

**Zufall Health Center, Inc.**

**Financial Statements,  
Schedule of Expenditures of Federal and  
State Awards, Internal Control and Compliance  
(With Supplementary Information)  
and Independent Auditor's Report**

**December 31, 2012**

# Zufall Health Center, Inc.

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## Independent Auditor's Report

To the Board of Directors  
Zufall Health Center, Inc.

### *Report on the Financial Statements*

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

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Center's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

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

### *Other Matters*

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of Federal and state awards, as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and State of New Jersey, Department of Treasury, Office of Management and Budget Circular 04-04, Single Audit Policy for Recipients of Federal Grants, State Grants and State Aid, is presented for purposes of additional analysis and is not a required part of the financial statements. The schedules of disbursements by grant included in the accompanying financial statements on pages 26 through 28 are presented for purposes of additional analysis and are not a required part of the financial statements. The schedule of expenditures of Federal and state awards and schedules of disbursements by grant are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole. The financial statements of the Center as of December 31, 2011, none of which are presented herein, were audited by other auditors whose report dated September 21, 2012, expressed an unqualified opinion on those statements. The December 31, 2011 Schedule of Disbursements by Grant – Prior Year Expenditures on pages 26 through 28 was subjected to the auditing procedures applied in the December 31, 2011 audit of the basic financial statements by other auditors, whose report on such information stated that it was fairly stated in all material respects in relation to the December 31, 2011 financial statements as a whole.

### *Other Reporting Required by Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 26, 2013 on our consideration of the Center's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Center's internal control over financial reporting and compliance.

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

New York, New York  
September 26, 2013

Zufall Health Center, Inc.

Statement of Financial Position  
December 31, 2012

Assets

Current assets:	
Cash and cash equivalents	\$ 1,305,770
Investments	2,099,869
Patient services receivable, net	905,925
Contracts and other grants receivable	359,279
Prepaid expenses and other current assets	152,123
Total current assets	<u>4,822,966</u>
Property and equipment, net	7,681,502
Security deposits	9,300
Total assets	<u>\$ 12,513,768</u>

Liabilities and Net Assets

Current liabilities:	
Accounts payable and accrued expenses	\$ 655,242
Accrued payroll and employee benefits	300,703
Refundable advances	220,639
Current portion of mortgage payable	15,065
Total current liabilities	<u>1,191,649</u>
Mortgage payable	749,106
Total liabilities	<u>1,940,755</u>
Commitments and contingencies	
Net assets:	
Unrestricted:	
Undesignated	8,493,118
Board-designated	1,679,895
Total unrestricted net assets	<u>10,173,013</u>
Temporarily restricted net assets	400,000
Total net assets	<u>10,573,013</u>
Total liabilities and net assets	<u>\$ 12,513,768</u>

See Notes to Financial Statements.

Zufall Health Center, Inc.

Statement of Activities and Changes in Net Assets  
Year Ended December 31, 2012

	Unrestricted	Temporarily Restricted	Total
Revenue:			
Patient services (net of contractual allowances)	\$ 5,661,050		\$ 5,661,050
Provision for bad debts	(139,698)		(139,698)
Net patient services revenue net of provision for bad debts	5,521,352		5,521,352
DHHS grants	2,619,428		2,619,428
Contract services and other grants	713,053		713,053
340B pharmacy	434,228		434,228
Meaningful use incentive	148,750		148,750
Donated vaccines	309,255		309,255
Other	348,990		348,990
Total revenue	<u>10,095,056</u>		<u>10,095,056</u>
Expenses:			
Salaries and related taxes and benefits	6,311,926		6,311,926
Other than personnel services	2,671,620		2,671,620
Interest	35,048		35,048
Total expenses	<u>9,018,594</u>		<u>9,018,594</u>
Operating income prior to depreciation and amortization and nonoperating revenue	1,076,462		1,076,462
Depreciation and amortization	234,062		234,062
Income from operations	842,400		842,400
Nonoperating revenue - DHHS capital grants	<u>2,846,577</u>		<u>2,846,577</u>
Increase in net assets	3,688,977		3,688,977
Net assets, beginning of year	<u>6,484,036</u>	\$ 400,000	<u>6,884,036</u>
Net assets, end of year	<u>\$ 10,173,013</u>	<u>\$ 400,000</u>	<u>\$ 10,573,013</u>

**Zufall Health Center, Inc.**

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

	Program Services	General and Administrative	Total
Salaries and wages	\$ 4,274,864	\$ 921,956	\$ 5,196,820
Payroll taxes and fringe benefits	917,278	197,828	1,115,106
Consultants and contractual services	388,261	63,497	451,758
Insurance	33,089	8,793	41,882
Consumable supplies	1,071,436		1,071,436
Occupancy	64,213	17,063	81,276
Equipment rental and maintenance	75,825	20,214	96,039
Office expenses	215,558	69,306	284,864
Professional fees		72,720	72,720
Utilities	73,557	19,547	93,104
Repairs and maintenance	86,358	4,784	91,142
Licenses and fees	23,897	2,280	26,177
Public information	31,574	6,075	37,649
Dues and subscriptions	42,507	8,212	50,719
Travel, conferences and meetings	36,643	50,810	87,453
Telephone	26,564	7,978	34,542
Interest		35,048	35,048
Other	112,263	38,596	150,859
Total	7,473,887	1,544,707	9,018,594
Depreciation and amortization	184,924	49,138	234,062
Total functional expenses	\$ 7,658,811	\$ 1,593,845	\$ 9,252,656

See Notes to Financial Statements.

