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MEDSTAR HEALTH RESEARCH INSTITUTE

Financial Statements and Supplementary Schedule
of Expenditures of Federal Awards and Reports
under OMB Circular A-133

June 30, 2012 and 2011

(With Independent Auditors' Report Thereon)

MEDSTAR HEALTH RESEARCH INSTITUTE

Table of Contents

	Page(s)
Independent Auditors' Report	1 – 2
Financial Statements:	
Balance Sheets	3
Statements of Activities and Changes in Net Assets	4
Statements of Cash Flows	5
Notes to Financial Statements	6 – 15
Schedule of Expenditures of Federal Awards	15 – 18
Notes to Schedule of Expenditures of Federal Awards	19
Independent Auditors' 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*	20 – 21
Independent Auditors' 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	22 – 23
Schedule of Findings and Questioned Costs	24 – 28

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Baltimore, MD 21202-1128

Independent Auditors' Report

The Board of Directors
MedStar Health Research Institute:

We have audited the accompanying balance sheets of MedStar Health Research Institute (the Institute), a wholly owned subsidiary of MedStar Health, Inc. (MedStar), as of June 30, 2012 and 2011 and the related statements of activities and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Institute's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Institute's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of MedStar Health Research Institute as of June 30, 2012 and 2011, and the results of its activities and changes in net assets, and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 6, 2013, on our consideration of the Institute'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 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 2012 audit.

Our audit was performed for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by 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

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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.

KPMG LLP

March 6, 2013

MEDSTAR HEALTH RESEARCH INSTITUTE

Balance Sheets

June 30, 2012 and 2011

Assets		**2012**	**2011**
Current assets:			
Cash and cash equivalents	$	20,829	21,749
Grants receivable, net of allowance for uncollectible accounts of $2,099,222 and $3,523,636 in 2012 and 2011, respectively		9,296,758	7,041,585
Prepaid expenses and other assets		16,901	9,306
Total current assets		9,334,488	7,072,640
Assets limited as to use or restricted		4,083,740	4,140,319
Property and equipment:			
Building and building improvements		3,324,499	3,387,135
Equipment and leasehold improvements		6,065,168	6,212,242
		9,389,667	9,599,377
Less accumulated depreciation and amortization		(7,933,384)	(8,011,572)
Property and equipment, net		1,456,283	1,587,805
Other assets		66,165	66,165
Total assets	$	14,940,676	12,866,929
Liabilities and Net Assets			
Current liabilities:			
Accounts payable and accrued expenses	$	1,088,848	1,705,034
Accrued salaries and benefits payable		1,980,262	2,019,357
Deferred grant revenue and other current liabilities		1,414,015	755,072
Total current liabilities		4,483,125	4,479,463
Other long-term liabilities		171,242	127,086
Due to affiliates		—	940,902
Total liabilities		4,654,367	5,547,451
Net assets:			
Unrestricted		8,776,377	5,311,755
Temporarily restricted		1,235,919	1,741,866
Permanently restricted		274,013	265,857
Total net assets		10,286,309	7,319,478
Total liabilities and net assets	$	14,940,676	12,866,929

See accompanying notes to financial statements.

MEDSTAR HEALTH RESEARCH INSTITUTE

Statements of Activities and Changes in Net Assets

Years ended June 30, 2012 and 2011

	2012	2011
Changes in unrestricted net assets:		
Revenues and gains:		
Grant and contract revenue	$ 27,866,418	29,451,540
Net (losses) gains on investments and investment income	(62,928)	395,386
Contributions from parent, net	5,571,644	38,110
Net assets released from restrictions and other revenue	964,589	179,298
Total revenues and gains	34,339,723	30,064,334
Program expenses:		
Personnel	19,058,360	17,634,087
Purchased services	2,601,182	4,297,164
Supplies	1,558,912	1,577,286
Facilities	233,404	513,022
Risk management	7,935	9,952
Depreciation	—	1,835
Applied overhead and other	6,380,575	5,713,268
Total program expenses	29,840,368	29,746,614
General and administrative expenses:		
Unapplied overhead	1,034,733	2,704,894
Increase (decrease) in unrestricted net assets	3,464,622	(2,387,174)
Change in temporarily restricted net assets:		
Restricted gifts	389,836	440,000
Net assets released from restrictions	(851,380)	(146,234)
Net (losses) gains on investments and investment income	(44,403)	161,088
(Decrease) increase in temporarily restricted net assets	(505,947)	454,854
Change in permanently restricted net assets:		
Restricted gifts	14,225	19,325
Net (losses) gains on investments and investment income	(6,069)	30,632
Increase in permanently restricted net assets	8,156	49,957
Increase (decrease) in net assets	2,966,831	(1,882,363)
Net assets at beginning of year	7,319,478	9,201,841
Net assets at end of year	$ 10,286,309	7,319,478

See accompanying notes to financial statements.

