

**Community Health Services, Inc.**

**Federal Awards in  
Accordance with Circular A-133**

**December 31, 2012**

# Community Health Services, Inc.

## Index

	<u>Page</u>
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 <i>Government Auditing Standards</i>	2-3
Independent Auditor's Report on Compliance for Each Major Federal Program; Report on Internal Control over Compliance; and Report on the Schedule of Expenditures of Federal Awards Required by OMB Circular A-133	4-6
Schedule of Expenditures of Federal Awards	7
Notes to Schedule of Expenditures of Federal Awards	8
Schedule of Findings and Questioned Costs	9-19

**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***

To the Board of Directors  
Community Health Services, Inc.

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 Community Health Services, Inc. (the "Center"), which comprise the statement of financial position as of December 31, 2012, and the related statements of activities and changes in net assets, functional expenses and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated May 28, 2013.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Center'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Center's internal control. Accordingly, we do not express an opinion on the effectiveness of the Center's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified a certain deficiency in internal control that we consider to be a material weakness.

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 deficiencies described in the accompanying schedule of findings and questioned costs to be material weaknesses (Finding # 2012-1).

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Center'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*.

## The Center's Response to Finding

The Center's response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The Center's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

## Purpose of this Report

This 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 Center's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Cohn Reznick LLP". The signature is written in a cursive, flowing style.

Glastonbury, Connecticut  
May 28, 2013

**Independent Auditor's Report on Compliance for Each Major Federal Program;  
Report on Internal Control over Compliance; and Report on the  
Schedule of Expenditures of Federal Awards Required  
by OMB Circular A133**

To the Board of Directors  
Community Health Services, Inc.

Report on Compliance for Each Major Federal Program

We have audited Community Health Services, Inc.'s (the "Center") 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 the Center's major Federal programs for the year ended December 31, 2012. The Center's major Federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its Federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Center's major Federal programs based on our audit of the types of compliance requirements referred to above. 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 the Center'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 on compliance for each major Federal program. However, our audit does not provide a legal determination of the Center's compliance.

Basis for Qualified Opinion on Major Federal Programs (CFDA # 93.224, 93.527, 93.703, 93.918 and 93.268)

As described in the accompanying schedule of findings and questioned costs, the Center did not comply with the following requirements:

<u>Finding #</u>	<u>CFDA #</u>	<u>Compliance Requirement</u>
2012-2	93.224, 93.527, 93.703 and 93.918	Activities Allowed or Unallowed - Time and effort reporting
2012-3	93.224, 93.527, 93.703 and 93.918	Cash Management - Non-interest bearing accounts
2012-4	93.224 and 93.527	Special Tests and Provisions - Board member compliance
2012-5	93.268	Special Tests and Provisions - Vaccines

Compliance with such requirements is necessary, in our opinion, for the Center to comply with requirements applicable to those programs.

Qualified Opinion on Major Federal Programs (CFDA # 93.224, 93.527, 93.703, 93.918 and 93.268)

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, the Center complied, in all material respects, with the types of compliance requirements referred to above that could have direct and material effect on each of its major Federal programs for the year ended December 31, 2012.

Other Matters

The Center's responses to the noncompliance findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The Center's responses were not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on those responses.

Report on Internal Control Over Compliance

Management of the Center is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Center's internal control over compliance with the types of requirements that could have a direct and material effect on each major Federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major Federal program 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 the Center's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses.

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

The Center's responses to the internal control over compliance findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The Center's responses were not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the responses.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

#### Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

We have audited the financial statements of the Center as of and for the year ended December 31, 2012, and have issued our report thereon dated May 28, 2013, which contained an unmodified opinion on those financial statements. 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 OMB Circular A133, 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.



Glastonbury, Connecticut  
May 28, 2013

**Community Health Services, Inc.**

**Schedule of Expenditures of Federal Awards  
Year Ended December 31, 2012**

<b>Federal Grantor / Pass-Through Grantor / Program Title</b>	<b>Federal CFDA Number</b>	<b>Pass-Through ID/ Grantor's Number</b>	<b>Federal Expenditures</b>
U.S. Department of Health and Human Services:			
Consolidated Health Centers	93.224	N/A	\$ 1,511,487
Passed through the Massachusetts League of Community Health Centers:			
Consolidated Health Centers	93.224	CRVFHP	49,568
Total CFDA 93.224			<u>1,561,055</u>
Affordable Care Act - Grants for New and Expanded Services Under the Health Center Program	93.527	N/A	1,598,370
Total Health Center Cluster			<u>3,159,425</u>
Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	93.918	N/A	359,327
American Recovery and Reinvestment Act (ARRA):			
Grants to Health Center Programs	93.703	N/A	501,679
Passed through Community Health Center Association of Connecticut:			
Centers for Disease Control and Prevention - Investigations and Technical Assistance	93.283	2010-0193-4	26,573
Coordinated Services and Access to Research for Women, Infants, Children and Youth	93.153	H12HA00008-220-0	127,629
Cooperative Agreements to States/Territories For the Coordination and Development of Primary Care Offices	93.130	N/A	1,000
			<u>155,202</u>
Passed through the City of Hartford:			
HIV Emergency Relief Project Grants	93.914	HHS2012-39E	<u>104,386</u>
Passed through State of Connecticut Department of Mental Health and Addiction Services:			
Substance Abuse and Mental Health Services - Projects of Regional and National Significance	93.243	12MHA2051AA	25,000
Passed through the Hartford Hispanic Council, Inc.			
Substance Abuse and Mental Health Services - Projects of Regional and National Significance	93.243	N/A	67,205
Total CFDA 93.243			<u>92,205</u>
Block Grants for Prevention and Treatment of Substance Abuse	93.959	12MHA2051AA	54,675
			<u>146,880</u>
Passed through the State of Connecticut Department of Social Services:			
Social Services Block Grant	93.667	12DSS1202PC	<u>12,540</u>
Passed through the State of Connecticut Department of Public Health:			
Healthy Start Initiative	93.926	2010-0182	69,216
Immunization Cooperative Agreements (non-cash award)	93.268	N/A	335,823
			<u>405,039</u>
Total Expenditures of Federal Awards			<u>\$ 4,844,478</u>

See Notes to Schedule of Expenditures of Federal Awards.

