

**PEOPLE'S COMMUNITY HEALTH  
CENTERS AND SUBSIDIARIES**

**FINANCIAL REPORT  
(IN ACCORDANCE WITH OMB CIRCULAR A-133)**

**JUNE 30, 2012 AND 2011**

**These financial statements  
may be reproduced only  
in their entirety.**

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

JUNE 30, 2012 AND 2011

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## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors  
People's Community Health Centers and Subsidiaries  
Baltimore, Maryland

We have audited the accompanying consolidated statements of financial position of People's Community Health Centers and Subsidiaries (a nonprofit organization) as of June 30, 2012, and the related consolidated statements of activities and changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Center's management. Our responsibility is to express an opinion on these financial statements based on our audit. The consolidated financial statements of People's Community Health Centers and Subsidiaries as of June 30, 2011, were audited by other auditors whose report dated July 13, 2012, expressed an unqualified opinion on those statements

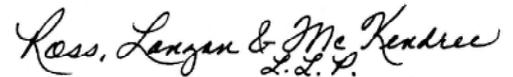
We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of People's Community Health Centers and Subsidiaries as of June 30, 2012 and 2011, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 29, 2013, on our consideration of People's Community Health Centers and Subsidiaries' 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* and should be considered in assessing the results of our audit.

To the Board of Directors  
People's Community Health Centers and Subsidiaries  
Baltimore, Maryland  
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Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements 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 consolidated 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 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated 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 consolidated financial statements as a whole.



CERTIFIED PUBLIC ACCOUNTANTS

March 29, 2013

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

ASSETS

	June 30,	
	<u>2012</u>	<u>2011</u>
<b>CURRENT ASSETS</b>		
Cash	\$ 168,991	\$ 31,586
Accounts receivable (net of allowance for doubtful accounts of \$803,199 and \$1,682,283)	1,796,904	720,738
Grants receivable	249,183	519,983
Other receivables	415,391	236,030
Inventory	123,771	323,000
Prepaid expenses	<u>28,435</u>	<u>43,182</u>
Total current assets	..... <u>2,782,675</u>	..... <u>1,874,519</u>
<b>PROPERTY AND EQUIPMENT</b>		
Property and equipment (net of accumulated depreciation of of \$2,786,613 and \$2,364,545)	4,970,334	4,819,027
Construction in progress	<u>809,321</u>	<u>985,117</u>
Total property and equipment	5,779,655	5,804,144
<b>OTHER ASSETS</b>		
Investments	100	100
Deposits	<u>75,314</u>	<u>75,314</u>
Total other assets	<u>75,414</u>	<u>75,414</u>
<b>TOTAL ASSETS</b>	<u>\$ 8,637,744</u>	<u>\$ 7,754,077</u>

See independent auditor's report. The accompanying notes and supplemental schedule are an integral part of these consolidated financial statements.

## PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

## LIABILITIES AND NET ASSETS

	June 30,	
	<u>2012</u>	<u>2011</u>
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 668,950	\$ 1,356,854
Accrued expenses	347,321	192,834
Accrued payroll and related taxes	1,938,890	1,515,968
Lines of credit	520,025	326,136
Deferred revenue	250,000	-
Current maturities of long-term debt	809,919	412,789
Current portion of capital lease obligations	<u>241,284</u>	<u>249,597</u>
Total current liabilities	.....4,776,389	.....4,054,178
<b>LONG-TERM LIABILITIES</b>		
Deferred rent	227,025	175,059
Long-term debt, net of current maturities	1,186,143	1,773,403
Long-term portion of capital lease obligations	<u>192,362</u>	<u>426,778</u>
Total long-term liabilities	<u>1,605,530</u>	<u>2,375,240</u>
<b>TOTAL LIABILITIES</b>	.....6,381,919	.....6,429,418
<b>NET ASSETS</b>		
Unrestricted	1,388,948	360,106
Temporarily restricted	<u>866,877</u>	<u>964,553</u>
Total net assets	<u>2,255,825</u>	<u>1,324,659</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u>\$ 8,637,744</u>	<u>\$ 7,754,077</u>

## PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF ACTIVITIES AND CHANGE IN NET ASSETS  
FOR THE YEARS ENDED JUNE 30, 2012 AND JUNE 30, 2011

	2012		2011
	Unrestricted	Temporarily Restricted	Total
<b>REVENUE, GAINS AND SUPPORT</b>			
Pharmacy sales	\$ 885,396	\$ -	\$ 885,396
Cost of sales	( 488,350)	-	( 488,350)
Gross Profit	<u>397,046</u>	<u>-</u>	<u>397,046</u>
Program service fees	10,870,308	-	10,870,308
Less: allowances and refunds	(4,033,192)	-	(4,033,192)
Total Program service fees, net	<u>6,837,116</u>	<u>-</u>	<u>6,837,116</u>
Income from Investment in Partnership	<u>987,921</u>	<u>-</u>	<u>987,921</u>
Total net revenue	<u>8,222,083</u>	<u>-</u>	<u>8,222,083</u>
Federal grants	3,624,961	-	3,624,961
Contributions, grants, and other	<u>1,256,121</u>	<u>-</u>	<u>1,256,121</u>
Total support	<u>4,881,082</u>	<u>-</u>	<u>4,881,082</u>
Total revenue, gains and support	<u>13,103,165</u>	<u>-</u>	<u>13,103,165</u>
<b>EXPENSES</b>			
Program services	9,549,575	-	9,549,575
General and administrative	<u>3,183,191</u>	<u>-</u>	<u>3,183,191</u>
Total expenses	12,732,766	-	12,732,766
<b>EXCESS OF REVENUE AND SUPPORT OVER EXPENSES</b>	370,399	-	370,399
Nonoperating income			
In-kind contributions related to capital acquisitions	384,300	-	384,300
Grants for capital expenditures	176,467	-	176,467
Release of restriction	<u>97,676</u>	<u>( 97,676)</u>	<u>-</u>
CHANGE IN NET ASSETS	1,028,842	( 97,676)	931,166
NET ASSETS, BEGINNING OF YEAR	<u>360,106</u>	<u>964,553</u>	<u>1,324,659</u>
NET ASSETS, END OF YEAR	<u>\$ 1,388,948</u>	<u>\$ 866,877</u>	<u>\$ 2,255,825</u>

See independent auditor's report. The accompanying notes and supplemental schedule are an integral part of these consolidated financial statements.

## PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED

	<u>June 30,</u>	
	<u>2012</u>	<u>2011</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Change in unrestricted net assets	\$.....931,166	\$(.....74,569)
Adjustments to reconcile change in unrestricted net assets to net cash provided by (used in) operating activities:		
Depreciation	650,686	381,251
Donated inventory	( 128,155)	( 257,541)
In-kind contribution related to capital acquisition	( 384,300)	( 976,763)
Grants for capital expenditures	( 176,467)	( 721,771)
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	( 1,076,166)	342,173
(Increase) decrease in grants receivable	270,800	( 145,794)
(Increase) decrease in other receivables	( 179,361)	691,806
Increase (decrease) in inventory	327,384	335,755
Increase (decrease) in prepaid expenses and other assets	14,747	21,391
Increase (decrease) in accounts payable	( 687,904)	171,104
Increase (decrease) in accrued expenses	154,487	257,982
Increase (decrease) in accrued payroll and related taxes	422,922	-
Increase (decrease) in deferred revenue	250,000	( 574,084)
Increase (decrease) in deferred rent	<u>51,966</u>	<u>57,190</u>
Total adjustments	<u>( 489,361)</u>	<u>( 417,301)</u>
Net cash provided by (used in) operating activities	.....441,805	...(.....491,870)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Property and equipment acquisitions	<u>( 241,897)</u>	<u>( 1,854,385)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net borrowings (repayments) on lines of credit	193,889	( 254,194)
Proceeds from long-term debt	-	1,487,962
Principal payments of long-term debt	( 190,130)	( 256,456)
Principal payments on capital lease obligations	( 242,729)	( 157,241)
Grants for capital expenditures	<u>176,467</u>	<u>721,771</u>
Net cash (used in) provided by financing activities	<u>( 62,503)</u>	<u>1,541,842</u>
<b>NET INCREASE (DECREASE) IN CASH</b>	137,405	( 804,413)
<b>CASH AT BEGINNING OF YEAR</b>	<u>31,586</u>	<u>835,999</u>
<b>CASH AT END OF YEAR</b>	<u>\$ 168,991</u>	<u>\$ 31,586</u>
<b><u>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</u></b>		
Cash paid during the year for interest	<u>\$ 330,449</u>	<u>\$ 84,261</u>

See independent auditor's report. The accompanying notes and supplemental schedule are an integral part of these consolidated financial statements.

## PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 - THE ORGANIZATION AND ITS SIGNIFICANT ACCOUNTING POLICIES

##### General

People's Community Health Centers, Inc. (People's) is a community-based health care organization that provides primary health care services to all individuals regardless of economic status. People's operate several clinics in Baltimore City and Anne Arundel County, Maryland, as well as a pharmacy to support the services of the clinics. People's was incorporated under the laws of Maryland in April 1970 and is a Federally Qualified Health Center.

On October 6, 2010, People's established the People's Community Health Centers Foundation for the Elimination of Health Disparities, Inc. (the Foundation) for the purpose of supporting and assisting the charitable, educational and scientific purposes of People's.

In May 2010, People's was given control of Medbank of Maryland, Inc. (Medbank), a charitable organization dedicated to accessing free prescription drugs for low-income, chronically ill residents of Maryland, from the world's largest pharmaceutical manufacturers. Medbank also has developed a software database application to assist other organizations in obtaining medications for use from other patient assistance programs.

People's, the Foundation, and Medbank form People's Community Health Centers, Inc. and Subsidiaries (collectively, the Center). All material intercompany transactions and amounts have been eliminated in consolidation.

##### Basis of Accounting

The Center maintains its records on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

##### Financial Statement Presentation

Financial statement presentation follows the recommendations of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC), which is the sole source of authoritative generally accepted accounting principles in the United States. The Center reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

*Unrestricted net assets* – Unrestricted net assets are the net assets that are neither permanently restricted nor temporarily restricted by donor-imposed stipulations.

*Temporarily restricted net assets* – Temporarily restricted net assets result from contributions whose use is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the Center pursuant to these stipulations. Net assets may be temporarily restricted for various purposes, such as use in future periods or use for specified purposes. The Center held temporarily restricted net assets as of June 30, 2012 and 2011 in the amount of \$866,877 and \$964,553, respectively.

*Permanently restricted net assets* – Permanently restricted net assets result from contributions whose use is limited by donor-imposed stipulations that neither expire by the passage of time nor can be fulfilled or otherwise removed by the Center's actions. The Center has no permanently restricted net assets as of June 30, 2012 or 2011.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - THE ORGANIZATION AND ITS SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash and Cash Equivalents

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

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable consist of amounts due from third-party payers for medical services. The Center uses the allowance method to recognize losses on realization of receivables. The allowance for doubtful accounts is maintained at a level considered adequate to provide for contractual allowances, charity care and bad debts that can be reasonably anticipated. Management's periodic evaluation of the adequacy of the allowance is based on past collection experience. This evaluation is inherently subjective, as it requires estimates that may be susceptible to significant change, including the amounts and timing of future cash flows expected to be received from government and other third party payers. The allowance for doubtful accounts totaled approximately \$803,199 and \$1,682,283 as of June 30, 2012 and 2011, respectively. The allowance for doubtful accounts represents a significant estimate. Actual results may vary and any variances could be material to the consolidated financial statements.

Inventory

Inventory of \$123,771 and \$323,000 as of June 30, 2012 and 2011, respectively, is valued at the lower of cost or market. Cost is generally determined by the first-in, first-out method. During the years ended June 30, 2012 and 2011, the Center received donated inventory of approximately \$128,155 and \$257,541, respectively. Of this amount, approximately \$88,000 and \$441,000 had been distributed to patients during 2012 and 2011, respectively, at no cost. The donations were recorded at fair value as an in-kind contribution in the consolidated statements of activities and changes in net assets.

Property and Equipment

Property and equipment purchases in excess of \$5,000 and a useful life of two years are capitalized and stated at cost. Donated property is carried at the approximate fair value at the date of donation. Expenditures for maintenance, repairs and improvements that do not materially extend the useful lives of the assets are charged to expense when incurred. Depreciation and amortization are computed using the straight-line method over the following estimated useful lives of the assets:

Furniture and equipment	3 - 7 years
Buildings and improvements	Lesser of lease term or useful life of asset

Depreciation and amortization expense for the years ended June 30, 2012 and 2011, totaled \$650,686 and \$381,251, respectively.

## PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 - THE ORGANIZATION AND ITS SIGNIFICANT ACCOUNTING POLICIES (continued)

##### Valuation of Long-Lived Assets

The Center reviews the valuation of long-lived assets and certain identifiable intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of the long-lived asset is measured by a comparison of the carrying amount of the asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. Assets to be disposed of are reportable at the lower of the carrying amount or fair value, less costs to sell.

##### Donated Assets

Donated marketable securities, inventory, and other noncash donations are recorded as contributions at their estimated fair values at the date of donation. The Center received donated prescription medication totaling approximately \$128,155 and \$257,541 during the years ended June 30, 2012 and 2011, respectively. In addition, the Center received a donation in conjunction with the acquisition of a building valued at \$384,300.