MEDSTAR HEALTH RESEARCH INSTITUTE

Statements of Cash Flows

Years ended June 30, 2012 and 2011

		2012	2011
Cash flows from operating activities:			
Increase (decrease) in net assets	$	2,966,831	(1,882,363)
Adjustments to reconcile increase (decrease) in net assets to net cash and cash equivalents (used in) provided by operating activities:			
Depreciation expense		367,091	431,780
(Gain) loss on sale of equipment		(689)	378
Provision for uncollectible accounts		(992,143)	(311,001)
Unrealized (gains) losses on investments		146,612	(439,670)
Realized (gains) losses on investments		26,768	(84,046)
Restricted gifts		(404,061)	(459,325)
Contributions from parent, net		(5,571,644)	(38,110)
Changes in operating assets and liabilities:			
Grants receivable		(1,263,030)	2,920,461
Prepaid expenses and other assets		(7,595)	6,376
Accounts payable and accrued expenses		(616,186)	557,845
Accrued salaries and benefits payable		(39,095)	(1,219)
Deferred grant revenue and other liabilities		703,099	(602,030)
Amounts due from third party payors and other		—	2,480
Net cash (used in) provided by operating activities		(4,684,042)	101,556
Cash flows from investing activities:			
Net purchases of marketable securities		(116,801)	(349,893)
Purchases of property and equipment, net		(234,880)	(247,653)
Net cash used in investing activities		(351,681)	(597,546)
Cash flows from financing activities:			
Contributions from parent, net		4,630,742	38,110
Restricted gifts		404,061	459,325
Net cash provided by financing activities		5,034,803	497,435
Net (decrease) increase in cash and cash equivalents		(920)	1,445
Cash and cash equivalents, beginning of year		21,749	20,304
Cash and cash equivalents, end of year	$	20,829	21,749

See accompanying notes to financial statements.

(1) Description of Organization and Summary of Significant Accounting Policies

(a) Organization

The MedStar Health Research Institute (the Institute or MHRI) is organized for the purpose of conducting scientific research in all fields of medicine, surgery, pharmaceutics, health care delivery and all other sciences related to the healing and the curing of human ills. The Institute is a controlled entity of MedStar Health, Inc. (MedStar or the Corporation), a not-for-profit corporation.

MedStar is a tax-exempt, Maryland membership corporation which, through its controlled entities and other affiliates, provides and manages healthcare services in the region encompassing Maryland, Washington D.C. and Northern Virginia. MedStar became operational on June 30, 1998 by the transfer of the membership interests of Helix Health, Inc. (Helix – a not-for-profit Maryland Corporation) and Medlantic Healthcare Group, Inc. (Medlantic – a not-for-profit Delaware Corporation) in exchange for the guarantee of the debt of both Helix and Medlantic by the Corporation. The trade names of the principal tax-exempt and taxable entities of MedStar are:

Tax-Exempt

- Bay Development Corporation
- Church Home and Hospital of the City of Baltimore, Inc.
- MedStar Franklin Square Medical Center
- MedStar Harbor Hospital
- HH MedStar Health, Inc.
- MedStar Georgetown University Hospital
- MedStar Health Research Institute
- MedStar Health Visiting Nurse Association
- MedStar Surgery Center, Inc.
- MedStar Montgomery Medical Center
- MedStar National Rehabilitation Network
- MedStar Good Samaritan Hospital
- MedStar Union Memorial Hospital
- MedStar St. Mary's Hospital
- MedStar Washington Hospital Center

Taxable

- Greenspring Financial Insurance, LTD.
- MedStar Enterprises, Inc. and Subsidiaries
- MedStar Physician Partners, Inc.
- Parkway Ventures, Inc. and Subsidiaries

(Continued)

(b) ***Basis of Presentation***

The financial statements of the Institute are prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles.

Programs for the purpose of scientific research as described in note 1(a) are combined into one program for purposes of reporting on the statement of activities and changes in net assets.

The financial statements reflect the accounts of the Institute, including an allocation of general and administrative expenses from MedStar for financial, legal, accounting, human resources and information technology services. Such allocations, calculated on a percentage of revenue, are based on determinations that management believes to be reasonable. Accordingly, expense allocations to the Institute may not be representative of the costs of such services if the Institute were not affiliated with MedStar.

(c) ***Use of Estimates***

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(d) ***Cash and Cash Equivalents***

All highly liquid investments with a maturity date of three months or less when purchased are considered to be cash equivalents.

(e) ***Grants***

The Institute has been awarded various cost-reimbursable grants by the federal government and private sources. The Institute has also been awarded various grants from pharmaceutical and device companies, the funding of which is on a per-unit basis. Grant and contract revenue is recognized during the period the related expenses are incurred for cost-reimbursable awards. Fee-based award revenues are recognized when specified milestones are achieved.

The Institute is reimbursed for a portion of its general and administrative expenses as an overhead component of the awarded grants. Total general and administrative expenses were $7,026,030 and $8,369,183 for the years ended June 30, 2012 and 2011, respectively. The Institute allocated $5,991,297 and $5,664,289 for the years ended June 30, 2012 and 2011, respectively, to applied overhead based on the amounts that are reimbursable under the grant agreements. The remaining overhead of $1,034,733 and $2,704,894 for the years ended June 30, 2012 and 2011, respectively, is included in unapplied overhead in the statement of activities and changes in net assets.

Bad debt expense is included in unapplied overhead as a component of general and administration expenses in the statement of activities and changes in net assets. Amounts recorded for bad debt expense are credits of $(992,143) and $(311,001) for the years ended June 30, 2012 and 2011, respectively, primarily due to improved collections in 2012 and 2011.

(Continued)

Amounts received in excess of incurred expenses are recorded as deferred grant revenue. Expenses incurred in excess of amounts received are recorded as grants receivable, to the extent allowed under the grants. The carrying value of grants receivable approximates their fair value.

(f) Assets Limited as to Use or Restricted

The Institute participates in an investment pool with other MedStar affiliates.

MedStar's investment portfolio is considered trading and is classified as current or noncurrent assets based on management's intention as to use. All debt and equity securities are reported at fair value principally based on quoted market prices on MedStar's consolidated balance sheets.

MedStar has investments, which under U.S. generally accepted accounting principles are considered alternative investments, including commingled equity funds, inflation hedging equity, commodity and fixed income funds, hedge fund of funds, and private equity funds. These funds utilize various types of debt and equity securities and derivative instruments in their investment strategies. Alternative investments are recorded under the equity method.