**Zufall Health Center, Inc.**  
**Statement of Cash Flows**  
**Year Ended December 31, 2012**

Cash flows from operating activities:	
Cash received from patient services	\$ 5,561,776
Cash received from contract services and other grants	3,741,608
Cash received from 340(B) pharmacy revenue	392,963
Cash received from meaningful use incentive	148,750
Cash received from other	181,470
Cash paid to employees	(6,254,191)
Cash paid to vendors	(2,397,258)
Cash paid for interest	(35,048)
Net cash provided by operating activities	<u>1,340,070</u>
Cash flows from investing activities:	
Purchase of property and equipment	(3,518,305)
Proceeds from sale of investments	260,455
Purchase of investments	(308,568)
Net cash used in investing activities	<u>(3,566,418)</u>
Cash flows from financing activities:	
Payment of mortgage	(15,005)
Proceeds from non-operating DHHS capital grants	2,846,577
Net cash provided by financing activities	<u>2,831,572</u>
Net increase in cash and cash equivalents	605,224
Cash and cash equivalents, beginning of year	<u>700,546</u>
Cash and cash equivalents, end of year	<u>\$ 1,305,770</u>
Reconciliation of increase in net assets to net cash provided by operating activities:	
Increase in net assets	\$ 3,688,977
Adjustments to reconcile increase in net assets to net cash provided by operating activities:	
Non-operating DHHS capital grants	(2,846,577)
Provision for bad debts	139,698
Depreciation and amortization	234,062
Realized and unrealized gain on investments	(155,353)
Donated investment included in other income	(24,508)
Changes in operating assets and liabilities:	
Patient services receivable	(252,829)
Grants and contracts receivable	409,127
Prepaid expenses and other current assets	(25,624)
Security deposits	(3,300)
Accounts payable and accrued expenses	(34,893)
Accrued payroll and employee benefits	57,735
Refundable advances	153,555
Net cash provided by operating activities	<u>\$ 1,340,070</u>

See Notes to Financial Statements.

## Zufall Health Center, Inc.

### Notes to Financial Statements

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

##### **Organization:**

Zufall Health Center, Inc. (the "Center") operates healthcare centers across four counties in Northwest New Jersey: Morris, Warren, Sussex and Hunterdon. The Center provides a broad range of health services to a largely medically underserved population.

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

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

The accompanying financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America.

##### **Use of estimates:**

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

##### **Classification of net assets:**

The Center reports information regarding its financial position and activities according to the following three categories:

Unrestricted net assets are not externally restricted for identified purposes by donors or grantors. Unrestricted net assets include resources that the governing board may use for any designated purpose and resources whose use is limited by agreement between the Center and an outside party other than a donor or grantor.

Temporarily restricted net assets are those whose use by the Center has been limited by donors to a specific purpose. When donor restrictions expire, that is, when a time restriction ends or a purpose restriction is accomplished, temporarily restricted net assets are recorded as net assets released from restrictions.

Permanently restricted net assets are net assets whose use is limited by donor-imposed stipulations that neither expire by the passage of time nor can be fulfilled or otherwise removed by actions of the Center. Generally, the donors of these assets permit the Center to use all or part of the income earned on related investments for general or specific purposes. The Center does not have any permanently restricted net assets at December 31, 2012.

## Zufall Health Center, Inc.

### Notes to Financial Statements

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

The Center maintains its cash and cash equivalents in bank deposit accounts which, at times, may exceed Federally-insured limits. The Center has not experienced any losses in such accounts. At December 31, 2012, the Center's cash and cash equivalents balance did not exceed Federally-insured limits. All highly liquid investments with maturities of three months or less when purchased are considered to be cash equivalents.

#### **Investments:**

Investments are comprised of common stocks, mutual funds, exchange traded funds and fixed income instruments which are valued at fair value with realized and unrealized gains and losses included in the statement of activities and changes in net assets. Realized gains or losses are recognized on the specific identification method.

#### **Patient services receivable:**

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

Receivables due directly from patients are carried at the original charge for the service provided less discounts provided under the Center's charity care policy, less amounts covered by third-party payors and less an estimated allowance for doubtful receivables. Management determines the allowance for doubtful accounts by identifying troubled accounts and by historical experience applied to an aging of accounts. The Center considers accounts past due when they are outstanding beyond 90 days with no payment. The Center generally does not charge interest on past due accounts. Patient receivables are written-off against the allowance for doubtful accounts when deemed uncollectible. Recoveries of receivables previously written-off are recorded as a reduction of bad debt expense when received.

#### **Concentrations of credit risk:**

Financial instruments that potentially subject the Center to concentrations of credit risk consist principally of cash and cash equivalents, patient services receivable, grants receivable and contracts receivable. The Center places its cash and cash equivalents with high-quality financial institutions. The Center monitors its financial institutions and the concentration of credit risk on a regular basis and does not anticipate nonperformance by the financial institutions.

**Zufall Health Center, Inc.**

**Notes to Financial Statements**

Patient services receivable credit risk is limited because the receivables are reported at their outstanding unpaid principal balances reduced by an allowance for doubtful accounts. The Center estimates doubtful accounts based on historical bad debts, factors related to specific payors' ability to pay and current economic trends. The Center writes off accounts receivable against the allowance when a balance is determined to be uncollectible.

Contracts and other grants receivable credit risk is limited due to the nature of the contracts and grants. The Center regularly monitors its contracts and other grants receivable by investigating delayed payments and differences when payments received do not conform to the amount billed. The Center considers all contracts and grants as collectible.

**Property and equipment:**

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization is calculated using the straight-line method over the estimated useful lives of the assets ranging from 5-40 years. Leasehold improvements are amortized over the shorter of the useful life of the asset or the lease term. Expenditures over \$5,000 are capitalized. Maintenance, repairs and minor renewals are expensed as incurred. When assets are retired or otherwise disposed of, their costs and related accumulated depreciation and amortization are removed from the accounts and any resulting gains or losses are included in changes in net assets.

