Project Renewal, Inc.
and Affiliates

Consolidated Financial Statements and
OMB Circular A-133 Financial Report
Together With Independent Auditors' Report

June 30, 2012

Project Renewal, Inc. and Affiliates

Consolidated Financial Statements and
OMB Circular A-133 Financial Report

June 30, 2012

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O'CONNOR DAVIES

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Independent Auditors' Report

Board of Trustees
Project Renewal, Inc. and Affiliates

We have audited the accompanying consolidated statement of financial position of Project Renewal, Inc. and affiliates (the "Organization") as of June 30, 2012, and the related consolidated statements of operations, changes in stockholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 Organization'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 the 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 Project Renewal, Inc. and affiliates as of June 30, 2012, and the changes in their net assets and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 23, 2012 on our consideration of the Organization's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements of the Organization taken as a whole. The accompanying consolidated 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 together with the consolidating schedule of financial position and consolidating schedule of activities, are 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 information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

O'Connor Davies, LLP

New York, New York
October 23, 2012

O'CONNOR DAVIES, LLP
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Project Renewal, Inc.

Consolidated Statement of Financial Position
June 30, 2012

ASSETS	
Cash and cash equivalents	$ 3,070,142
Investments	31,733
Accounts and grants receivables, net	5,685,038
Pledges receivable, net	390,134
Rent receivable	58,441
Due from affiliates, net	78,405
Prepaid expenses	229,847
Tax credit monitoring fees, net	14,294
Security deposits and other assets, net	370,907
Mortgage receivable	12,500,000
Restricted sponsor reserve	8,958,289
Assets held for others	979,666
Investments in rental property, net	22,163,732
Deferred debt issuance costs	572,915
Property and equipment, net	7,954,724
Total Assets	$ 63,058,267
LIABILITIES AND NET ASSETS	
Liabilities	
Accounts payable and accrued expenses	$ 3,691,907
Accrued payroll and related liabilities	948,453
Accrued interest	291,083
Construction payable	941,434
Developer's fee payable	1,760,047
Due to afffiliates	987,405
Deferred revenue	4,541,659
Deferred rent	879,234
Loans payable	18,651,791
Sponsor reserve held in custody	8,958,289
Enforcement note payable	12,500,000
Total Liabilities	54,151,302
Net Assets	
Unrestricted	
Operating	2,310,329
Nonoperating	88,871
Non-controlling limited partners' interests in consolidated affiliate	5,034,664
Total Unrestricted Net Assets	7,433,864
Temporarily restricted	1,473,101
Total Net Assets	8,906,965
	$ 63,058,267

See notes to financial statements

Project Renewal, Inc.

Consolidated Statement of Activities
Year Ended June 30, 2012

	Unrestricted	Temporarily Restricted	Total
REVENUE AND SUPPORT			
Grants	$ 42,901,827	$ -	$ 42,901,827
Rental income	2,264,724	-	2,264,724
Proceeds from sale of property	2,810,000	-	2,810,000
Miscellaneous income	177,877	-	177,877
Special events, net of direct benefit to donors of $100,065	693,022	-	693,022
Contributions	371,119	1,052,086	1,423,205
Net assets released from restrictions	840,483	(840,483)	-
Total Revenue and Support	50,059,052	211,603	50,270,655
EXPENSES			
Program Services			
Outreach	437,528	-	437,528
Treatment and transitional housing	26,401,227	-	26,401,227
Medical services	6,036,753	-	6,036,753
Employment services	4,831,563	-	4,831,563
Permanent housing	6,107,429	-	6,107,429
Total Program Services	43,814,500	-	43,814,500
Supporting services			
Management and general	5,552,566	-	5,552,566
Fundraising	598,023	-	598,023
Total Supporting Services	6,150,589	-	6,150,589
Total Expenses	49,965,089	-	49,965,089
Increase in Net Assets Before Non-Controlling Limited Partners' Capital Contributions to Consolidated Affiliate	93,963	211,603	305,566
Captial contributions	4,766,283	-	4,766,283
Change in Net Assets	4,860,246	211,603	5,071,849
NET ASSETS			
Beginning of the year, restated	2,573,618	1,261,498	3,835,116
End of the year	$ 7,433,864	$ 1,473,101	$ 8,906,965

See notes to financial statements

Project Renewal, Inc.