The Institute's board of directors has designated funds for purposes of future program development and other future obligations. The principal of the related investments will not be utilized without a two-thirds vote of the board of directors.

Investment income (interest and dividends) including realized gains and losses on investment sales are included in unrestricted net assets in the accompanying statement of activities and changes in net assets unless the income or loss is restricted by the donor or law. Investment income and net gains (losses) that are restricted by the donor are recorded as a component of changes in temporarily or permanently restricted net assets, in accordance with donor imposed restrictions. Realized gains and losses are determined based on the specific security's original purchase price or adjusted cost if the investment was previously determined to be other-than-temporarily impaired. Unrealized gains and losses are included in the Institute's changes in net assets.

(g) Property and Equipment

Property and equipment acquisitions are recorded at cost and are depreciated or amortized over the estimated useful lives of the assets. Estimated useful lives range from three to forty years. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. In 2012 and 2011, no interest was capitalized. Depreciation expense is computed on a straight-line basis. The Institute recognized depreciation expense of $367,091 and $431,780 for fiscal years 2012 and 2011, respectively. Major classes and estimated useful lives of property and equipment are as follows:

Leasehold improvements	Lease term
Buildings and improvements	10 – 40 years
Equipment	3 – 20 years

(h) ***Contributions***

Unconditional promises to give cash and other assets to the Institute are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. 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 reported in the statement of activities and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying financial statements.

(i) ***Income Taxes***

The principal operations of the Institute are exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and the applicable income tax regulations of the District of Columbia. The Institute accounts for uncertain tax positions in accordance with the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 740, *Income Taxes*.

(j) ***Temporarily and Permanently Restricted Net Assets***

Temporarily restricted net assets are those whose use by the Institute has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Institute in perpetuity.

(k) ***Fair Value of Financial Instruments***

The following methods and assumptions were used to estimate the fair value of financial instruments:

Cash and cash equivalents, receivables, other current assets, other assets, current liabilities and long-term liabilities: The carrying amount reported in the balance sheets for each of these assets and liabilities approximates their fair value.

The fair value of investments, assets limited as to use or restricted is discussed in note 4.

(l) ***Reclassifications***

Certain prior year amounts have been reclassified to conform with current period presentation, the effect of which is not material.

(2) Related-Party Transactions

The Institute's board of directors is comprised of members of the community, physicians, and certain members of the board of trustees of MedStar and its subsidiaries.

The Institute provides and receives various management and support services from MedStar and its subsidiaries. Charges for services received in 2012 and 2011 are $1,691,073 and $1,826,340, respectively.

MedStar has committed to fund the continued operations of the Institute to July 1, 2013 by funding operating cash deficits and capital expenditures. The amount of cash contributions from MedStar during the years ended June 30, 2012 and 2011 were $4,630,742 and $38,110, respectively. These amounts correspond to cash needs for the Institute during the years ended June 30, 2012 and 2011, respectively.

(3) Assets Limited as to Use or Restricted

The Institute pools its portfolio of marketable securities with other MedStar marketable securities to centralize investment management and custody. The Institute's interest in the pooled investment funds and related investment income is accounted for on a percentage basis. Investment income earned from the Institute's ownership of interests in the pooled investment funds reflects its proportionate share of the interest, dividends, realized gains and losses and unrealized appreciation and depreciation of the securities held in the pool. The Institute's proportionate share of the pool's investment income from the underlying securities is reported as such in the Institute's statement of activities and changes in net assets.

MedStar's investments and assets whose use is limited or restricted, in the MedStar Corporate Investment Pool, as of June 30, 2012 and 2011, at fair value or under the equity method of accounting in the case of alternative investments, consists of the following (in millions):

		2012	2011
Collateralized guaranteed investment contract and cash	$	33.9	38.6
Fixed income securities and funds		220.5	202.7
Equity securities		347.7	351.2
Alternative investments:			
Commingled equity funds		59.6	86.5
Inflation hedging, commodity, fixed income fund		56.9	64.9
Hedge fund of funds and private equity		120.8	91.9
Total investments and assets whose use is limited or restricted	$	839.4	835.8

The Institute has $4,083,740 and $4,140,319 of investable assets included in the MedStar Corporate Investment Pool above representing approximately 0.5% of the total shares at June 30, 2012 and 2011. The Institute's assets limited as to use or restricted as of June 30, 2012 and 2011, at fair value, identified by restriction is as follows:

		2012	2011
Board/management designated assets	$	2,409,276	2,033,067
Self-insurance trust funds		164,532	99,529
Temporarily and permanently restricted programs/research funds		1,509,932	2,007,723
	$	4,083,740	4,140,319

Investment income and (losses) gains, for unrestricted, temporarily and permanently restricted, for assets limited as to use are comprised of the following for the years ended June 30, 2012 and 2011:

		2012	2011
Changes in unrestricted net assets:			
Investment income	$	59,980	63,390
Net realized (losses) gains on sale of investments		(33,505)	37,038
Unrealized (losses) gains on trading investments		(89,403)	294,958
		(62,928)	395,386
Other changes in net assets:			
Realized net gains on temporarily and permanently restricted net assets		6,737	47,008
Changes in unrealized (losses) gains on temporarily and permanently restricted net assets		(57,209)	144,712
Total investment return	$	(113,400)	587,106

(4) Fair Value of Financial Instruments

MedStar follows ASC Topic 820, *Fair Value Measurement* which provides for the following:

- Defines fair value 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, and establishes a framework for measuring fair value;
- Establishes a three-level hierarchy for fair value measurement;
- Requires consideration of MedStar's nonperformance risk when valuing liabilities; and
- Expands disclosures about instruments measured at fair value.

