under agreements with third-party payors. Approximately 49% of patient revenue was derived under federal and state third-party reimbursement programs in 2012 and 2011. Revenue is recorded when services are provided at standard charges adjusted to amounts estimated to be received under governmental programs and other third-party contractual arrangements based on contractual terms and historical experience. The revenue and receivables are reported at their estimated net realizable amounts and are subject to audit and retroactive adjustment.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 1: Summary of Significant Accounting Policies (Continued)

Retroactive adjustments are estimated in the recording of revenue in the period the related services are rendered. These amounts are adjusted in future periods as adjustments become known or as cost reporting years are no longer subject to audits, reviews, or investigations. Due to the complexity of the laws and regulations governing the Medicare and Medicaid programs, there is at least a possibility that recorded estimates will change by a material amount in the near term. The methods of making such estimates are reviewed periodically, and differences between the net amounts accrued and subsequent settlements or estimates of expected settlements are reflected in the current period results of operations.

Revenue Recognition and Deferred Revenue: Approximately 13% and 14% of the Center's revenue as of June 30, 2012 and 2011, respectively, was derived from conditional grants and contracts from governmental agencies that are recognized as revenue in proportion to the related expenses incurred. All other revenue, including pharmacy, fees for service, managed care capitation payments and investment income, is recognized as revenue when earned.

Any conditional grants or contract proceeds in excess of the related expenses incurred are classified as deferred revenue in the statements of financial position.

Contributions: Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Recognition of Donor Restrictions: Donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. Upon the expiration of a restriction, temporarily restricted net assets are reclassified to unrestricted net assets on the statements of activities.

Donated Assets: Donated marketable securities and other noncash donations are recorded as contributions at their estimated fair values at the date of donation.

Donated Services: Donated services are recognized as contributions if the services (a) create or enhance nonfinancial assets or (b) require specialized skills, are performed by individuals with those skills, and would otherwise be purchased by the Center. For the years ended June 30, 2012 and 2011, the Center recognized, as contribution revenue and corresponding expense in the statements of activities, donated medical and legal services in the amounts of \$24,825 and \$28,977, respectively. A substantial number of unpaid volunteers have made significant contributions of their time and services to the Center. The value of this contributed time is not recorded as a contribution in these financial statements since the recognition criteria was not met.

Advertising: Advertising costs are charged to operations when incurred. The Center had no significant direct-response advertising. Advertising expense for the years ended June 30, 2012 and 2011 was \$135,331 and \$57,048, respectively.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 1: Summary of Significant Accounting Policies (Continued)

Tax Status: The Center has been recognized by the Internal Revenue Service (IRS) as a tax-exempt organization, as defined by Section 501(c)(3) of the Internal Revenue Code (IRC), that is publicly supported and, therefore, not a private foundation. Income that is not related to exempt purposes, less applicable deductions, is subject to federal and state income taxes. The Center had no unrelated business income for the years ending June 30, 2012 and 2011. Accordingly, no provision for income taxes is reflected in these statements. The Center's federal exempt organization tax returns are subject to examination by the IRS, generally for a period of three years after the returns are filed.

Reclassifications: Certain amounts previously reported in the financial statements for the year ended June 30, 2011 have been reclassified to conform to the financial statement presentation for the year ended June 30, 2012. These changes had no effect on previously reported net assets or the changes in net assets.

Note 2: Investments

Investments consisted of the following as of June 30, 2012 and 2011:

	2012		2011	
	Fair Value	Cost	Fair Value	Cost
Mutual funds	\$ 15,063,455	\$ 14,662,872	\$ 18,590,900	\$ 17,737,916
Investment in partnership	6,620	6,620	5,675	5,675
Money market funds	10,280,029	10,280,029	1,695,320	1,695,320
Miscellaneous investments	3,390	3,390	3,567	3,567
Closely held stock	100	100	100	100
	<hr/>			
Total investments	\$ 25,353,594	\$ 24,953,011	\$ 20,295,562	\$ 19,442,578
	<hr/>			
Investments, current portion	<u>\$ 25,350,104</u>		<u>\$ -0-</u>	
Investments, long-term portion				
Board-designated	\$ -0-		\$ 20,286,220	
Other investments, unrestricted	<u>3,490</u>		<u>9,342</u>	
	<hr/>			
Total Investments, long-term	<u>\$ 3,490</u>		<u>\$ 20,295,562</u>	

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 2: Investments (Continued)

Investment income (loss), net, for the years ended June 30, 2012 and 2011 consisted of the following:

	2012	2011
Dividends and interest	\$ 332,973	\$ 437,649
Net realized and unrealized gains (losses)	(408,864)	2,461,493
	<u>\$ (75,891)</u>	<u>\$ 2,899,142</u>