## Community Health Services, Inc.

### Notes to Schedule of Expenditures of Federal Awards

**Note 1 - General information:**

The accompanying schedule of expenditures of Federal awards presents the activities in all Federal awards of Community Health Services, Inc. (the "Center"). All financial assistance received directly from the Federal agencies as well as financial assistance passed through other government agencies or nonprofit organization is included on the schedule.

**Note 2 - Basis of accounting:**

The accompanying schedule of expenditures of Federal awards is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organization*. The amounts reported in the schedule may differ from certain financial reports submitted to Federal funding agencies due to those reports being submitted on either a cash or modified accrual basis of accounting.

**Note 3 - Relationship to basic financial statements:**

Federal expenditures are reported on the statement of functional expenses as program services. In certain programs, the expenditures reported in the basic financial statements may differ from the expenditures reported in the schedule of expenditures of Federal awards due to program expenditures exceeding grant or contract budget limitations or agency-matching or in-kind contributions which are not included in the statement of activities and changes in net assets.

**Note 4 - Subrecipients**

There were no Federal awards provided to subrecipients.

**Community Health Services, Inc.**

**Schedule of Findings and Questioned Costs**

**I. Summary of Auditor's Results:**

Financial Statements:

Type of auditor's report issued:

Unmodified

- Material weakness(es) identified?  yes  no
- Significant deficiency(ies) identified?  yes  none reported

Noncompliance material to financial statements noted?

yes  no

Federal Awards:

Internal control over major programs:

- Material weakness(es) identified?  yes  no
- Significant deficiency(ies) identified?  yes  none reported

Type of auditor's report issued on compliance for major programs:

Qualified

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133?

yes  no

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
	U.S. Department of Health and Human Services:
	Health Center Cluster:
93.224	Consolidated Health Centers
93.527	Affordable Care Act - Grants for New and Expanded Services Under the Health Center Program
93.703	American Recovery and Reinvestment Act (ARRA) – Grants to Health Center Programs
93.918	Grants to Provided Outpatient Early Intervention Services with Respect to HIV Disease
93.268	Immunization Cooperative Agreements

Dollar threshold used to distinguish between type A and type B programs

\$300,000

Auditee qualified as low-risk auditee?

yes  no

**Community Health Services, Inc.**

**Schedule of Findings and Questioned Costs**

**II. Financial Statements Findings:**

FINDING # 2012-1 Payroll Approval

Criteria

Internal controls for time reporting and payroll processing should be designed and implemented to have appropriate personnel approve hours worked prior to being disbursed and recorded to the general ledger.

Condition

The Center did not have effective internal controls in place throughout the entire year to approve employee time prior to being transmitted through payroll. In July 2012, management did implement an automated control to not allow the submission of payroll without approval. We noted several instances where employee time worked was not approved prior to being processed, before the aforementioned control was implemented.

Cause

Policies regarding electronic supervisor approval were not being followed consistently during the year. In addition, the Center did not have automated controls within the payroll system to prevent unapproved time from being processed the entire year.

Effect

Employee time could potentially be misstated or allocated to the incorrect grant cost center without being detected or prevented on a timely basis.

Recommendation

We recommend that the Center continue to utilize the automated control described above to prevent unapproved time from being processed. In addition, we recommend that the importance of supervisor approval continue to be communicated to appropriate individuals.

Management's Response

The Center has implemented a new time reporting system during the fiscal year and has conducted supervisor meetings and other training sessions to emphasize the importance of time approval for financial statement and grant reporting purposes. In addition, during 2012 the payroll system has been updated with an automated control to not allow the submission of payroll without approval.

## Community Health Services, Inc.

### Schedule of Findings and Questioned Costs

#### III. Federal Award Findings and Questioned Costs:

##### Finding # 2012-2 - Activities Allowed or Unallowed - Time and Effort Reporting

Grantor: U.S. Department of Health and Human Services ("DHHS")  
Federal Program Names: Consolidated Health Centers, Affordable  
Care Act - Grants for New and Expanded Services  
Under the Health Center Program, American Recovery and  
Reinvestment Act – Grants to Health Center Programs and  
Grants to Provide Outpatient Early Intervention Services with  
Respect to HIV Disease  
CFDA Numbers: 93.224, 93.527, 93.703 and 93.918

##### Criteria:

As prescribed by OMB Circular A-122, written after-the-fact time and effort reporting should be maintained that accounts for the total activity of employees and the programs/funding sources charged. These reports should be as stipulated in DHHS regulations.

The reports must be signed by the individual employee or by a responsible supervisory official having first-hand knowledge of the activities performed by the employee, indicating that the distribution of activity represents a reasonable estimate of the actual work performed by the employee during the periods covered by the reports.

##### Condition:

The Center allocated personnel costs to each program/funding source through use of full time equivalent ("FTE") allocations that were budgeted at the beginning of the funding period. Although grant expenditure reports were based on actual time worked, the effort percentages used in the allocated based on budgets and not approved using after-the-fact analysis.

##### Questioned Cost:

None

##### Effect:

Certain personnel costs allocated to funding sources are not supported by after-the-fact time and effort reports.

##### Cause:

Time and effort reporting procedures were in process, but not fully implemented by the Center during the course of the year.

##### Recommendation:

We recommend that time and effort reporting be fully implemented and consistently followed.

##### Management's Response:

Management has implemented a new time reporting system in 2012 and hired a new Director of Human Resources who will be tasked to develop and implement a time and effort reporting process that will be adopted by the Center. The system was in place in July 2012 and was effectively functioning through the end of the year.

**Community Health Services, Inc.**

**Schedule of Findings and Questioned Costs**

Finding # 2012-3 - Cash Management - Non-interest Bearing Accounts

Grantor: U.S. Department of Health and Human Services  
Federal Program Names: Consolidated Health Centers, Affordable Care Act - Grants for New and Expanded Services Under the Health Center Program, American Recovery and Reinvestment Act – Grants to Health Center Programs and Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease  
CFDA Numbers: 93.224, 93.527, 93.703 and 93.918

Criteria:

The award agreement stipulates, under compliance requirement C, the Center should draw down grant funds into an interest bearing account.

Condition:

The Center did not properly draw down Federal funding into an interest bearing account during the entire year.

Questioned Cost:

None

Effect:

The Center was in violation of compliance requirements stipulated under the grant award.

Cause:

In 2012 the Center had opened an interest-bearing account; however, due to technical difficulties were unable to implement the draws into the account until December 2012.