##### Investments

The Center investments consist of ownership in Priority Partners Managed Care Organization, Inc. (Priority Partners), and in Maryland Community Health Systems Limited Liability Partnership (the Partnership) are recorded at cost as the Center owns less than 20 percent of each of these companies and the market value is not readily determinable.

##### Security Deposits and Other Assets

Security deposits and other assets consist primarily of deposits required to be placed in conjunction with the leases of administrative and clinical space.

##### Revenue and Expenses

A substantial portion of The Center's revenue is derived from conditional grants and contracts under which revenue is recognized as the related expenses are incurred. Grant or contract proceeds received in excess of related expenses incurred are classified as deferred revenue in the consolidated balance sheets.

The Center has agreements with third-party payers that provide for payments to the Center at negotiated amounts different from established rates. Third party payers include Medicare, commercial insurance carriers and preferred provider organizations. Medicaid revenue is recorded at net realizable amounts from the State of Maryland (the State) for services rendered. Pharmacy sales are recorded when the product is delivered. Revenue from Medicaid accounted for approximately 65 percent, of the Center's net patient revenue for 2012.

Program expenses include costs that are specifically identified with a particular program and an allocation of costs associated with the administration of all of the Center's programs.

## PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 - THE ORGANIZATION AND ITS SIGNIFICANT ACCOUNTING POLICIES (continued)

##### Donated Services

A substantial number of unpaid volunteers and professionals have made significant contributions of their time and services to the Center. Donated services are recorded as contributions at the estimated fair values of the services provided only if the services provided require specialized skills provided by individuals possessing those skills, or the services create or enhance a nonfinancial asset.

##### Charity Care

The Center is a Federally Qualified Health Center (FQHC), which is a type of provider defined by Section 330 of the Public Health Services Act. The Center provides care to patients utilizing a sliding-fee scale with discounts based on patient family size and income in accordance with federal poverty guidelines. The Center is open to all, regardless of their ability to pay. The amount not recovered under the sliding-fee scale is not reported as revenue as it is not expected to be paid. The Center maintains records to identify and monitor the level of charity care it provides. The amount of charity care provided during the years ended June 30, 2012 and 2011, was \$3,206,107 and \$2,581,755, respectively.

##### Income Taxes

The Center is a not-for-profit corporation exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code (IRC) and is classified by the Internal Revenue Service (IRS) as other than a private foundation.

The Center is required to measure, recognize, present, and disclose in its financial statements uncertain income tax positions that the Center has taken in the tax years that remain subject to examination or expects to take on an income tax return. The Center recognizes the tax benefits from uncertain income tax positions only if it is more likely than not that the tax position will be sustained on examination by tax authorities. Prior year income tax returns may be subject to examination in various tax jurisdictions, most of which define open tax years as three years from the later of the due date of the return or the date the return was filed. The Center has not recorded a liability for uncertain income tax positions for any open tax years.

##### Recent Accounting Pronouncements

In July 2011, the FASB issued ASU 2011-07, Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities, which requires that bad debts associated with patient service revenue must be reclassified from an expense to a deduction from patient services revenue. The ASU requires enhanced disclosures about an entity's policies for recognizing revenue and assessing bad debts. The ASU also requires disclosures of patient service revenue (net of contractual allowances and discounts) as well as qualitative and quantitative information about changes in the allowance for doubtful accounts. The guidance in this ASU is effective for fiscal years beginning after December 15, 2011. The adoption of this standard is expected to result in changes in the presentation of the Center's bad debt expense and enhanced disclosures regarding bad debt and patient service revenue, but is not required to be adopted by the Center until fiscal year 2013, with earlier adoption permitted.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - THE ORGANIZATION AND ITS SIGNIFICANT ACCOUNTING POLICIES (continued)

Estimates

Management uses estimates and assumptions in preparing these financial statements in accordance with accepted accounting principles. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenue and expenses. Actual results could differ from those estimates.

Reclassifications

Certain prior year amounts have been reclassified to conform with current year presentation.

Subsequent Events

The Center has evaluated subsequent events through March 29, 2013, which is the date the financial statements were available to be issued.

NOTE 2 - ACCOUNTS RECEIVABLE AND ALLOWANCE FOR DOUBTFUL ACCOUNTS

The Center has claims outstanding against Medical Capital for factored receivables. The Center has been approved by the bankruptcy receiver for Medical Capital for payment of \$1.2 million owed. The date and amount of the final distribution has not been determined. Given the uncertain nature of the settlement, no receivable has been recorded as of June 30, 2012 or 2011.

The Center has claims outstanding against the State of Maryland for unpaid dental claims. The Center has received a portion of the amounts it has recorded as due from the State of Maryland on dental services provided. The balance outstanding from the State has been placed under review by an administrative law judge. As of June 30, 2012 and 2011, the receivable balance recorded as due from the State was \$351,641 and \$236,030, respectively. Pending the outcome of the claim, the amount collected could exceed the receivable recorded.

Details of accounts receivable at June 30, 2012 are as follows:

Medicaid	\$ 1,305,757
Medicare	258,863
Commercial insurance	423,853
Private payers	<u>611,630</u>
Subtotal	2,600,103
Less: Allowance for doubtful accounts	<u>( 803,199)</u>
Total	<u>\$ 1,796,904</u>

See independent auditor's report. The accompanying notes and supplemental schedule are an integral part of these consolidated financial statements.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 - INVESTMENTS

Limited Liability Partnership

The Center has a 12.5 percent limited partnership interest in Maryland Community Health Systems Limited Liability Partnership (the Partnership). The partners of the Partnership are composed of eight community health centers, each of which has been recognized by the IRS as a not-for-profit, tax-exempt organization.

The Partnership owns a 50 percent interest in Priority Partners Managed Care Organization, Inc. (Priority Partners), a Maryland corporation, which is a joint venture with Johns Hopkins HealthCare, LLC (JHHC), for the purpose of operating an authorized managed care organization under the terms of the Maryland Health Choice Medicaid Managed Care Program. JHHC has assumed sole responsibility for the expenses of Priority Partners, including any capital calls required to fund any operating deficiencies. By agreement, Priority Partners is obligated to pay the Partnership investment income payments in the amount of 1 percent of revenue received by Priority Partners from the State.

The Center was not required to make any capital contributions to the Partnership, nor is it expected to be required to make any capital contributions in the future. Therefore, The Center does not have any cost relative to this investment. Distributions received or due from the Partnership are recorded as investment income in the accompanying consolidated statements of operations and changes in net assets. For the years ended June 30, 2012 and 2011, the Center earned investment income from the partnership of \$987,921 and \$810,636, respectively.