Consolidated Statement of Functional Expenses
Year Ended June 30, 2012

	Program Services								
	Outreach	Treatment and Transitional Housing	Medical Services	Employment Services	Permanent Housing	Total	Management and General	Fundraising	Total
Salaries	$ 294,821	$ 14,486,388	$ 3,324,240	$ 1,650,543	$ 1,442,448	$ 21,198,440	$ 2,427,835	$ 293,946	$ 23,920,221
Employee benefits and payroll related taxes	82,353	4,058,092	928,577	449,517	402,926	5,921,465	680,208	82,109	6,683,782
Total Salaries and Related Expenses	377,174	18,544,480	4,252,817	2,100,060	1,845,374	27,119,905	3,108,043	376,055	30,604,003
Food and kitchen supplies	387	1,354,599	-	1,717,838	66,177	3,139,001	4,798	-	3,143,799
Client supplies	10,163	683,863	119,563	243,766	59,272	1,116,627	5,688	4,768	1,127,083
Lab fees	4,254	18,121	98,739	-	10	121,124	1,780	-	122,904
Office rent and occupancy expense	17,687	1,985,964	24,000	185,063	2,370,645	4,583,359	475,434	-	5,058,793
Utilities	2,447	440,529	-	14,798	201,084	658,858	64,229	-	723,087
Facility maintenance	2,818	1,179,467	9,757	2,818	3,803	1,198,663	31,229	-	1,229,892
Telephone	2,121	147,466	22,921	8,864	21,073	202,445	13,331	114	215,890
Office expense	3,715	714,396	281,170	21,064	350,731	1,371,076	348,452	37,921	1,757,449
Staff travel	225	42,691	16,446	8,911	4,361	72,634	23,383	5,160	101,177
Printing	34	6,595	10,131	692	439	17,891	1,051	92,473	111,415
Professional fees	-	134,974	159,311	188,722	22,559	505,566	837,358	71,603	1,414,527
Temporary help	-	295,167	526,314	16,999	37,984	876,464	8,987	-	885,451
Vehicle expense	11,228	71,161	165,534	71,798	-	319,721	32,351	-	352,072
Insurance	5,249	270,014	119,597	33,989	23,323	452,172	68,720	-	520,892
Recruiting	-	744	13,600	770	1,748	16,862	4,941	200	22,003
Bad debts expense	-	39,030	-	181,518	2,275	222,823			222,823
Data processing	-	-	-	930	-	930	113,994	50	114,974
Depreciation and amortization	-	66,255	212,902	19,090	648,977	947,224	257,822	-	1,205,046
Interest expense	-	-	-	-	293,933	293,933	-	-	293,933
Contribution to affiliates	-	-	-	-	-	-	61,977	-	61,977
Miscellaneous	26	56,775	3,951	13,873	153,661	228,286	88,998	9,679	326,963
Total Operating Expenses	437,528	26,052,291	6,036,753	4,831,563	6,107,429	43,465,564	5,552,566	598,023	49,616,153
Interest expense	-	134,685	-	-	-	134,685	-	-	134,685
Depreciation and amortization	-	214,251	-	-	-	214,251	-	-	214,251
Total Nonoperating Expenses	-	348,936	-	-	-	348,936	-	-	348,936
Total Expenses	$ 437,528	$ 26,401,227	$ 6,036,753	$ 4,831,563	$ 6,107,429	$ 43,814,500	$ 5,552,566	$ 598,023	$ 49,965,089

Project Renewal, Inc.

Consolidated Statement of Cash Flows
Year Ended June 30, 2012

CASH FLOWS FROM OPERATING ACTIVITIES	
Change in net assets	$5,071,849
Adjustments to reconcile change in net assets to net cash provided by operating activities	
Depreciation and amortization	1,419,297
Provision for doubtful accounts	222,823
Unrealized loss on investments	593
Gain from sale of property and equipment	(2,799,595)
Change in operating assets and liabilities:	
Accounts and grant receivables	50,757
Pledges receivable	33,878
Rent receivable	(58,441)
Prepaid expenses	15,190
Security deposits and other assets	(47,849)
Due to/from affiliates	188,746
Accounts payable and accrued expenses	(1,450,418)
Accrued payroll and related liabilities	(761,817)
Accrued interest	291,083
Deferred revenue	110,898
Deferred rent	(33,909)
Net Cash from Operating Activities	2,253,085
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of property and equipment	(1,766,398)
Proceeds from sale of property and equipment	2,810,000
Investment in rental property	(3,302,494)
Assets held for others	(174,195)
Net Cash Used in Investing Activities	(2,433,087)
CASH FLOWS FROM FINANCING ACTIVITIES	
Borrowings on construction loans	2,655,781
Debt issuance costs incurred	(586,770)
Tax credit costs	(15,000)
Payments of loan principal	(2,393,277)
Net Cash Used in Financing Activities	(339,266)
Change in Cash	(519,268)
CASH	
Beginning of year, restated	3,589,410
End of year	$3,070,142
SUPPLEMENTAL CASH FLOWS INFORMATION	
Cash paid for interest	$ 137,535

See notes to financial statements

1. Organization and Related Parties

Project Renewal, Inc. and its affiliates (the "Corporation") operate facilities in the City of New York that offer a variety of services in accessible settings to homeless and formerly homeless people suffering from mental illness, alcoholism, and substance abuse. Project Renewal, Inc. receives substantial grant awards from various Federal, New York State and City agencies. The consolidated financial statements include the following entities:

- Project Renewal Housing Development Fund Corporation ("PRI HDFC"), whose sole member is Project Renewal, Inc., provides housing for low income persons with mental illness and/or chemical dependency in the Bronx called the Fletcher Place Residence (the "Project").

- Washington OMH Corporation ("Washington OMH") the general partner of Washington Fletcher OMH L.P. ("Washington Fletcher"), a limited partnership controlled by PRI HDFC.

