July 27, 2010

TO: Mary Wakefield, Ph.D., R.N.
Administrator
Health Resources and Services Administration

FROM: /Lori S. Pilcher/
Assistant Inspector General for Grants, Internal Activities,
and Information Technology Audits

SUBJECT: Results of Limited Scope Review at Harbor Homes, Inc. (A-01-10-01502)

The attached final report provides the results of our review of Harbor Homes, Inc.

Section 8L of the Inspector General Act, 5 U.S.C. App., requires that the Office of Inspector General (OIG) post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at http://oig.hhs.gov.

Please send us your final management decision, including any action plan, as appropriate, within 60 days. If you have any questions or comments about this report, please do not hesitate to contact me at (202) 619-1175 or through email at Lori.Pilcher@oig.hhs.gov. Please refer to report number A-01-10-01502 in all correspondence.

Attachment

cc:
Patricia Reese
Director, HRSA
Office of Federal Assistance Management/Division of Financial Integrity

Department of Health & Human Services

**OFFICE OF
INSPECTOR GENERAL**

RESULTS OF LIMITED SCOPE REVIEW AT HARBOR HOMES, INC.

Daniel R. Levinson
Inspector General

July 2010
A-01-10-01502

Office of Inspector General

http://oig.hhs.gov

The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health & Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

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Section 8L of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site.

OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS

The designation of financial or management practices as questionable, a recommendation for the disallowance of costs incurred or claimed, and any other conclusions and recommendations in this report represent the findings and opinions of OAS. Authorized officials of the HHS operating divisions will make final determination on these matters.

EXECUTIVE SUMMARY

BACKGROUND

The Health Centers Consolidation Act of 1996 (P.L. No. 104–299) consolidated the Health Center Program under Section 330 of the Public Health Service Act (PHS Act), codified at 42 U.S.C. § 254(b). Pursuant to 42 U.S.C. § 254(b), the Health Center Program is a national program designed to provide comprehensive primary health care services to medically underserved populations through planning and operating grants to health centers. Within the U.S. Department of Health & Human Services, the Health Resources and Services Administration (HRSA) administers the Health Center Program.

Under the American Recovery and Reinvestment Act of 2009, P.L. No. 111-5 (Recovery Act), enacted February 17, 2009, HRSA received $2.5 billion, including $2 billion to expand the Health Center Program to serve more patients, stimulate new jobs, and meet the significant increase in demand for primary health care services among the Nation's uninsured and underserved populations.

Harbor Homes, Inc. (HHI) has been in operation since 1980 and is a nonprofit agency that serves the people and communities of Greater Nashua, New Hampshire by fulfilling its mission to create and provide quality residential and supportive services for persons (and their families) challenged by mental illness and/or homelessness. In addition to housing and supportive services, HHI also provides substance-abuse services, health and medical care, HIV/AIDS support, mental health counseling, and peer support and training.

HHI is funded primarily through HRSA, Veteran's Administration, and Homeland Security grants, Medicaid, State grants, and donations. During Federal fiscal year 2009, HRSA awarded HHI three separate 2-year Recovery Act grants totaling $1,274,618.

OBJECTIVES

Our objective was to assess HHI's financial viability, capacity to manage and account for Federal funds, and capability of operating a community health center program in accordance with Federal regulations.

SUMMARY OF FINDINGS

Based on our review of HHI's audited financial statements ending June 30, 2009, we found that HHI would not have been considered financially viable. Specifically, its current asset to current liability ratio was less than one and it had a negative working capital ratio. Although HHI has provided us with unaudited financial statements as of March 31, 2010 which demonstrates that HHI has improved its short-term liquidity, HHI has only slightly improved its long-term stability. HHI attributes these improvements to an increase in its investment balance, a reduction in staffing costs, a reduction in rental expenses and tightening their collection process of all receivable balances. However, HHI needs to continue its efforts to become more financially viable.

HHI's financial management system is able to adequately manage and account for Federal funds. We also found that HHI has the capability to operate a community health center in accordance with Federal regulations.

RECOMMENDATION

We recommend that HRSA consider the information presented in this report in assessing HHI's capability as a recipient of HRSA funds.