Limited liability limited partnership: The Center has a 12.375% limited partnership interest in Maryland Community Health Systems Limited Liability Limited Partnership (the Partnership). The Partnership is composed of eight community health centers, each of which is a not-for-profit, tax-exempt organization. The eight health centers are limited partners, with MCHS, Inc. serving as the general partner. The Partnership owns a 50% interest in Priority Partners, a Maryland corporation, which is a joint venture with Johns Hopkins HealthCare (JHHC), for the purpose of operating an authorized managed care organization under the terms of HealthChoice. JHHC has assumed sole responsibility for the expenses of Priority Partners, including any capital calls to fund any operating deficiencies. By agreement, Priority Partners is obligated to pay the Partnership payments in the amount of 1% of the revenue received by Priority Partners from the state of Maryland. Partnership income earned from the limited partnership was \$899,410 and \$885,161 for the years ended June 30, 2012 and 2011, respectively.

Closely held corporation: The Center owns one share (12.5%) of MCHS, Inc., a Maryland for-profit corporation, with a cost basis of \$100.

Note 3: Related Party Transactions

Managed care capitation program: The Center has a managed care contract with Priority Partners with which the Center has an affiliation (Note 2). Total revenue earned from this contract during the years ended June 30, 2012 and 2011, was \$3,227,045 and \$4,036,522, respectively.

Estimated claims incurred but not reported: Management has accrued an estimate of amounts due to Priority Partners under its capitation program for Estimated Claims Incurred But Not Reported (IBNR). This amount represents claims for covered services provided on behalf of the Center before year end. The IBNR due as of June 30, 2012 and 2011 was \$716,615 and \$610,785, respectively. Total claims expense for the years ended June 30, 2012 and 2011, was \$2,037,127 and \$2,701,095, respectively. The amount due to Priority Partners is noninterest bearing and due on demand as the claims are submitted.

The Center set aside \$716,615 and \$610,785 of its cash and cash equivalents as of June 30, 2012 and 2011, respectively, to cover the payment of these estimated claims.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 4: Commitments and Contingencies

Pension plan: The Center established an annuity program under IRC 403(b) for all of its eligible employees who work at least 20 hours or more per week, as defined in the plan document. Under the terms of the plan, any eligible participant may contribute pre-tax dollars toward the purchase of the annuity. In turn, the employees are eligible to receive matching contributions from the Center if their individual contribution percentage to the plan is at least 3%. The Center will match 100% of employee contributions up to a maximum of 5% of compensation. Employer contributions for the years ended June 30, 2012 and 2011, were \$215,753 and \$209,764, respectively.

Eligible plan participants' contributions and the employer matching contributions are always 100% vested.

Letter of credit: The Center has a letter of credit with a bank in the amount of \$500,000 for the purpose of guaranteeing payment related to its capitation program. The letter of credit was unused as of June 30, 2012 and 2011. The letter of credit is secured by a certificate of deposit in the amount of \$500,667 as of June 30, 2012 and matures October 24, 2012.

Operating leases: The Center began leasing additional administrative office space in Baltimore, Maryland, in February 2006. This lease required monthly payments of \$8,864 for the initial year which escalated 3% per annum. In October 2007, the Center leased additional space, the term of which was consistent with the terms of the original lease. This additional lease required monthly payments in the amount of \$2,465 for the initial year, which escalated 3% per annum. In September, 2011, the Center amended these leases to extend the lease term until June 30, 2013. The base rent for the extended term through June 30, 2013 is \$113,016. The lease also requires the Center to pay as additional rent its proportionate share of common area maintenance costs.

The Center has a lease for clinical space in Columbia, Maryland, under a lease that requires monthly payments of \$9,023, which are subject to an annual escalation clause. The lease also required the Center to pay as additional rent its proportionate share of common area maintenance costs and real estate taxes. In October 2008, the Center entered into its first lease modification agreement for additional space. The lease modification expires in September 2013 and requires monthly payments in the amount of \$3,073 for the initial year which escalate 3% per annum. During 2009, the Center entered into a second lease modification agreement for additional space, which requires monthly payments in the amount of \$2,454 for the initial year which escalate 3% per annum. In February 2012, the Center entered into a third modification agreement for additional space and to extend the terms of all prior lease agreements and amendments. The commencement date of this new lease is contingent on the date in which renovations are finalized to the newest additional space. Management expects the renovations to be completed in October 2012. The lease term is for a period of 7 years and requires minimum monthly payments of \$28,518 upon its commencement. The lease has a yearly escalation clause of 2.5% and requires the Center to pay as additional rent its proportionate share of common area maintenance costs and real estate taxes.