- Bronx Boulevard Housing Development Fund Corporation ("Bronx Boulevard HDFC"), whose sole member is Project Renewal, Inc., provides housing for men with mental illness.

Other related entities are:

- Project Renewal Fund Inc. ("PRF") a not-for-profit entity that is the sole member of Project Renewal, Inc. and other non-profit entities.

- The Corporation shares certain common facilities and management personnel with Manhattan Bowery Management Corporation ("MBMC"), a not-for-profit entity. PRF is the sole member of MBMC.

- MRG Partners, L.P. ("MRG"), operates the Holland House, a low-income rental housing project. The general partner is Starting Homes, Inc., a for-profit corporation controlled by a housing development fund corporation that is owned by PRF.

- St. Nicholas House L.P. ("St. Nicholas") operates the St. Nicholas House project for occupancy by low income tenants. The general partner is St. Nicholas House GP Corporation, a for-profit corporation controlled by a housing development fund corporation that is owned by PRF.

- North Star Housing, Inc. ("NSH"), a not-for-profit entity develops and manages affordable housing. PRF is the sole member of NSH.

2. Principles of Consolidation

These financial statements are prepared on a consolidated basis and include the activities for the year ended June 30, 2012 of entities controlled by Project Renewal, Inc. through its sole membership in not for profit entities or its controlling interest in for profit entities. The consolidated entity is collectively referred to as the "Corporation." All intercompany transactions and balances have been eliminated in consolidation.

3. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP).

Use of Estimates

The preparation of financial statements 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. Accordingly, actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents consist of highly liquid investments with maturities of three months or less at the time of purchase.

Fair Value of Financial Instruments

The Corporation follows Financial Accounting Standards Board ("FASB") guidance on fair value measurements which defines fair value and establishes a fair value hierarchy organized into three levels based upon the input assumptions used in pricing assets. Level 1 inputs have the highest reliability and are related to assets with unadjusted quoted prices in active markets. Level 2 inputs relate to assets with other than quoted prices in active markets that can be corroborated by observable market data. Level 3 inputs are observable inputs and are used to the extent that observable inputs do not exist.

Allowance for Doubtful Accounts

An allowance for doubtful accounts is established for amounts where there exists doubt as to whether an amount will be fully collected. The determination of this allowance is an estimate based on the Corporation's historical experience, review of account balances and expectations relative to collections.

3. Summary of Significant Accounting Policies *(continued)*

Deferred Debt Issuance Costs

Deferred debt issuance costs represent costs incurred to obtain long term debt. Amortization of these costs is provided using the straight-line method. The Corporation incurred debt issuance costs of $586,770 on the mortgage obtained in fiscal year 2012. At June 30, 2012, accumulated amortization was $13,855.

Property and Equipment

Property and equipment is stated at cost and depreciated using the straight-line method over the estimated useful lives of the assets as follows:

Buildings and leasehold improvements	25-30 years
Equipment	4-7 years

The Corporation capitalizes all purchases of property and equipment greater than $1,000. Equipment acquired under terms of grant provisions, title to which reverts to the grantor at the termination of the contract, is recorded as an asset.

Non-controlling Limited Partners' Interests

Non-controlling Limited Partners' Interest in the consolidated statement of activities represents the capital contributions and profits or losses of the Limited Partnership allocated to limited partners for that period. Limited Partners' Interest in the consolidated statement of financial position represents the equity in net assets of the Limited Partnership owned by limited partners.

Net Asset Presentation

The classification of the Corporation's net assets and its support, revenue and expenses is based on the existence or absence of donor-imposed restrictions. It requires that the amounts for each of three classes of net assets, permanently restricted, temporarily restricted and unrestricted, be displayed in the consolidated statement of financial position and that the amounts of change in each of those classes of net assets be displayed in the consolidated statement of activities.

The classes of net assets are defined as follows:

Permanently Restricted - Net assets resulting from contributions and other inflows of assets whose use by the Corporation is limited by donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of the Corporation.

3. Summary of Significant Accounting Policies *(continued)*

Net Asset Presentation (continued)

Temporarily Restricted - Net assets resulting from contributions and other inflows of assets whose use by the Corporation is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the Corporation pursuant to those stipulations. When such stipulations end or are fulfilled, such temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities.

Unrestricted - The part of net assets that is neither permanently nor temporarily restricted by donor-imposed stipulations.

Contributions and Pledges

Contributions received are recorded as unrestricted, temporarily restricted or permanently restricted support, depending on the existence and/or nature of any donor restrictions. Contributions with purpose or time restrictions (defined by management as unrestricted amount due in more than one year) are reported as increases in temporarily restricted net assets. When a donor restriction expires, that is, when a time restriction ends or purpose restriction is fulfilled, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions.

Unconditional promises to give are recognized as contribution revenue in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received and are classified as either unrestricted, temporarily restricted, or permanently restricted support. Promises to give are recorded at net realizable value if expected to be collected in one year. Unconditional promises to give that are expected to be collected in the future years are recorded at the present value of these estimated future cash flows.

Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at the estimated fair value.

Recognition of Revenue

Grant revenue is recognized in amounts equal to expenses incurred. Upon termination, the unexpended cash funds received under the terms of the grant provisions revert to the grantor. Grant revenue is recognized when earned.