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

According to Federal regulations, any property and equipment obtained through Federal funds are subject to a lien by the Federal government. Provided that the Center maintains its tax-exempt status and the property and equipment are used for their intended purpose, the Center is not required to reimburse the Federal government. If the stated requirements are not met, the Center would be obligated to the Federal government in an amount equal to the fair value of the property and equipment.

## Zufall Health Center, Inc.

### Notes to Financial Statements

#### **Impairment of long-lived assets:**

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

#### **Patient services revenue:**

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

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

Revenue from government grants and contracts designated for use in specific activities is recognized in the period when the expenditures have been incurred in compliance with the grantor's restrictions. Grants and contract awards for the acquisition of long-lived assets are reported as unrestricted nonoperating revenue, in the absence of donor stipulations to the contrary, during the fiscal year in which the assets are acquired. Cash received in excess of revenue recognized is recorded as refundable advances.

At December 31, 2012, the Center has received conditional grants and contracts from governmental and private entities in the aggregate amount of approximately \$3,398,600 that have not been recorded in the accompanying financial statements as they have not yet been earned. These grants require the Center to provide certain services during specified periods. If such services are not provided, the governmental entities are not obligated to expend the funds allotted under the grants.

## Zufall Health Center, Inc.

### Notes to Financial Statements

#### **340B pharmacy revenue:**

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

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

Donated vaccines are recognized in the accompanying financial statements based on fair value. Donated vaccines received in 2012 amounted to \$309,255.

#### **Contributions:**

Contributions are recorded at fair value when received or pledged. Amounts are recorded as temporarily or permanently restricted revenue if they are received with donor stipulations that limit the use of the donated asset. Contributions received with no donor stipulations are recorded as unrestricted revenue. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statement of activities and changes in net assets as net assets released from restrictions. Donor restricted contributions whose restrictions expire during the same fiscal year are recognized as unrestricted revenue. Conditional contributions are recognized in the period when expenditures have been incurred in compliance with the grantor’s restrictions.

#### **Meaningful use incentive:**

The American Recovery and Reinvestment Act of 2009 (“ARRA”) amended the Social Security Act to establish one-time incentive payments under the Medicare and Medicaid programs for certain professionals that: (1) meaningfully use certified Electronic Health Record (“EHR”) technology, (2) use the certified EHR technology for electronic exchange of health information to improve quality of healthcare, and (3) use the certified EHR technology to submit clinical and quality measures. These provisions of ARRA, together with certain of its other provisions, are referred to as the Health Information Technology for Clinical and Economic Health (“HITECH”) Act. The criteria for meaningful use incentives will be staged in three steps over the course of the next six years and be paid out based on a transitional schedule. The Center’s providers have met the criteria for Stage 1 and have earned \$148,750 from the Medicaid incentive program for the year ended December 31, 2012.

#### **Interest earned on Federal funds:**

Interest earned on Federal funds is recorded as a payable to the United States Public Health Services (“PHS”) in compliance with the regulations of the United States Office of Management and Budget.

## Zufall Health Center, Inc.

### Notes to Financial Statements

#### Functional expenses:

The cost of providing the various services and other activities has been summarized on a functional basis in the statement of functional expenses. Accordingly, certain costs have been charged to program services or general and administrative based on a combination of specific identification and allocation by management.

#### Performance indicator:

The statement of activities and changes in net assets includes operating income prior to non-operating activities as the performance indicator. Changes in unrestricted net assets which are excluded from the performance indicator include capital grants.

#### Tax status:

The Center was incorporated as a not-for-profit corporation under the laws of the State of New Jersey and is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. Therefore, there is no provision for income taxes.

The Center has no unrecognized tax benefits at December 31, 2012. The Center's Federal and state income tax returns prior to fiscal years 2009 and 2008, respectively, are closed and management continually evaluates expiring statutes of limitations, audits, proposed settlements, changes in tax law and new authoritative rulings.

The Center recognizes interest and penalties associated with tax matters such as operating expenses and includes accrued interest and penalties with accrued expenses in the statement of financial position.

The Center has filed all required payroll tax returns and payroll taxes due have been paid.

#### Subsequent events:

The Center has evaluated subsequent events through September 26, 2013, which is the date the financial statements were available to be issued (see Note 15).

#### Note 2 - Patients services receivable:

Patient services receivable, net, consist of the following at December 31:

Medicaid (including Medicaid managed care)	\$ 321,754
Medicare	144,494
Private insurance	76,410
New Jersey Managed Care Wraparound	236,656
New Jersey Uncompensated Care	<u>404,403</u>
Total	1,183,717
Less allowance for doubtful accounts	<u>277,792</u>
Total	<u>\$ 905,925</u>

**Zufall Health Center, Inc.**

**Notes to Financial Statements**

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

The Center's allowance for doubtful accounts was 23 percent of patient services receivable at December 31, 2012. The Center had \$442,418 of direct write-offs for the year ended December 31, 2012. The Center has not changed its charity care or uninsured discount policies during fiscal year 2012.