The three-level valuation hierarchy for fair value measurements is based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect MedStar's market assumptions. The three-level valuation hierarchy is defined as follows:

- Level 1 – Quoted prices for identical instruments in active markets;
- Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar investments in markets that are not active; and model-derived valuations whose significant inputs are observable; and
- Level 3 – Instruments whose significant inputs are unobservable.

MedStar has incorporated an Investments Policy Statement (IPS) into the investment program. The IPS, which has been formally adopted by MedStar's Board of Directors, contains numerous standards designed to ensure adequate diversification by asset class and geography. The IPS also limits all investments by manager and position size, and limits fixed income position size based on credit ratings, which serves to further mitigate the risks associated with the investment program. At June 30, 2012 and 2011, management believes that all investments were being managed in a manner consistent with the IPS.

The table below presents the MedStar Corporate Investment Pool investable assets as of June 30, 2012, aggregated by the three-level valuation hierarchy (in millions):

		Level 1	Level 2	Level 3	Total
Assets:					
Cash and cash equivalents	$	33.6	—	—	33.6
U.S. treasury bonds		34.5	—	—	34.5
U.S. agency mortgage backed securities		45.1	—	—	45.1
Corporate bonds		—	59.2	—	59.2
Fixed income mutual fund		0.6	54.4	—	55.0
All other fixed income securities		2.6	24.1	—	26.7
Equity mutual funds and ETF's		67.7	—	—	67.7
Common stocks		279.9	—	—	279.9
Total assets	$	464.0	137.7	—	601.7

The Institute's investable assets approximate MedStar's allocation in the above three level valuation hierarchy.

The table below presents the MedStar Corporate Investment Pool investable assets as of June 30, 2011, aggregated by the three-level valuation hierarchy (in millions):

		Level 1	Level 2	Level 3	Total
Assets:					
Cash and cash equivalents	$	38.6	—	—	38.6
U.S. treasury bonds		34.4	—	—	34.4
U.S. agency mortgage backed securities		41.7	—	—	41.7
Corporate bonds		—	52.9	—	52.9
Fixed income mutual fund		0.4	46.3	—	46.7
All other fixed income securities		—	27.0	—	27.0
Equity mutual funds and ETF's		105.9	—	—	105.9
Common stocks		245.3	—	—	245.3
Total assets	$	466.3	126.2	—	592.5

The Institute's investable assets approximate MedStar's allocation in the above three level valuation hierarchy. For the years ended June 30, 2012 and 2011, there were no significant transfers into or out of Levels 1, 2 or 3.

(5) Retirement Plans

The Institute participates in the MedStar Health, Inc. Cash Balance Retirement Plan (the Plan), a contributory defined benefit pension plan administered by MedStar, which covers substantially all employees of the Institute who have completed all service and age vesting requirements.

Benefits under the plan are substantially based on years of service and the employees' career earnings. The Institute contributes to the plan based on actuarially determined amounts necessary to provide assets sufficient to meet benefits to be paid to plan participants and to meet the minimum funding requirements of the Employee Retirement Income Security Act of 1974, as amended by the Pension Protection Act of 2006, and Internal Revenue Service regulations. Pension expense of $188,032 and $301,000 was allocated to the Institute by MedStar during the years ended June 30, 2012 and 2011, respectively. In 2012, the liability associated with the Institute's participation in the Plan was transferred to the Corporation and removed from the Institute's liabilities at June 30, 2012. The transferred amount is included in contributions from parent, net for the year ended June 30, 2012. The Institute had an accrued liability for its participation in the Plan of $940,902 included on the balance sheet as of June 30, 2011. At June 30, 2012, the Plan's zone status was considered to be yellow as the Plan was funded between 65-80%. Additional disclosures are not included in this report, as separate information on pension assets and liabilities for the Institute's employees is not available.

(6) Leases

The Institute leases office space at a number of locations and several pieces of equipment under noncancelable operating leases expiring through 2020. Rent expense for office space and equipment for the years ended June 30, 2012 and 2011 was $1,186,667 and $1,282,022, respectively.

Future minimum lease payments existing as of June 30, 2012 are as follows:

2013	$	931,022
2014		922,713
2015		901,345
2016		923,393
2017		917,163
2018 and thereafter		2,861,437
Total future minimum lease payments	$	7,457,073

(7) Self-Insurance Programs

MedStar maintains self-insurance programs for professional and general liability risks, employee health and workers' compensation. Estimated liabilities have been recorded based on actuarial estimation of reported and incurred but not reported claims. MedStar indemnifies the Institute for all unrecorded self-insurance liabilities incurred but not reported claims.

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MedStar's self insurance program for professional and general liability is responsible for the following exposures at June 30, 2012:

(a) For professional liability, the first $5,000,000 exposure for each claim with an inner aggregate of $2,500,000 for the period July 1, 2010 through December 31, 2010. For the period January 1, 2011 through June 30, 2012, the Corporation is responsible for the first $5,000,000 exposure for each claim plus an inner aggregate (effective January 1, 2011, the inner aggregate was changed from a $2,500,000 annual inner aggregate to a $5,000,000 inner aggregate spread over a 24-month exposure period ending December 31, 2012; effective January 1, 2012 the inner aggregate was changed to a $5,000,000 inner aggregate with a $7,500,000 aggregate spread over a 36-month exposure period dated January 1, 2011).

(b) For general liability, MedStar is responsible for the first $3,000,000 exposure for each claim.

Commercial excess re-insurance has been purchased above this self-insured retention in multiple layers and in twin towers. Each tower has seven layers of excess re-insurance coverage. These seven layers combine to provide up to $100,000,000 per claim and $100,000,000 in the annual aggregate for professional liability and general liability exposure. MedStar maintains reinsurance contracts with various highly rated commercial insurance companies.