In May 2012, the Center entered into a lease-back agreement with the owners of a building formally owned by the Center. The lease requires monthly payments of \$1 through March 31, 2013. The Center has the option to extend the lease on a month to month basis through September 2013 if renovations to the new building purchased by the Center are not completed by March 2013. The extension agreement requires monthly rental payments of \$24,531. As required by generally accepted accounting principles when rent payments are below market, the Center has elected to record the fair value monthly rent of \$24,531 as a contribution and as a corresponding rent expense in the statements of activities. The lease also requires the Center to pay as additional rent its proportionate share of common area maintenance costs and real estate taxes.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 4: Commitments and Contingencies (Continued)

The Center has a lease for clinical space in Randallstown, Maryland, which expires on October 31, 2025 and can be renewed for an additional term of ten years. The lease requires monthly payments of \$9,100, which escalates 13% every five years, commencing November 1, 2015. The lease also requires the Center to pay as additional rent its proportionate share of common area maintenance costs and real estate taxes.

The Center had a lease for clinical space in Easton, Maryland which expired on March 31, 2012, and required monthly payments of \$1,800. The Center continues to lease this space on a month to month basis until renovations are completed at a new location in Easton. The Center entered into a lease agreement for the new location that commenced in May 2012. The lease requires initial monthly payments of \$2,100, which escalate at 3% annually. The lease expires on February 28, 2017 and can be extended for an additional term of three years.

Total rent expense under the operating leases for the years ended June 30, 2012 and 2011, was \$505,057 and \$505,192, respectively.

The minimum annual lease payments required under the current leases as of June 30, 2012 are as follows:

Year ending June 30,	
2013	\$ 504,988
2014	481,910
2015	491,353
2016	510,603
2017	515,584
Thereafter	<u>2,017,496</u>
	<u>\$ 4,521,934</u>

Note 5: Community Development Block Grants

The Center received a grant advance of \$312,000 from the Department of Housing and Community Development (DHCD) through the Community Development Block Grant (CDBG) Program. The grant advance stipulated that the proceeds be used for the acquisition of the Center's facilities at 1001 Cathedral Street. If the Center maintains the property and uses it to operate a community based health clinic and AIDS treatment center in compliance with the CDBG Program, no interest will accrue or be payable. The advance will be forgiven if the Center owns and uses the property as a community-based health clinic and AIDS treatment center for a 20-year period ending March 2015. The grant is collateralized by a deed of trust on the property located at 1001 Cathedral Street.

On May 31, 2012, the Center sold the property located at 1001 Cathedral Street. Per the agreement with DHCD, the Center is required to pay back the grant advance in full. At the time of settlement, the Center was required to place \$312,000 into an escrow account to cover the repayment of the grant (Note 11). Management has received a tentative verbal approval from DHCD that the grant will be forgiven, but has not yet received any official notification of release. As a result, this liability has been recorded as a grant payable in the statements of financial position.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 5: Community Development Block Grants (Continued)

The Center received an additional grant advance of \$400,000 from the DHCD through the CDBG Program. The grant advance stipulated that the proceeds be used for the acquisition of the Center's facilities at 10 West Eager Street. If the Center maintains the property and uses it to operate a community based health clinic and AIDS treatment center in compliance with the CDBG Program, no interest will accrue or be payable. The advance will be forgiven if the Center owns and uses the property as a community-based health clinic and AIDS treatment center for a 20-year period ending November 2022. The grant is collateralized by a subordinate deed of trust on the property located at 10 West Eager Street.

Note 6: Board-Designated Net Assets

Board-designated net assets were designated for the following purposes as of June 30, 2011:

	<u>2011</u>
Capital reserve	\$ 652,500
Operating reserve	19,864,366
Incentives reserve	<u>200,000</u>
	<u>\$ 20,716,866</u>

The capital reserve was to be used for capital improvements. The operating reserve was to be used to fund program expansion, severe cash flow deficiencies, expenses related to governmental audits, payments of claims settled that would exceed existing limits of insurance and unforeseen major expenses. The incentives reserve was to be used to cover bonuses earned by the employees under the Center's incentive plan.

During the year ended June 30, 2012, the Board determined that the Center is in a fiscally sound financial position and therefore authorized the elimination of these reserves.

Board-designated net assets consisted of the following as of June 30, 2011:

	<u>2011</u>
Board designated cash	\$ 430,646
Investments	<u>20,286,220</u>
	<u>\$ 20,716,866</u>

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 7: Temporarily Restricted Net Assets

Temporarily restricted net assets were available for the following purposes at June 30, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Case management	\$ 11,062	\$ 11,062
Primary care	3,016	21,296
NCJW, Columbia	200	-0-
Dental, Columbia	175	175
	<u>\$ 14,453</u>	<u>\$ 32,533</u>

Net assets released from restriction were \$18,280 and \$1,400 for the years ended June 30, 2012 and 2011, respectively.