**Note 3 - Contracts and other grants receivable:**

Contracts and other grants receivable consist of the following at December 31:

U.S. Department of Health and Human Services	\$236,112
New Jersey Department of Health and Senior Services	101,046
Other	<u>22,121</u>
Totals	<u>\$359,279</u>

## Zufall Health Center, Inc.

### Notes to Financial Statements

#### Note 4 - Investments:

At December 31, 2012, investments consisted of the following:

	<u>Cost</u>	<u>Fair Value</u>
Investments:		
Common stocks	\$ 452,068	\$ 557,245
Mutual funds	1,240,437	1,382,509
Exchange traded funds	126,857	120,040
Fixed income	<u>40,000</u>	<u>40,075</u>
Total	<u>\$1,859,362</u>	<u>\$2,099,869</u>

Realized (loss) and unrealized gains on investments for the year ended December 31, 2012 are as follows:

Investments:	
Realized losses	\$ (7,634)
Unrealized gains	<u>162,987</u>
Total	<u>\$155,353</u>

Realized and unrealized gains on investments are recorded under other revenues in the statement of activities and changes in net assets.

#### Note 5 - Fair value measurements:

The Center values its financial assets based on the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, a fair value hierarchy prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in inactive markets; or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated with observable market data.

Level 3: Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

## Zufall Health Center, Inc.

### Notes to Financial Statements

In determining fair value, the Center utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible as well as considers counterparty credit risk in its assessment of fair value.

The following table sets forth by level, within the fair value hierarchy, the Center's investments as of December 31, 2012:

	Assets at Fair Value as of December 31, 2012			
	Level 1	Level 2	Level 3	Total
Fixed income		\$ 40,075		\$ 40,075
Common stocks:				
Financial	\$ 55,871			55,871
Healthcare	72,213			72,213
Technology	74,665			74,665
Services	145,452			145,452
Basic materials	86,060			86,060
Industrial goods	38,136			38,136
Consumer goods	50,673			50,673
Investment manager	19,734			19,734
Utilities	14,441			14,441
Mutual funds:				
Index fund	124,659			124,659
Short-term bond	333,862			333,862
Nontraditional bond	331,040			331,040
Multi-national interim	118,287			118,287
Small blend	20,090			20,090
Small value	31,367			31,367
Diversified emerging markets	193,306			193,306
Foreign small/mid value	123,734			123,734
Market neutral	76,407			76,407
Equity-energy	29,757			29,757
Exchange-traded funds:				
Index fund	80,772			80,772
Equity-energy	39,268			39,268
	<u>\$ 2,059,794</u>	<u>\$ 40,075</u>	<u>\$ -</u>	<u>\$ 2,099,869</u>

The following is a description of the valuation methodologies used for investments at fair value.

Investments in common stocks, mutual funds and exchange traded funds are designated as Level 1 and are valued using market prices on active markets and valuations are obtained from real-time quotes for transactions in active exchange markets involving identical assets.

Investments in fixed income securities which are certificates of deposit are designated as Level 2 and are valued using real-time quotes for transactions in active exchange markets involving similar assets.

**Zufall Health Center, Inc.**

**Notes to Financial Statements**

The preceding methods may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Center believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The Center's policy is to recognize transfers into and transfers out of a level as of the actual date of the event or change in circumstance that caused the transfer. There were no transfers among the three levels in 2012.

**Note 6 - Property and equipment:**

Property and equipment consists of the following at December 31, 2012:

Land and buildings	\$1,488,990
Building and leasehold improvements	5,467,629
Vehicles	313,987
Furniture and equipment	<u>1,271,084</u>
Total	8,541,690
Less accumulated depreciation and amortization	<u>(965,506)</u>
Sub-total	7,576,184
Construction in progress	<u>105,318</u>
Total	<u>\$7,681,502</u>

In the event the DHHS grants are terminated, the DHHS reserves the right to transfer all property and equipment purchased with grant funds to the PHS or third parties.

No depreciation has been provided on assets classified as construction in progress as these assets have not yet been placed in service.

**Note 7 - Refundable advances:**

Refundable advances consist of the following at December 31, 2012:

New Jersey Department of Health and Senior Services	\$ 22,244
Community Foundation of New Jersey	80,000
The Horizon Foundation for New Jersey	50,000
Susan G. Komen Foundation	11,904
NJPCA Veterans' Community	10,000
Other	<u>46,491</u>
Total	<u>\$ 220,639</u>

**Zufall Health Center, Inc.**

**Notes to Financial Statements**

**Note 8 - Mortgage Payable:**

Long-term debt consists of Mortgage Payable - \$800,000 face amount, maturing on July 14, 2020, payable in equal monthly installments of \$5,258. Under the agreement, the Fulton Bank of New Jersey shall provide financing up to a maximum amount of \$800,000 for a period of 10 years commencing on July 14, 2010 and maturing on July 14, 2020. Interest on the outstanding principal is fixed at 6.125% per year and may change every five years thereafter beginning on July 14, 2015 based on the five-year Federal Home Loan rate of the Bank of New York plus 3%, subject to a minimum interest rate of 6% and a maximum interest rate of 9.5%. Unpaid principal and interest of approximately \$614,000 on July 14, 2020 will be due on July 14, 2020. The properties located at 18 West Blackwell Street and 23-25 South Warrant Street both in Dover, New Jersey, serve as collateral for the loan; such properties had net book values of \$4,474,521 and \$99,905, respectively, as of December 31, 2012.

Outstanding amounts of mortgage payable at December 31, 2012 are as follows:

Mortgage payable balance	\$764,171
Less current portion	<u>15,065</u>
Long-term portion	<u>\$749,106</u>

Future maturities of long-term debt in each of the five years subsequent to December 31, 2012 and thereafter are as follows:

<u>Year Ending</u> <u>December 31,</u>	<u>Amount</u>
2013	\$ 15,065
2014	17,052
2015	18,161
2016	19,301
2017	21,846
Thereafter	<u>672,746</u>
Total	<u>\$764,171</u>

**Zufall Health Center, Inc.**

**Notes to Financial Statements**

**Note 9 - Temporarily Restricted Net Assets:**

On September 6, 2000, the Center purchased the building located at 17-19 South Warren Street, Dover, New Jersey for \$400,000, using funds borrowed from the Town of Dover, New Jersey. The Town of Dover applied for and received, a \$400,000 Community Development Block Grant to acquire a property to be owned and operated by the Center. This is an eligible activity under Section 105(a)(14) of the Housing and Community Development Act of 1974, as amended, provided that the Center property be located at 17-19 South Warren Street in Dover, New Jersey and serve low and moderate-income persons.