Contributions required to fund professional and general liability, employee health benefits and workers' compensation programs are determined by the plans' administrators based on appropriate actuarial assumptions. The professional and general liability programs are administered through an offshore wholly owned captive insurance company, Greenspring Financial Insurance Limited (GFIL), which is domiciled in Grand Cayman Island.

GFIL determines premiums for participating entities based on the individual entities' experiences and exposures. The Institute records premiums on an annual basis as allocated by GFIL. Premiums allocated to the Institute were $4,319 and $7,861 in fiscal years 2012 and 2011, respectively.

The Institute has an accrued liability for workers' compensation of $176,138 and $136,561 as of June 30, 2012 and 2011, respectively, which is included in deferred grant revenue and other current liabilities on the balance sheet. The workers' compensation liabilities at June 30, 2012 and 2011 have been discounted at a rate of 1.5% and 3.5%, respectively.

MedStar and the Institute, in the normal course of business, are parties to a number of legal and regulatory proceedings. Management does not expect that the results of these proceedings will have a material adverse effect on the financial position or results of operations of the Institute.

(8) Subsequent Events

Management evaluated all events and transactions after June 30, 2012 and through March 6, 2013. The Institute did not have any subsequent events that were required to be recognized or disclosed during this period.

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

MEDSTAR HEALTH RESEARCH INSTITUTE

Schedule of Expenditures of Federal Awards

Year ended June 30, 2012

Federal awarding agency/program title	Federal CFDA #		Federal expenditures
Research and development:			
DHHS:			
Ryan White Title III Program	93.918	$	473,602
TeleRehab Home	93.865		3,381
Glyburide Protocol	93.865		676
Community Child Health Network	93.865		23,701
Total 93.865			27,758
GMS/University of Pittsburgh PROCESS	93.859		32,907
GUH Post-Grad Residents	93.855		121,495
Transplant Multi Site FC	93.855		1,765
Organ Transplant in HIV	93.855		29,698
Total 93.855			152,958
NINDS	93.853		130,292
NINDS/University of South Carolina SAMMPRIS	93.853		5,368
NIH/GU/NRH Protect DC	93.853		66,292
NIH/University of Southern California ICARE	93.853		53,696
Geo U: SA/Biostat Sharma	93.853		2,898
Geo Univ: EMR Translation CTSA	93.853		119,870
GHU CCTS: MEDIC	93.853		12,510
Total 93.853			390,926
NIDDK/New England Research Institute VALUE	93.849		9,924
TINSAL T2D	93.847		4,174
Dietary Studies	93.847		591,918
Colonoscopy Forc	93.847		21,372
DPPOS Accelerometer Ancillary Study	93.847		6,952
Total 93.847			624,416
PEA in HIV + Patients	93.839		6,858
NHLBI/Yale: VIRGO	93.837		246
NIH/U Washington Cerebrovascular Disease	93.837		404,412
NIH/U Rochester: RAID	93.837		437
Gocadan Project	93.837		61,990
NHLBI Prenatal Stressed Mice	93.837		246,229
Strong Heart Study	93.837		372,423
Cardiovascular Outcomes in Renal Atherosclerotic Lesions	93.837		14,638
NHLBI/Ms. Sinai SOM-NYU SCCOR	93.837		3,414
Arsenic and CVD in SHS	93.837		166,493

(Continued)

MEDSTAR HEALTH RESEARCH INSTITUTE

Schedule of Expenditures of Federal Awards

Year ended June 30, 2012

Federal awarding agency/program title	Federal CFDA #		Federal expenditures
NHLBI University of Minnesota Stress and Platel	93.837	$	10,920
NCI/Blacks Hills BCAIH/CVD Management	93.837		39,729
Total 93.837			1,320,931
ARRA LACRC	93.701		49,275
ARRA NHLBI/Duke: PROMISE	93.701		264
ARRA NIH/GU/NRH Protect DC	93.701		24,086
ARRA NIA/NCMHD Today's Truth	93.701		193,724
ARRA NIH/U of AK Eskimo Collaborative	93.701		40,938
ARRA NIH/GMS/University of Pittsburgh PROCESS	93.701		20,873
ARRA NIH/GWU DC Cohort HIV	93.701		117,915
Total 93.701			447,075
NSABP: P5 Recruit Support	93.399		1,379
WHC Cancer Research – CALGB Services	93.395		19,018
University of Chicago – CALGB Services	93.395		1,943
NCI/Bringham: CALCB-GSH	93.395		2,541
NCI/Bringham: CALCB-UMH	93.395		2,599
NCI/Bringham CALGB Services	93.395		99,417
Total 93.395			125,518
NIH-NCCR/Georgetown University CTSA DBPS	93.389		291,926
NIH-NCCR/Georgetown University CTSA PCIR	93.389		186,939
NIH-NCCR/Georgetown University CTSA PCIR	93.389		33,933
NIH-NCCR/Georgetown University CTSA RETCD	93.389		127,697
NCRR/Geo U: Chemo-Induced Ovar	93.389		3,299
NCRR/Geo U: Polymorphism App	93.389		2,689
NCRR/Geo U: Stress Prem Aging	93.389		2,500
NCRR/Geo U: CTSA-Telehealth	93.389		26,370
NCRR/Howard: CTSA Life Coach	93.389		1,902
Total 93.389			677,255
U Cal/UMB: POINT	93.310		5,858
NIH/NIBIB HFE Image System	93.286		157,967
NIBIB/Cath U: Scar Invivo	93.286		79,586
Total 93.286			237,553
NIH/Geo U: Kaltman BioStat	93.281		2,396
Child Research Inst: 5908-08-02	93.242		255,987
NIH/Geo U: BioStat GU-Green	93.242		2,427
NIH/U.Penn: Diabetic Wound Ste	93.242		4,194
NIH: Guest Speaker Honorarium	93.242		232
Total 93.242			262,840