Recommendation:

We recommend that the Center continue to use the interest-bearing account for drawdown purposes in order to comply with the requirement.

Management's Response:

The new account is currently in use.

**Community Health Services, Inc.**

**Schedule of Findings and Questioned Costs**

Finding # 2012-4 - Special Tests and Provisions - Board Member Compliance

Grantor: U.S. Department of Health and Human Services  
Federal Program Name: Consolidated Health Centers and Affordable Care Act - Grants for New and Expanded Services Under the Health Center Program  
CFDA Numbers: 93.224 and 93.527

Criteria:

The award agreement stipulates, under compliance requirement N, the Center's board must be composed of individuals, a majority of whom are being served by the Center and who, as a group, represent the individuals being served by the Center.

Condition:

The Center's board was not comprised of a majority of individuals who were served by the Center.

Questioned Cost:

None

Effect:

The Center was in violation of compliance requirements stipulated under the grant agreement.

Cause:

During the fiscal year, the Center became aware that the board did not meet the compliance requirement.

Recommendation:

The Center's board should encompass individuals who are representatives of the health center and are users of the Center as well as representatives of the populations served.

Management's Response:

Management has communicated the compliance violation with the board. During 2013, the Center added three members to the Board who are all patients of the Center.

## Community Health Services, Inc.

### Schedule of Findings and Questioned Costs

#### Finding # 2012-5 - Special Tests and Provisions - Vaccines

Grantor: U.S. Department of Health and Human Services  
Federal Program Name: Immunization Cooperative Agreements  
CFDA Number: 93.268

#### Criteria:

The award agreement stipulates, under compliance requirement N, the vaccines used in the program must be adequately safeguarded and used solely for authorized purposes. This includes administration only to children eligible under the Vaccines for Children program.

#### Condition:

The Center did not have documented and approved policies around all aspects of the donated vaccines program. We encountered one instance of an expired vaccine being administered to a patient and some vaccines that did not include a documented expiration date. In addition, we determined that vaccines under the program were administered to ineligible patients of the Center.

#### Questioned Cost:

None

#### Effect:

The Center administered multiple doses of donated vaccines to patients that were ineligible under the grant program. The Center also administered a vaccine that was expired and vaccines that did not have a documented expiration date. Finally, the Center was also not in compliance based on the lack of approved policies and procedures.

#### Cause:

The non-compliance noted above is the result of lack of clear and communicated policies regarding donated vaccines.

#### Recommendation:

We recommend that Center document policies for all aspects of the donated vaccines program including order placement, inventory tracking, physical safeguarding, inventory lot location procedures, expiration date tracking and administering vaccines to eligible patients. These policies should be communicated to all employees and providers involved in the process and periodically tracked to verify compliance with the grant program.

#### Management's Response:

The Center is in the process of developing and approving policies around use of vaccines. Once approved, these policies will be communicated to appropriate individuals.

**Community Health Services, Inc.**

**Schedule of Findings and Questioned Costs**

**IV. Prior Year Financial Statements Findings:**

**FINDING # 2011-1 Payroll Approval**

Condition

The Center did not have effective internal controls in place to approve employee time prior to being transmitted through payroll. We noted several instances where employee time worked was not approved prior to being processed.

Current Status:

Reference Finding # 2012-1 for documentation of this finding in the current year.

**FINDING # 2011-2 Revenue and Expense Cut-off**

Condition

The Center did not have adequate controls implemented to monitor proper cut-off of both revenue and expenses at year-end.

Current Status

The Center has implemented financial policies that include monitoring of year-end cut-off. There were no similar findings in 2012.

**FINDING # 2011-3 Patient Service Receivable and Revenue**

Condition:

During the course of the year, the computerized billing system was not reconciled to general ledger control accounts on a regular basis. In addition, the Center could not reconcile gross charges and contractual allowances to general ledger control accounts.

Current Status:

The Center has hired key personnel in the finance department who were tasked to address the discrepancies between the general ledger controls accounts and patient receivable subsidiary ledger. The ledgers are reconciled to each other on a monthly basis and included in the standard closing process. There were no similar findings in 2012.

## Community Health Services, Inc.

### Schedule of Findings and Questioned Costs

#### V. Prior Year Federal Award Findings and Questioned Costs:

##### 2011-4 - Activities Allowed or Unallowed - Disbursements

Grantor: U.S. Department of Health and Human Services  
Federal Program Names: Consolidated Health Centers, Affordable  
Care Act - Grants for New and Expanded Services  
Under the Health Center Program  
CFDA Number: 93.224 and 93.527

##### Condition:

During our test of activities allowed or unallowed, we noted instances where documentation provided was not adequate to determine proper allocation and coding of expenses to proper grant codes. In addition, we noted one instance where documentation for a selected disbursement could not be located by the Center.

##### Current Status:

The Center has implemented controls that require all invoices be coded and approved through use of a stamp that identifies expense and grant codes and approval of expenses being processed. Our audit procedures resulted no related findings in 2012.

##### 2011-5 – Activities Allowed or Unallowed - Time and Effort Reporting

Grantor: U.S. Department of Health and Human Services  
Federal Program Names: Consolidated Health Centers, Affordable  
Care Act - Grants for New and Expanded Services  
Under the Health Center Program  
CFDA Number: 93.224 and 93.527

##### Condition:

The Center allocated personnel costs to each program/funding source through use of FTE allocations that were budgeted at the beginning of the funding period.

##### Current Status:

The Center has implemented new time reporting software in 2012 and is currently working to implement a method to accurately and efficiently verify time and effort reporting as it relates to grant programs; however, the Center is still not in compliance with this requirement. As such, reference Finding #2012-2 for documentation of the 2012 finding.

## Community Health Services, Inc.

### Schedule of Findings and Questioned Costs

#### 2011-6 – Cash Management - Non-interest Bearing Accounts

Grantor: U.S. Department of Health and Human Services  
Federal Program Names: Consolidated Health Centers, Affordable Care Act - Grants for New and Expanded Services Under the Health Center Program, American Recovery and Reinvestment Act – Grants to Health Center Programs  
CFDA Numbers: 93.224, 93.527 and 93.703

Condition:

The Center did not properly draw down Federal funding into an interest bearing account.

Current Status:

As noted in Finding # 2012-3, the Center has obtained interest-bearing accounts to be used for grant drawdowns; however, the account was not operational during 2012. During 2013, this account was being used to drawdown funding.