Summary financial information (in thousands) of Priority Partners is as follows at of June 30:

	<u>2012</u>	<u>2011</u>
Total assets	\$ 215,551	\$ 132,628
Total liabilities	<u>145,201</u>	<u>73,899</u>
Total equity	<u>\$ 70,350</u>	<u>\$ 58,729</u>
Total revenues	\$ 889,999	\$ 841,442
Total expenses	<u>878,378</u>	<u>833,236</u>
Net income	<u>\$ 11,621</u>	<u>\$ 8,206</u>

Closely Held Corporation

The Center owns one share (12.5 percent) of Maryland Community Health Systems, Inc. (MCHS), a Maryland not-for-profit corporation, at a cost of \$100. MCHS is the general partner of the Partnership.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4 - CONCENTRATION OF CREDIT RISK

The Center maintains cash in bank deposit accounts which, at times, may exceed the federally insured amounts. Management considers this to be a normal business practice. The Center has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash. At various times during the year, the Center had deposits with its principal bank in excess of that insured by the Federal Deposit Insurance Corporation (FDIC). The bank account balance did not exceed the \$250,000 FDIC insurance limit at June 30, 2012.

The Center provides services to patients primarily located in the Baltimore City and surrounding counties. The concentrations of credit by type of payer are set forth in Note 2. Although the patients are covered by health insurance, including the Medicare and Medicaid programs, the Center's ability to collect from patients is affected by the policies and procedures of these payers.

The Center received approximately 44 percent and 59 percent of its revenue and support for the years ended June 30, 2012 and June 30, 2011, respectively, from the U.S. Department of Health and Human Services.

Approximately 65 percent and 58 percent of the Center's patient revenue for the years ended June 30, 2012 and June 30, 2011, respectively, was from Medicaid.

NOTE 5 - PROFIT-SHARING PLAN

The Center has established a salary deferral plan under Section 401(k) of the Internal Revenue Code. The plan allows eligible employees to defer a portion of their compensation ranging from 0 percent to 96 percent. Such deferrals accumulate on a tax deferred basis until the employee withdraws the funds. The Center does not match employee contributions.

NOTE 6 - LONG-TERM DEBT

Long-term debt consists of the following:

	<u>2012</u>	<u>2011</u>
Mortgage payable, secured by the land, building and improvements of 3011-3013 Greenmount Avenue, interest at the one-year treasury rate plus 3 percent but not less than 8.75 percent (8.75 percent at June 2012 and 2011), payable in monthly installments of principal and interest of \$353 through May 2015.	\$ 10,859	\$ 13,990
Note payable to Partners for the Common Good, Inc., secured by the building of 3028-3032 Greenmount Avenue, interest fixed at 5.5 percent, payable in monthly principal and interest installments of \$3,390 through January 2014. This note contains certain restrictive covenants which were not met for the year ended June 30, 2012. Partners for the Common Good, Inc. has waived the covenant violation for the year ended June 30, 2012.	415,923	435,051

See independent auditor's report. The accompanying notes and supplemental schedule are an integral part of these consolidated financial statements.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 - LONG-TERM DEBT (continued)

	<u>2012</u>	<u>2011</u>
Note payable to BB&T, secured by the land, building and improvements of 3011-3013 and 3026 Greenmount Avenue, interest at the bank's prime rate plus 5 percent (8.25 percent at June 30, 2012 and 2011), payable in monthly principal and interest installments of \$6,047 through May 14, 2013, at which time all remaining unpaid principal and interest is due. This note contains certain non-financial restrictive covenants which were not met for the year ended June 30, 2012.	479,568	489,378
Note payable to Bank of America, secured by the land, building, and improvements of 1734 Maryland Avenue, along with 1715, 1717, 1719, 1721 Maryland Avenue, interest fixed at 7.16 percent, payable in monthly installments of \$7,749 beginning in June 2011 and continuing until May 2016. This note contains certain restrictive covenants which were not met for the year ended June 30, 2012. Bank of America has waived the covenant violation for the year ended June 30, 2012.	812,741	845,311
Promissory note to Baltimore City Department of Housing and Community Development (DHCD), secured by a deed of trust, assignment of rents and security agreement and assumption agreement for the property at 1734 Maryland Avenue, no interest, payable in quarterly installments of \$62,500 beginning August 2011 and continuing until August 2012. This note carries a default penalty of \$1,337,000, the only recourse for which is the exercise of the DHCD's rights under the agreement. As of June 30, 2012, Peoples was delinquent on the payments for this loan. Per the loan agreement, DHCD must declare the loan delinquent for the default penalty to occur. As of the date of this report, the balance on the loan is \$27,000 as confirmed by DCHD and no default has been declared.	187,500	312,500
Note payable to the Maryland Department of Labor, Licensing, and Regulation in conjunction with the purchase of the property at 1734 Maryland Avenue, interest fixed at 6 percent. All interest will be waived if monthly payments of \$3,243 are paid until the debt is repaid.	<u>89,471</u>	<u>89,862</u>
	1,996,062	2,186,092
Less current maturities	<u>809,919</u>	<u>412,789</u>
	<u>\$ 1,186,143</u>	<u>\$ 1,773,303</u>

See independent auditor's report. The accompanying notes and supplemental schedule are an integral part of these consolidated financial statements.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 - LONG-TERM DEBT (continued)

Contractual maturities of long-term debt are as follows:

<u>Years Ending June 30,</u>	<u>Amount</u>
2013	\$ 809,919
2014	445,771
2015	44,542
2016	<u>695,830</u>
Total	<u>\$ 1,996,062</u>

NOTE 7 - LINES OF CREDIT

In January 2007, the Center entered into a line of credit with a bank in the amount of \$100,000, which bears interest at the bank's prime rate plus 1.00 percent. The interest rate at both June 30, 2012 and 2011, was 4.25 percent. The line of credit is payable on demand and is collateralized by a second position lien on three existing mortgages that People's has with the bank. As of June 30, 2012 and 2011, the outstanding balance on the line was \$72,223 and \$78,334, respectively. This line is subject to certain non-financial restrictive covenants.

In April 2009, People's entered into a line of credit with a bank in the amount of \$290,000, which carried interest at the Prime rate. The interest rate at both June 30, 2012 and 2011, was 3.25 percent. This loan was used to finance the purchase of land at Reece Road where People's had intended to develop a medical-dental facility and community center. The loan was payable on demand and was collateralized by the land at Reece Road. The outstanding balance on this line of credit was \$247,802 and \$247,802 as of June 30, 2012 and 2011, respectively. This line is subject to certain non-financial restrictive covenants.

In December 2011, People's entered into a revolving line of credit with a bank in the amount of \$200,000, which carried interest at the Prime rate plus 7 percent. The interest rate at June 30, 2012 was 10.25 percent. This loan was used to finance the operations of People's. The loan matured on May 31, 2012 and was subsequently renewed through July 5, 2013. The loan was collateralized by all equipment and fixtures, inventory and receivables owned by the People's. The outstanding balance on this line of credit was \$200,000 as of June 30, 2012. This line is subject to certain financial restrictive covenants to which People's was not in compliance at June 30, 2012.