MEDSTAR HEALTH RESEARCH INSTITUTE

Schedule of Expenditures of Federal Awards

Year ended June 30, 2012

Federal awarding agency/program title	Federal CFDA #	Federal expenditures
AHRQ/NYU Improving Patient Safety	93.226	$ 62,230
AHRQ/CNA: HAI Action	93.226	219,805
Total 93.226		282,035
NCCAM/GEoUniv BB-12 Yogurt Study	93.213	11,826
Stroke Study	93.173	1,289,485
Genetic Counselor	93.172	78,591
NHGRI/Chapel Hill CALiCo	93.172	8,287
Total 93.172		86,878
Ryan White Title IV Program	93.153	54,137
CDC: Serum Repository/Fibromya	93.069	5,118
NIA	93.000	5,154,930
Check Issuance Services – FC	93.000	242,361
ALTA – Eden Omega	93.000	107
NCI/Black Hills CINCO Study	93.000	84,719
NHLBI/JHU SAILS	93.000	18,907
NHLBI/RTI GenTAC II Registry	93.000	247,397
NHLBI/UNY WHI Extension	93.000	294,466
FDA Swan-Ganz Balloon Flotati	93.000	11,690
NHRC/McConnell Force Cont	93.000	126,911
FDA Safety of Live Cases	93.000	26,082
FDA/RTI: Task Order #8	93.000	16,897
NEI/EMMES: Genetic Consultants	93.000	88,140
DHHS/CIA/Scitor: Iris Scan	93.000	13,088
Total 93.000		6,325,695
Total DHHS		12,855,328
U.S. Department of Education (ED):		
SCI Rehab	84.133	120,575
RRTC	84.133	788,102
Smart Over-Ground Gait	84.133	150,715
NCSCI Model System	84.133	69,543
Total USDE		1,128,935
U.S. Department of Defense (DOD):		
Army Coagulopathy Burn Patients	12.431	307,039
DoD: SBS SDS Mus Musculus	12.431	17,768
Total 12.431		324,807

(Continued)

MEDSTAR HEALTH RESEARCH INSTITUTE

Schedule of Expenditures of Federal Awards

Year ended June 30, 2012

Federal awarding agency/program title	Federal CFDA #		Federal expenditures
Assistive Technology and Research Center	12.420	$	433,651
DOD/Avita Medical Recell Trial	12.420		11,398
NRH – Assistive Tech and Research	12.420		12,542
Total 12.420			457,591
DOD/SED Tech: Shupp Consulting	12.000		6,147
DOD/Geneva Ramp-in PTSD	12.000		31,914
USAMRAA/ABA: Burn Patient Study	12.000		686
Total 12.00			38,747
Total DOD			821,145
U.S. Department of Agriculture:			
USDA: REQ AG-32SD-P-12-0029	10.000		4,222
USDA Nutrition Research Study	10.001		144,191
Total USDA			148,413
U.S. Department of Veterans Affairs:			
VA/Atlas Communication Strategies	64.013		933
VA Med Center: Lab Measures	64.013		25,065
VA Med Center: PACEART	64.013		20,730
VA Med: Lab Measures-Tsai	64.013		3,250
VA Medical Center MIME Extension	64.013		33,928
Total USDVA			83,906
Total research and development			15,037,727
Total federal expenditures		$	15,037,727

See accompanying notes to schedule of expenditures of federal awards.

MEDSTAR HEALTH RESEARCH INSTITUTE

Notes to Schedule of Expenditures of Federal Awards

Year ended June 30, 2012

(1) Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) includes federal grant activity of the MedStar Health Research Institute (the Institute or MHRI) and is presented on the accrual basis of accounting. 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*. Therefore, some amounts presented in the Schedule may differ from amounts presented in, or used in the preparation, of the basic financial statements.

(2) Indirect Costs

The Institute operates under predetermined fixed indirect cost rates. The indirect cost rate effective at the grant award date was effective throughout the grant period. The indirect rate for eligible nonpayroll costs during fiscal year 2012 for on-site programs ranged from 19% to 55% for most studies. The rate was 38% for all off-site programs. The indirect rate for fringe benefits during the year ended June 30, 2012 is 41% of payroll costs.

(3) Subrecipients

Of the federal expenditures presented in the Schedule, the Institute provided federal awards to subrecipients as follows:

Federal awarding agency/program title	Federal CFDA number	Amount provided to subrecipients
ED RRTC	84.133	$ 340,895
ED NCSCI Model System	84.133	32,175
Total 84.133		373,070
ARRA LACRC	93.701	49,274
NHLBI Prenatal Stressed Mice	93.837	44,381
		$ 466,725

KPMG

KPMG LLP
1 East Pratt Street
Baltimore, MD 21202-1128

Independent Auditors' 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*

The Board of Directors
MedStar Health Research Institute:

We have audited the financial statements of MedStar Health Research Institute (the Institute or MHRI) as of and for the year ended June 30, 2012, and have issued our report thereon dated March 6, 2013. 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 the Institute is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Institute'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 the Institute's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Institute's internal control over financial reporting.

A deficiency in internal control over financial reporting 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 combination of deficiencies, in internal control over financial reporting, 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.

Our consideration of internal control over financial reporting 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 financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified a deficiency in internal control over financial reporting that we consider to be a significant deficiency and that is described in the accompanying schedule of findings and responses as item 12-01. A significant deficiency is a deficiency, or combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Institute'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 determination of financial statement amounts. However, providing an opinion on compliance with those

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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*.