Note 8: Rental Income

The Center subleases a portion of its Columbia location. The lease agreement requires the tenant to make annual rental payments of \$3,967. The lease currently expires on December 31, 2012 and can be renewed on an annual basis by mutual agreement. In addition, the Center had leased a portion of its Cathedral Street building to a tenant that was set to expire on May 31, 2013. Upon the sale of this building in May 2012, this lease agreement was rolled over to the new owner of the building.

Net rental income was composed of the following for the years ended June 30, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Rental income	\$ 82,459	\$ 149,261
Rental expenses	<u>(53,609)</u>	<u>(103,287)</u>
Net rental income	<u>\$ 28,850</u>	<u>\$ 45,974</u>

Note 9: Major Vendors

Transactions with one vendor accounted for approximately \$20,250,000 and \$18,200,000 of pharmaceutical purchases during the years ended June 30, 2012 and 2011, respectively. Accounts payable related to this vendor were \$885,107 and \$742,578 as of June 30, 2012 and 2011, respectively.

Note 10: Fair Value of Financial Instruments

The Financial Accounting Standards Board's (FASB) fair value measurement standard establishes a framework for measuring fair value. The framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements).

The three levels of the fair value hierarchy are as follows:

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2: Inputs to the valuation methodology include:

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

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

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

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

Money Market Funds: Valued at original cost, which equals fair value.

Mutual Funds: Valued at the last sales price reported on the active market in which the individual fund is traded.

Other Investments and Closely Held Stock: Valued at cost since the Center owns less than 20% of each investment.

Investment in Limited Liability Limited Partnership: The valuation of the Center's investment in the limited liability limited partnership is currently based on the respective partner's equity account balance. Any valuation would require significant judgment by the Center's management due to the absence of quoted market values, inherent lack of liquidity and the long-term nature of the asset. Therefore, the Center's management has elected not to determine a value for this investment beyond the partner's equity account value.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 10: Fair Value of Financial Instruments (Continued)

In determining the appropriate levels, the Center performs a detailed analysis of the assets and liabilities that are subject to fair value measurements. The table below presents the balances of assets measured at fair value on a recurring basis by level within the hierarchy, as of June 30, 2012.

	Total	Level 1	Level 2	Level 3
<u>June 30, 2012</u>				
Mutual funds, equity	\$ 15,063,455	\$ 15,063,455	\$ -0-	\$ -0-
Money market funds	10,280,029	10,280,029	-0-	-0-
Investment in partnership	6,620	-0-	-0-	6,620
Miscellaneous investments	3,390	-0-	-0-	3,390
Closely held stock	100	-0-	-0-	100
	<u>\$ 25,353,594</u>	<u>\$ 25,343,484</u>	<u>\$ -0-</u>	<u>\$ 10,110</u>

The table below presents the balances of assets measured at fair value on a recurring basis by level within the hierarchy, as of June 30, 2011.

	Total	Level 1	Level 2	Level 3
<u>June 30, 2011</u>				
Mutual funds, equity	\$ 16,599,621	\$ 16,599,621	\$ -0-	\$ -0-
Mutual funds, fixed income	1,991,279	1,991,279	-0-	-0-
Money market funds	1,695,320	1,695,320	-0-	-0-
Investment in partnership	5,675	-0-	-0-	5,675
Miscellaneous investments	3,567	-0-	-0-	3,390
Closely held stock	100	-0-	-0-	100
	<u>\$ 20,295,562</u>	<u>\$ 20,286,220</u>	<u>\$ -0-</u>	<u>\$ 9,165</u>

The change in investments in the partnership, closely held stock and other investments measured at fair value, for which the Center has used Level 3 inputs to determine fair value, is as follows:

	2012	2011
Balance at beginning of year	\$ 9,165	\$ 10,723
Contributions	-0-	-0-
Distributions	(899,410)	(885,161)
Investment Income	900,355	883,603
Unrealized gains (losses), net	-0-	-0-
Balance at end of year	<u>\$ 10,110</u>	<u>\$ 9,165</u>

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 11: Other Matters

Certain Significant Risks and Uncertainties: The Center receives revenue from Medicare, Medicaid, private insurance, private patients, and other third-party payors. As a result, the Center is directly affected by federal and state legislation, the interpretation or administration of such legislation, and any other government initiatives regarding the healthcare industry. Accordingly, there can be no assurance that any future healthcare legislation will not adversely affect the Center's business. Although the Center has not experienced any adverse affects, there can be no assurance that payments under government and private third-party payor programs will be timely, will remain at levels comparable to present levels, or will, in the future, be sufficient to cover the costs allocable to patients eligible for reimbursement pursuant to such programs. The Center's industry is complex and can involve lengthy delays between the time that revenue is recognized and the time that reimbursement amounts are settled.