As part of the grant terms, a loan agreement between the Town of Dover and the Center setting forth the terms of the assistance and the activities authorized was incorporated into this grant agreement, whereby \$400,000 of the amount borrowed was for acquisition of the premises which is the subject matter of this loan and constituted a loan at 0% interest and was recorded as a TRNA due to the nature of the agreement. If the Center ceases to use the premises as a community clinic serving low and moderate-income persons or if the Center ceases to exist temporarily restricted net assets will be decreased then the title to the premises will revert to the Town of Dover and the loan will be forgiven in full.

**Note 10 - Patient services revenue, net:**

The Center recognizes patient service revenue associated with services provided to patients who have Medicaid, Medicare, third party payor and managed care plans coverage on the basis of contractual rates for services rendered. For uninsured patients that do not qualify for charity care, the Center recognizes revenue on the basis of its standard rates for services provided or on the basis of discounted rates, if negotiated or provided by policy. Charity care services are computed using a sliding fee scale based on patient income and family size. On the basis of historical experience, a significant portion of the Center's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Center records a significant provision for bad debts related to uninsured patients in the period the services are provided. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the period from these major payor sources, is as follows:

Medicaid (including Medicaid managed care)	\$1,104,966
Medicare	204,568
Self-pay	1,087,439
Private insurance	97,573
New Jersey Managed Care Wraparound	704,326
New Jersey uncompensated care	<u>2,462,178</u>
Total	<u>\$5,661,050</u>

Based on the cost of patient services, charity care and community benefit expenses for the year ended December 31, 2012 amounted to approximately \$2,000,000 and \$600,000 respectively.

**Zufall Health Center, Inc.**

**Notes to Financial Statements**

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

**Note 11 - DHHS grants:**

For the year ended December 31, 2012, the Center recognized grant revenue from the DHHS as follows:

<u>Grant Number</u>	<u>Grant Period</u>	<u>Total Grant</u>	<u>Revenue Recognized</u>
6H80CS04211-08-05	12/01/11 – 11/30/12	\$ 2,468,874	\$ 2,278,457
6H80CS04211-09-10	12/01/12 – 11/30/13	2,576,304	195,879
1H76HA24737-01-00	07/01/12 – 06/30/13	290,184	<u>145,092</u>
Sub-total			<u>2,619,428</u>
Non-operating: capital grant			
1C80CS17142-01-00	12/09/09 – 05/31/12	3,920,442	2,833,277
4C76HF19672-01-00	09/01/10 – 05/31/13	222,750	2,400
1C8BCS23952-01-00	05/01/12 – 04/30/14	481,954	<u>10,900</u>
Sub-total			<u>2,846,577</u>
Total			<u>\$5,466,005</u>

**Note 12 - Contract services and other grants:**

For the year ended December 31, 2012, contracts and other grants revenue consist of the following:

City of Newark:	
Ryan White Part A	\$ 125,935
New Jersey Department of Health and Senior Services:	
Affordable Care Act – Medicare Improvements for patients and providers	19,554
Operation of Offices of Rural Health	95,426
Daiichi Sankyo	170,000
Robert Wood Johnson Foundation	44,086
The Horizon Foundation of New Jersey	50,000
Susan G. Komen Foundation	46,556
Johnson & Johnson Behavioral Health	44,237
Community Foundation of New Jersey	37,000
Delta Dental	25,000
Other	<u>55,259</u>
Total	<u>\$713,053</u>

## Zufall Health Center, Inc.

### Notes to Financial Statements

#### **Note 13 - Retirement plan:**

The Zufall Health Center, Inc. Employees' Retirement Plan (the "Plan") is a defined contribution plan established on June 1, 2008. It is available to substantially all employees of the Center who have attained 21 years of age and who have completed one year of eligible service with a minimum of 1,000 hours of service. Contributions may be invested in available investment funds elected by the employee. The Plan has met the requirements of the Employee Retirement Income Security Act of 1974 ("ERISA") and is therefore subject to the provisions of ERISA. The Plan provides for benefit distributions to Plan participants or their beneficiaries upon the participant's retirement, termination of employment or death. Any participant may apply to borrow all or part of his or her vested account balance subject to criteria in the Plan set by Internal Revenue Service regulations and limits and the approval of the Plan administrator. Participants are fully vested after five years of service in the employer match but forfeit all of the employer contributions and earnings thereon if the participant leaves with less than two years of service. Pension expense for 2012 amounted to \$124,813.

Effective January 1, 2012, the Center established a 162 Bonus Plan which provides eligible employees discretionary bonuses intended to fund certain life insurance benefits. The bonus plan is exempt from ERISA. Employees become eligible to participate on the 1<sup>st</sup> day of the plan year upon completing 3 years of service on the 30<sup>th</sup> of September of the same plan year. The Center's discretionary contribution to the bonus plan shall be used to pay for the premium on the participating employees' life insurance policy. The Center contributed \$116,319 to the bonus plan for the year ended December 31, 2012; the expense is included in salaries and related taxes and benefits in the statement of activities and changes in net assets.