#### 2011-7 - Special Tests and Provisions - Board Members Compliance

Grantor: U.S. Department of Health and Human Services  
Federal Program Names: Consolidated Health Centers, Affordable Care Act - Grants for New and Expanded Services Under the Health Center Programs and American Recovery and Reinvestment Act – Grants to Health Center Programs  
CFDA Number: 93.224, 93.527 and 93.703

Condition:

The Center's board was not comprised of a majority of individuals who were served by the Center.

Current Status:

Reference Finding # 2012-4 for documentation of this finding in 2012.

**Community Health Services, Inc.**

**Schedule of Findings and Questioned Costs**

2011-8 – Equipment and Real Property Management - Property Management Standards

Grantor: U.S. Department of Health and Human Services  
Federal Program Name: American Recovery and Reinvestment Act – Grants to Health Center Programs  
CFDA Number: 93.703

Condition:

We noted that the Center has not performed a physical inventory of fixed assets in the past two years. In addition, the Center does not have a system for property identification.

Current Status:

The Center conducted a physical inventory of fixed assets in October 2012. The Center is working to transfer fixed asset information to the fixed asset module within the newly implemented accounting software to assist with tracking and maintenance of assets. There were no similar findings in 2012.

2011-9 - Eligibility

Grantor: U.S. Department of Health and Human Services  
Federal Program Name: Consolidated Health Centers and Affordable Care Act - Grants for New and Expanded Services Under the Health Center Program  
CFDA Number: 93.224 and 93.527

Condition:

Although the Center has a sliding fee policy, we noted that the policies involving proof of income and insurance eligibility verification were not being consistently followed by the Center.

Current Status:

The Center appears to be properly following the sliding fee policies. There were no similar findings in 2012.

## Community Health Services, Inc.

### Schedule of Findings and Questioned Costs

#### 2011-10 - Reporting - Grant Reporting Approval

Grantor: U.S. Department of Health and Human Services  
Federal Program Name: American Recovery and Reinvestment Act – Grants to Health Center Programs  
CFDA Number: 93.703

Condition:

In 2011, we noted two instances where quarterly Federal Financial Reports were submitted without adequate approval by authorized personnel.

Current Status:

In 2012, all reports tested were properly approved and filed timely. This finding has been cleared in 2012.

#### 2011-11 – Procurement, Suspension and Debarment

Grantor: U.S. Department of Health and Human Services  
Federal Program Names: Consolidated Health Centers, Affordable Care Act - Grants for New and Expanded Services Under the Health Center Program and American Recovery and Reinvestment Act – Grants to Health Center Programs  
CFDA Number: 93.224, 93.527 and 93.703

Condition:

It was noted that the Federal procurement standards, as required by the Center's policy, were not consistently followed for the first four months of the year.

Current Status:

During 2012 the Center was properly following Federal procurement policies and standards. There were no similar findings in 2012.

**Community Health Services, Inc.**  
**Financial Statements**  
**and Independent Auditor's Report**  
**December 31, 2012 and 2011**

# Community Health Services, Inc.

## Index

	<u>Page</u>
Independent Auditor's Report	2-3
Statements of Financial Position	4
Statements of Activities and Changes in Net Assets	5
Statements of Functional Expenses	6-7
Statements of Cash Flows	8
Notes to Financial Statements	9-19

## Independent Auditor's Report

To the Board of Directors  
Community Health Services, Inc.

### *Report on the Financial Statements*

We have audited the accompanying financial statements of Community Health Services, Inc. (the "Center"), which comprise the statements of financial position as of December 31, 2012 and 2011, and the related statements of activities and changes in net assets, functional expenses and cash flows for the years then ended, and the related notes to the financial statements.

### *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 an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States 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 opinion.

### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Community Health Services, Inc. as of December 31, 2012 and 2011, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Other Reporting Required by Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated May 28, 2013 on our consideration of Community Health Services, Inc.'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 Community Health Services, Inc.'s internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "CohnReznick LLP".

Glastonbury, Connecticut  
May 28, 2013

**Community Health Services, Inc.**

**Statements of Financial Position  
December 31, 2012 and 2011**

<u>Assets</u>	<u>2012</u>	<u>2011</u>
Current assets:		
Cash and cash equivalents	\$ 2,874,504	\$ 1,006,086
Marketable securities	8,908	9,501
Receivables:		
Grants and contracts	721,433	772,256
Patient service, net	681,697	1,081,537
Other receivables	170,357	250,609
Prepaid expenses and other	165,881	154,883
Total current assets	<u>4,622,780</u>	<u>3,274,872</u>
Property and equipment, net	15,813,824	15,313,309
Security deposits	<u>10,133</u>	<u>-</u>
Total assets	<u><u>\$ 20,446,737</u></u>	<u><u>\$ 18,588,181</u></u>
<u>Liabilities and Net Assets</u>		
Current liabilities:		
Current portion of note payable	\$ 73,337	\$ 69,646
Capital lease obligations	-	12,731
Accounts payable	1,061,778	629,845
Accrued liabilities	461,899	473,367
Total current liabilities	<u>1,597,014</u>	<u>1,185,589</u>
Noncurrent liabilities:		
Note payable, net of current portion	<u>526,423</u>	<u>599,665</u>
Total liabilities	<u>2,123,437</u>	<u>1,785,254</u>
Commitments and contingencies		
Net assets:		
Unrestricted net assets	18,315,827	16,753,259
Temporarily restricted net assets	7,473	49,668
Total net assets	<u>18,323,300</u>	<u>16,802,927</u>
Total liabilities and net assets	<u><u>\$ 20,446,737</u></u>	<u><u>\$ 18,588,181</u></u>

See Notes to Financial Statements.