NOTE 8 - COMMITMENTS AND CONTINGENCIES

Leased Facilities

The Center leases its administrative offices, several clinics and equipment under noncancelable operating leases expiring on various dates through October 2043. The office lease, which expires in October 2017, contains a renewal option for three additional two-year periods. In addition to a fixed annual rental, the Center is responsible for its pro-rata share of any increases in real estate taxes and insurance premiums for certain facilities. Monthly rental payments range from \$10 to \$11,232 at June 30, 2012, and substantially all leases contain escalation clauses increasing the required payment by 1.25 percent to 4 percent annually.

See independent auditor's report. The accompanying notes and supplemental schedule are an integral part of these consolidated financial statements.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8 - COMMITMENTS AND CONTINGENCIES (continued)

Deferred rent of \$227,025 and \$175,059 at June 30, 2012 and 2011, respectively, represents the difference between straight-line rent expenses versus cash paid. Rent expense for the years ended June 30, 2012 and 2011 totaled \$489,101 and \$527,631, respectively.

Future minimum rental payments for all leased facilities as of June 30, 2012, are as follows:

<u>Years Ending June 30,</u>	<u>Amount</u>
2013	\$ 297,505
2014	304,428
2015	287,923
2016	294,317
2017	300,894
Thereafter	<u>9,775,845</u>
Total	<u>\$ 11,260,912</u>

During 2011, the Center entered into several leases primarily related to the upgrade of the computer system. The cost of the equipment under these leases is included in the consolidated balance sheets as property and equipment, was \$833,616 as of June 30, 2012 and 2011, respectively. Accumulated amortization of the leased equipment was \$543,341 and \$113,383 as of June 30, 2012 and 2011, respectively. Amortization of assets under capital leases is included in depreciation expense.

The following is a schedule by years of the future minimum lease payments under the capital leases together with the present value of the net minimum lease payments as of June 30, 2012:

<u>Years Ending June 30,</u>	<u>Amount</u>
2013	\$ 241,284
2014	131,580
2015	92,135
2016	69,060
2017	<u>38,555</u>
	572,614
Less amount representing interest	<u>( 138,968)</u>
	433,646
Less current portion	<u>( 241,284)</u>
	<u>\$ 192,362</u>

Litigation

The Center is involved in litigation arising in the ordinary course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the Center's future financial position or results from operations.

## PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 8 - COMMITMENTS AND CONTINGENCIES (continued)

The Center engaged a joint venture with P&J Contracting Company, Inc. and American Contractors of Baltimore, Inc. (collectively, the "Contractor") to perform renovations on property at 3028 Greenmount Avenue. The Contractor claims that the work is complete and that it is owed approximately \$70,000. The Center asserts that the work has not been satisfactorily completed and, if the work had been satisfactorily completed, the Contractor would be owed \$50,000 or less. The Center has not filed suit. The Center is currently dealing directly with the Contractor to reach a resolution.

#### Construction in Progress

People's is constructing a new building on land it is leasing from the Board of Education of Anne Arundel County. The building will house a health clinic and a community and activity center. The project is still in early stages, but will be funded by grants. People's has secured a \$5,000,000 Federal capital grant as well as a \$1,600,000 State capital grant and two \$250,000 State bond fund awards to be used for this project. The projected total cost is approximately \$9,597,889. As of June 30, 2012, People's had incurred approximately \$143,000 in costs on the project which has been requested from state funds.

#### NOTE 9 - TEMPORARILY RESTRICTED NET ASSETS

During the year ended June 30, 2011, the Center recorded temporarily restricted net assets of \$976,673 from an in-kind donation related to the purchase of the HERO building. As a condition of the sale, the building must be used to provide healthcare services to the underserved community for a period of 10 years. The restriction expires in May 2021. During the year ended June 30, 2012, \$97,667 of the restriction was considered met and was transferred to unrestricted net assets.

#### NOTE 10 - MEDICAL MALPRACTICE

People's is protected from medical malpractice claims under Section 224(a) of the Public Health Service (PHS) Act which provides liability protection under the Federal Tort Claims Act (FTCA), 28 U.S.C. §§ 1346(b), 2672, or by alternative benefits provided by the United States where the availability of such benefits precludes a remedy under the FTCA, for damage for personal injury, including death, resulting from the performance of medical, surgical, dental, or related functions by PHS employees while acting within the scope of such employment. By letter dated December 15, 2011, People's is deemed an employee of PHS through December 31, 2012.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
 YEAR ENDED JUNE 30, 2012  
 FEDERAL ID#: 52-0905681

Federal Grantor/ Pass-Through Grantor Program Title	Federal CFDA Number	Period Covered	Grant Number	Federal Disbursements/ Expenditures (Allowable)
U.S. Department of Health and Human Services				
Consolidated Health Centers	93.224	May 1, 2011 through April 30, 2012	H80CS00588	\$ 1,220,722
		May 1, 2012 through April 30, 2013	H80CS00588	496,692
Affordable Care Act	93.527	May 1, 2011 through April 30, 2012	H80CS00588	827,817
		May 1, 2012 through April 30, 2013	H80CS00588	<u>331,128</u>
				.....2,876,359
Passed-Through Baltimore City Health Department Ryan White Part A	93.914	March 1, 2011, through February 28, 2012	11-2478	361,962
		March 1, 2012, through February 28, 2013	12-2478	<u>159,064</u>
				.....521,026
U.S. Department of Health and Human Services				
Passed-Through Baltimore City Health Department Ryan White Part B	93.917	July 1, 2011, through June 30, 2012	C034261	.....47,063
U.S. Department of Health and Human Services				
Ryan White Title III Early Intervention Services Program	93.918	April 1, 2011, through March 31, 2012	H76HA00809	170,625
		April 1, 2012, through March 31, 2013	H76HA00809	<u>108,348</u>
				<u>278,973</u>
Total federal awards				<u>\$ 3,723,421</u>

See independent auditor's report. The accompanying note to the schedule of expenditures federal awards are an integral part of these consolidated financial statements.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

NOTE TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

The accompanying schedule of expenditures of federal awards includes the federal grant activity of People's Community Health Centers, Inc. and Subsidiaries and is presented on the accrual basis of accounting. The information on 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 this schedule may differ from the amounts presented in, or used in the preparation of, the basic consolidated financial statements.



**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**

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To the Board of Directors  
People's Community Health Centers and Subsidiaries  
Baltimore, Maryland

We have audited the consolidated financial statements of People's Community Health Centers and Subsidiaries (collectively, the Center) as of and for the year ended June 30, 2012, and have issued our report thereon dated March 29, 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 Center is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Center'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 Center's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Center's internal control over financial reporting.

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs as Findings 2012-1, 2012-2, and 2012-3 to be material weaknesses.