Escrow Receivable: On May 31, 2012, the Center sold its building located at 1001 Cathedral Street. As part of the settlement, the Center was required to establish an escrow account in the amount of \$609,000 to be held until the Center received certain releases against the title of the property. The escrow is comprised of two components: \$312,000 is held to repay the DHCD block grant obligation (Note 5) and \$297,000 is held to repay Baltimore City related to a lien they had against the property in connection with a grant. Subsequent to year end, Baltimore City released the Center from its lien obligation and the \$297,000 was released from the escrow account. The Center has been in contact with DHCD to either obtain a release from these obligations or to make the required payment.

Environmental Matters: In June 2011, the Center purchased a building located at 1111 North Charles Street, which is comprised of four separate but connected buildings. Each of these buildings contains asbestos. As of the report date, the Center has not been utilizing this new building as it needs to have demolition and renovation work performed. The Center's management intends to renovate and use two of the buildings, but has no current or foreseeable plans to utilize the other two buildings. Until the building is renovated, management has restricted access to the contaminated area to authorized individuals only. The Center has not received any notification from any Federal, State, City or legal authority that they are required to contain or remove the asbestos. The Center's management is aware that any use of or renovations to this space would require either proper containment or removal. For the planned renovations of the two building spaces, the Center has entered into a contract for the complete removal of the asbestos (see Note 12). These costs have not been accrued as of June 30, 2012 since the contract was signed after year end and the work has not yet begun. For the other two buildings, the Center has not assessed the monetary value of containment or removal of the asbestos and has not conducted any studies or hired any consultants to address the issue of the asbestos as of the report date. Therefore, the Center has not recorded any accrual for environmental remediation related to these two buildings because the cost of removal is unknown and no plans for remediation have begun.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Financial Statements
June 30, 2012 and 2011

Note 12: Subsequent Events

In preparing these financial statements, the Center has evaluated events and transactions for potential recognition or disclosure through October 5, 2012, the date the financial statements were available to be issued.

Line of Credit: In September 2012, the Center obtained a \$1 million unsecured line of credit from a bank that expires on December 31, 2013. The line of credit bears interest at the 30-Day LIBOR rate plus 2.5% and requires interest only monthly payments on any outstanding balance.

Renovations: The Center currently operates out of three locations in Baltimore City. With the purchase of the building at 1111 North Charles Street in Baltimore, the Center's management has decided to consolidate all operations into this new building once renovations to the building have been completed. Subsequent to year end, the Center has entered into a commitment agreement with a contractor to perform the renovations to the two building locations at 1111 North Charles Street, but as of the report date, the cost of the project has not been finalized. Management estimates the cost of renovations could range from \$27 to \$29 million. In addition, as part of these renovations, the Center has entered into a contract for \$371,200 with a vendor in August 2012 for the removal of the asbestos in these buildings prior to the start of any demolition and renovations to the buildings.

Other than the subsequent events listed above, during the period from July 1, 2012 through October 5, 2012, the Center did not have any other material recognizable subsequent events.

CHASE BREXTON HEALTH SERVICES, INC.

SUPPLEMENTARY INFORMATION

JUNE 30, 2012 AND 2011

CHASE BREXTON HEALTH SERVICES, INC.
Schedules of Expenditures of Federal Awards
Year Ended June 30, 2012

<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Entity Identifying Number</u>	<u>Grant Period</u>	<u>Program or Award Amount</u>	<u>Federal Expenditures (Allowable)</u>
U.S. Department of Health and Human Services					
Consolidated Health Centers					
Section 330 Grant	93.224		01/01/11 - 12/31/11	1,611,715	\$ 813,231
Section 330 Grant	93.224		01/01/12 - 12/31/12	1,645,958	864,823
					<u>1,678,054</u>
Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease					
Ryan White HIV/AIDS Program Part C	93.918		01/01/11 - 12/31/11	1,169,001	585,552
Ryan White HIV/AIDS Program Part C	93.918		01/01/12 - 12/31/12	1,344,001	719,255
					<u>1,304,807</u>
ARRA - Community Health Applied Research Network	93.420		09/01/10 - 08/31/11	108,706	12,079
ARRA - Community Health Applied Research Network	93.420		09/01/11 - 06/30/12	108,859	83,412
					<u>95,491</u>
Special Projects of National Significance (SPNS)	93.928		09/01/11 - 08/31/12	90,000	<u>74,538</u>
Passed through Maryland Department of Health and Mental Hygiene					
Centers for Disease Control and Prevention Investigations and Technical Assistance	93.283	FHA-G912	07/01/11 - 06/30/12	100,000	<u>100,000</u>
Passed through the Baltimore City Health Department:					
HIV Care Formula Grants - Ryan White Part B					
Ryan White B - Primary Care	93.917	34795	07/01/11 - 06/30/12	320,585	320,585
Ryan White B - Oral Health	93.917	34794	07/01/11 - 06/30/12	60,000	60,000
Ryan White B - MAI Outreach	93.917	34798	07/01/11 - 06/30/12	50,508	50,508
Ryan White B - Case Management	93.917	34792	07/01/11 - 06/30/12	67,542	67,542
Ryan White B - Substance Abuse	93.917	34796	07/01/11 - 06/30/12	49,348	49,348
Ryan White B - Treatment Adherence	93.917	34797	07/01/11 - 06/30/12	78,000	78,000
Ryan White B - Mental Health	93.917	34793	07/01/11 - 06/30/12	79,487	79,487
Ryan White B - Eastern Shore	93.917	10-10264	07/01/11 - 06/30/12	235,431	235,431
					<u>940,901</u>
HIV Prevention Activities - Health Department Based					
HIV Prevention Program	93.940	34983	07/01/11 - 06/30/12	100,000	<u>100,000</u>
Passed through Friends Research Institute, Inc.:					
Drug Abuse and Addiction Research Programs	93.279	5R01DA030771	09/30/10 - 06/30/12	171,762	<u>143,033</u>