Grant revenue received for the purchase of equipment is recorded as deferred revenue. The Corporation recognizes the revenue as the asset is amortized over the useful life of the related asset.

3. Summary of Significant Accounting Policies *(continued)*

Contract Disallowances

The contractual agreements with various funding sources include provisions for claims and program audits in subsequent years. These audits may result in disallowance and repayment of costs previously reimbursed by the funding sources. Management estimates potential disallowances based on past experiences. Accordingly, management has established a contingency reserve to cover the cost of future disallowances, if any. At June 30, 2012, the contingency reserve amounted to $361,865 and is reflected in accounts payable and other liabilities in the accompanying consolidated statement of financial position.

Nonoperating Revenue and Expenses

Nonoperating revenue and expenses include government grant income, depreciation and interest expense relating to the residential care facility for mentally ill individuals and mortgage.

Functional Allocation of Expenses

The costs of providing various program and other activities have been summarized on a functional basis in the consolidated statement of activities and in the consolidated statement of functional expenses. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Income Taxes

Project Renewal, Inc. is exempt from federal income taxes pursuant to Section 501(c)(3) of the Internal Revenue Code and from state and local taxes under comparable laws.

PRI HDFC, Bronx Boulevard HDFC and Washington OMH are for profit Corporations subject to Federal income tax and applicable state and local taxes.

The Corporation recognizes the effect of income tax positions only when they are more likely than not to be sustained. Management has determined that the Corporation had no uncertain tax positions that would require financial statement recognition. The Corporation is no longer subject to examinations by the applicable taxing jurisdictions for the periods prior to 2009.

Subsequent Events

Management has evaluated subsequent events for disclosure and/or recognition in the consolidated financial statements through the date that the consolidated financial statements were available to be issued, which is October 23, 2012.

4. Concentration of Credit Risk

The Corporation maintains its cash in bank deposit accounts with major financial institutions, which, at times, may exceed federally insured limits. The Corporation has not experienced any losses in such accounts and believes its cash balances are not exposed to any significant risk.

5. Assets Held for Others

Assets held for others consist of custodial and other funds required to be maintained in separate accounts for specific purposes or future periods. The corresponding liability is reflected in accounts payable and accrued expenses.

6. Investments

Investments stated at fair value at June 30, 2012, consist of mutual funds based on Level 1 inputs for fair value. The cost of investments is $10,000.

7. Accounts and Grants Receivable, Net

Accounts and grants receivable, net at June 30, 2012 consist of the following:

Accounts receivable	$ 832,367
Grants receivable:	
Federal	1,664,747
New York State	718,957
New York City	2,714,039
Total	5,930,110
Less: Allowance for doubtful accounts	(245,072)
Accounts and grants receivable, net	$ 5,685,038

Accounts receivable represent amounts due to the Corporation from other not-for-profit agencies and private companies for services provided by one of the Corporation's social purpose ventures that are part of employment services.

8. Pledges Receivable

Pledges receivable, net at June 30, 2012 consist of the following:

Total pledges receivable	$ 424,134
Less: Allowance for doubtful accounts	(34,000)
Pledges receivable, net	$ 390,134
Amounts due in less than one year	$ 390,134

9. Property and Equipment

Property and equipment, net at June 30, 2012 consist of the following:

Land	$ 2,272,210
Buildings	7,295,703
Equipment	4,046,843
Automobiles	1,866,070
Building and leasehold improvements	1,799,597
Mortgage acquisition costs	127,795
Construction-in-progress	1,392,414
Total	18,800,632
Accumulated depreciation and amortization	(10,845,908)
Property and equipment, net	$ 7,954,724

10. Related Party Transactions Not Disclosed Elsewhere

Such transactions with related entities are as follows:

(a) During the year ended June 30, 2012, the Corporation charged MBMC for rental expense of $94,798 and a management fee of $24,000.

(b) During the year ended June 30, 2012, the Corporation contributed $61,977 to NSH.

Amounts due (to) from related parties at June 30, 2012 are non-interest bearing, payable on demand and consist of the following:

MBMC	$ (157,761)
NSH	(590,896)
MRG	724,300
St. Nicholas	(238,748)
Total	(263,105)
Allowance for doubtful accounts	(645,895)
Total related party, net	$ (909,000)

Management considers these transactions to be conducted at arms length.

11. Mortgage Receivable and Enforcement Note Payable

The Corporation is the sponsor of the Geffner House (formally the Holland House) project, which is operated and owned by MRG. The Corporation has a $12,500,000 mortgage note receivable from MRG as a result of transferring land to the Holland House property for use in the project. Principal and interest, at the rate of 5.97% per annum, are not due and payable until December 30, 2026. MRG has paid approximately $3.7 million of interest which has been deposited into a Restricted Sponsor Reserve account maintained by the Corporation.

11. Mortgage Receivable and Enforcement Note Payable *(continued)*

This mortgage receivable is subordinated to a $12,500,000 enforcement note held by the City of New York. The enforcement note may be forgiven if the Corporation operates certain social service programs at the Geffner House site during the term of the agreement. The Corporation records the interest received from MRG as a liability until the enforcement note is either paid or forgiven.