HARBOR HOMES, INC.'S COMMENTS

In its response to the draft report, the Grantee identified that its deferred loan balance should have been backed out of the long-term stability ratio calculation. Specifically, the long-term stability ratio for June 2009 would have decreased from approximately 87 percent to 74 percent, and the ratio for March 2010 would have decreased from approximately 79 percent to 59 percent. HHI stated that it is confident that the long-term stability of the organization is financially sound. HHI's comments are included in the Appendix.

OFFICE OF INSPECTOR GENERAL COMMENTS

We have adjusted our calculations by removing the deferred liability amounts identified in the Grantee's response and have revised our report accordingly. However, despite revisions to HHI's total liabilities and long-term stability ratio calculation, more than half of HHI's assets remain financed through debt, and therefore HHI will need to continue its efforts to become more financially viable.

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INTRODUCTION

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Health Center Program

The Health Centers Consolidation Act of 1996 (P.L. No. 104–299) consolidated the Health Center Program under Section 330 of the Public Health Service Act (PHS Act), codified at 42 U.S.C. § 254(b). Pursuant to 42 U.S.C. § 254(b), the Health Center Program is a national program designed to provide comprehensive primary health care services to medically underserved populations through planning and operating grants to health centers. Within the U.S. Department of Health & Human Services, the Health Resources and Services Administration (HRSA) administers the Health Center Program.

The Health Center Program provides grants to nonprofit private or public entities that serve designated medically underserved populations, including migrant and seasonal farm workers, the homeless, and residents of public housing. Health centers funded by HRSA are community-based, patient-directed organizations that meet the definition of "health center" under 42 U.S.C. § 254(b).

Recovery Act Funds

Under the American Recovery and Reinvestment Act of 2009, P.L. No. 111-5 (Recovery Act), enacted February 17, 2009, HRSA received $2.5 billion, including $2 billion to expand the Health Center Program to serve more patients, stimulate new jobs, and meet the significant increase in demand for primary health care services among the Nation's uninsured and underserved populations. HRSA made four types of grants available to health centers to provide for new access points, increased demand for services, facilities investment programs, and capital improvement programs. Grants were provided to new and existing health centers, and a center could receive more than one type of grant.

Requirements for Federal Grantees

Pursuant to 45 CFR § 74.21, grantees are required to maintain financial management systems that contain written procedures for determining the reasonableness, allocability, and allowability of costs. Grantees must maintain accounting records that are supported by source documentation and must maintain financial systems that provide for accurate and complete reporting of grant-related financial data. Grantees are also required to compare outlays with budget amounts for each award and may use grant funds only for authorized purposes. In addition, Federal regulations specify the size, composition, and responsibilities of a Grantee's board of directors. The Recovery Act and Office of Management and Budget (OMB) guidance M-09-15 set forth further requirements for transparency and accountability.

Harbor Homes, Inc.

Harbor Homes, Inc. (HHI) has been in operation since 1980 and is a nonprofit agency that serves the people and communities of Greater Nashua, New Hampshire by fulfilling its mission to create and provide quality residential and supportive services for persons (and their families) challenged by mental illness and/or homelessness. In addition to housing and supportive services, HHI also provides substance-abuse services, health and medical care, HIV/AIDS support, mental health counseling, and peer support and training.

HHI is funded primarily through HRSA, Veteran's Administration, and Homeland Security grants, Medicaid, State grants, and donations. During Federal fiscal year 2009, HRSA awarded HHI three separate 2-year Recovery Act grants totaling $1,274,618. The awards include $930,000 for new access points, $100,650 for increased demand for services, and $243,968 for capital improvement programs.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to assess HHI's financial viability, capacity to manage and account for Federal funds, and capability of operating a community health center program in accordance with Federal regulations.

Scope

We reviewed HHI's audited financial statements for FYs 2007 through 2009, as well as unaudited financial statements through March 31, 2010. We also reviewed HHI's accounting and personnel policies and procedures for FY 2009. This limited-scope review is part of a series of reviews planned by the Office of Inspector General to provide oversight of funds provided by the Recovery Act. Therefore, we did not perform an overall assessment of HHI's internal control structure.

We performed our fieldwork at HHI's administrative office in Nashua, New Hampshire, during March 2010.