**Community Health Services, Inc.**

**Statements of Activities and Changes in Net Assets  
Years Ended December 31, 2012 and 2011**

	2012	2011
Changes in unrestricted net assets:		
Operating revenue and support:		
Patient service revenue (net of contractual allowances and discounts)	\$ 9,895,766	\$ 11,243,235
Provision for bad debts	(221,988)	(1,221,494)
Net patient service revenue, less provision for bad debts	9,673,778	10,021,741
Pharmacy revenue	656,886	610,766
Government grants	4,847,061	4,022,435
Local and other grants	82,625	214,856
Contributions	4,959	39,071
Rental income and other	48,163	66,656
Loss on disposal of property and equipment	-	(9,767)
Other revenue	409,137	4,650
Total operating revenue and support	15,722,609	14,970,408
Operating expenses:		
Program services	11,069,712	11,535,288
Management and general	4,247,920	3,320,079
Total operating expenses	15,317,632	14,855,367
Operating income	404,977	115,041
Nonoperating income:		
Capital projects grants	1,086,896	4,447,696
Net assets released from restriction	70,695	32,332
Total nonoperating income	1,157,591	4,480,028
Increase in unrestricted net assets	1,562,568	4,595,069
Changes in temporarily restricted net assets:		
Restricted contributions	28,500	52,000
Net assets released from restriction	(70,695)	(32,332)
Increase (decrease) in temporarily restricted net assets	(42,195)	19,668
Change in net assets	1,520,373	4,614,737
Net assets, beginning of year	16,802,927	12,188,190
Net assets, end of year	\$ 18,323,300	\$ 16,802,927

See Notes to Financial Statements.

**Community Health Services, Inc.**

**Statement of Functional Expenses  
Year Ended December 31, 2012**

	<u>Program Services</u>	<u>Management and General</u>	<u>Total</u>
Salaries and wages	\$ 6,019,092	\$ 2,602,576	\$ 8,621,668
Employee benefits	1,258,700	716,224	1,974,924
Contracted services	1,095,490	230,406	1,325,896
Program activities, supplies and materials	526,725	-	526,725
Equipment rental and maintenance	497,271	179,472	676,743
Consultants and subcontractors	53,923	19,730	73,653
Donated supplies	337,823	-	337,823
Professional services	147,330	91,205	238,535
Occupancy	166,258	60,005	226,263
Travel, conferences and meetings	45,099	44,673	89,772
Insurance	100,771	36,370	137,141
Other	59,608	15,946	75,554
Rent	24,236	-	24,236
Postage and supplies	130,350	34,859	165,209
Interest	28,174	7,534	35,708
	<u>10,490,850</u>	<u>4,039,000</u>	<u>14,529,850</u>
Depreciation	<u>578,862</u>	<u>208,920</u>	<u>787,782</u>
Total functional expenses	<u>\$ 11,069,712</u>	<u>\$ 4,247,920</u>	<u>\$ 15,317,632</u>

See Notes to Financial Statements.

**Community Health Services, Inc.**

**Statement of Functional Expenses  
Year Ended December 31, 2011**

	<u>Program Services</u>	<u>Management and General</u>	<u>Total</u>
Salaries and wages	\$ 6,610,507	\$ 1,894,575	\$ 8,505,082
Employee benefits	1,441,362	525,248	1,966,610
Contracted services	752,940	156,564	909,504
Program activities, supplies and materials	552,990	-	552,990
Equipment rental and maintenance	380,232	140,204	520,436
Consultants and subcontractors	310,669	64,599	375,268
Donated supplies	308,623	-	308,623
Professional services	165,737	82,653	248,390
Occupancy	135,139	49,830	184,969
Travel, conferences and meetings	76,176	100,520	176,696
Insurance	117,255	43,236	160,491
Other	60,707	32,944	93,651
Postage and supplies	56,497	20,832	77,329
Interest	27,080	9,986	37,066
	<u>10,995,914</u>	<u>3,121,191</u>	<u>14,117,105</u>
Depreciation	<u>539,374</u>	<u>198,888</u>	<u>738,262</u>
Total functional expenses	<u>\$ 11,535,288</u>	<u>\$ 3,320,079</u>	<u>\$ 14,855,367</u>

See Notes to Financial Statements.

**Community Health Services, Inc.**  
**Statements of Cash Flows**  
**Years Ended December 31, 2012 and 2011**

	2012	2011
Operating activities:		
Change in net assets	\$ 1,520,373	\$ 4,614,737
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Provision for bad debts	221,988	1,221,494
Depreciation	787,782	738,262
Loss on disposal of property and equipment	-	9,767
Capital projects grants and restricted contributions	(1,115,396)	(4,499,696)
Changes in operating assets and liabilities:		
Grants and contracts receivable	50,823	(586,328)
Patient service receivables, net	177,852	(905,593)
Other receivables	80,252	(108,787)
Prepaid expenses and other and security deposits	(21,131)	(96,645)
Accounts payable	431,933	83,389
Accrued liabilities	(11,468)	(16,597)
Net cash provided by operating activities	2,123,008	454,003
Investing activities:		
Net proceeds from sale of marketable securities	593	2,284
Purchases of property and equipment	(1,288,297)	(4,524,545)
Net cash used in investing activities	(1,287,704)	(4,522,261)
Financing activities:		
Capital projects grants and restricted contributions	1,115,396	4,499,696
Principal payments on notes payable	(69,551)	(66,212)
Principal payments on capital leases	(12,731)	(49,030)
Net cash provided by financing activities	1,033,114	4,384,454
Net increase in cash and cash equivalents	1,868,418	316,196
Cash and cash equivalents, beginning of year	1,006,086	689,890
Cash and cash equivalents, end of year	\$ 2,874,504	\$ 1,006,086
Supplemental disclosure of cash flow data:		
Cash paid for interest	\$ 35,708	\$ 37,066

See Notes to Financial Statements.

## Community Health Services, Inc.

### Notes to Financial Statements

#### Note 1 - Organization and summary of significant accounting policies:

##### **Organization:**

Community Health Services, Inc. (the "Center") is a non-profit organization formed for the purpose of providing medical services for residents of the Greater Hartford, Connecticut area.

The U.S. Department of Health and Human Services (the "DHHS") provides substantial support to the Center. The Center is obligated under the terms of the DHHS grants to comply with specified conditions and program requirements set forth by the grantor.

##### **Basis of presentation:**

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. The Center reports information regarding its financial position and activities according to three classes of net assets: unrestricted, temporarily restricted and permanently restricted. They are described as follows:

*Unrestricted* - Net assets that are not subject to explicit donor-imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of the Board of Directors.

*Temporarily Restricted* - Net assets whose use by the Center is subject to either explicit donor-imposed stipulations or by the operation of law that can be fulfilled by actions of the Center or that expire by the passage of time.

*Permanently Restricted* - Net assets subject to explicit donor-imposed stipulations that they be maintained permanently by the Center and stipulate the use of income and/or appreciation as either unrestricted or temporarily restricted based on donor imposed stipulations or by operation of law. At December 31, 2012 and 2011, there were no permanently restricted net assets.