See accompanying notes to Schedule of Expenditures of Federal Awards.

CHASE BREXTON HEALTH SERVICES, INC.
Schedules of Expenditures of Federal Awards (Continued)
Year Ended June 30, 2012

Federal Grantor/Program Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Grant Period	Program or Award Amount	Federal Expenditures (Allowable)
U.S. Department of Health and Human Services (Continued)					
Passed through the Baltimore City Health Department:					
Passed through Associated Black Charities, Inc.:					
HIV Emergency Relief Project Grants					
Ryan White A - Mental Health	93.914	11-2434	03/01/11 - 02/28/12	96,915	70,173
Ryan White A - Mental Health	93.914	12-2434	03/01/12 - 02/28/13	99,823	31,997
Ryan White A - Case Management	93.914	11-2434	03/01/11 - 02/28/12	140,000	97,003
Ryan White A - Case Management	93.914	12-2434	03/01/12 - 02/28/13	144,200	43,851
Ryan White A - Case Management STCS	93.914	11-2434	03/01/11 - 02/28/12	105,000	75,267
Ryan White A - Case Management STCS	93.914	12-2434	03/01/12 - 02/28/13	108,150	32,654
Ryan White A - Transportation	93.914	11-2434	03/01/11 - 02/28/12	16,125	11,311
Ryan White A - Transportation	93.914	12-2434	03/01/12 - 02/28/13	20,258	6,839
Ryan White A - Primary Care	93.914	11-2434	03/01/11 - 02/28/12	654,000	483,749
Ryan White A - Primary Care	93.914	12-2434	03/01/12 - 02/28/13	650,000	200,029
Ryan White A - Substance Abuse	93.914	11-2434	03/01/11 - 02/28/12	130,000	90,030
Ryan White A - Substance Abuse	93.914	12-2434	03/01/12 - 02/28/13	124,172	38,017
Ryan White A - Housing	93.914	11-2434	03/01/11 - 02/28/12	20,000	14,163
Ryan White A - Housing	93.914	12-2434	03/01/12 - 02/28/13	20,000	9,388
Ryan White A - EFA OAHS	93.914	11-2434	03/01/11 - 02/28/12	54,844	45,576
Ryan White A - EFA OAHS	93.914	12-2434	03/01/12 - 02/28/13	54,844	15,062
Ryan White A - EFA OAHS STSC	93.914	11-2434	03/01/11 - 02/28/12	4,894	3,263
Ryan White A - EFA OAHS STSC	93.914	12-2434	03/01/12 - 02/28/13	8,000	3,145
Ryan White A - Health Insurance	93.914	11-2434	03/01/11 - 02/28/12	45,000	34,000
Ryan White A - Health Insurance	93.914	12-2434	03/01/12 - 02/28/13	45,000	16,066
Ryan White A - Nutritional Counseling	93.914	11-2434	03/01/11 - 02/28/12	24,531	17,120
Ryan White A - Nutritional Counseling	93.914	12-2434	03/01/12 - 02/28/13	24,531	7,444
Ryan White A - Oral Health Care	93.914	11-2434	03/01/11 - 02/28/12	160,754	121,397
Ryan White A - Oral Health Care	93.914	12-2434	03/01/12 - 02/28/13	150,753	60,618
Ryan White A - Co-Morbidity	93.914	12-2434	03/01/12 - 02/28/13	60,000	19,886
Ryan White A - Legal Services	93.914	11-2434	03/01/11 - 02/28/12	50,000	37,040
Ryan White A - Legal Services	93.914	12-2434	03/01/12 - 02/28/13	51,500	16,086
Ryan White MAI - Mental Health	93.914	11-2434MAI	03/01/11 - 02/28/12	71,676	51,676
Ryan White MAI - Mental Health	93.914	12-2434MAI	03/01/12 - 02/28/13	74,034	22,615
Ryan White MAI - Case Management	93.914	11-2434MAI	03/01/11 - 02/28/12	90,000	60,000
Ryan White MAI - Case Management	93.914	12-2434MAI	03/01/12 - 02/28/13	90,000	27,226
Ryan White A - Outreach	93.914	11-2434	03/01/11 - 02/28/12	63,000	47,442
Ryan White A - Outreach	93.914	12-2434	03/01/12 - 02/28/13	50,000	15,699
					<u>1,825,832</u>
Total U.S. Department of Health and Human Services					<u>6,262,656</u>
U.S. Department of Housing and Urban Development					
Passed through the City of Baltimore, Department of Housing and Community Development					
Housing Opportunities for Persons with AIDS	14.241	C034584	07/01/11 - 06/30/12	152,368	152,311
Total Expenditures of Federal Awards					<u>\$ 6,414,967</u>