To the Board of Directors  
People's Community Health Centers and Subsidiaries  
Baltimore, Maryland  
Page Two

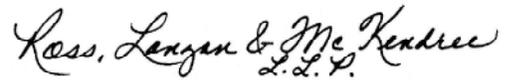
### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Center's consolidated 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as Finding 2012-4, 2012-5, and 2012-6.

We noted certain matters that we reported to management of the Center in a separate letter dated March 29, 2013.

The Center'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 Center's responses, and accordingly, we express no opinion on them.

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



CERTIFIED PUBLIC ACCOUNTANTS

March 29, 2013



INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS  
THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR  
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN  
ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Directors  
People's Community Health Centers and Subsidiaries  
Baltimore, Maryland

**Compliance**

We have audited People's Community Health Centers and Subsidiaries (collectively, 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 June 30, 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. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Center's management. Our responsibility is to express an opinion on the Center'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 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. Our audit does not provide a legal determination on the Center's compliance with those requirements.

As described in Findings 2012-4, 2012-5, and 2012-6 in the accompanying schedule of findings and questioned costs, the Center did not comply with requirements regarding program income that is applicable to its Consolidated Health Centers program and reporting requirements applicable to all federal awards. Compliance with such requirements is necessary, in our opinion, for the Center to comply with requirements applicable to those programs.

In our opinion, except for the noncompliance described in the preceding paragraph, the Center complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

To the Board of Directors  
People's Community Health Centers and Subsidiaries  
Baltimore, Maryland  
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### **Internal Control Over Compliance**

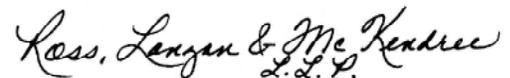
Management of the Center is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Center's internal control over compliance with the 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 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 significant deficiencies or material weaknesses, and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

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 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 deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as Finding 2012-6 to be a material weakness.

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

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



CERTIFIED PUBLIC ACCOUNTANTS

March 29, 2013

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**Section I. Summary Of Independent Auditor's Results Financial Statements:**

Financial Statements:

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified?  X  Yes   No
- Significant deficiency(ies) identified that are not considered to be material weaknesses?   Yes  X  None Reported
- Noncompliance material to financial statements noted?  X  Yes   No

Federal Awards:

Internal control over major programs:

- Material weakness(es) identified?  X  Yes   No
- Significant deficiency(ies) identified that are not considered to be material weaknesses?   Yes  X  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 OMB Circular A-133?  X  Yes   No

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
93.224	Consolidated Health Centers
93-527	Consolidated Health Centers
93.914	Ryan White Part A
93.918	Ryan White Title III Early Intervention Services Program

Dollar threshold used to distinguish between Type A and Type B programs: \$300,000

Auditee qualified as low-risk auditee?   Yes  X  No

See independent auditor's report on internal control over financial reporting and on compliance and other matters

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**Section II. Findings Related To The Financial Statement Audit As Required To Be Reported In Accordance  
With Government Auditing Standards Generally Accepted In The United States Of America**

**A. Material Weaknesses Relating To Internal Control**

Finding 2012-1 - Account Reconciliations and Review

Criteria: All material general ledger balances should be reconciled at least monthly and the reconciliations should be independently reviewed by management to ensure balances are reasonably stated and financial reporting is timely and accurate.

Condition: We noted that reconciliations completed for areas of the audit including grants receivable, inventory, property and equipment, accounts payable, debt and net assets were not completed accurately. We also noted that financial statement information is not available on a timely basis to management and Those Charged with Governance as the Center does not perform month-end close procedures on a routine schedule.

Effect: During the course of the audit, management recorded approximately 47 adjusting journal entries to reconcile general ledger accounts. These journal entries decreased assets by \$284,328, increased liabilities and net assets by \$462,574 and decreased the change in net assets by \$746,902. Due to the significant number of journal entries and the lack of timely financial information, management cannot make informed, appropriate decisions.

Cause: During the year, management experienced significant turnover within the accounting department, including the retirement of the CFO. Management, based on the demands of the position, decided to divide the role into two separate positions – a Director of Finance and a Director of Accounting. The Director of Finance was hired in December 2012 and Management is still searching for a Director of Accounting.

Recommendation: We recommend that management ensure adherence to its documented internal control policies and procedures. In addition, we recommend that management hire a Director of Accounting with significant general ledger experience to independently review all material general journal entries, general ledger accounts and financial information. We also recommend that management limit the number of personnel with access to enter journal entries into the accounting software to one person with supervisory experience. We recommend that management prepare a schedule for month-end close whereby books and records are completed by no later than the 15th day of the following business month.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**A. Material Weaknesses Relating To Internal Control (continued)**

Finding 2012-1 - Account Reconciliations and Review (continued)

Corrective action planned or taken: PCHC's prior CFO undertook acquisition of a software upgrade of PCHC's General Ledger software in August, 2012, including data migration of the legacy system into the new system. The firm retained for the installation of the upgrade, a large national company, did not execute the upgrade well and PCHC's quality oversight and testing procedures produced requests for this company to remedy flawed programming matters on many occasions. Therefore, the installation produced delays in the month-end close procedures and produced a need for multiple validations of end-of-month reports. PCHC eventually terminated the agreement with the vendor who originally installed the software. PCHC retained a local software support company, certified as a reseller of this product, to repair the newly-installed general ledger upgrade; and provide training and support for existing staff. Subsequently, PCHC improved and expanded its month end close procedures. The impact of the corrective actions therefore, was not fully evident to the audit firm due to this audit period including the time frame that experienced this upgrade process. The meetings of the governing body occur the fourth week of every month. At these monthly meetings, the Board of Trustees is provided monthly the income/expense statement and balance sheet for the prior month and year to date. Recently, comparative statements have been added. The governing body is provided sufficient information on a monthly basis, in order to be effective. A CPA serves as Treasurer of the Board and assures that information is received timely and communicated in an understandable format to the governing body. Because PCHC operates 10 geographically disparate sites, effort was directed in 2012 to improve the use of tools between the sites and headquarters. Sites perform activities that impact the month end close process, such as completion of the clinical notes in order to produce visit and claims data; disposal of inoperable equipment, and other items that must be transmitted timely to headquarters for proper inclusion in monthly statements. Performance improvement included revamping of workflows and acquisition of tools such as Sharepoint and Optical Character Recognition software for PCHC's scanners. Upon further analysis of competency needs, the top position in the fiscal department has been split into two leadership positions – the Director of Finance and the Director of Accounting, due to the demands of the highly regulated and complex fields of medical, dental, mental health, substance abuse program, and pharmacy industries, since PCHC operates all of these lines of business. The Director of Finance was hired in December, 2012. The requirements of the Director of Finance are strategic in nature, including the analysis of trends, initiation of corporate initiatives that improve financial ratios, UDS measures and fiscal measures.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**A. Material Weaknesses Relating To Internal Control (continued)**

Finding 2012-1 - Account Reconciliations and Review (continued)