##### **Cash and cash equivalents:**

For purposes of the statement of cash flows, the Center considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

##### **Marketable securities:**

Investments in marketable securities are carried at fair market value.

##### **Patient service receivables:**

The collection of receivables from third-party payors and patients is the Center's primary source of cash for operations and is critical to its operating performance. The primary collection risks relate to uninsured patient accounts and patient accounts for which the primary insurance payor has paid, but patient responsibility amounts (deductibles and copayments) remain outstanding. Patient receivables from third-party payors are carried at a net amount determined by the original charge for the service provided, less an estimate made for contractual adjustments or discounts provided to third-party payors.

## Community Health Services, Inc.

### Notes to Financial Statements

Management determines the allowance for doubtful accounts by identifying troubled accounts and by historical experience applied to an aging of accounts. The Center considers accounts past due when they are outstanding beyond 60 days with no payment. The Center generally does not charge interest on past due accounts. Patient receivables are written off to the allowance for doubtful accounts when deemed uncollectible. Recoveries of receivables previously written off are recorded as a reduction of bad debts expense when received.

#### **Pharmacy revenue:**

The Center participates in Section 340B of the Public Health Service Act ("PHS Act"), "Limitation on Prices of Drugs Purchased by Covered Entities". Participation in this program allows the Center to purchase pharmaceuticals at discounted rates for prescription to eligible patients. The Center has outsourced the administration of this program to a commercial pharmacy. The Center records revenue based on the price of the pharmaceuticals dispensed.

#### **Property and equipment:**

Property and equipment acquisitions that individually exceed \$5,000 and have a useful life of greater than one year are capitalized at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. Estimated useful lives of assets are as follows:

Building	39 years
Improvements	20 years
Office and medical equipment	10 years
Furniture and fixtures	7 years

Expenditures for repairs and maintenance are charged to expense as incurred. For assets sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in the statement of activities and changes in net assets.

The Center reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In performing a review for impairment, the Center compares the carrying value of the assets with their estimated future undiscounted cash flows. If it is determined that impairment has occurred, the loss would be recognized during the period. The impairment loss is calculated as the difference between the asset carrying values and the present value of estimated net cash flows or comparable market values giving consideration to recent operating performance and pricing trends. The Center does not believe that any material impairment currently exists related to its long-lived assets.

Construction-in-progress is recorded at cost. The Center capitalizes construction, and other costs during the period of construction. Depreciation is recorded when construction is substantially complete and the assets are placed in service.

## **Community Health Services, Inc.**

### **Notes to Financial Statements**

Certain property and equipment acquired with Federal Government and State of Connecticut grant funds are considered to be owned by the Center while used in the program or in future authorized programs. However, the Federal Government and the State of Connecticut retain a reversionary interest in these assets, as well as the right to determine the use of any proceeds from their sale or disposal. Accordingly, the Center may not transfer, mortgage, assign, lease or in any other manner encumber these assets without prior approval from the Federal Government and the State of Connecticut.

#### **Recognition of support and revenue:**

##### **Patient service revenue:**

The Center has agreements with third-party payors that provide for payments to the Center at amounts different from its established rates. Payment arrangements include predetermined fee schedules and discounted charges. Service fees are reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including retroactive adjustments under reimbursement agreements with third-party payors, which are subject to audit by administering agencies. These adjustments are accrued on an estimated basis and are adjusted in future periods as final settlements are determined. The Center provides care to certain patients under Medicaid and Medicare payment arrangements. Laws and regulations governing the Medicaid and Medicare programs are complex and subject to interpretation. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action. Self-pay revenue is recorded at published charges with charity care deducted to arrive at gross self-pay revenue.

##### **Grants and contracts:**

Grants and contracts revenue from government grants and contracts designated for use in specific activities is recognized in the period when expenditures have been incurred in compliance with the grantor's requirements. Grants and contracts awarded for the acquisition of long-lived assets are reported as unrestricted nonoperating income, in the absence of donor stipulations to the contrary, during the fiscal year in which the assets are acquired. Cash received in excess of revenue recognized is recorded as refundable advances. These grants and contracts require the Center to provide certain healthcare services during specified periods. If such services are not provided during the periods, the governmental entities are not obligated to expend the funds allocated under the grants and contracts.

##### **Contributions:**

Contributions are recorded as either temporarily or permanently restricted revenue if they are received with donor stipulations that limit the use of the donated asset. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and are reported in the statements of activities and changes in net assets as net assets released from restrictions.

## **Community Health Services, Inc.**

### **Notes to Financial Statements**

Donor restricted contributions whose restrictions expire during the same fiscal year are recognized as unrestricted revenue. Conditional contributions are recognized in the period when expenditures have been incurred in compliance with the grantor's restrictions.

#### **In-kind contributions:**

Donated goods and services are recorded at fair value at the time of the donation. In-kind contributions consist primarily of medical supplies. The fair value of those goods as provided by a funding source is \$335,823 and \$308,623 for the years ended December 31, 2012 and 2011, respectively, and is recorded as government grants, along with a corresponding charge to donated supplies in the accompanying statements of functional expenses.

#### **Charity care:**

The Center's charity care policy is to provide care to all patients regardless of their ability to pay or lack of available third party reimbursement. Charity care services are computed using a sliding fee scale based on patient income and family size. The amount of patient service revenue foregone under the Center's charity care policy totaled \$2,332,503 and \$2,588,990 for the years ended December 31, 2012 and 2011, respectively. The cost of providing this charity care was \$2,271,774 and \$1,789,909 for the years ended December 31, 2012 and 2011, respectively.

#### **Meaningful use incentives:**

The American Recovery and Reinvestment Act of 2009 ("ARRA") amended the Social Security Act to establish one-time incentive payments under the Medicare and Medicaid programs for certain professionals that: (1) meaningful use certified Electronic Health Records ("EHR") technology, (2) use the certified EHR technology for electronic exchange of health information to improve quality of health care and (3) use the certified EHR technology to submit clinical and quality measures. These provisions of ARRA, together with certain of its other provisions, are referred to as the Health Information Technology for Clinical and Economic Health Act. The criteria for meaningful use incentives will be staged in three steps over the course of the next seven years and be paid out based on a transitional schedule. The Center's providers have met the criteria and have earned \$382,500 from the Medicaid incentive program during the year ended December 31, 2012.