#### **Note 14 - Commitments and contingencies:**

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

The Center maintains its medical malpractice coverage under the Federal Tort Claims Act ("FTCA"). FTCA provides malpractice coverage to eligible PHS-supported programs and applies to the Center and its employees while providing services within the scope of employment included under grant-related activities. The Attorney General, through the U.S. Department of Justice, has the responsibility for the defense of the individual and/or grantee for malpractice cases approved for FTCA coverage.

## Zufall Health Center, Inc.

### Notes to Financial Statements

The healthcare industry is subject to voluminous and complex laws and regulations of Federal, state and local governments. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement laws and regulations, anti-kickback and anti-referral laws, and false claims prohibitions. In recent years, government activity has increased with respect to investigations and allegations concerning possible violations of reimbursement, false claims, anti-kickback and anti-referral statutes and regulation by healthcare providers. The Center believes that it is in material compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. Upon audit, if discrepancies are discovered, the Center could be held responsible for refunding the amount in question.

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

The Center entered into various lease agreements for the use of space and office equipment which have been classified as operating leases and expire through December 31, 2016. As of December 31, 2012, the Center is obligated to make future minimum payments in each of the subsequent years as follows:

<u>Year Ending</u> <u>December 31,</u>	<u>Amount</u>
2013	\$ 60,907
2014	62,598
2015	57,614
2016	33,953
Total	<u>\$ 215,072</u>

Rent expense under these operating leases was \$81,276.

## Zufall Health Center, Inc.

### Notes to Financial Statements

#### **Note 15 - Subsequent event:**

On July 15, 2013, the Center entered into a memorandum of agreement (“MOA”) with a not-for-profit, community-based medical practice that provides primary, preventative and healthcare services. The MOA was entered for the purpose of a merger between the Center and the other entity. Under the MOA, the parties agreed to a January 1, 2014 merger effectivity date, unless both parties agree to postpone such date. As of the date of this report, the two parties are still in the process of creating a plan of merger.

**Zufall Health Center, Inc.**

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

Federal Grantor/ Pass-through Grantor/Program Title	Federal CFDA Number	Pass-through Grantor's Number	Total Expenditures
Federal awards:			
U.S. Department of Health and Human Services:			
Health Center Cluster:			
Consolidated Health Centers	93.224	N/A	\$ 1,707,215
Affordable Care Act (ACA) Grants for New and Expanded Services under the Health Center Program	93.527	N/A	767,121
Total - Health Center Cluster			<u>2,474,336</u>
ARRA - Grants to Health Center Programs:			
Facility Investment Program	93.703	N/A	2,833,277
Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	93.918	N/A	145,092
Health Care and Other Facilities	93.887	N/A	2,400
Affordable Care Act (ACA) Grants for Capital Development in Health Centers	93.526	N/A	10,900
Passed through New Jersey Department of Health and and Senior Services:			
National Bioterrorism Hospital Preparedness Program	93.889	PHLP12MNI041	18,759
Affordable Care Act (ACA) Medicare Improvements for Patients and Providers (MIPPA)	93.518	DACS11MPB004	19,554
Centers for Disease Control and Prevention Investigations and Technical Assistance	93.283	DFHS12CED023	55,666
Grants to States for Operation of Offices of Rural Health	93.913	DFHS13CED024	39,760
Total New Jersey Cancer Education and Early Detection			<u>95,426</u>
Passed through City of Newark, Department of Child and and Family Well-Being:			
HIV Emergency Relief Project Grants	93.914	N/A	125,935
Total Federal awards			<u><u>\$ 5,725,679</u></u>
State awards:			
State of New Jersey Department of Health and Senior Services:			
Preventive and Primary Care Program	N/A	05-2192-CHS-N-0	*

\* See Note 4 to the Schedule of Expenditures of Federal and State Awards.

See Notes to Schedule of Expenditures of Federal and State Awards.

## Zufall Health Center, Inc.

### Notes to Schedule of Expenditures of Federal and State Awards

#### **Note 1 - General information:**

The accompanying schedule of expenditures of Federal and state awards (the "Schedule") presents the activities in all Federal and state awards of Zufall Health Center, Inc. (the "Center") and is presented using the accrual basis of accounting. The Federal awards were provided primarily by the U.S. Department of Health and Human Services, while the state awards were provided by the New Jersey Department of Health and Senior Services.

#### **Note 2 - Basis of presentation:**

The accompanying Schedule has been prepared in the format required under OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and State of New Jersey Department of Treasury Circular OMB 04-04, Single Audit Policy for Recipients of Federal Grants, State Grants, and State Aid. The purpose of this Schedule is to present a summary of those grant activities of the Center for the year ended December 31, 2012, which have been financed, in part, by the Federal and state governments. For the purpose of this Schedule, Federal and state awards include any assistance provided by Federal and state governments directly or indirectly in the form of grants, contracts, cooperative agreements, loans, loan guarantees, property, interest subsidies, insurance, direct appropriations and other noncash assistance.

#### **Note 3 - Relationship to the financial statements:**

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

#### **Note 4 - Preventive and Primary Care Program:**

The Center contracted with the State of New Jersey Department of Health to provide health and medical services to the uninsured population under the Preventive and Primary Care Program. This letter of agreement pays the Center a fixed amount per visit regardless of the actual costs incurred. During the year ended December 31, 2012, the amount earned and recognized as net revenue under this letter of agreement for the contract period July 1, 2011 to June 30, 2012 was \$1,202,102 and for the contract period July 1, 2012 to June 30, 2013 was \$1,260,076.

Revenue for this program is included in patient services revenue in the basic financial statements. Allowances are calculated based on expected cash collections.

Zufall Health Center, Inc.