12. Sponsor Reserve

As of June 30, 2012, the Corporation holds $8,152,519 received from MRG Partners, L.P., which represents interest received on the purchase money mortgage (Note 11). In addition, the Corporation is entitled to an escrow account with a balance of $805,770 at June 30, 2012. This escrow account is held by New York City Housing Development Corporation. According to the terms of the agreement, these funds are held in custody by the Corporation on behalf of MRG Partners, L.P. The funds may only be used for specific purposes.

13. Loans Payable

Fletcher Place Project

Construction on the Fletcher Place project is being financed using the proceeds provided to PRI HDFC of (1) a construction / permanent mortgage loan from the New York State Housing Finance Agency ("HFA") in the amount not to exceed $14,250,000 to be financed with funds from the proceeds of tax exempt Affordable Housing Revenue Bonds 2009 Series B Bonds, (2) a subordinate loan from HFA in the approximate principal amount of $200,000 (together with (1) the "HFA Loan"), (3) a building and project loan from New York State Homeless Housing and Assistance Corporation in the principal amount of $4,632,300 ("HHAC Loan"), (4) a mortgage loan from the Sponsor in the approximate principal amount of $759,205 ("Sponsor Loan"), and (5) an equity investment in the amount of $8,132,569 made in connection with the sale of Federal low income housing tax credits generated by the Project.

As a condition of the HFA Loan, Washington Fletcher secured an irrevocable standby letter of credit from JPMorgan Chase Bank, N.A. Also as a condition of the HFA Loan, Washington Fletcher will be required to enter into an agreement with HFA that will regulate the rents and incomes of eligible occupants of the Project for a period of at least 30 years.

The construction loan portion of the financing was converted to permanent financing and the Letter of Credit from JPMorgan Chase Bank, N.A. for the Project was released on October 12, 2012.

13. Loans Payable *(continued)*

Fletcher Place Project (continued)

The project is eligible to receive certain operating subsidies from OMH for management and operation of the Project and provide special services to tenants. In addition, the Corporation is eligible for debt service subsidies for payments on the HFA loan.

As of June 30, 2012, HFA and HHAC advanced $10,528,183 and $4,238,094, respectively to the Corporation.

Bronx Boulevard Construction

Construction on the Bronx Boulevard project is being financed by JP Morgan Chase Bank and Contact Fund loans for $10,222,649 and $404,747 respectively. The interest rate is 2.75% per annum plus the adjusted LIBOR rate for JP Morgan Chase Bank and 1.75% plus prime rate for Contact Fund. Both loans mature on May 3, 2014. As of June 30, 2012 JP Morgan Chase Bank and Contact Fund advanced $2,251,034 and $404,747 under the loans respectively.

Clinton Residence

The residential care facility for mentally ill individuals at the Clinton Residence is subject to a $1,229,733 mortgage note which matures in May 2015. The mortgage is payable in semiannual installments of $240,030 consisting of principal and interest at the rate of 9.42% per annum. The mortgage is secured by the building and related personal property.

Future loan amortization payments on loans payable are as follows for the years ending June 30:

2013	$ 480,060
2014	480,060
2015	480,060
	$ 1,440,180
Less: Interest payments	(210,447)
	$ 1,229,733

14. Line of Credit

The Corporation has a $3,000,000 line of credit with a financial institution maturing on January, 2013. Interest payments on all borrowings are due on a monthly basis. Interest is charged at the financial institution's prime rate (3.25% at June 30, 2012) plus 1%. The line of credit is collateralized by all property of the Corporation, MBMC and Project Renewal Fund. There were no outstanding borrowings at June 30, 2012.

15. Temporarily Restricted Net Assets

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

Treatment and transitional housing	$ 46,017
Medical	440,410
Employment services	859,517
Permanent Housing	127,157
	$ 1,473,101

Net assets were released from restrictions during the year ended June 30, 2012 by incurring expenses satisfying the restricted purposes as follows:

Treatment and transitional housing	$ 34,588
Medical	234,003
Employment services	568,832
Permanent Housing	3,060
	$ 840,483

16. Pension Plan

The Corporation has a defined contribution pension plan under Section 401(a) of the Internal Revenue Code. The Corporation makes discretionary contributions to the plan for eligible employees. There were no pension contributions or expense for the year ended June 30, 2012.

In addition, the Corporation has a defined contribution plan under Section 403(b) of the Internal Revenue Code. The Corporation does not make any matching contributions to this plan.

17. Commitments and Contingencies

Lease Commitments

The Corporation rents office space at 200 Varick Street, New York under a lease expiring June 30, 2020 with an option to extend the lease for an additional 5 years. In addition, the Corporation leases apartments, which are subleased to tenants in the supportive housing program, and storage space. Rent and occupancy expense for the year ended June 30, 2012 was $5,058,793.