Corrective action planned or taken (continued): A search for a director of accounting has been underway since December, 2012, prior to the recent retirement of the CFO. The Director of Accounting will supervise staff accountants and grant accountant, and the new position of accounting clerk. The Director of Accounting will oversee and assure quality of journal entries, assure separation of duties, perform internal audits, assure that the general ledger is an accurate, useful management tool; assure a timely and accurate month end close process, provide guidance to accounting staff to assure accuracy in a double entry system with proper offset accounts for each entry. This will eliminate the re-entry/correction notations observed by the audit firm. Specifically regarding journal entries, the check-writing and accounts payable system represent the only electronic systems linked within the software for electronic transfer of data. Due to all the disparate electronic financial transaction and encounter databases in place at PCHC, 90% of the entries into the ledger are through journal entries including fixed assets, depreciation, accounts receivable, etc. For example, there is a stand-alone point of sale system for pharmacy, a separate medical/dental billing system connected to the Electronic Patient Record system, a separate web-based database that processes payroll operated by an outside company. None of these systems drop data directly into the general ledger package and manual journal entries must routinely be made into the ledger. Quality review prior to journal entry by the Director of Accounting will replace retrospective review of entries made during the end-of-month procedure, upon the filling of this position.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**A. Material Weaknesses Relating To Internal Control (continued)**

Finding 2012-2 - Document Retention and Support

Criteria: Adequate accounting records and source documents must be maintained in order to have an effective and accurate financial management and reporting system.

Condition: For several of the transaction samples selected as part of our audit procedures, including journal entries posted to the general ledger, documentation was not able to be located or support for the transaction was not retained. For several of the transactions tested in accounts payable, we noted that the invoice date rather than the date of service was used to record amounts payable to vendors.

Effect: Amounts reported within the general ledger may not be fully supported by appropriate documented evidence, and may not be properly recorded in the correct period to which the service relates.

Cause: During the year, management experienced significant turnover within the accounting department and hired inexperienced staff who were not properly trained. We noted that personnel entered approximately 307 journal entries many of which were corrections of previous entries. In the course of performing our audit, we prepared approximately 30 journal entries to correct the accounting records.

Recommendation: We recommend that management adhere to the process for retaining support for all transactions, including journal entries posted to the general ledger, and ensure that proper controls have been established for retaining critical supporting documentation of transactions recorded by the Center. We also recommend that management limit the number of personnel with access to enter journal entries into the accounting software to one person with supervisory experience.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**A. Material Weaknesses Relating To Internal Control (continued)**

Finding 2012-2 - Document Retention and Support (continued)

Corrective action planned or taken: PCHC has received technical assistance regarding the structure and job requirements for these financial job positions. The duties of a current Senior Accountant have been revised so that one person is making all journal entries. An accounting clerk position has been created to perform certain unskilled functions that this senior accountant once performed to create capacity to shift all journal entries to this qualified accountant staff member. PCHC has additionally received bids for Optical Character Recognition (OCR) software to add to its scanner hardware. This will produce the ability to sort scanned files by any parameter and therefore will be retrievable in a user-defined format. With a new clerical position devoted to organization of the documents electronically, this will support the efforts of the senior accountant so that all documents are well organized upon receipt and are filed timely in an electronic database. The prospective review of journal entries will improve the quality review of the work of the one person assigned to perform these entries, thus minimizing the need for reversing entries and correcting entries.

Finding 2012-3 - Payroll Tax Returns

Criteria: Tax returns filed to the Federal, State and Local government are filed on a timely basis and are complete and accurate.

Condition: Review of Form 941 tax filings during fiscal year 2012 revealed that the Center filed its tax returns reporting that all liabilities had been paid. The returns were signed by the Chief Financial Officer on behalf of the Center, and we noted that a portion of the payroll taxes were not remitted to the IRS. The same condition exists for unemployment returns filed with the State of Maryland.

Effect: Amounts reported within the general ledger may not be fully supported by appropriate documented evidence, and may not be properly recorded in the correct period to which the service relates.

Cause: During the year, management experienced significant cash flow issues and was unable to make payments in a timely manner.

Recommendation: We recommend that management of the Center should ensure that all tax returns filed to the Federal, State and Local government are filed on a timely basis and are complete and accurate. We also recommend the Center's payroll service assume responsibility for remitting withholding and other payroll taxes.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**A. Material Weaknesses Relating To Internal Control (continued)**

Finding 2012-3 -Payroll Tax Returns (continued)

Corrective action planned or taken: PCHC remains current with its payments to federal and state entities. PCHC has documentation demonstrating compliance with timely payments and shared these documents with the audit firm. PCHC's accounts payables were reduced by 51% between 2011 and 2012, as evidenced in this audit report; and total liabilities were reduced by 1%. PCHC has entered payment plans with certain government entities relating to the assumption of the obligations of another non-profit corporation. The assumption of these debts was memorialized in documents created at the point of official merger/acquisition of this former's company's assets and liabilities into PCHC's book of business in 2011. This created additional financial burden for PCHC in 2012, however, payment plans instituted with government entities as well as this company's prior commercial vendors was accomplished. The majority of these obligations are satisfied, and the impact of these additional expenses will not be continued in 2013. The external payroll company that is under contract with PCHC does perform the reporting requirements to government entities regarding payroll related matters, and has assumed responsibility for remittances in this regard.

**B. Compliance Findings**

Finding 2012-4 See Findings 2012-1, 2012-2, and 2012-3 above.

**Section III. Findings and Questioned Costs for Federal Awards**

**A. Material Weakness Relating to Internal Control**

Finding 2012-5 See Findings 2012-1, 2012-2, 2012-3, and 2012-4 above

**B. Compliance Findings**

Finding 2012-6 - Program Income for Sliding Fee Discount and Eligibility Under Federal Awards

Agency and Awards: U.S. Department of Health and Human Services Consolidated Health Centers program, CFDA number 93.224, Ryan White Part A, CFDA number 93.914, Ryan White Part B, CFDA number 93.917, and Ryan White Title III Early Intervention Services Program, CFDA number 93.918

Criteria: OMB Circular A-133 states that the auditee must have a schedule of fees or payments for the provision of their health services consistent with locally prevailing rates or charges and designed to cover their reasonable costs of operation. They are also required to have a corresponding schedule of discounts applied and adjusted on the basis of the patient's ability to pay.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**B. Compliance Findings (continued)**

Finding 2012-6 - Program Income for Sliding Fee Discount and Eligibility Under Federal Awards (continued)

Condition: For several of the patients selected for compliance testing, we were unable to locate supporting documentation of residency, intake forms completed and provided by the Center did not pertain to proper period, patient's income as reported on intake form supported a higher fee than patient was charged based on sliding fee documentation, and in one selection, the patient was charged more than the intake forms indicated was proper. Management was subsequently able to provide documentation to support some of the low income sliding fee classifications, however this documentation was not properly maintained in the patient's medical records as originally provided.