#### **Functional expenses:**

Expenses are charged to program services or management and general based on a combination of specific identification and allocation based on management estimates.

#### **Income taxes:**

The Center is incorporated as a not-for-profit entity and is exempt from Federal income tax under the provisions of the Internal Revenue Code Section 501(c)(3).

The Center has no unrecognized tax benefits at December 31, 2012 and 2011. The Center's Federal and state information returns prior to calendar year 2009 are closed and management continually evaluates expiring statutes of limitations, audits, proposed settlements, changes in tax law and new authoritative rulings.

## Community Health Services, Inc.

### Notes to Financial Statements

If the Center had unrelated business income taxes, it will recognize interest and penalties associated with uncertain tax positions as part of the income tax provision and include accrued interest and penalties with the related tax liability in the statements of financial position.

#### Use of estimates:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

#### Reclassifications:

Certain amounts in the 2011 financial statements have been reclassified to conform to the 2012 presentation. Net assets and changes in net assets are unchanged due to these reclassifications.

#### Subsequent events:

The Center has evaluated events and transactions for potential recognition or disclosure through May 28, 2013, which is the date the financial statements were available to be issued.

#### Note 2 - Concentrations:

##### Concentrations of credit risk:

The Center's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents, patient service revenue and receivables and grants and contracts revenue and receivables.

##### Cash and cash equivalents:

The Center maintains cash in bank accounts which at times, may exceed Federally insured limits. The Center has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash and cash equivalents. As of December 31, 2012, the Center had approximately \$530,000 of cash and cash equivalents in excess of Federally insured limits.

##### Patient service revenue and receivables, net:

The Center grants credit without collateral to its patients, most of whom are local residents. The mix of receivables from patients and third-party payors as of December 31, 2012 and 2011 is as follows:

	2012	2011
Medicaid	\$ 453,866	\$ 652,240
Medicare	96,757	213,530
Third-party payors	162,802	218,186
Patients	218,871	816,895
	932,296	1,900,851
Less allowance for doubtful accounts	(250,599)	(819,314)
	<u>\$ 681,697</u>	<u>\$ 1,081,537</u>

## Community Health Services, Inc.

### Notes to Financial Statements

Patient service receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of patient service receivable, the Center analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, the Center analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Center records a provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates provided by the Center's policy) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

The Center's allowance for doubtful accounts for self-pay patients was 99% and 96% of self-pay patient service receivable at December 31, 2012 and 2011, respectively. The Center has not changed its charity care or uninsured discount policies during 2012 and 2011.

The Center recognizes patient service revenue associated with services provided to patients who have Medicaid, Medicare, third-party payor and Managed Care plans coverage on the basis of contractual rates for services rendered. For uninsured self-pay patients that do not qualify for charity care, the Center recognizes revenue on the basis of its standard rates for services provided or on the basis of discounted rates provided by the Center's policy. On the basis of historical experience, a significant portion of the Center's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Center records a provision for bad debts related to uninsured patients in the period the services are provided.

## Community Health Services, Inc.

### Notes to Financial Statements

Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the period from these major payor sources, is as follows:

	2012	2011
Medicaid	\$ 8,379,824	\$ 9,874,943
Medicare	368,732	393,391
Third-party payors	653,092	499,394
Patients	494,118	475,507
	9,895,766	11,243,235
Less provisions for bad debts	221,988	1,221,494
	\$ 9,673,778	\$ 10,021,741

Medicaid and Medicare revenue is reimbursed to the Center at the net reimbursement rates as determined by each program. Reimbursement rates are subject to revisions under the provisions of reimbursement regulations. Adjustments for such revisions are recognized in the fiscal year incurred.

#### **Grants and contracts revenue and receivables:**

Grants and contracts receivable are evidenced by contracts with a variety of Federal and state government agencies and, based on historical experience, management believes these receivables represent negligible credit risk. Accordingly, management has not established an allowance for doubtful accounts.

Grants and contracts receivable at December 31, 2012 and 2011 are as follows:

	2012	2011
Federal	\$ 227,026	\$ 643,487
State	467,266	96,812
Other	27,141	31,957
	\$ 721,433	\$ 772,256

The Center receives a significant amount of grants and contracts from DHHS. As with all government funding, these grants and contracts are subject to reduction or termination in future years. For the years ended December 31, 2012 and 2011, grants and contracts from DHHS (including both direct awards and awards passed through other organizations) consisted of 81% and 86% of the total government grants revenue, respectively.

#### **Note 3 - Property and equipment:**

	2012	2011
Land	\$ 133,022	\$ 133,022
Building and improvements	18,313,036	13,001,617
Medical furniture and equipment	1,266,206	1,750,969
Office furniture and equipment	2,290,537	890,333
	22,002,801	15,775,941
Less accumulated depreciation and amortization	(6,784,743)	(5,996,961)
	15,218,058	9,778,980
Construction in progress	595,766	5,534,329
	\$ 15,813,824	\$ 15,313,309

## Community Health Services, Inc.

### Notes to Financial Statements

In connection with various State of Connecticut grants received for building renovations, forgivable liens have been placed on the real property of the Center. These liens are forgiven at a rate of 10% per year, and will be completely forgiven by 2022. If the Center were to not fulfill the requirements of these grants, a liability for the remaining balance of the liens would be incurred.

Depreciation expense was \$787,782 and \$738,262 for the years ended December 31, 2012 and 2011, respectively. No depreciation has been provided on assets classified as construction in progress as these assets have not yet been placed in service.

#### Note 4 - Operating leases:

The Center leases certain medical and office equipment under operating lease arrangements. During 2012, the Center entered into two new leases for a temporary site in Bloomfield, Connecticut and a permanent new facility in Windsor, Connecticut. The lease in Bloomfield, Connecticut is for 6 months and expires on March 2013 with payments of \$2,296 per month. The lease in Windsor, Connecticut is for 5 years at a rate of \$5,067 per month through August 2017.

Future minimum lease payments relating to all operating leases as of December 31, 2012 are as follows:

<u>Year Ending December 31,</u>	
2013	\$ 112,406
2014	105,519
2015	101,337
2016	60,800
2017	40,533
	<u>\$ 420,595</u>

Total rent expense for these operating leases was \$70,724 and \$36,594 for the years ended December 31, 2012 and 2011, respectively.