Methodology

To accomplish our objectives, we;

- reviewed relevant Federal laws, regulations, and guidance;
- reviewed HHI's HRSA grant application packages and supporting documentation;
- reviewed HHI's fiscal policies and procedures related to accounting documentation and preparation of financial reports;

- reviewed HHI's administrative procedures related to personnel, conflict resolution, and nonfinancial matters;

- reviewed HHI's procedures in place to address the Recovery Act reporting requirements;

- performed liquidity and stability analyses of HHI's finances for FY 2007 through 2009 and as of March 2010 to determine whether HHI was financially viable;

- reviewed HHI's audited financial statements and audits conducted pursuant to OMB Circular A-133 for FYs 2007 through 2009;

- interviewed HHI's personnel to gain an understanding of HHI's operations;

- reviewed minutes from HHI's Board of Directors' meetings; and

- discussed findings with HHI's officials.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

FINDINGS AND RECOMMENDATION

Based on our review of HHI's audited financial statements ending June 30, 2009, we found that HHI would not have been considered financially viable. Specifically, its current asset to current liability ratio was less than one and it had a negative working capital ratio. Although HHI has provided us with unaudited financial statements as of March 31, 2010 which demonstrates that HHI has improved its short-term liquidity, it has only slightly improved its long-term stability. HHI attributes these improvements to an increase in its investment balance, a reduction in staffing costs, a reduction in rental expenses and tightening their collection process of all receivable balances. However, HHI needs to continue its efforts to become more financially viable.

HHI's financial management system is able to adequately manage and account for Federal funds. We also found that HHI has the capability to operate a community health center in accordance with Federal regulations.

FINANCIAL VIABILITY

Federal Regulations

Pursuant to 45 CFR § 74.14, grantees should be financially viable. Specifically, this regulation states that the awarding agency may impose additional requirements as needed if an applicant or recipient has a history of poor performance or is not financially stable.

Harbor Homes, Inc.'s Financial Viability

We determined that as of June 30, 2009, HHI would not be considered financially viable by analyzing its short-term liquidity, defined by the ratio of its assets to its liabilities, and its long-term stability, defined by its reliance on debt for asset formation. Although HHI has provided us with unaudited financial statements as of March 31, 2010 which demonstrates that HHI has improved its short-term liquidity, it has only slightly improved its long-term stability.

Short-Term Liquidity

HHI has improved its short-term liquidity since June 2009.

Specifically:

- HHI's current assets-to-liabilities ratio (current assets divided by current liabilities) increased from 0.8 to 1.3 between the end of June 2009 and March 31, 2010. Generally, for an organization to be considered fiscally sound, its current assets should be valued higher than its current liabilities.

- HHI's working capital (current assets minus current liabilities) increased between the end of June 2009 and March 31, 2010, from a negative $260,034 to a positive $446,452. Positive working capital is a common measure of an organization's liquidity, efficiency, and overall health.

HHI attributes its improved liquidity between FY ending June 30, 2009 and March 31, 2010 to organizational changes, including:

- Implementing a five percent pay decrease for executive employees,
- Reducing its workforce through layoffs,
- Reducing benefits and requiring employees to take furlong days,
- Reducing rental expense, and
- Tightening the collections process on all accounts receivable

Long-Term Stability

HHI's total debt (liabilities) for June 2009 was $5,701,008 and its total assets were $7,747,830. Thus, approximately 74 percent of HHI's assets were financed through debt, indicating that the grantee does not currently have long-term stability. HHI's long-term stability improved slightly as of March 31, 2010 as HHI’s total debt was $7,269,837 and its total assets were $12,299,326, resulting in approximately 59 percent of HHI’s assets being financed through debt. In general, the lower an organization’s reliance on debt for assets formation, the greater the organization’s long-term stability because excessive debt can lead to heavy interest and principal repayment burden.

RECOMMENDATION

We recommend that HRSA consider the information presented in this report in assessing HHI’s capability as a recipient of HRSA funds.

HARBOR HOMES, INC.’S COMMENTS

In its response to the draft report, the Grantee identified that its deferred loan balance should have been backed out of the long-term stability ratio calculation. Specifically, the long-term stability ratio for June 2009 would have decreased from approximately 87 percent to 74 percent, and the ratio for March 2010 would have decreased from approximately 79 percent to 59 percent. HHI stated that it is confident that the long-term stability of the organization is financially sound. HHI’s comments are included in the Appendix.