See accompanying notes to Schedule of Expenditures of Federal Awards.

CHASE BREXTON HEALTH SERVICES, INC.
Notes to Schedule of Expenditures of Federal Awards
June 30, 2012

Note A: Basis of Presentation

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal grant activity of Chase Brexton Health Services, Inc. under programs of the federal government for the year ended June 30, 2012. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of Chase Brexton Health Services, Inc., it is not intended to and does not present the financial position, changes in net assets, or cash flows of Chase Brexton Health Services, Inc.

Note B: Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-122, *Cost Principles for Non-profit Organizations*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

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*

To the Board of Directors
Chase Brexton Health Services, Inc.

We have audited the financial statements of Chase Brexton Health Services, Inc. as of and for the year ended June 30, 2012, and have issued our report thereon dated October 5, 2012. 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.

Internal Control Over Financial Reporting

Management of Chase Brexton Health Services, Inc. is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Chase Brexton Health Services, Inc.'s internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Chase Brexton Health Services, Inc.'s internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Chase Brexton Health Services, Inc.'s internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

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. We consider the deficiency described as Finding #2012-1 in the accompanying schedule of findings and questioned costs to be a material weakness.

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* (Continued)

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Chase Brexton Health Services, Inc.'s financial statements are free of 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*.

We noted certain matters that we reported to management of Chase Brexton Health Services, Inc. in a separate letter dated October 5, 2012.

Chase Brexton Health Services, Inc.'s response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit Chase Brexton Health Services, Inc.'s response and, accordingly, we express no opinion on it

This report is intended solely for the information and use of the Board of Directors, management, others within the entity, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Gross, Mendelsohn & Associates, P.A.

Baltimore, Maryland
October 5, 2012

Independent Auditor's Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control over Compliance
in Accordance with OMB Circular A-133

To the Board of Directors
Chase Brexton Health Services, Inc.

Compliance

We have audited Chase Brexton Health Services, Inc.'s compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Chase Brexton Health Services, Inc.'s major federal programs for the year ended June 30, 2012. Chase Brexton Health Services, Inc.'s major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Chase Brexton Health Services, Inc.'s management. Our responsibility is to express an opinion on Chase Brexton Health Services, Inc.'s compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Chase Brexton Health Services, Inc.'s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Chase Brexton Health Services, Inc.'s compliance with those requirements.

In our opinion, Chase Brexton Health Services, Inc. complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

Independent Auditor's Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control over Compliance
in Accordance with OMB Circular A-133 (Continued)

Internal Control Over Compliance

Management of Chase Brexton Health Services, Inc. is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Chase Brexton Health Services, Inc.'s internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Chase Brexton Health Services, Inc.'s internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the Board of Directors, management, others within the entity, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Gross, Mendelsohn & Associates, P.A.

Baltimore, Maryland
October 5, 2012

CHASE BREXTON HEALTH SERVICES, INC.
Schedule of Findings and Questioned Costs
Year Ended June 30, 2012

Summary of Auditor's Results

1. The auditor's report expresses an unqualified opinion on the financial statements of Chase Brexton Health Services, Inc.
2. One material weakness relating to the audit of the financial statements is reported in the 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*.
3. No instances of noncompliance material to the financial statements of Chase Brexton Health Services, Inc., which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.
4. No significant deficiencies relating to the audit of the major federal award programs are reported in the report on Compliance with Requirements That Could Have a Direct and Material Effect on Each major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133.
5. The auditor's report on compliance for the major federal award programs for Chase Brexton Health Services, Inc. expresses an unqualified opinion on all major federal programs.
6. No audit findings are required to be reported in accordance with Section 510(a) of the OMB Circular A-133 are reported on this schedule.
7. The following grants were tested as major programs:
 - a. Consolidated Health Centers - Section 330 (CFDA No. 93.224)
 - b. Grants to Provide Outpatient Early Intervention Services with Respects to HIV Disease - Ryan White HIV/AIDS Program Part C (CFDA No. 93.918)
 - c. HIV Care Formula Grants - Ryan White Part B (CFDA No. 93.917)
 - d. HIV Emergency Relief Project Grants - Ryan White A (CFDA No. 93.914)
8. The threshold used for distinguishing between Type A and B programs was \$300,000.
9. Chase Brexton Health Services, Inc. did not qualify as a low risk auditee as defined by OMB Circular A-133.