Effect: We were unable to determine, based upon our sample, if patients are being charged consistently and fairly in accordance with the fee schedule established by the Center.

Cause: Individuals responsible at each center did not adhere to the Center's policies and procedures for verifying a patient's information and maintaining reliable and accurate documentation.

Recommendation: We recommend that management develop a checklist of required forms to ensure the proper forms are kept in each patient file which identifies the proof of income provided (or notes that no proof was provided), documents the calculation of annual income and household size, and the fee the patient was charged based upon the information collected and that they are maintained properly. We recommend the Center perform random inspections of documentation in order to ensure this process is functioning properly.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**B. Compliance Findings (continued)**

Finding 2012-6 - Program Income for Sliding Fee Discount and Eligibility Under Federal Awards (continued)

Corrective action planned or taken: PCHC implemented extensive change in its work-flow practices in its implementation of means testing during FY2012. PCHC established a visit type for out stationed eligibility (a required service of an FQHC) inside of PCHC's practice management software system. The out stationed eligibility service including document collection from the patient, became an appointment type and a service, rather than an activity done concurrently with another type of visit. PCHC took this approach since many patients come to PCHC for eligibility for other things besides medical care; including pharmacy assistance programs through which PCHC acts as a portal, dental services for clients not seen for medical care (since Maryland Medicaid does not cover adult dental services, the dental eligibility system is impacted), gray-zone mental health patients who are covered by State-only Medicaid, cancer screening programs, and SSI disability application processes. Clients are scheduled for a visit with an out stationed eligibility worker just as they are scheduled with any other care-giver or case manager or licensed staff. These out stationed eligibility case management visits establish the individual as a PCHC client/patient. The dates of these visits and the subsequent turning in of documentation now occur well in advance (days or weeks) of an appointment for another type of service at PCHC. Some patients receive access to Pharmacy Assistance Programs only, and do not see a PCHC licensed provider excepting for the pharmacist (which is not recognized as a visit by HRSA). Some patients who complete the eligibility determination process end up "no-showing" for their clinical visits. PCHC therefore now has individuals listed on their panels who have documents for sliding scale fees, but no "clinical visits" in the time period being audited. In addition, PCHC serves many undocumented aliens who have no residency documentation. This is a required service for FQHC's in that FQHC's are exempt from the public benefit rule and are required to serve those without residency documentation. Documentation of residency is therefore not possible with certain populations which PCHC is required to serve. In order to minimize the incomplete means test files, PCHC began in 2011 to grant only a 30-day window for individuals to be considered in a grace period for a discounted payment while waiting for them to bring in their documents. The State of Maryland allows hospitals and skilled nursing facilities to have a 2-day window only before charging full fee to the clients. PCHC will evaluate reducing the amount of days from 30 to some shorter time period, so that clients are not characterized as sliding scale patients for this 30 day length of time, but are reverted back to full-pay self-pay quickly. This will allow the sample that is tested by the audit firm to include only those who have completed the means test process fully and not those in that grace period who may or may not have provided all required document.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**B. Compliance Findings (continued)**

Finding 2012-6 - Program Income for Sliding Fee Discount and Eligibility Under Federal Awards (continued)

Corrective action planned or taken (continued) PCHC converted completely from paper clinical records to electronic patient record during 2012. The means test data had no "tab" built into the electronic patient record by the software vendor; therefore, PCHC had to create a work-around for filing this data electronically elsewhere. For the Ryan White clients, in particular, the eligibility documentation, other than labs, was difficult to import into the patients' medical records. PCHC purchased a software product known as i2i for proper panel management in preparation for patient-centered health home certification. This provided an electronic database that was linked to, but not inside of, the patients' clinical records for storing means test information. Subsequently, the Electronic Patient Record vendor has created a tab inside of the software and PCHC has implemented the scanning feature into its Electronic Patient Record system. This will finally allow for the means test documentation to be scanned and inputted into a tab within the Electronic record, rather than being maintained on paper or in a separate file not connected to the Electronic record - except in the case where the patient has only a pharmacy or SSI visit in which case there is no and will be no subsequent record in the Electronic patient record system.

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES  
SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**Section I: Schedule of Prior Year Audit Findings**

Finding 2011-1 - Account reconciliation's and review

Condition: We noted that reconciliations were not completed or reviewed for many areas of the audit, including patient and grants receivable, inventory, property and equipment, accounts payable, deferred rent, and debt. In addition, we noted that an analysis of the allowance for doubtful accounts related to patient receivables had not been prepared.

Current status: Toward the end of fiscal year 2012, Management hired a CPA, a Director of Finance and a Grant Accounting Manager to ensure reconciliations are performed accurately and timely. The Center also continues to recruit for a Director of Accounting, however due to the lack of qualified, capable candidates in the accounting field has been unable to fill this position. Management has performed an analysis of the allowance account. See Finding 2012-1.

Finding 2011-2, 2011-3, 2011-4, 2011-5 - Grant Management and Schedule of Expenditures of Federal Awards Completion

Condition: As of the start of our audit fieldwork, management prepared an incomplete and inaccurate Schedule of Expenditures of Federal Awards and was unable to provide an accurate listing of grants receivable. As a result, several audit adjustments were recorded to correct the Schedule of Expenditure of Federal Awards.

Current status: Management hired a Grant Accounting Manager toward the end of fiscal year 2012 and the Schedule of Expenditures of Federal Awards has been completed accurately.

Finding 2011-3 - Document Retention and Support

Condition: For several of the transaction samples selected as part of our audit procedures, including legal invoices and journal entries posted to the general ledger, documentation was not able to be located or support for the transaction not retained. In addition, adequate controls had not been established to ensure proper record retention as support for the inventory balances at year-end could not be found. We specifically noted 13 Federal expenditures totaling \$3,052 for which supporting documentation could not be provided.

Current status: See Finding 2012-3

PEOPLE'S COMMUNITY HEALTH CENTERS AND SUBSIDIARIES  
SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2012

**Section I: Schedule of Prior Year Audit Findings (continued)**

Finding 2011-6 Program Income for Sliding Fee Discount Under Consolidated Health Centers Program

Condition: For several of the patients selected for compliance testing, we were unable to independently recalculate the fee that should have been charged to the patient based upon the schedule of fees and proof of income provided. The proof of income was either not included in the patient files, was inconsistent with the information required to be provided by the patient on data collection forms or information contained within the patient billing system, or there was no other documentation retained to support that the patient did not or was not able to provide proof of income.

Current status: See Finding 2012-6

Finding 2011-7: Timely Report Filing

Condition: The data collection form and reporting package of all expenditures of Federal awards was not filed within nine months after the end of the Center's fiscal year 2011.

Current status: The report was filed timely; therefore, the Center is in compliance with the terms of its grant agreements.