Schedule of Disbursements by Grant  
Year Ended December 31, 2012

Award: Medicare Improvements for Patients and Providers Act (MIPPA)  
Grant Year: April 1, 2011 - March 31, 2012  
Grant Number: DACS11MPB004

Category	(Unaudited) Final Budget	Prior Year Expenditures	Current Year Expenditures	Final Expenditures Expenditures	Questioned Costs
<b>PERSONNEL:</b>					
Salaries	\$ 45,508	\$ 34,131	\$ 11,377	\$ 45,508	\$ -
Fringe benefits	9,102	6,826	2,274	9,100	
TOTAL PERSONNEL	54,610	40,957	13,651	54,608	
<b>OTHER COST CATEGORIES:</b>					
Facility costs					
Office expense and related costs					
Program expense and related costs	6,000	2,363	4,950	7,313	
Travel, conference and meetings	4,390	2,126	953	3,079	
TOTAL DIRECT COSTS	65,000	45,446	19,554	65,000	
<b>INDIRECT COSTS</b>					
TOTAL COSTS	65,000	45,446	19,554	65,000	
Less program income					
<b>NET TOTAL COSTS</b>	<u>\$ 65,000</u>	<u>\$ 45,446</u>	<u>\$ 19,554</u>	<u>\$ 65,000</u>	<u>\$ -</u>

Zufall Health Center, Inc.

Schedule of Disbursements by Grant  
Year Ended December 31, 2012

Award: New Jersey Cancer Education and Early Detection  
Grant Year: July 1, 2011 - June 30, 2012  
Grant Number: DFHS12CED023

Category	(Unaudited) Final Budget	Prior Year Expenditures	Current Year Expenditures	Total Program Expenditures	Questioned Costs
<b>PERSONNEL:</b>					
Salaries	\$ 94,746	\$ 48,438	\$ 46,308	\$ 94,746	\$ -
Fringe benefits	19,186	9,809	9,377	19,186	
TOTAL PERSONNEL	113,932	58,247	55,685	113,932	
<b>OTHER COST CATEGORIES:</b>					
Facility costs					
Office expense and related costs					
Program expense and related costs					
Travel, conference and meetings	139	158	(19)	139	
TOTAL DIRECT COSTS	114,071	58,405	55,666	114,071	
<b>INDIRECT COSTS</b>					
TOTAL COSTS	114,071	58,405	55,666	114,071	
Less program income					
<b>NET TOTAL COSTS</b>	<u>\$ 114,071</u>	<u>\$ 58,405</u>	<u>\$ 55,666</u>	<u>\$ 114,071</u>	<u>\$ -</u>

**Zufall Health Center, Inc.**

**Schedule of Disbursements by Grant  
Year Ended December 31, 2012**

Award: New Jersey Cancer Education and Early Detection  
 Grant Year: July 1, 2012 - June 30, 2013  
 Grant Number: DFHS13CED024

Category	(Unaudited) Final Budget	Current Year Expenditures	Total Program Expenditures	Questioned Costs
<b>PERSONNEL:</b>				
Salaries	\$ 67,160	\$ 33,064	\$ 33,064	\$ -
Fringe benefits	13,600	6,696	6,696	
<b>TOTAL PERSONNEL</b>	<b>80,760</b>	<b>39,760</b>	<b>39,760</b>	
<b>OTHER COST CATEGORIES:</b>				
Facility costs	-	-	-	
Office expense and related costs	-	-	-	
Program expense and related costs	-	-	-	
Travel, conference and meetings	-	-	-	
<b>TOTAL DIRECT COSTS</b>	<b>80,760</b>	<b>39,760</b>	<b>39,760</b>	
<b>INDIRECT COSTS</b>	<b>-</b>	<b>-</b>	<b>-</b>	
<b>TOTAL COSTS</b>	<b>80,760</b>	<b>39,760</b>	<b>39,760</b>	
Less program income	-	-	-	
<b>NET TOTAL COSTS</b>	<b>\$ 80,760</b>	<b>\$ 39,760</b>	<b>\$ 39,760</b>	<b>\$ -</b>

**Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards**

To the Board of Directors  
Zufall Health Center, Inc.

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Zufall Health Center, Inc., (the "Center"), which comprise the statement of financial position as of December 31, 2012, and the related statements of activities and changes in net assets, functional expenses and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated September 26, 2013

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Center's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Center's internal control. Accordingly, we do not express an opinion on the effectiveness of the Center's internal control.

*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. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weakness or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Center's financial statements are free from 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 certain 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 items 2012-1 and 2012-2.

## The Center's Responses to Finding

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

## Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Center's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Center's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

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

New York, New York  
September 26, 2013

**Independent Auditor's Report on Compliance for Each Major Federal  
and State Program and Report on Internal Control over Compliance Required  
by OMB Circular A-133 and New Jersey OMB Circular 04-04**

To the Board of Directors  
Zufall Health Center, Inc.

Report on Compliance for Each Major Federal and State Program

We have audited Zufall Health Center, Inc.'s (the "Center") compliance with the types of compliance requirements described in the U.S. Office of Management and Budget ("OMB") Circular A-133 Compliance Supplement and New Jersey OMB Circular 04-04 that could have a direct and material effect on each of its major Federal and state programs for the year ended December 31, 2012. The Center's major Federal and state programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Center's major Federal and state programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations; and State of New Jersey, Department of Treasury, Office of Management and Budget Circular 04-04, Single Audit Policy for Recipients of Federal Grants, State Grants and State Aid. Those standards and OMB Circular A-133 and New Jersey OMB Circular 04-04 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 or state program occurred. An audit includes examining, on a test basis, evidence about the Center's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major Federal and state program. However, our audit does not provide a legal determination of the Center's compliance.