This report is intended solely for the information and use of the Institute's management, board of directors, others within the organization, 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.

KPMG LLP

March 6, 2013

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Independent Auditors' 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

The Board of Directors
MedStar Health Research Institute:

Compliance

We have audited MedStar Health Research Institute's (the Institute or MHRI) compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct or material effect on each of the Institute's major federal program for the year ended June 30, 2012. The Institute's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grant agreements applicable to its major federal program is the responsibility of the Institute's management. Our responsibility is to express an opinion on the Institute'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 the Institute'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 the Institute's compliance with those requirements.

In our opinion, the Institute complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2012. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as item 12-02.

Internal Control over Compliance

Management of the Institute 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 the Institute's internal control over compliance with requirements that could have a direct and material effect on a major federal program 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

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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 Institute'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. However, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies as described in the accompanying schedule of findings and questioned costs as items 12-01 and 12-02. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

The Institute's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit the Institute's responses, and accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of the Institute's management, board of directors, others within the organization, 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.

KPMG LLP

March 6, 2013

MEDSTAR HEALTH RESEARCH INSTITUTE

Schedule of Findings and Questioned Costs

Year ended June 30, 2012

Section I – Summary of Auditors' Results

Financial Statements

Type of auditors' report issued:	Unqualified
Internal control over financial reporting:	
• Material weaknesses	No
• Significant deficiencies	Yes
Noncompliance material to financial statements:	No

Federal Awards

Internal control over major programs:	
• Material weaknesses	No
• Significant deficiencies	Yes
Type of auditors' report issued on compliance for major programs:	Unqualified
Audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133:	Yes. Findings 12-01 and 12-02
Identification of major program:	
Research and Development Cluster	(See schedule of expenditures of federal awards for the CFDA numbers)
Dollar threshold used to distinguish between type A and type B programs	$451,224
Auditee qualified as low-risk auditee?	No

Section II – Findings Relating to the Financial Statements Reported in Accordance with *Government Auditing Standards*

Finding 12-01

Criteria

The COSO Internal Control Framework is designed to provide reasonable assurance regarding the achievement of objectives in the following categories: (1) Effectiveness and Efficiency of Operations, (2) Reliability of Financial Reporting, and (3) Compliance with Applicable Laws and Regulations. It also identifies the five components of internal control, which include Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring.

With regard to Control Activities and Monitoring, the COSO Internal Control Framework states that control activities are the policies and procedures that help ensure management directives are carried out and include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets, and segregation of duties. They help ensure that necessary actions are taken to address risks to achieve the entity's objectives and occur throughout the organization, at all levels and in all functions. These internal control systems need to be monitored—a process that assesses the quality of the system's performance over time and is accomplished through ongoing monitoring activities, separate evaluations, or a combination of the two.

Condition

During the course of the financial statement audit, we determined that the Institute had not properly accrued for three 2012 invoices related to capital assets at June 30, 2012. In addition, we noted in our compliance testwork over expenses included in the 2012 Schedule of Expenditure of Federal Awards (SEFA) that there were 5 invoices that related to the year ended June 30, 2011. However, we determined that such amounts were in compliance with the respective grant requirements.

Cause

MHRI did not maintain adequate internal control over its cutoff procedures to ensure that expenses were recognized in the proper period.

Effect

MHRI did not properly accrue certain invoices in its June 30, 2012 financial statements and included certain expenses related to the year ended June 30, 2011 in its Schedule of Expenditures of Federal Awards for the year ended June 30, 2012.

Recommendation

We recommend that management improve its process over its cutoff controls to ensure that the expenses related to both capital assets and operating expenses are recognized in the proper period.

Management Response

MedStar Health Research Institute (MHRI) is committed to accruing invoices in the proper period, in particular within the appropriate fiscal year. Annually, communications are sent to all manager-level staff providing guidance on the accrual process and requesting timely submission of invoices for any goods and/or services received in the current fiscal year. For the year ended June 30, 2012, the communication was issued on June 25, 2012. In order to mitigate similar findings in future periods, the Institute will 1) provide communications with greater advance notice, 2) include frequent reminders, 3) require written confirmation from recipients that they have read and understood their responsibilities, and 4) provide greater emphasis on the need to carefully consider potentially eligible but unbilled expenses and, if necessary, to contact vendors in a timely manner to obtain appropriate documentation to support an accrual.

Section III – Federal Award Findings and Questioned Costs

Finding 12-02 (Prior Year Finding No. 11-03)

Federal Agency

Research and Development Cluster

Program Title

Various

CFDA Number

Various

Area

Reporting

Criteria

OMB Circular A-110 requires that nonfederal entities receiving federal awards establish and maintain internal control designed to reasonably ensure compliance with federal laws, regulations, and program compliance. In addition, nonfederal entities must ensure proper internal controls are in place to maintain compliance with the frequency and timeliness of reporting to the cognizant agencies as specified in the grant agreements.

Condition

MHRI did not submit a report to the cognizant agency within the required time frame as specified by the grant agreement. MHRI is required to submit this report within 12 days after the reporting period. We identified that the NIA enrollment report (detail of women/minority participants) was not submitted timely as required by the grant agreement. The length of delinquency in reporting was 18 days.

Cause

MHRI did not maintain adequate internal control over reporting to ensure compliance with the requirements of OMB Circular A-110. Accordingly, MHRI failed to submit required enrollment reports within the time frame as specified by the grant agreement, hence, MHRI is not in compliance with the grant agreements' reporting requirements.

Effect

MHRI is not in compliance with OMB Circular A-110 and the applicable grant agreement that require nonfederal entities to submit reports to the cognizant agency within the time periods established by the grant agreements.