#### Note 5 - Rental income:

The Center leases portions of its facility to unrelated third-parties with leases that expire at various dates through November 2015. Rental income for the years ended December 31, 2012 and 2011 was \$48,163 and \$66,656, respectively.

Future minimum lease payments as of December 31, 2012 are as follows:

<u>Year Ending December 31,</u>	
2013	\$ 44,100
2014	44,100
2015	31,050
	<u>\$ 119,250</u>

## Community Health Services, Inc.

### Notes to Financial Statements

#### Note 6 - Note payable:

The Center has a term note payable with a bank, with an interest rate of 5%. Payments of equal monthly installments, consisting of principal and interest, are made until December 22, 2019. The note is secured with a lien on the real property owned by the Center.

Maturities of the note payable are as follows:

<u>Year Ending December 31,</u>	
2013	\$ 73,337
2014	77,089
2015	81,033
2016	85,179
2017	89,537
Thereafter	193,585
	<u>\$ 599,760</u>

#### Note 7 - Lines of credit:

As of December 31, 2012, the Center has a line of credit with a bank for \$500,000 that expires on August 31, 2013, with an interest rate per year equal to the bank's prime rate plus one percentage point. During 2012, the Center initiated a line of credit for a construction loan with a bank for \$500,000 that expires on June 30, 2013, with an interest rate equal to the bank's prime rate plus one percentage point. Both lines of credit had a balance of \$0 at December 31, 2012 and 2011. Pursuant to the terms of the lines of credit, the Center is required to comply with, among other things, certain financial covenants including the debt service coverage ratio.

#### Note 8 - Capital lease:

The capital lease is collateralized by the underlying leased asset. The interest rate on the lease is 8.9% and payments are due monthly. The lease was paid in full during 2012.

#### Note 9 - Employee benefit plan:

The Center maintains a 401(k) defined contribution plan for the employees. This plan allows the Center to make matching employer contributions. The employer contributions made during the years ended December 31, 2012 and 2011 were \$105,610 and \$137,898, respectively.

The Center has 403(b) benefit plans. These plans do not allow the Center to make matching employer contributions.

**Community Health Services, Inc.**

**Notes to Financial Statements**

**Note 10 - Net asset restrictions and designations:**

Temporarily restricted net assets are available for the following purposes as of December 31, 2012 and 2011:

	2012	2011
Dental mission	\$ -	\$ 44,668
Use for uninsured	5,000	-
Diabetic care	2,437	5,000
Total temporarily restricted net assets	<u>\$ 7,473</u>	<u>\$ 49,668</u>

**Note 11 - DHHS Grants:**

For the year ended December 31, 2012, the Center directly received the following grants from DHHS:

<u>Grant Number</u>	<u>Grant Period</u>	<u>Total Grant</u>	<u>Revenue Recognized</u>
C80CS16976	12/9/09 - 8/31/12	\$ 6,160,675	\$ 501,679
H8OCS00612	2/1/11 - 1/31/13	8,113,173	3,109,867
H76HAO8064	7/1/10 - 6/30/12	1,155,375	359,327
Total DHHS Grants			<u>3,970,873</u>
Less grant funds used for capital expenditures			501,679
Total DHHS funds used for operations			<u>\$ 3,469,194</u>

For the year ended December 31, 2011, the Center received the following grants from DHHS:

<u>Grant Number</u>	<u>Grant Period</u>	<u>Total Grant</u>	<u>Revenue Recognized</u>
C80CS16976	12/9/09 - 8/31/12	\$ 6,160,675	\$ 4,447,696
H8BCS11571	3/27/09 - 3/26/11	268,774	12,161
H8OCS00612	2/1/10 - 1/31/12	4,983,965	2,384,427
H76HAO8064	7/1/10 - 6/30/12	770,250	419,297
Total DHHS Grants			<u>7,263,581</u>
Less grant funds used for capital expenditures			(4,447,696)
Total DHHS funds used for operations			<u>\$ 2,815,885</u>

The DHHS funds are included in government grants on the statements of activities and changes in net assets.

**Note 12 - Commitments and contingencies:**

The Center has contracted with various funding agencies to perform certain healthcare services, and receives Medicaid and Medicare revenue from Federal, state and local governments. Reimbursements received under these contracts and payments from Medicaid and Medicare are subject to audit by Federal, state and local governments and other agencies. Upon audit, if discrepancies are discovered, the Center could be held responsible for refunding the amounts in question.

## **Community Health Services, Inc.**

### **Notes to Financial Statements**

The healthcare industry is subject to voluminous and complex laws and regulations of Federal, state and local governments. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement laws and regulations, anti-kickback and anti-referral laws and false claims prohibitions.

In recent years, government activity has increased with respect to investigations and allegations concerning possible violations of reimbursement, false claims, anti-kickback and anti-referral statutes and regulation by healthcare providers. The Center believes that it is in material compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. Upon audit, if discrepancies are discovered, the Center could be held responsible for refunding the amounts in question.

The Center maintains its medical malpractice coverage under the Federal Tort Claims Act (the "FTCA"). The FTCA provides malpractice coverage to eligible Public Health Service supported programs and applies to the Center and its employees while providing services within the scope of employment included under grant-related activities. The Attorney General, through the U.S. Department of Justice, has the responsibility for the defense of the individual and/or grantee for malpractice cases approved for FTCA coverage. The Center maintains gap insurance for claims that are not covered by the FTCA. The gap insurance is on a claims-made basis and the coverage limits are \$1,000,000 per occurrence and in the aggregate.

The Center is involved in various claims and legal actions arising in the ordinary course of business. Management is of the opinion that the ultimate outcome of these matters would not have a material adverse impact on the financial position, results of operations or cash flows of the Center.

#### **Note 13 - Pharmacy:**

The Center has a service agreement with Arrow Pharmacy to operate a pharmacy on site. The original agreement expired in April 2009 but is extended on a month to month basis. Arrow Pharmacy bills and collects for prescriptions, pays all pharmacy expenses and remits income to the Center. The Center records pharmacy income as part of patient service revenue. Income from pharmacy operations was \$656,886 and \$610,766 for the years ended December 31, 2012 and 2011, respectively. As of December 31, 2012 and 2011, the Center has \$169,926 and \$248,020 of receivables relating to the pharmacy program, respectively.