17. Commitments and Contingencies *(continued)*

Minimum future lease payments under the lease agreement are payable as follows:

2013	$ 2,702,394
2014	683,576
2015	683,580
2016	683,580
2017	683,580
Thereafter	2,209,954
	$ 7,646,664

Contingencies

The Corporation is a defendant in several lawsuits that have arisen in the ordinary course of business. It is management's belief that any settlements that arise from these suits will be within the limits of the Corporation's insurance policies. Therefore, no provision has been made in the accompanying financial statements.

18. Change in Non-Controlling Limited Partners' Interests

	Total	Controlling Interest	Non-Controlling Interest
Balance, June 30, 2011	$ 1,468,053	$ -	$ 1,468,053
Net loss	(1,199,792)	(120)	(1,199,672)
Capital contributions	4,766,283	-	4,766,283
Balance, June 30, 2012	$ 5,034,544	$ (120)	$ 5,034,664

19. Prior Period Adjustment

Certain balances have been restated at July 1, 2011 to reflect the non-controlling limited partners interest in the Corporation, pursuant to FASB ASC 958-810-15-4(b), which states that a not for profit entity that is a general partner of a for profit limited partnership should apply the guidance in FASB ASC 810-20. This guidance requires that the non-controlling interest be reported in the consolidated statement of financial position within net assets.

19. Prior Period Adjustment *(continued)*

The adjustments provide for the inclusion of the assets and liabilities of Washington Fletcher at July 1, 2011 are as follows:

Cash and cash equivalents	$ 888,124
Investment in rental property	19,495,378
Due to related parties	(607,423)
Accounts payable	(2,888,938)
Mortgage payable	(15,419,534)
Net assets	(1,467,607)

* * * * *

Supplementary Financial Information

Project Renewal, Inc.

Consolidating Schedule of Financial Position
June 30, 2012

	Project Renewal, Inc.	PRI HDFC	Washington Fletcher OMH	Bronx Boulevard HDF	Eliminating Entries	Total
ASSETS						
Cash and cash equivalents	$ 2,283,015	$ 153,811	$ 495,425	$ 137,891	$ -	$ 3,070,142
Investments	31,733	-	-	-	-	31,733
Accounts and grants receivables, net	5,621,136	-	63,902	-	-	5,685,038
Pledges receivable, net	390,134	-	-	-	-	390,134
Rent receivable	-	-	58,441	-	-	58,441
Due to affiliates, net	142,237	-	154,461	-	(218,293)	78,405
Prepaid expenses	229,847	-	-		-	229,847
Tax credit monitoring fees, net	-	-	14,294	-		14,294
Security deposits and other assets, net	366,622	-	-	4,285	-	370,907
Mortgage receivable	12,500,000	14,766,261	-	-	(14,766,261)	12,500,000
Restricted Sponsor reserve	8,958,289	-	-	-	-	8,958,289
Assets held for others	979,666	-	-	-	-	979,666
Investments in rental property, net	-	-	22,163,732	-	-	22,163,732
Deferred loan costs, net	-	-	572,915	-	-	572,915
Property and equipment, net	4,858,719	-	-	3,096,005	-	7,954,724
Total Assets	$36,361,398	$14,920,072	$23,523,170	$ 3,238,181	$(14,984,554)	$63,058,267
LIABILITIES AND NET ASSETS						
Liabilities						
Accounts payable and accrued expenses	$ 3,397,819	$ -	$ 74,511	$ 219,577	$ -	$ 3,691,907
Accrued payroll and related liabilities	948,453	-	-	-	-	948,453
Accrued interest	-	-	291,083	-	-	291,083
Construction payable	-	-	941,434	-	-	941,434
Developer's fee payable	-	-	1,760,047	-	-	1,760,047
Due to affiliates	388,419	154,461	655,273	7,545	(218,293)	987,405
Deferred revenue	4,186,359	-	-	355,300	-	4,541,659
Deferred rent	879,234	-	-	-	-	879,234
Loans payable	1,229,732	14,766,261	14,766,278	2,655,781	(14,766,261)	18,651,791
Sponsor reserve held in custody	8,958,289	-	-	-	-	8,958,289
Enforcement note payable	12,500,000	-	-	-	-	12,500,000
Total Liabilities	32,488,305	14,920,722	18,488,626	3,238,203	(14,984,554)	54,151,302
Net Assets						
Unrestricted						
Operating	2,311,121	(650)	(120)	(22)	-	2,310,329
Nonoperating	88,871					88,871
Non-controlling limited partners' interest in consolidated affiliate	-	-	5,034,664	-	-	5,034,664
Total Unrestricted Net Assets	2,399,992	(650)	5,034,544	(22)	-	7,433,864
Temporarily restricted	1,473,101	-	-	-	-	1,473,101
Total Net Assets	3,873,093	(650)	5,034,544	(22)	-	8,906,965
	$36,361,398	$14,920,072	$23,523,170	$ 3,238,181	$(14,984,554)	$63,058,267

See independent auditors' report

Project Renewal, Inc.