### Opinion on Each Major Federal and State Program

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

### Other Matters

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2012-1 and 2012-2. Our opinion on each major Federal and state program is not modified with respect to this matter.

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

### Report on Internal Control over Compliance

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

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 and state 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 and state will not be prevented, or detected and corrected, on a timely basis. . A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a Federal and state that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weakness. However, we identified certain deficiencies in internal control over compliance as described in the accompanying schedule of findings and questioned costs as items 2012-1 and 2012-2 that we consider to be significant deficiencies

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

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

*CohnReznick LLP*

New York, New York  
September 26, 2013

Zufall Health Center, Inc.

Schedule of Findings and Questioned Costs  
Year Ended December 31, 2012

**Section I - Summary of Auditor's Results:**

Financial Statements:

Type of auditor's reports issued: Unmodified

Internal control over financial reporting:

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

Noncompliance material to financial statements noted?  yes  no

Federal and State Awards:

Internal control over major programs:

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

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

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133?  yes  no

Identification of major programs:

<u>CFDA and State Number(s)</u>	<u>Name of Federal and State Program</u>
	U.S. Department of Health and Human Services: Health Center Cluster:
93.224	Consolidated Health Centers
93.527	Affordable Care Act (ACA) Grants for New and Expanded Services under the Health Center Program
93.703	ARRA Grants to Health Centers Programs: Facilities Improvement Program
	State of New Jersey Department of Health and Senior Services: Preventive and Primary Care Program
05-2192-CHS-N-0	

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

Auditee qualified as low-risk auditee?  yes  no

Zufall Health Center, Inc.

Schedule of Findings and Questioned Costs  
Year Ended December 31, 2012

**Section II - Financial Statement Findings:**

None

**Section III - Federal and State Award Findings and Questioned Costs:**

Item 2012-1: Drawdown of Grant Funds: U.S. Department of Health and Human Services: Health Center Cluster (CFDA 93.224 and 93.527), ARRA-Grants to Health Center Programs: Facilities Improvement Program (CFDA 93.703)

Criteria:

In accordance with the requirements of OMB Circular A-110 and the Cash Management Improvement Act (31 USC 6503; 31 CF part 205), grantees must place Federal funds to draw down in interest-bearing accounts and any interest earned must be submitted to the U.S. Treasury.

Statement of Condition:

During the year, the Center made draw-downs of Federal funds which were not deposited into an interest-bearing account in accordance with OMB Circular A-110.

Questioned Costs:

None

Effect:

The Center was not in compliance with OMB Circular A-110 guidelines.

Cause:

Management was aware of the cash management compliance requirement that stipulates that an interest-bearing account must be used for Federal funds drawn-down. However, Management represented that due to restrictions to their banking arrangement, they were unable to maintain an interest-bearing account.

Recommendation:

The Center should ensure that all Federal funds are deposited into an interest-bearing account in accordance with the grant requirements and OMB Circular A-110. Interest earned on Federal grant advances are required to be remitted to the Federal government on a timely basis, if in excess of \$250.

Management's Response:

Management concurs with this finding and has since implemented the procedures necessary. The bank account was initially established as an interest-bearing account as per Federal requirements. Sometime in 2010, a change was made to the account structure at the bank and the account became a non-interest bearing account. Management has contacted the bank and has since re-established the interest-bearing account.

**Zufall Health Center, Inc.**

**Schedule of Findings and Questioned Costs  
Year Ended December 31, 2012**

Item 2012-2: Time and Effort Reporting: U.S. Department of Health and Human Services: Health Center Cluster (CFDA 93.224 and 93.527), ARRA-Grants to Health Center Programs: Facilities Improvement Program (CFDA 93.703)

Criteria:

OMB Circular A-122 requires that the distribution of salaries and wages to awards must be supported by timesheets or personnel activity reports (time and effort report). The said report is required to meet certain standards, two of which are that the time and effort report must be signed and dated by the individual employee or responsible supervisory official having first-hand knowledge that the distribution of activity represents a reasonable estimate of the actual work performed by the employee during the periods covered and that the time and effort report must be prepared at least monthly and must coincide with one or more pay periods.

Statement of Condition:

The Center's time and effort reports were not signed by the employees or the supervisory officials having first-hand knowledge of the distribution of activity and actual work performed by the employees.

Questioned Costs:

None

Effect:

The Center did not comply with the requirement in relation to affixing the employees' or supervisors' signature in the time and effort report.

Cause:

The Center utilized the time sheets completed for purposes of processing payroll and also the schedules supporting vouchers as basis for time and effort spent on programs. However, the system used to document such time sheets was not established in a way that enabled reviewers or the employees to electronically sign off on the time sheet.

Recommendation:

We recommend that the Center ensure that employees or supervisors sign and review the time and effort reports.

Management's Response:

Management concurs with this finding and will implement the procedures necessary. While the previous paper-based payroll system did require employee and supervisor signatures documenting time and effort, management recently implemented a new time and attendance system to better track the distribution of salaries and wages to awards per Federal regulations. Management has now updated the system so the supervisor will review the employees associated program/grant on the time sheet and approve that time sheet electronically. Additionally for the limited number of employees that have multiple programs/grants, the labor distribution report will be distributed to the supervisor for signature/approval and kept as supporting documentation.

Zufall Health Center, Inc.

Schedule of Prior Year's Findings  
Year Ended December 31, 2012

Item #	Description of Condition	Status of Corrective Action
2011-1	Reconciliation and closing procedures were not properly implemented for the following: (1) Ensuring the validity of account balances, especially with regards to verifying the completeness of revenues and receivables recorded; (2) Verifying completeness of revenues and receivables recorded; (3) Verifying the reasonableness of accrued expenses	This condition was corrected in the current year.