OFFICE OF INSPECTOR GENERAL COMMENTS

We have adjusted our calculations by removing the deferred liability amounts identified in the Grantee’s response and have revised our report accordingly. However, despite revisions to HHI’s total liabilities and long-term stability ratio calculation, more than half of HHI’s assets remain financed through debt, and therefore HHI will need to continue its efforts to become more financially viable.

APPENDIX

45 High Street
Nashua, NH 03060
www.harborhomes.org

HARBOR HOMES, INC.

Phone: 603-882-3616
603-881-8436
Fax: 603-595-7414

A Beacon for the Mentally Ill and Homeless for Over 25 Years

June 16, 2010

Department of Health & Human Services
Office of Inspector General
Office of Audit Services
Region 1
John F. Kennedy Federal Building
Room 2425
Boston, Ma 02203

ATT: Michael Armstrong
RE: Results of Limited Scope Review

Dear Mr. Armstrong:

We are in receipt of the draft Limited Scope Review Report of Harbor Homes, Inc. dated June 10, 2010. We noted that there is one finding relating to the Long-Term Stability of the Organization. The following is Management's response.

The overall mission of Harbor Homes, Inc. is to provide quality residential and supportive services for persons (and their families) challenged by mental illness and/or homelessness. With this mission comes substantial investment in properties to house these individuals resulting in substantial long-term debt. However, within the long-term debt are loans that are considered to be deferred that have no expectation or requirement of repayment as long as the property is operated as affordable rental housing.

These deferred loans are grants from the New Hampshire Housing Finance Authority (NHHFA) or the Federal Home Loan Bank. These funding sources require that the grants be recorded as a mortgage backed property which requires them to be recorded as long-term mortgages.

According to the auditors and NHHFA, see Note 13 in the June 30, 2009 audited financial statements and the letter from NHHFA, subsequently emailed for your records, which defines the requirements of these types of loans. At June 30, 2009 and March 31, 2010, the deferred loan balance was $1,038,485 and $2,389,088, respectively. It is Managements opinion that these amounts be backed out of the Long-Term Stability ratio calculation.

This would affect the ratio calculation as follows:

June 30, 2009: the percentage of HHI's assets financed through debt decreased from 87% to 74%
March 31, 2010: the percentage of HHI's assets financed through debt decreased from 79% percent to 59%.

The Organization has been in business for approximately 30 years and has invested heavily in property to house the homeless and mentally challenged. Over the years, HHI has purchased approximately 25 properties. Per Generally Accepted Accounting Principles, the values of the buildings remain on the books at net book value. These buildings have been repaired, upgraded and maintained over the years and the equity in the buildings is not reflected in the ratio calculations showing the true value of the assets against the long-term debt.

We would like to note the following:

Equity	Book Value	Replacement Value
Value of fixed assets:	$ 5,839,324	$ 15,429,000
Assets financed by long-term debt	$ 3,931,269	$ 3,931,269
Total equity	$ 1,908,055	$ 11,497,731

Replacement value is based on the insured cost at June 30, 2009. Based on the above, the Organization is in a good financial equity position.

Management is constantly working to reduce the liabilities and increase the assets and with the implementation of a corrective action plan beginning in February, we have increased our cash flow and profits over the last four months.

Additionally, the financial position is expected to improve over the next six months with the following additional actions:

- Major construction project will close within a few weeks that have come in with over budgeted donations and grants. This will result in the release of a government earmark grant for project development funds that will come back to the Organization and will be used to pay down the short term debt. It is expected that a $250K reduction on the line of credit will be paid by the end of August 2010.
- A previously used administrative building located in a commercial downtown district is expected to be sold by December 31, 2010. Equity in this building is substantial, as the mortgage balance is approximately $150K and estimated value is approximately $700K. With the proceeds, the Organization is expected to pay-down the line of credit which will decrease the current liabilities by another $250 and the balance of the proceeds will be put in an investment account.

The Organization recognizes that the debt service will always be a challenge given the type of mission that we strive to accomplish and the great need for housing. However, Management is confident that the long-term stability is sound and has the equity and the financial capability to sustain any long-term challenges that the Organization will face now and in the future.

Sincerely,

Patricia Robitaille, CPA
Vice President of Finance