Consolidating Schedule of Activities
Year Ended June 30, 2012

	Project Renewal, Inc.							
	Operating	Non-Operating	Total Unrestricted	Temporarily Restricted	PRI HDFC	Washington Fletcher OMH	Bronx Boulevard HDF	Total
REVENUE AND SUPPORT								
Grants	$ 42,384,726	$ 517,101	$ 42,901,827	$ -	$ -	$ -	$ -	$ 42,901,827
Rental income	2,078,136	-	2,078,136	-	-	186,588	-	2,264,724
Proceeds from sale of property	2,810,000	-	2,810,000	-	-	-	-	2,810,000
Miscellaneous income	177,801	-	177,801	-	76	-	-	177,877
Special events, net of direct benefit to donors of $100,065	693,022	-	693,022	-	-	-	-	693,022
Contributions	371,119	-	371,119	1,052,086	-	-	-	1,423,205
Net assets released from restrictions	840,483	-	840,483	(840,483)	-	-	-	-
Total Public Support and Revenue	49,355,287	517,101	49,872,388	211,603	76	186,588	-	50,270,655
EXPENSES								
Program Services								
Outreach	437,528	-	437,528	-	-	-	-	437,528
Treatment and transitional housing	26,052,291	348,936	26,401,227	-	-	-	-	26,401,227
Medical services	6,036,753	-	6,036,753	-	-	-	-	6,036,753
Employment services	4,831,563	-	4,831,563	-	-	-	-	4,831,563
Permanent housing	4,721,049	-	4,721,049	-	-	1,386,380	-	6,107,429
Total Program Services	42,079,184	348,936	42,428,120	-	-	1,386,380	-	43,814,500
Supporting services								
Management and general	5,552,279	-	5,552,279	-	265	-	22	5,552,566
Fundraising	598,023	-	598,023	-	-	-	-	598,023
Total Supporting Services	6,150,302	-	6,150,302	-	265	-	22	6,150,589
Total Expenses	48,229,486	348,936	48,578,422	-	265	1,386,380	22	49,965,089
Increase in Net Assets Before Non-Controlling Limited Partners' Capital Contributions to Consolidated Affiliate	1,125,801	168,165	1,293,966	211,603	(189)	(1,199,792)	(22)	305,566
Capital contributions	-	-	-	-	-	4,766,283	-	4,766,283
Change in Net Assets	1,125,801	168,165	1,293,966	211,603	(189)	3,566,491	(22)	5,071,849
NET ASSETS								
Beginning of the year	1,185,320	(79,294)	1,106,026	1,261,498	(461)	1,468,053	-	3,835,116
End of the year	$ 2,311,121	$ 88,871	$ 2,399,992	$ 1,473,101	$ (650)	$ 5,034,544	$ (22)	$ 8,906,965

See independent auditors' report

OMB Circular A-133 Schedules and Reports

Project Renewal, Inc. and Affiliates

Consolidated Schedule of Expenditures of Federal Awards

Year Ended June 30, 2012

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	*Federal CFDA Number*	*Pass-Through Entity Identifying Number*	*Federal Expenditures*
Health Centers Cluster			
Department of Health and Human Services Direct Programs			
Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, Public Housing Primary Care, and School Based Health Centers)	93.224		$ 2,298,842
Immunization Cluster			
Department of Health and Human Services Pass-Through Programs			
Passed-through New York City Department of Health and Mental Hygiene			
Immunization Cooperative Agreements	93.268	N/A	19,787
Non Cluster Programs			
Department of Health and Human Services Direct Programs			
Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	93.918		100,000
Substance Abuse and Mental Health Services_Projects of Regional and National Significance	93.243		425,627
Total Department of Health and Human Services Direct Programs			525,627
Department of Health and Human Services Pass-Through Programs			
Passed-through HIV Care Services			
Substance Abuse and Mental Health Services_Projects of Regional and National Significance	93.243	07-COF-779	130,287
HIV Prevention Activities_Health Department Based	93.940	07-COF-779	32,554
HIV Emergency Relief Project Grants	93.914	H89HA00015	190,216
Passed-through New York City Department of Health and Mental Hygiene			
Block Grants for Prevention and Treatment of Substance Abuse	93.959	8160810776B1	63,566
Block Grants for Community Mental Health Services	93.958	816 0810 210	145,791
Total Department of Health and Human Services Pass-Through Programs			562,414
Total Department of Health and Human Services			3,406,670

See independent auditors' report and notes to schedule of expenditures of federal awards

Project Renewal, Inc. and Affiliates

Consolidated Schedule of Expenditures of Federal Awards

Year Ended June 30, 2012

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	*Federal CFDA Number*	*Pass-Through Entity Identifying Number*	*Federal Expenditures*
continued			
Department of Housing and Urban Development Direct Programs			
Supportive Housing Program	14.235		2,568,916
Department of Housing and Urban Development Pass-Through Programs			
Passed-through New York City Department of Homeless Services			
Emergency Solutions Grant Program	14.231	20070001138/ 20070001104	597,378
Passed-through New York City Human Resources Administration			
Housing Opportunities for Persons with AIDS	14.241	20111423027	247,553
Passed-through New York State Office of Alcoholism and Substance Abuse Services			
Shelter Plus Care	14.238	C-003764 / C-003782	326,460
Total Department of Housing and Urban Development Pass-Through Programs			1,171,391
Total Department of Housing and Urban Development			3,740,307
Total Expenditures of Federal Awards			$ 7,146,977

See independent auditors' report and notes to schedule of expenditures of federal awards

Project Renewal, Inc. and Affiliates

Notes to Consolidated Schedule of Expenditures of Federal Awards

Year Ended June 30, 2012

1. Basis of Presentation

The accompanying consolidated schedule of expenditures of federal awards (the "Schedule") includes the federal grant activity for Project Renewal, Inc. and affiliates under programs of the federal government for the year ended June 30, 2012. The information in this Schedule is presented in accordance with the requirements of the Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of Project Renewal Inc. and affiliates, it is not intended to and does not represent the financial position, operations, changes in stockholders' equity or cash flows of Project Renewal Inc. and affiliates.