Questioned Costs

There are no questioned costs related to this finding.

Recommendation

We recommend that MHRI establish an appropriate level of monitoring as an internal control to ensure that reports are submitted to the cognizant agencies within the required periods as specified by the grant agreements.

Management's Response

Filing timely progress reports to the project officer of a grant is the primary responsibility of the principal investigator. Upcoming progress report due dates and timely submission are incorporated into the monthly review of federal grants conducted by the finance, administrative and research teams. The NIA enrollment report that was not submitted timely was the only NIA report due within 12 days, rather than the standard 30 day time frame. MHRI formally requested that the due date for the annual enrollment report be changed to 30 calendar days following the end of the reporting period. This change will align the due date for all deliverables under this contract to be 30 days following the end of the applicable reporting period. The Contract Officer approved the request via e-mail on February 28, 2013; the approval is expected to be reflected in the next contract modification estimated to be issued in April 2013.

MANAGEMENT'S RESPONSE TO THE 2011 SCHEDULE OF FINDINGS AND QUESTIONED COSTS

MEDSTAR HEALTH RESEARCH INSTITUTE

Summary of Prior Year Findings

Year ended June 30, 2012

Federal Award Findings and Questioned Costs

Finding 11-01 (Prior Year Finding No. 10-02)

Federal Agency

Research and Development Cluster

Program Title

Various

CFDA Number

Various

Area

Activities Allowed/Unallowed and Allowable Costs/Costs Principles

Condition

During our testing of compliance over the allowability of payroll costs, we selected a sample of 65 items (employee timesheets for a specific period), which totaled $190,176, out of a total population of expenditures of $4,526,227. Of these selected items, we determined that supporting payroll records for 2 sample items, which totaled $581, were not in agreement with the amounts charged to the grants.

Status

There was $581 of questioned costs related to this finding. Costs transfers were processed to move these costs to the appropriate cost centers. In addition, there was a situation where the submission of 39 hours by a non-exempt employee was considered to constitute a full week of work (40 hours). The extra hour was adjusted and reduced from the costs of the study.

To prevent this from recurring, the MHRI Human Resources department is working closely with the Office of Financial Management (OFM) and the Scientific Research Center staff to specifically identify the cost centers to be adjusted in those cases where a payment adjustment involves several federal grants. In addition, the MHRI Human Resources department now conducts yearly reviews of the status of all federal supported employees in the MHRI time and effort collection system to ensure that the status is accurate.

Finding 11-02 (Prior Year Finding No. 10-04)

Federal Agency

Research and Development Cluster

Program Title

Various

CFDA Number

Various

Area

Cash Management

Condition

During our testing of cash management, we selected a sample of 65 expenditures and identified that certain costs were paid by the Institute after the request was made for reimbursement of the expenditure from the federal government. We identified 1 item, which totaled $26,119, out of a sample of 65 items, with expenditures of $589,522, where the expenditure was paid for after request for reimbursement was made to the federal government. The total population of expenditures totaled $2,110,239.

Status

MHRI's expenditures continue to be recorded on the accrual basis of accounting. As such, expenditures are recorded at the time they are incurred and not necessarily at the time of payment. MHRI also utilizes the centralized payment services of MedStar Health and abides by MedStar Health's policies and practices pertaining to payment terms. MHRI's General Accounting team completes a manual review of cost payment dates prior to the request for reimbursement from the Federal Government. A detailed analysis is submitted to the Office of Financial Management for review prior to approval of every draw of funding to the Federal Government. This process was implemented during Fiscal Year 2011 and the exception occurred prior to the process change.

Finding 11-03

Federal Agency

Research and Development Cluster

Program Title

Various

CFDA Number

Various

Area

Reporting

Condition

MHRI did not submit certain of its quarterly and annual progress reports to the cognizant agencies within the required time fame as specified by the grant agreement. MHRI is generally required to submit such reports within 10 to 90 days after the grant ending period. We identified that 3 reports out of a sample selection of 9 items that were not submitted timely as required by the grant agreement. The length of delinquency in reporting ranged from 1 to 12 months.

Status

Review of upcoming progress and financial reports was incorporated into the monthly financial review meetings of federal grants conducted by the Scientific Center Administration, the Office of Financial Management, the Office of Contracts and Grants Management, and the Office of Grants and Contracts Accounting. Emphasis is placed on ensuring the reports are submitted to the granting agency on a timely basis.

MEDSTAR HEALTH RESEARCH INSTITUTE

Summary of Prior Year Findings

Year ended June 30, 2012

Finding 11-04

Federal Agency

Research and Development Cluster

Program Title

Various

CFDA Number

Various

Area

Subrecipient Monitoring

Condition

MHRI has sent letters to all of its subrecipients requesting for them to provide the most recent A-133 Single Audit report, if applicable. We determined that in 9 out of 11 responses from the subrecipients obtained by MHRI in fiscal year 2011 that there were findings noted in the subrecipient's A-133 Single Audit report. However, MHRI did not contact each subrecipient in a timely manner to ensure that the subrecipient took timely and appropriate corrective action.

Status

The subrecipient monitoring process has been enhanced to ensure compliance with A-133 requirements. Letters are sent to all subrecipients working on federally funded studies that receive payments in excess of $500,000.

A follow up process is in place to ensure that subrecipient organizations confirm they have completed their A-133 audit and that it fairly presents the standing of the organization on all material aspects.

Upon receipt of the A-133 audit from subrecipients the Office of Financial Management reviews the audit report to ensure that there are no findings related to federal funds provided by the Institute. In addition, a letter is sent to subrecipients to request corrective action plans for any identified audit findings. Follow up letters are sent if corrective actions plans are not received within 30 days.