CHASE BREXTON HEALTH SERVICES, INC.
Schedule of Findings and Questioned Costs
Year Ended June 30, 2012

Findings - Financial Statement Audit

Finding #2012-1

Statement of Condition: Pharmacy revenue is posted to the general ledger based on a report that is provided to the Finance Department by the Pharmacy Department. It was the Finance Department's understanding that this report reflected the actual revenue to be collected after adjustment for any contractual allowances through third party payor contracts, which they believed was electronically approved for payment by the third party payors. Individuals without insurance, unless covered under one of the Center's grant programs, are required to pay in full for their prescriptions at the time of pick-up. As a result, the Finance Department did not monitor or analyze the pharmacy revenue and receivables. During our testing of pharmacy receivables, we noted that there were write-offs and additional contractual adjustments of these receivables and upon further investigation learned that the revenue report provided by the Pharmacy Department does not reflect the actual amount to be received, but is an estimate of the potential collection from the third party payors. In addition, we learned that prescriptions billed to third party payors that are not picked up by the individual in a specified timeframe are restocked and the billing is cancelled. This restock information was not communicated to the Finance Department. Had the Finance Department been properly and timely monitoring and analyzing pharmacy receivables, these issues would have been discovered and the balance of pharmacy receivables at month end would have reflected the actual month end balances.

Criteria: In order to properly record pharmacy revenue, pharmacy receivables and determine an appropriate allowance for doubtful accounts, appropriate policies, procedures and segregation of duties need to be implemented.

Effect: By not having appropriate policies, procedures and segregation of duties over pharmacy revenue, there exists the possibility of fraud occurring and not being detected.

Cause: The Finance Department's understanding of the pharmacy revenue tracking system was not correct. In addition, there are no policies and procedures in place to monitor revenue recognition and to monitor and assess the collectability of outstanding receivables.

Recommendation: We recommend that the Center update their internal control policies and procedures related to the pharmacy and that the Finance Department monitor the pharmacy revenue and related receivables as well as assess collectability on a monthly basis. In addition, all reports generated by the pharmacy that affect pharmacy revenue and receivables, including restocking information, must be provided to the Finance Department at least monthly. The Finance and Pharmacy Department should work more closely together to insure that the pharmacy activity has been properly reflected in the financial records of the Center.

Auditors Summary of Auditee's Comments: Management agrees with the auditor's findings and has developed an action plan to address the control deficiencies. The plan includes updating policies and procedures related to the recordation of pharmacy revenue and receivables. There policies will include obtaining proper and complete revenue and receivable reports and performing periodic reconciliation and follow-up.

CHASE BREXTON HEALTH SERVICES, INC.
Schedule of Findings and Questioned Costs
Year Ended June 30, 2012

Findings and Questioned Costs - Major Federal Award Programs Audit

None

Summary Schedule of Prior Audit Findings

Finding #2011-1

Statement of Condition: In accordance with the Ryan White A grant requirements, Ryan White C grant requirements and the AARA Capital Improvement Program and Increase Services to Health Centers, the Center must charge a patient for services based on the sliding fee scale. The costs per the sliding fee scale are based on the patient's income level. The Center imposed charges on patients that were above and below the allowed amount based on the patient's income level and the sliding fee scale.

Status: The Center's Revenue Cycle Committee addressed this finding and reviewed and updated existing policies and procedures to ensure that they are up to date for current requirements and that appropriate internal control has been implemented to ensure that the Center is in compliance with the sliding fee scale requirements. Existing staff and managers were provided with training to ensure they are following the updated policies and procedures. During the current year's testing of the sliding fee scale requirements, we noted no findings.

Finding #2011-2

Statement of Condition - Section 505 of Circular A-133 includes specific auditor reporting requirements. The data collection form is required to be submitted to the Federal Audit Clearinghouse by the auditee. That submission should be completed within the earlier of 30 days after receipt of the auditor's reports or nine months after the end of the audit period, unless a longer period is agreed in advanced by the cognizant or oversight agency for the audit. The Center filed the year ended June 30, 2010 Data Collection Form with the Federal Audit Clearinghouse on July 26, 2011, which was after the timely filing period described above. However, management provided complete reporting packages under OMB Circular A-133 to all of its federal funding sources shortly after the final auditor's reports were received.

Status: Management has established a calendar of due dates for all external filings. The due dates were added to the electronic calendars of persons responsible for filing and finance management to ensure timely filing of reports. The data collection form for the year ended June 30, 2011 was filed timely.