2. Summary of Significant Accounting Policies

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

3. Subrecipients

For the year ended June 30, 2012, Project Renewal Inc. and affiliates provided no funds to subrecipients.

O'CONNOR DAVIES

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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*

Board of Trustees
Project Renewal, Inc. and Affiliates

We have audited the consolidated financial statements of Project Renewal Inc. and affiliates (the "Organization") as of and for the year ended June 30, 2012, and have issued our report thereon dated October 23, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of the Organization is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Organization'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 Organization's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control over financial reporting.

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 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.

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 previously. However, we identified a certain deficiency in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs as Item 2012-1, that we consider to be a significant deficiency in internal control over financial reporting. A *significant deficiency* is a deficiency, or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Organization'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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the Organization in a separate letter dated October 23, 2012.

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

This report is intended solely for the information and use of the audit committee, board of directors and stockholders, management, others within the Organization, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

O'Connor Davies, LLP

New York, New York
October 23, 2012

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

Independent Auditors' Report

Board of Trustees
Project Renewal, Inc. and Affiliates

Compliance

We have audited Project Renewal Inc. and affiliates' (the "Organization") 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 Organization's major federal programs for the year ended June 30, 2012. The Organization's major federal programs are 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 grants applicable to each of its major federal programs is the responsibility of the Organization's management. Our responsibility is to express an opinion on the Organization'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 Organization'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 Organization's compliance with those requirements.

In our opinion, Project Renewal Inc. and affiliates 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.

Internal Control Over Compliance

Management of the Organization 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 Organization'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 Organization's internal control over compliance.

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

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

This report is intended solely for the information and use of the audit committee, board of directors and stockholders, management, others within the Organization, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

O'Connor Davies, LLP

New York, New York
October 23, 2012

Project Renewal, Inc. and Affiliates

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 weakness(es) identified?	____ yes __X__ no
Significant deficiency(ies) identified?	__X__ yes ____ none reported
Noncompliance material to financial statements noted?	____ yes __X__ no

Federal Awards

Internal control over major programs:	
Material weakness(es) identified?	____ yes __X__ no
Significant deficiency(ies) identified?	____ yes __X__ none reported
Type of auditors' report issued on compliance for major programs:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133?	____ yes __X__ no

Identification of major programs:

CFDA Number(s)	Name of Federal Program or Cluster
14.231	Emergency Solutions Grant Program
14.235	Supportive Housing Program
93.243	Substance Abuse and Mental Health Services Projects of Regional and National Significance

Dollar threshold used to distinguish between Type A and Type B programs:	$300,000
Auditee qualified as low-risk auditee?	__X__ yes ____ no

Project Renewal, Inc. and Affiliates

Schedule of Findings and Questioned Costs
Year Ended June 30, 2012

Section II – Financial Statement Findings

Item 2012-1 **Sage MIP Backup Failures**

Condition

MIP is the core financial application used by the Organization. We reviewed the backup methodology and the data selected for backup to ensure that the status of the backups were reviewed for successes or failures and the backup selections contained all necessary data.

During our review of the MIP backup status, we noted that a successful backup of the application has not occurred since January 2012. In our discussion with the IT Manager, we noted that the failure was a result of the server not restarting after the application responsible for performing the back-up was installed. As a result of the MIP Server not restarting, the application never registered with the central management application responsible for monitoring the back-up status. As such, the alerts configured to notify of back-up failures did not function. If the MIP data was corrupted or destroyed, the Organization would have been at risk of a significant amount of financial data loss.

We are pleased to note that the IT Manager immediately corrected the issue upon the identification of the failure. We subsequently confirmed the success of the MIP back-up.

Recommendation

We recommend that the Organization require a periodic manual review of all application back-ups to ensure all the necessary applications are registered with the back-up server and the back-ups are functioning as designed.

Management's Response

See Corrective Action Plan attached.

Section III – Federal Award Findings and Questioned Costs

During our audit, we noted no material instances of noncompliance and none of the costs reported in the federal financially assisted programs are questioned or recommended to be disallowed.

* * * * *

PROJECT RENEWAL

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Finding 2012-1 and Corrective Action Plan

Finding:	A successful backup of the MIP application had not occurred since January 2012.
Questioned cost:	None
Status:	Corrective action in progress.
Corrective action:	Management concurs with this finding. The issue was corrected immediately upon identification of the failure. In the future, the IT department will be required to provide a periodic report, with supporting documentation, indicating all the applications registered with the back-up server and the status of all critical back-ups.